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The Political Economy of Mahathir's China Policy: Economic Cooperation, Political and Strategic Ambivalence

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Malaysia's China policy has changed from mutual suspicion and at times hostility during Tunku Abdul Rahman's leadership (1957-1970) to détente, diplomatic normalization and peaceful coexistence under Abdul Razak (1970-1976) and Hussein Onn's administrations (1976-1981) and finally to economic cooperation, political and strategic ambivalence during Mahathir's era (1981 to 2003).[1]

These changing phases in Malaysia's foreign policy toward China have reflected the dynamic changes, in both internal as well as external conditions, which have brought about different diplomatic interactions between the two countries. While the early periods of Malaysia's China policy have already been studied by this writer,[2] this paper analyzes Malaysia's China policy under Mahathir's leadership, focusing on the political and economic dimension of his policy. The main thesis of this paper is to argue that Mahathir's economic policy toward China is pragmatism and cooperation, but his thinking on strategic-cum security issues is ambivalent.

Economic Cooperation: Trade and Investment

Malaysia-China economic relations can be divided into three periods, that is first, the pre-diplomatic recognition period: 1957-1973; second, the recognition era: 1974-1984 and finally, the period since 1985, after Mahathir's first important official visit to Beijing on 20 November 1985. The following sections analyze trade and investment in Malaysia's economic relations with China.

The first period from 1957-1973, can be characterized as trade via non-official channels as it took place through the private sectors, mainly Chinese middlemen in Singapore and Hong Kong. The main reason for not using direct trade was the Tunku's non-recognition policy (1957-1970) of China. Furthermore, it was also due to the economic embargo by the U.S. against China, which made it difficult for Malaysia-China trade to develop normally. In 1957, the total value of bilateral trade was only US$59.94 million.[3] In 1970, Sino-Malaysian total trade was US$95.6 million.[4] The data showed that these low trade figures were a function of the Tunku's non-recognition policy and both Malaysia's and China's mutual suspicion given the cold war struggle between the Soviet Union and the U.S.

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However, when Razak succeeded the Tunku in September 1970, it marked the end of the first period of indirect trade and ushered in a new phase of more active and direct trade between the two countries. Razak's pragmatic China policy resulted in a breakthrough, i.e. the first unofficial visit to Beijing in May 1971 by Tunku Razaleigh, the then head of the Perbadanan Nasional (PERNAS, National Trading Corporation). Three months later, China sent an international trade delegation to visit Kuala Lumpur. The trip resulted in China purchasing 40,000 tons of Malaysia's natural rubber, which was double the amount of the preceding years.[5] The significance of this purchase marked the beginning of direct trade between the two countries. After normalization in 1974, total trade jumped to US$159.17 million in 1974 that is up from US$27.8 million in 1971. Thereafter, with the exception of 1976, (US$136.41 million), trade between the two countries progressively increased to US$424.40 million in 1980. Thus one can hypothesize that the increase in trade was positively correlated to the establishment of diplomatic recognition.[6] Although the trade volume between the two countries increased from 1974 to 1984, the pattern of trade remained stable around 2% to 2.5% of the total trade in both countries. In 1980, for example, China exported to Malaysia about 2.3% of its total trade volume, whereas Malaysia's exports to China consistently hovered around 2% of its total export.[7] Thus China was not an important trading partner for Malaysia, and neither was Malaysia that important for China. One of the reasons why Malaysia-China trade ties did not get stronger was due to the downturn of economic growth in Malaysia from 1980-1985.

The third period in Malaysia-China trade began after 1988. The impetus came after Mahathir's first official visit to Beijing in November 1985. The trade data showed that the volume jumped from around US$289 million from 1981 to US$557 million in 1987 and again to US$877 million in 1988, and finally to US$1183 million in 1990.[8] Malaysia-China bilateral trade has continued to grow rapidly since the post-cold war era. In 1991, the total trade was US$1.33 billion and in 1998 it jumped to US$4.26 billion. Thus bilateral trade expanded more than six-fold from US$1.475 billion in 1992 to US$7.6 billion in 2001.[9] In 2002, Malaysia for the first time overtook Singapore as China's largest trading partner in the Association of Southeast Asian Nations (ASEAN) grouping. Of its total exports, US$325.64 billion, China exported 1.5%, that is US$5 billion, to Malaysia. China, of its total imports, US$295.30 billion, imported US$9.30 billion (3.2%) from Malaysia; this resulted in a trade deficit of US$4.3 billion vis-à-vis Malaysia. Thus between 1996 and 2002, Malaysia's trade with China grew about four times, i.e. from US$3.6 billion to US$14.3 billion in 2002.[10]

What were the reasons for this jump in Malaysia-China trade after 1990? First, in January 1988, the Malaysian Cabinet decided to abolish the administrative rule to get special permission to import Chinese goods. The 5% administrative charge was also abolished in the same year. Secondly, the Malaysian government also lifted the restrictions on businessmen and traders, which had limited their visits to the Canton Trade Fair. Thirdly, in order to facilitate Malaysian businessmen (mainly ethnic Chinese) doing business in China, the Malaysian immigration authorities altered the multiple exit permits to allow businessmen a longer stay in China. The Malaysian government also loosened its control by not insisting that business delegations to China require officials from the Ministry of Interior to accompany them. In April 1988, both governments signed a Sino-Malaysian Trade Agreement wherein both sides agreed to give preferential treatment to custom tariffs on imported goods. In

June 1988, both sides signed an air flight agreement. In November 1988, the two parties signed an Investment Guarantee Agreement and an accord on the establishment of a Sino-Malaysian Economic and Trade Joint Committee. The Ministry of Education also encouraged Chinese students to study in Malaysian schools and universities. By the end of 2001 for example, there were 4,691 Chinese students studying in Malaysia.[11] Moreover, to attract more Chinese tourists to Malaysia, visas for Chinese group tours were granted at all major points of entry into Malaysia after March 2001.[12] All these agreements and measures have strengthened and enhanced economic and trade co-operation between the two countries.

The bilateral trade structure shows that Malaysia's exports to China shifted from primary resources in the 1970s and 1980s to the manufacturing sector in the 1990s. In 2001, electrical and electronic products (49.1%), chemicals and chemical products (10.6%), machinery, appliances and parts were the main exports (4.5%); whereas, primary products, such as palm oil (10%) and crude petroleum (3.8%) were of secondary importance.[13] In 2001, Malaysia's imports from China also mainly concentrated on the manufacturing sector such as electrical and electronic products (52.7%), machinery, appliances and parts (7.2%), chemicals and chemical products (5.5%), textile and clothing (4.6%).[14] These trade patterns indicate that both Malaysia's and China's economies became more industrialized in the 1990s than in the 1980s. The trade structure shows that Sino-Malaysian trade relations are more complimentary than competitive.

Data in Table 1 shows that China consistently suffered from trade deficit with Malaysia after 1990, which was a reversal of the trade surplus from 1971 to 1984.[15] Did China's trade deficit adversely affect the political relations between the two countries? Unlike the Sino-US trade deficit which can easily have spill-over effects to diplomatic relations between Beijing and Washington, China's continuous trade deficit with Malaysia did not have any adverse diplomatic repercussions on the political relations between China and Malaysia, as there has been the will on both sides to strengthen their economic and trade ties. China in fact has been using the trade deficit as an incentive for those ASEAN states, which are enjoying a surplus, to promote better diplomatic ties with Beijing. Trade also serves China's larger longer economic and strategic interests in Southeast Asia. In August 1996 for example, during a four-day working visit to Beijing, Mahathir witnessed the signing of fifteen agreements between Malaysian businessmen and their Chinese counterparts undertaking joint venture projects ranging from the construction of toll highways, the manufacture of vehicles and spare parts, to the construction of mills and power plants.[16] Mahathir felt that both China and Malaysia could do more in economic cooperation in the areas of communication and air transport, besides increasing the volume of investments between the two countries.[17]

The shift in trade patterns is also reflected in the changing investing patterns between the two countries, from primary commodities to the manufacturing sector of the economy. This was evident from the shift in Chinese investments in Malaysia. Given Malaysia's rich resources of rubber, tin and palm oil, naturally, China's earliest investments in Malaysia were mainly concentrated in resources. As Malaysia became more industrialized, Chinese investments in Malaysia moved more towards the manufacturing sector. From 1996 to 2000, China's cumulative investments in Malaysia concentrated mainly in metal and related sectors (39%), electronics and

electrical (33%), light manufacturing (14%), machinery and equipment (8%), petroleum and chemicals (5%), non-metal minerals (3%).[18]

At the ASEAN Foreign Ministers' meeting in July 1997, Mahathir criticized the West. He said that the West intended to weaken the ASEAN economies by undermining the currencies of the ASEAN states. Mahathir was critical about the globalization processes when he said, "we are told that we must open up, that trade and commerce must be totally free. Free for whom? For rogue speculators? For anarchists wanting to destroy weak countries in their crusade for open societies, to force us to submit to the dictatorship of international manipulators?"[19] Although Mahathir was critical about the West, he appreciated China's assurance not to devalue the Chinese currency. In apparent indirect effort to praise China, Mahathir reminded the West that ASEAN would not become a military alliance and should not label anyone as a potential enemy (implying China).[20]

On 31 May 1999, both Malaysia and China signed a twelve-point agreement in Beijing entitled: "Framework for Future Bilateral Cooperation" which aimed at facilitating "all directional relationship and good neighborliness, friendship and cooperation based on mutual trust and support."[21] Malaysia and China covered comprehensive economic cooperation in many areas including trade, investment, banking, finance, education, medicine, defense, security, science/technology, information, health, transport, environment, agriculture, forestry, mining, culture, tourism and friendly youth sports among others.[22] Besides, Malaysia and China continued to show positive upward trends in investments between the two countries after the signing of the Bilateral Trade Agreement in 1988. From June 1993 to August 1994, Malaysia and China signed forty-nine investment agreements amounting to US$1 billion.[23] Malaysia became China's tenth largest investor.[24] In 1997, China's investment in Malaysia was US$400 million.[25] In 1998, total Malaysian investment in China was estimated at US$1.4 billion, ranging from real estate, manufacturing services to retailing and infrastructure facilities.[26] In June 1999, both Malaysia and China agreed to undertake a US$2.5 billion mega-joint development project to develop a Trans-Asia Railway System, starting from Singapore to Kunming.[27] From 18 August to 20 August 1999, Mahathir led a two hundred and five (193 ethnic Malaysian Chinese) strong business delegation to Beijing.[28] The thrust of Mahathir's visit was trade, business and joint investment. Besides, the August 1999 visit boosted cultural ties between China and Malaysia. Mahathir hoped his visit to Beijing could help him gain popularity from the Chinese community to compensate for his loss of support from the Malay voters as a result of the trial and imprisonment of former Deputy Prime Minister Anwar Ibrahim. During Mahathir's talks with Chinese Premier Zhu Ronji on trade and investment issues in the areas of automobile, banking and paper pulp business, two Malaysian companies, Lion Forest Industries and Innoprise Corporation entered an agreement with their Chinese counterparts, China Fuxin Pulp and Paper Industries Co. for a joint venture project in paper pulp in Sabah, involving US$1 billion.[29] The Malaysian companies held 60% equity while the Chinese company had a share of 40% of the joint investment project.[30]

The two-way investment data shows that Malaysia invests more in China than vice versa. By the end of 2001, Malaysia had invested in 2216 projects in China. The agreed amount was US$5.42 billion, whereas the actual investment amounted to

US$2.45 billion. By the end of June 2002, China agreed to investments amounting to US$71.14 million whereas actual investments were only US$34.96 million.[31] This data shows that there is plenty of room for expansion in Sino-Malaysian investment ties.

Mahathir also proposed the establishment of an Asian Monetary Fund (AMF) to bail out the troubled regional economies. Mahathir argued that such a regional fund would help to protect the troubled Asian economies from the harmful effects of the International Monetary Fund's (IMF) stringent reform requirements.[32] On 19 August 1999, he also proposed the urgent need for China and Malaysia to set up an "Asian Media" to prevent the Western media from reporting "slanted and distorted" facts of world events to the Asian audiences.[33] He also blamed Westerners' jealousy of the success of the Asian economies for causing the Asian economic and financial crisis.[34] In order to minimize and prevent currency speculations, Mahathir proposed the creation of a new global financial architecture. Mahathir again tried to revitalize his idea of creating an East Asian Economic Grouping (EAEG), a consultative mechanism for East and Southeast Asian nations to get together to deal with matters of regional concern.[35] China responded favorably to Mahathir's idea and agreed to the idea of an EAEG and the establishment of an AMF.

Taking the opportunity of Chinese Premier Zhu Ronji's four-day official visit to Kuala Lumpur from 22-25 November 1999, Mahathir again called upon China and other East Asian nations to seriously consider setting up an AMF. At a dinner in honor of visiting Premier Zhu Ronji, Mahathir said, "It's crucial these weaknesses be overcome by putting in place a new financial mechanism. With the participation of developed and developing countries, Malaysia hopes very much China will play a positive role in this matter."[36] In response, Zhu Ronji announced on 23 November 1999 that China would give full support for the creation of an AMF. [37]

Mahathir wanted to send a message to the West that East Asia could be a unified economic force, capable of dealing with its own financial crisis. However, the establishment of an AMF has been opposed by the West, especially the U.S. and the IMF. Furthermore, how far Japan will go to render its support, considering possible U.S. pressure and the availability of Japanese funds is another question. Moreover, political infighting among the Asian member states may hinder economic and financial cooperation. How would the member states decide on the criteria for disbursing the funds and who would have the priority to be the first recipient? Thus it is easy for Mahathir to put forward` his idea of an AMF, but difficult to implement it.[38]

On bilateral economic cooperation, both Mahathir and Zhu witnessed the signing of three agreements: 1) cultural cooperation; 2) establishment of banking institutions; 3) exchange of animals between the State Forestry Administration of China and the Science, Technology and Environment Ministry of Malaysia. The Memorandum of Understanding signed between Malaysia and China was a general declaration of political intent without specifics. Mahathir however was confident after Zhu's visit that Malaysia-China ties will "go from strength to strength in the future. Malaysia and China were very close in terms of their understanding and approach towards the resolution of problems internationally."[39] Zhu reciprocated positively, and said, "There are no pressing issues between China and Malaysia. Even the problems that

exist now are not insurmountable through consultation."[40] Both leaders' remarks were rhetoric without good substance.

Political and Strategic Ambivalence

One of the challenges facing Malaysia is the rising military and economic power of China in the 21st century. Does China pose a serious threat to Malaysia? How is Mahathir's perception of rising China's power?

Malaysia's perception of the so-called "China threat" has undergone changes from the cold war period to the post-cold war era. During the cold war period i.e. from the 1950s to the 1970s Malaysia perceived China as an ideological and security threat, mainly because of Maoist support of the communist revolutionary movements in Southeast Asia. In 1982, Mahathir openly criticized China's continued links with the Malaysian communist insurgency and by implication that Beijing could pose a potential security threat to Malaysia. However, with the collapse of the communist insurgency movement in Malaysia in the late 1980s, the collapse of East European communism in 1989, the collapse of the Soviet Union in 1991, and Deng Xiao-ping's policy of economic modernization, Malaysia's perception of China has also changed, particularly under Mahathir's leadership. Mahathir's perception of the 'China threat' issue depended on timing and circumstances. Mahathir for instance did not have a coherent and consistent policy on China's strategic inroads into the South China Sea.

On the one hand, Mahathir did not perceive China could be an immediate security threat to Malaysia. In a forum on Malaysia-China relations held in Kuala Lumpur on 23 January 1995, Mahathir mentioned that China did not pose a political and military threat. In his view, China is a country, which offers ample economic opportunities for investments.[41] He reiterated that the countries of Southeast Asia should have no fear of a wealthy and strong China. Indeed Southeast Asia should welcome a wealthy China. It will share the wealth through trade and economic interaction. In Mahathir's view, a prosperous China will become the engine of growth, firstly for East Asia, and then the world.[42] On this occasion, Mahathir appeared to be "friendly" to Beijing when he said, "Beijing had not, historically exhibited colonization ambitions."[43] In response, China hailed Mahathir's stand.[44] Mahathir criticized the Western proponents of the "China threat" theory, which was based on past premises and were bad and dangerous.[45] But on the other hand, Mahathir's inconsistency could be seen on another occasion when he commented that the growing inflow of FDI to China at the expense of ASEAN could be an economic threat to Southeast Asia's trade with the world.[46] Malaysia has been losing out in attracting FDI after the Asian Financial Crisis, as the FDI has dropped from 6.4% of its GDP from 1990 to 1996 to 1.2% in 2002.[47] This is mainly due to China's attractiveness as a destination for low-tech manufacturing, low operating cost, plus being the largest market in the world. One can argue that the rise of the Chinese economy provides economic opportunities, particularly for employment of Malaysian workers, as exports to China have jumped by 43% in 2001-2002, compared to an increase of only 0.6% in Malaysia's overall exports.[48] The drop of FDI in Malaysia and in the ASEAN states in general may not necessarily be a zero-sum game as Multinational Corporations (MNCs) can increase their FDI in Malaysia and China concurrently, as they did prior to the Asian Financial Crisis.[49] In the 1980s MNCs have invested substantial amounts of FDI in Malaysia,

particularly in Penang for the electrical and electronics industry, which accounted for more than 60% of Malaysia's total exports.[50] Other countries in ASEAN, like Indonesia and Vietnam, still can compete with China due to their low cost labor.[51] One strategy for Malaysia to counter China's economic challenge is to adopt 'Malaysia plus China' joint partnerships in which both can gain based on the win-win model. Thus China can become an important 'economic strategic partner' for Malaysia in trade and investment through joint developments.

On the other hand, given the fact of China's continued economic modernization and increasing naval build-up, Beijing, from Mahathir's perspective can pose a potential long-term strategic-cum security threat for Malaysia. His long-term wariness of China could be seen from Mahathir's remark in 1985 when he said "Anything that might make her [China] too powerful might tempt a certain Chinese leadership to take over and move towards expansionism."[52]

Mahathir's political and strategic ambivalence towards China can best be seen from the sovereignty disputes with China over the Spratlys. In 1979, Malaysia formally claimed twelve reefs, shoals and atolls.[53] The Spratlys are strategically important for both China and Malaysia, because of their strategic location and due to their rich marine resources, as well as oil and gas. The sea surrounding the Swallow Reef is abundant in different species of tropical fish, especially tuna, which can generate good incomes for the fishermen. With the growing population of both Malaysia and China, the scramble for catching more fish to feed their people, and the dispute for controlling the maritime resources can be a real source of potential conflicts between the two countries. For China, they are important because they are situated at the southern tip of the maritime territory claimed by China.[54] China's claim is based on the historical ground of the nine dotted lines. Thus from China's perspective, Malaysia is China's close maritime neighbor. Of course, Malaysia challenges China's historical claim, because from Malaysia's perspective these reefs and shoals are not part of the Spratly island chain as they lay within Malaysia's continental shelf and the Exclusive Economic Zone (EEZ). Therefore from Malaysia's perspective, there is no sovereignty dispute over these reefs. [55]

The question is: how can the legal principle be reconciled with the claim based on the "historic rights"? Does China really want to resolve the Spratly disputes with Malaysia based on the principle of international law which China openly promised to do? Does China want to claim the whole water of the South China Sea or 80% of the water in the South China Sea? Is China only paying lip service to the adherence to the principle of international law while at the same time consolidating its control, waiting until such time its navy will be strong enough to "liberate" all the islands/reefs in the Spratlys?

China's behavior shows that Beijing has oscillated its position from moving from the "historic rights" to legal principles and vice-versa. At the same time, China is trying to expand its naval capabilities, such as acquiring sophisticated destroyers from Russia. Although Mahathir officially has said that China does not pose a security threat to Malaysia, most of the Malaysian security analysts view the growing assertiveness of China's Spratly policy and the upgrading of its naval capability with growing concern and anxiety. This can be seen from some Malaysian security analysts' comments, saying, "no matter what twists and turns Malaysia-China

relations may take, it can be argued that Malaysia has, and will in the foreseeable future regard China as its greatest threat in one form or another."[56] If China decided to push southward from the Mischief reef, the likely target would be James Shoal, which is claimed by Beijing as its southern point of its maritime territory. In the 1970s and 1980s, Vietnam was the target. In the 1990s the Philippines was the victim. In the 21st century, Malaysia as a target for China's further consolidation cannot be ruled out.

Since 1979, Malaysia's maritime policy can be described as assertive and pro-active in its claim against its adversaries. Malaysia's strategy is possession, presence and effective control. In order to consolidate its sovereignty claim over the Spratly islands, Malaysia decided to station a small amphibious force (about hundred and fifty members) and subsequently developed the Swallow Reef as a small tourist destination. Furthermore, Malaysia decided to upgrade its defense capability, by procuring more military hardware aimed at defending its sovereignty.[57] This pre-emptive move was to ensure a minimum hedge against the People's Liberation Army Navy (PLAN) intervention in the disputed islands and reefs. In this sense, Malaysia's assertiveness over the control of the Swallow Reef can be interpreted as "a strategic insurance."

Malaysia's determination to defend its sovereignty was clearly expressed by the then chief of the armed forces Hashim Mohamed Ali in April 1992, when he said: "The Malaysian armed forces will fight to the end to protect the nation's sovereignty should there be any use of force by countries claiming ownership of the Spratly archipelago."[58] Furthermore, he warned ASEAN to be "wary of China's military expansion,"[59] which, in his perception, could be destabilizing to the region's security. He reminded ASEAN that it should monitor closely developments in China, as it is still a socialist state ruled by the Chinese Communist Party.[60]

Malaysia, being a smaller power with its weak Royal Malaysian Navy (RMN), sees China's growing naval capability with concern and anxiety. With the Malaysian declaration of its EEZ in 1980, Malaysia has to cover more than 600,000 square kilometers of water. The RMN's maritime role has spread too thinly between Eastern and Peninsula Malaysia to be able to deal with China's navy adequately. As one Western maritime analyst put it, "Against the PLAN, it is doubtful that the RMN could even give the Chinese Navy a bloody nose."[61] Malaysia's geographical position is vulnerable to penetration of its maritime territory by external major powers, because there is a big gap between Western and Eastern Malaysia. Should a maritime war break out between the Chinese navy and the RMN, it would logistically be difficult for Malaysia to defend its occupied reefs in the South China Sea. To be more specific, the "Malay Sea" will likely be under pressure by the "Chinese Sea" given the continuing unabated rise in China's economic and military strength.

Mahathir recognizes that a military strategy may not be as effective as a political and economic engagement strategy in dealing with China because the RMN is militarily not strong enough to take on China's navy. But Malaysia hopes that through political interactions and economic cooperation with China, Beijing can be tied down to bilateral or multilateral mechanisms (such as the ASEAN Regional Forum) in such a way that potential armed conflicts over the Spratlys can be minimized, if not resolved. It was therefore no coincidence that Mahathir invited China to attend the post-ASEAN Ministerial meeting in 1991, when Malaysia was the host of the ASEAN

gathering in Kuala Lumpur. Despite the Malaysian and Western analysts' negative view about China's growing assertiveness in the South China Sea, Mahathir has been positive about China's behavior. In Mahathir's view, the South China Sea dispute is a problem but it is not unsolvable, as he once said, "There hasn't been a war yet. It has been predicted that we will fight each other, but we haven't yet. There have been light skirmishes here and there between Vietnamese and Chinese, but China has accepted that we should discuss this with ASEAN. When the Chinese put their rigs in what the Vietnamese claim to be their waters, we said that it is wrong. And China has responded to that very positively."[62]

Why is Mahathir's perception of China different from other Malaysian security analysts? Mahathir's ambivalent threat perception of China may be viewed from his personal contact with the Chinese top leadership since 1985. Since Mahathir's first official visit to Beijing in 1985, he has come to the conclusion that China's top priority has been and will be internal economic modernization and therefore in his assessment, China wants a genuine external stable environment so that Beijing can concentrate on its internal economic development.

It can be argued that Mahathir's thinking of China not being an immediate military threat is linked with his Vision 2020, which requires, like China, a stable external environment for transforming Malaysia into an affluent country by 2020. In order to make Mahathir's vision realizable, Mahathir needs a regional strategy "that intentionally de-emphasizes the Chinese threat while simultaneously asserting the need to contain if not moderate, Chinese foreign policy."[63] Mahathir's strategy of accommodation with China assumes that a successful economic development in China will be mutually beneficial to Malaysia-China relations. Hopefully, closer economic cooperation will eventually spill over to political and military cooperation.

Mahathir sees China's economic rise both as an opportunity and as a challenge for Malaysia's future economic development. On the one hand, Mahathir has been concerned with China's massive and cheap labor market, which has drained Foreign Direct Investment (FDI) from Malaysia; on the other hand, Mahathir adopts an economic bandwagon strategy by attempting to take advantage of the positives provided by the growing Chinese economy. Mahathir's administration has liberalized administrative measures, ranging from liberalizing visas, encouraging Malays to study the Chinese language, to changing the 'Look East' policy to include, besides Japan, learning from China, etc. as well as to entice Chinese students to study in Malaysia so as to promote economic benefits for Malaysia.

Mahathir's ambivalence can also be seen from his pro-Chinese business policy, encouraging ethnic Chinese Malaysians to invest in China as well as Chinese investments to Malaysia. What will be the political implications of these closer economic relations between the ethnic Chinese Malaysians versus the Malays, politically, economically and culturally in the context of nation building in Malaysia? Given the growing trend of closer economic cooperation between China and Malaysia, what will be the long-term impact and influence of China on Malaysia domestically? Will Malaysia, a Malay dominated multi-racial society slowly be sinicised by China's increasingly growing economic penetration?

One of the goals of Mahathir's developmental policy has been to resolve the 'Malays poverty dilemma' by implementing a 'Malay special rights' policy and administrative measures to uplift the Malays' social and economic status to a level comparable to the relatively wealthier ethnic Chinese. The fact remains however that there are fewer Malays than ethnic Chinese who benefit from China's economic growth. Malay capitalists are outnumbered by their Chinese counterparts in investments in China. The economic linkages between the 'red Chinese capitalists' and the Chinese Malaysian capitalists will eventually affect wealth concentration in favor of ethnic Chinese business groups at the expense of indigenous Malay capitalists and by implication may lead to political problems for Malaysia.

The Taiwan Factor: Politics of Trade and Investment

This section analyzes how Taiwan has been a factor in Sino-Malaysian political and economic relations. The main thesis is to show that Malaysian-Taiwanese trade and investments (particularly from Taiwan's perspective), cannot be separated from politics. An analysis of trade and volume of trade as well as the trade pattern is presented, followed by investments and finally by a brief discussion of the politics of trade and investments.

a) Trade

From Mahathir's perspective, Taiwan has been a relatively important trading partner for Malaysia. In 2001, the total trade between the two sides amounted to US$7.275 billion. Malaysia's exports to Taiwan consisted of US$4.213 billion whereas imports from Taiwan were US$3.061 billion, enjoying a surplus of US$1.152 billion. In 2002, the two-way trade slightly increased to US$7.284 billion, out of which Malaysia's imports accounted for US$3.132 billion with exports standing at US$4.151 billion, achieving a trade surplus of US$1.019 billion.[64] Taiwan was in fact Malaysia's fifth largest trading partner, accounting for 4.6% of Malaysia's total trade.[65]

The above trade data shows that Taiwan has been a relatively important trading partner for Malaysia.

Regarding the trade structure between Malaysia and Taiwan, electrical and electronic (E+E) LNG, chemical and chemical products (C+C) were the three major items of Malaysia's exports to Taiwan, which constituted about 75.2 % of the total exports in 2001. E+E were the largest items with a share of 58.2% of total exports, followed by LNG with 11.9% and C+C with 7.2% in 2001.[66]

In 2001, Malaysia's main imports from Taiwan were E+E (57.7%), machinery appliances and parts (11.6%), C+C products (7.4%) iron and steel products (4.2%) metals (3.9%).[67]

The above trade structure shows that the Malaysia-Taiwan trade pattern is more complimentary than competitive. Taiwan as a successful East Asian economic 'tiger' has been more important for Malaysia than vice-versa. Taiwan can continue providing Malaysia with high technology, particularly in the areas of information technology and electronics for Mahathir's vision of 2020 as an advanced industrialized economy. The hardworking Taiwanese work force, the Confucian culture of deference to political authority, the communitarian ideology and the entrepreneurial spirit of

capitalists fit into Mahathir's 'Look East' thinking, besides his admiration of Japanese economic success.

b) Investment

Taiwan's economic achievement as an "Asian Tiger" cannot be ignored from Mahathir's perspective. In the 1980s and early 1990s, Taipei has been a significant source of FDI for Malaysia. Mahathir was particularly interested in persuading Taiwanese entrepreneurs to transfer high-tech technology to Malaysia's Multi Media Super Corridor (MSC) project, a Malaysian version of 'Silicon Valley'. Because of cheap labor, political stability and the lure of a potential local market, Mahathir's pro-Taiwan business policy was successful in attracting Taiwanese entrepreneurs to invest heavily in Malaysia in the late 1980s and early 1990s. Taiwan has one advantage over Beijing in Malaysia, because of its earlier start of investments in Malaysia than China. In 1990, Taiwan's investment was US$2.383 billion involving 270 projects; it dropped to US$602million in 1992 and decreased to 237 projects. In 1994, 100 projects amounted to US$1.149 billion and in 1996, 79 projects were US$310 million.[68] By the end of 2002, Taiwan's cumulative investment was estimated at about US$9.2 billion.[69`] Taiwan was the third largest foreign investor, outstripped only by the US and Japan. Compared to China, Taiwan has invested more money in Malaysia than Beijing. In 2001, Taiwan invested about US$184 million, whereas China only invested US$ 5.2 million.[70]

From Taiwan's perspective, Malaysia has been a favorable destination for Taiwan's MNCs to invest, particularly in the areas of information technology and multimedia, due to Malaysia's political stability provided by Mahathir's administration's strong political leadership, the reliable and competitive work force, particularly the ethnic Chinese workforce and good infrastructure.

By the end of the 1990's, Malaysia had been under pressure to keep Taiwanese MNCs investing in the country. Due to China's relative cheap labor costs and larger market, there has been a tendency for Taiwanese companies to transfer their operations to China, particularly in the areas of manufacturing which needs more manpower.

c) Politics of Trade and Investment

The 'Taiwan factor' is an example where political ambivalence prevails in Mahathir's China-Taiwan policy. The challenge for Mahathir is how to maintain a delicate balance between the diplomatic struggle between Beijing and Taiwan. Officially, like all other ASEAN states, Malaysia has adopted a "one China" policy politically and a "one Taiwan" policy economically. Politically, Mahathir recognizes the growing importance of China as a regional player in international politics and economics in Southeast Asia and therefore has been careful not to invite Beijing's wrath by supporting Taipei's efforts to seek more political and diplomatic space in the ASEAN region. As far as Mahathir was concerned, the political contention between China and Taiwan was an internal issue of China's and therefore Malaysia did not want to be involved. In February 1995, Mahathir explained his position. 'We prefer to see China as a friend and partner in the pursuit of peace and prosperity for ourselves as well as for the region.' [71] Taiwan's 'southward policy' has been both politically and economically motivated. Its political aim was to compete with Beijing to seek greater diplomatic space and political leverage in Southeast Asia. In this sense, from

Beijing's perspective, Taiwanese economic presence was disguised political ambition to undercut China's diplomatic presence in Southeast Asia.[72] Hence, Beijing has been particularly sensitive to Taiwan's 'Dollar Diplomacy', 'Holiday diplomacy' and 'Flexible diplomacy', etc. – all these maneuvers Beijing has opposed relentlessly.

From Taiwan's perspective, Mahathir was an important leader in the ASEAN grouping, in view of his seniority as a regional spokesman for ASEAN in particular after the fall of Suharto in 1998. Mahathir is known as a strong leader, whose view on domestic economic development policy and regional issues cannot be ignored. His view on China and Taiwan was particularly significant for Taipei's authority to seek more diplomatic space vis-à-vis China in Southeast Asia.

Can Mahathir have both the Taiwanese bread and the Chinese butter simultaneously? The "Taiwan factor" may adversely affect not only Malaysia-China but also China-ASEAN relations. In 1996, for example, China showed its assertiveness, flexing its military muscles by launching some missiles over the Strait of Taiwan. This was a good example, why ASEAN was concerned about China's growing power. On the other hand, China was upset when some of the ASEAN states (the Philippines and Malaysia) tried to maintain diplomatic contact with Taiwan, although officially, Malaysia supports a "one China" policy. Thus in July 1998, Chinese Foreign Minister Tang Jiaxuan expressed concern about Taiwan's efforts to acquire more diplomatic leverage with Malaysia following the Taiwanese leader's visit to Kuala Lumpur. In December 1998, China again criticized Malaysia for allowing its Minister of Transport, Ling Liong Sik to travel to Taiwan.[73]

Conclusion

The above study shows that economic cooperation has been the central theme in Malaysia's China policy under Mahathir's leadership whereas the strategic-cum security dimensions remained of secondary importance. Economic primacy will continue to be the central consideration in Malaysia's China's policy even in the post-Mahathir era under the new leadership of Abdullah Ahmad Badawi since October 2003. However, the crux of the problem is how to deal with rising China both economically and militarily. As a small state with a relatively weaker economy vis-à-vis rising China, Mahathir's China policy has been constrained by the lack of the economy of scale when competing with China. In economic competition, Malaysia with its population of 24 million is loosing out to China with its large market and its huge population of 1.3 billion. This can be seen from the growing influx of FDIs into China and the corresponding decrease to Malaysia since the 1990s. This is particularly true since China's entry into the W.T.O. in 2001, when the Chinese economy became more competitive after economic reforms vis-à-vis Malaysia and the rest of the ASEAN states' economies.

With a cheaper Chinese Yuan and relatively lower labor costs, the Malaysian economy is under pressure from comparative advantages offered by the Chinese in regional economic competition, the challenges from globalization, EU protectionism and economic hegemony of the US. Mahathir came to the conclusion that the revival of the EAEG in the form of ASEAN 10 plus 3 should be one of Malaysia's long-term strategies to minimize its economic vulnerability and to ensure its long-term economic growth by locking in with the more powerful three Northeast Asian states'

economies (China, Japan and South Korea). China will be an important factor in Malaysia's drive to transform itself from a Third World economy to a Developed World economy by 2020. Thus, even in the post Mahathir era under Abdullah bin Ahmad Badawi's leadership, Malaysia will continue to see China as providing more economic opportunities rather than posing threats, notwithstanding irresolvable territorial disputes between the two countries over the Spratlys.

This study has shown that the central thrust of Mahathir's economic thinking of pragmatism has been overshadowing strategic-cum security dimensions in Sino-Malaysian relations. Although economic cooperation will be the main focus in future Sino-Malaysian relations, Malaysia, being a small power, facing a rising Chinese power, Kuala Lumpur remains uncertain and naturally worries about China's long-term strategic-cum security intentions towards Southeast Asia in general and Malaysia in particular. Thus Malaysia will likely continue to remain politically and strategically ambivalent toward China, despite fostering a mutually closer economic partnership.

Table 1 Malaysia's Trade with China: 1971-2002
(in US$ million)

Year	Total volume	Imports	Exports	Balance
1971	27.8	26.72	1.08	- 25.64
1972	44.37	40.67	3.70	- 36.97
1973	126.21	124.93	1.28	-123.65
1974	159.17	155.26	3.91	-151.35
1975	159.61	108.57	51.04	- 57.53
1976	136.41	87.38	49.03	- 38.35
1977	199.74	94.43	105.31	+ 10.88
1978	274.34	163.19	111.15	- 52.04
1979	360.51	171.37	189.14	+ 17.83
1980	424.40	184.47	239.93	+ 55.46
1981	289.29	194.34	94.85	- 99.39
1982	307.31	183.51	123.80	- 59.71
1983	346.70	198.91	147.79	- 51.12
1984	338.25	196.41	141.84	- 54.57
1985	341.50	170.31	171.12	+ 0.81
1986	314.01	180.34	133.67	- 46.67
1987	557.00	255.00	302.00	+ 47.00
1988	877.00	308.00	569.00	+261.00
1989	560.15	306.48	253.67	- 250.60
1990	1183.07	340.79	842.28	+501.49
1991	1331.89	527.89	804.00	+276.11
1992	1475.62	645.44	830.18	+184.74
1993	1788.01	704.37	1083.64	+379.27
1994	2740.32	1117.66	1622.67	+505.01
1995	3346.09	1280.99	2065.09	+784.10
1996	3614.14	1370.65	2243.48	+872.83
1997	4415.30	1919.93	2495.38	+545.45
1998	4264.32	1596.35	2667.98	+1071.63
1999	4294.00	1989.00	2305.00	+ 416.00
2000	8045.03	2565.03	5479.99	+2914.96
2001	9425.47	6205.21	3220.26	+2984.95
2002	14300.00	5000.00	9300.00	+4300.00

1989 to 1998 data from *Almanac of China's Foreign Economic Relations and Trade*, (Beijing: China National Economic Building House).
1999 data from *Key Indicators of Developing Asian and Pacific Countries*, Asian Development Bank, 2000, Vol. XXXI, (Hong Kong: Oxford University Press (China) Ltd. 2000), p.195-197.
2000 data from *China's Customs Statistics* (Monthly Exports & Imports), Series No. 136, 12 2000, (Hong Kong: Economic Information & Agency, 2000), p.4.
2001 and 2002 data from *China Statistical Yearbook 2002*, (Beijing: China Statistics Press), p.617.

Endnotes

[1] On November 1st 2003, after twenty-two years in power, Mahathir had finally decided to step down and let his deputy, Abdullah bin Badawi take over as the fifth Prime Minister of Malaysia.

[2] Shee Poon Kim, Malaysia's Diplomatic Recognition Policies Towards the People's Republic of China: 1957-1974, *Bulletin of the Sohei Nakayama IUJ Asia Development Research Programme*, International University of Japan, Vol. 1, March 1989, pp.19-40; see also Shee Poon Kim, 'Peking's Foreign Policy Toward Malaysia', *Issues and Studies*, (Taiwan), Vol. 23, No. 8, August 1987, p.137.

[3] Xia-Ming, 'Sino-Malaysian Trade Ties and Its Prospects', *Economic Quarterly*, (Singapore) April, 1990, p.21.

[4] John Wong, *The Political Economy of China's Changing Relations with Southeast Asia*, (London, MacMillan Press, 1984), p. 204.

[5] Xia-Ming, 'Sino-Malaysian Trade Ties and Its Prospects', *op. cit.*, p.22.

[6] See John Wong, *The Political Economy of China's Changing Relations with Southeast Asia, op. cit.*, p.101.

[7] John Wong, *The Political Economy of China's Changing Relations with Southeast Asia, ibid.*, p.101.

[8] See Table 1 for trade data.

[9] See Ministry of International Trade and Industry *http://www.miti.gov.my/speech-25sep02.html*

[10] Data from Malaysia External Trade Development Corporation, at *http://www.matrade.gov.my/Special_China/eco_china.htm*

[11] Chinese students form more than 30% in institutions of higher learning. See Ministry of International Trade and Industry, at *http://www.miti.gov.my/speech-25sep02.html*; see also Hong *Kong Standard*, 14 August 1999.

[12] In 1998, 300,000 Chinese tourists arrived in Malaysia. The number increased to more than 450,000 in 2001, out of a total of 12.8 million tourist arrivals, reaching almost 300,000 for the first half of 2002. *Hong Kong Standard*, 12 August 1999; Ministry of International Trade and Industry, at *http://www.miti.gov.my/speech-25sep02.html*; see also Asia Net at *http://asianet.hongkong.com/news/2002-09-27/news7.html*

[13] See Malaysia External Trade Development Corporation at *http://www.matrade.gov.my/cgi-bin/printhis.pl*

[14] *http://www.matrade.gov.my/cgi-bin/printhis.pl*, *ibid.*

[15] See Table 1 for trade data.

[16] *Bernama News*, 27 August 1996.

[17] *Bernama News*, 27 August 1996, *ibid*.

[18] China's Rising Investment in Southeast Asia: How ASEAN and Singapore can benefit? At *http://www.mti.gov.sg*

[19] *The West Australian*, 25 July 1997.

[20] *http://www.multiline.com.au/-georgist/exploit.htm*

[21] *New Straits Times*, 2 June 1999.

[22] *Xinhua Monthly Bulletin*, Vol.7, 1999, pp.175-176.

[23] *The Current Situation and Its Prospects of China-Malaysian Economic and Trade Ties, Asia Pacific Economic Cooperation*, Vol.5, 1998, p.10.

[24] Up to the end of 1996, there were about three hundred Chinese manufacturing companies investing in Malaysia, amounting to US$200million. *The Current Situation and Its Prospects of China-Malaysian Economic and Trade Ties, Asia Pacific Economic Cooperation,* Vol. 5, 1998, *ibid.,* p.10.

[25] *The Current Situation and Its Prospects of China-Malaysian Economic and Trade Ties, ibid*., p.10.

[26] *http://www.China.org.cn/BeijingReview/99Apr/bjr99-17e6.html*

[27] *The Straits Times*, 3 June 1999; see also *The Daily Yomiuri*, 18 November 2000.

[28] *Far Eastern Economic Review,* 26 August 1999.

[29] *Muzi Daily News*, 12 August 1999.

[30] *New Straits Times,* 19 August 1999. For informative data on Malaysian firms' investments in China, see Ho Khai Leong, 'Recent Developments in the Political Economy of China-Malaysian Relations', in Leo Suryadinata, ed., *Southeast Asian Chinese and China, the Politico-Economic Dimension*, (Singapore: Times Academic Press, 1995), pp.238-241.

[31] Ministry of Foreign Affairs of the People's Republic of China, 25 August 2003, at *http://www.fmprc.gov.cn/eng/wjb/zzjg/yzs/gjlb/2732/default.htm* accessed 14/9/03.

[32] *http://dailynews.muzi.com*

[33] *http://dailynews.muzi.com*

[34] *http://dailynews.muzi.com*

[35] See Mahathir's speech on 'Towards a Closer and More Outward Looking Partnership', *The New Straits Times*, 20 August 1999.

[36] *http://dailynews.muzi.com* 23 November 1999.

[37] *http://www.strafor.com/asia/commentary/M9911232150.htm*

[38] *http://www.strafor.com/asia/commentary/M9911232150.htm, ibid.*

[39] *The New Straits Times*, 24 November 1999.

[40] *The New Straits Times,* 24 November 1999, *ibid.*

[41] *Lianhe Zaobao,* 24 January 1995.

[42] *The Straits Times*, 13 May 1994.

[43] *The Straits Times,* 13 May 1994, *ibid.* Dr. Mahathir forgot that the Mongols had invaded Java in 1290.

[44] *The Straits Times*, 25 January 1995.

[45] *The Straits Times,* 27 January 1995.

[46] Daojiong, Zha. 'The Politics of China ASEAN Economic Relations: Assessing the Move toward a Free Trade Area,' in *Asian Perspective*, Vol. 26, No. 4, 2002, p.57-58.

[47] Mahathir's economic legacy, *BBC News*, 8. 10. 2003.

[48] BBC News, 2003/10/08.

[49] Wu, Friedrich. et al, ' Foreign Direct Investments to China and Southeast Asia: Has ASEAN Been Losing Out?' *Economic Survey of Singapore* – (Third Quarter 2002), p.109, at *http://www.mti.gov.sg* .

[50] *Business Times*, Singapore 27 August 2002.

[51] The hourly wage for a worker in the manufacturing sector in Indonesia is US$0.14, whereas it is US$0.52 in China, Wu, Friedrich. et al, *ibid.*, p.109.

[52] *New Straits Times*, 21 October 1985, in Stephen Leong, 'Malaysia and the People's Republic of China in the 1980's: Political Vigilance and Economic Pragmatism', *Asian Survey*, Vol. 27, No. 10, October 1987, p.1116-1117.

[53] They were Terembu Layang Layang (Swallow Reef, which is about 160 km north of Labuan island, off Sabah.), the Amboyna Reef, the Luconia Shoals, Friendship

Shoals, the South Luconia Shoals, the James Shoals which are about 63 nautical miles off the coast of Sarawak, as well as the two atolls of Terumbu Ubi (Station Uniform) and Terumbu Mantanani (Station Mike), etc., at the southern end of the Spratlys. See Chien Chung, 'Confidence-Building Measures in the South China Sea', in Hung-Mao Tien and Tun-jen Cheng, eds., *The Security Environment in the Asia-Pacific* (Armonk, New York: M.E Sharpe, 2000), p. 267

[54] Chien Chung, 'Confidence-Building Measures in the South China Sea', *ibid*., p. 267.

[55] *Lianhe Zabao*, 2 June 1995.

[56] J.N. Mak, The Chinese Navy and the South China Sea: A Malaysian Assessment', *The Pacific Review*, Vol. 4, No. 2, p.150.

[57] Stephen Leong, 'Malaysia and the People's Republic of China in the 1980's: Political Vigilance and Economic Pragmatism', *op. cit.*, p.1116. Malaysia bought 40 A4 Skyhawk jet fighters and two Corvette 1300-ton coastal patrol vessels. Subsequently Malaysia also planned to buy four submarines from Sweden. *Asiaweek*, 3 May 1991.

[58] *The Straits Times*, 2 April 1992.

[59] *The Sunday Times*, 29 March 1992.

[60] *The Sunday Times*, 29 March 1992, *ibid.*

[61] Ross Babbage and Sam Bateman, eds., *Maritime Change: Issues For Asia*, (Australia: Allen & Unwin Pte. Ltd., 1993), p118.

[62] *Asiaweek*, 9 May 1997.

[63] K.S. Nathan, 'Vision 2020 and Malaysian Foreign Policy: Strategic Evolution and the Mahathir Impact', *Southeast Asian Affairs*, 1995, (Singapore: Institute of Southeast Asian Studies, 1995), p.229.

[64] Directorate General of Customs, Ministry of Finance, ROC 2003, *http://cus.moeaboft.gov.tw./cgi-bin/pbisa60.dll/customs/uo_e_roc/of_o_fsrl12_report?* Accessed 12/1/03.

[65] Malaysia External Trade Development Corporation at *http://www.matrade.gov.my/cgi-bin/printhis.pl* Accessed 8/28/03.

[66] *http://www.matrade.gov.my/cgi-bin/printhis.pl* Accessed 8/28/03.

[67] *http://www.matrade.gov.my/cgi-bin/printhis.pl* Accessed 8/28/03.

[68] Ho, Khai Leong. 'Rituals, Risks and Rivalries: China and ASEAN in the coming Decades' *Journal of Contemporary China*, November 2001,Vol. 10, No. 29, p.692.

[69] *Sarawak Tribune* 15 July 2003, at *http://www.scci.net.my/headlines/2003/july/July_26.htm* accessed 12/1/03.

[70] *www.mcbc.org.my/en/misa/trade_FInvest.html* accessed 27 August 2003.

[71] *Far Eastern Economic Review* 23 February 1995, p.32.

[72] Ho, Khai Leong. *ibid*., pp. 692-693.

[73] *Hong Kong Standard*, 18 May 1999.