

China's Growth Deceleration – A New Normal for Malaysia Too?

Cheong Kee Cheok and Wang Qianyi****

Institute of China Studies, University of Malaya, Malaysia
Malaysian Chinese Research Centre, University of Malaya, Malaysia

Abstract

While the consequences of China's growth deceleration for China are hotly debated, its impact on Southeast Asia has received more balanced treatment, it being recognized that each country would be impacted differently. Malaysia's substantial trade with China, however, was said to be more likely affected than other countries trading less intensively with China. Statistics, however, show otherwise. Malaysia's exports and imports have both risen, thanks to process trade that was to see final assembly in China but destined to countries all over the world and to primary exports to China being only a small part of total exports. China's imports from Malaysia also show an upward trend. Driven by geo-strategic as well as economic considerations, China's investment in Malaysia also did not fall but instead experienced a significant increase. The former imperative is reflected in China's Maritime Silk Road while the latter is reflected by Chinese multinationals seeking overseas markets as domestic growth slows. Thus, Malaysia's post-Asian Crisis cannot be blamed on China. Instead a host of domestic (e.g., political scandal) and external (e.g. fall in crude oil prices) have conspired to undermine Malaysia's growth.

Keywords: *Growth deceleration, new normal, China, Malaysia*

1. Introduction

Just over three decades after its opening up, China's economy has grown to be the second largest (in current US\$ terms) in the world. The recent phenomenon of its growth deceleration and stock market rout has therefore sent shockwaves worldwide, worrying investors everywhere but delighting its naysayers who see every reversal as a sign of China's impending collapse. Hutton's (2015) remark is typical of this latter group:

China's banks are, in effect, bust: few of the vast loans they have made can ever be repaid, so they cannot now lend at the rate needed to sustain China's once super-high but illusory growth rates. China's growth is now below that of the Mao years: the economic crisis will spawn a crisis of legitimacy for the deeply corrupt communist party.

But he is hardly alone (see among others, Spence, 2015; Tobey, 2015). This view is contested by China scholars (for example Hu, 2015; Kaletsky, 2015; Quah, 2016) who lean towards what Chinese President Xi Jinping termed "China's New Normal".

We concur with the latter view, for the reason succinctly argued in a McKinsey opinion piece:

The reality is that China's economy is today made up of multiple sub-economies, each more than a trillion dollars in size. Some are booming, some declining. Some are globally competitive, others fit for the scrap heap. How you feel about China depends more than ever on the parts of the economy where you compete. (Orr, 2016)

The decline, even collapse, of parts of the economy, like stock markets, does not signal total collapse of the Chinese economy. To believe otherwise is to ignore the complexity of the Chinese economy that scholars like Lardy (2015) have also noted.

With this premise, the next issue that is of importance is the implications of China's slowdown for Southeast Asia. Commentaries on these tend to be cautionary, while also recognizing some countries being more vulnerable (DW, 2015; Schonhardt, 2015). But all countries in Southeast Asia are not the same. Even before China's economic slowdown, but after the Asian Financial Crisis of 1997, the early movers and shakers of ASEAN – Malaysia and Thailand – had lost steam while early laggards – Indonesia and the Philippines – and latecomers – Cambodia, Laos, Myanmar and Vietnam, collectively referred to as the CLMV countries – were gathering momentum. And as China's growth decelerated, this trend has continued. As Table 1 shows, even as China's growth decelerated from about 2012, growth rates of Cambodia, Lao PDR and Vietnam remained robust. Indonesia's and the Philippines' also held up well up to 2015. As for Malaysia and Thailand, growth rates had gone south well before China's growth deceleration. Still, there are studies that show the relatively greater impact of China's slowdown on Malaysia (Zhai and Morgan, 2016).

Just as it is inappropriate to think of Southeast Asia as an entity, so it is misleading to think of Malaysia, the focus of this paper, succumbing to China in the way that has been reported for Southeast Asia, i.e. that like the rest of ASEAN, Malaysia's loss of growth momentum can be blamed, at least partly, on China. Hence, in attempting to assess the overall impact of a

Table 1 Annual Growth Rates – China and Selected ASEAN Countries, 2008-2015

<i>Country</i>	<i>2008</i>	<i>2009</i>	<i>2010</i>	<i>2011</i>	<i>2012</i>	<i>2013</i>	<i>2014</i>	<i>2015</i>
China	9.6	9.2	10.6	9.5	7.8	7.7	7.3	6.9
Malaysia	4.8	-1.5	7.4	5.3	5.5	4.7	6.5	5.0
Cambodia	6.7	0.1	6.0	7.1	7.3	7.5	7.1	7.0
Indonesia	6.0	4.6	6.2	6.2	6.0	5.6	5.0	4.8
Lao PDR	7.8	7.5	8.5	8.0	8.0	8.5	7.5	7.4
Philippines	4.2	1.1	7.6	3.7	6.7	7.1	6.1	5.9
Thailand	1.7	-0.7	7.5	0.8	7.3	2.8	0.9	2.8
Vietnam	5.7	5.4	6.4	6.2	5.2	5.4	6.0	6.7

Source: World Bank database for 2008-2015.

China slowdown on Malaysia, this paper will examine the efficacy of each channel through which this impact is transmitted, and then look at prospects for Malaysia as China settles into its “New Normal”.

2. Malaysia's Trade with China

China's economic relations with Malaysia are manifested through primarily trade, and, more recently direct investment. The growing importance of bilateral trade between the countries has naturally made this the focus in assessing the impact of China's slowdown on Malaysia. But what is the reality of China-Malaysia bilateral trade?

As Table 2 shows, China's share of trade has been growing, so that by 2009, it had become Malaysia's largest trading partner. In 2016, exports to China represented 12.5% of Malaysia's total exports, slightly lower than the 13.1% in 2015, while imports from China reached 20.3% of total imports in 2016, the highest share since trade between the countries began. Taken together, Malaysia's bilateral trade with China accounted for 13% of the country's total merchandise trade.

With trade accounting for about 150% of GDP¹, any reduction in Malaysia's trade with China may be expected to impact total trade and hence Malaysia's GDP. This is a common theme of commentators of the Malaysian and ASEAN economies (e.g. SBR, 2013; Zurairi, 2013). Yet there is no indication of this from aggregate trade data (Table 2). Apart from the dip in trade as a result of the Global Financial Crisis in 2009, Malaysia's total exports have risen each year from 2000 to 2015, while total imports have risen monotonically. More telling has been Malaysia-China bilateral trade,

Table 2 Malaysia's Trade with China as a Share of Total Trade, 2000-2015

<i>Year</i>	<i>Exports to China (% of Total)</i>	<i>Imports from China (% of Total)</i>	<i>Net Exports (billion MYR)</i>	<i>Total Trade with China (% of Total)</i>
2000	3.2	3.9	0	3.5
2004	6.7	9.8	-7	8.0
2008	9.5	12.9	-4	11.0
2009	12.1	14.0	6	13.0
2010	12.5	12.2	14	12.4
2011	13.2	13.2	16	13.2
2012	12.7	15.2	-3	13.8
2013	13.5	16.3	-9	15.3
2014	12.2	17.0	-24	14.4
2015	13.1	18.8	-27	15.8
2016	12.5	20.3	-46	13.0

Source: Department of Statistics Malaysia: *METS Online*.

which, while moderating, continued to grow through 2015, although dipping in 2016. In addition, Malaysia exports about as much as it imports so that there is minimal net trade in either direction. This too had not changed much after China's growth began to slow in 2012. There is therefore as yet no basis for the argument, however nuanced, that China's deceleration would hit Malaysia's growth through a fall in the latter's exports. Malaysia's economic growth during this period might falter, or it might have held up, but no one should look to trade performance as an important factor to date.

What then might explain this lack of connection between China's slowdown and Malaysia's trade? Might the answer be found through a review of the details of bilateral trade between the countries? Table 3 shows the top five items of Malaysia's exports to and imports from China. With respect to exports, by far the largest item is SITC 77 – electrical machines, appliances and parts, the bulk of which is the output of the electronics and electrical industries and account for over 60% of the total value of Malaysia's top 5 exports to China.² And far from falling when China's growth slowed, these exports continued their rise until 2015, falling back a little in 2016. This rise mirrored and also contributed to the rise of Malaysia's total exports to China during the period 2015.

How could this have occurred in the face of China's slowdown? SITC77 exports come from Malaysia's participation in global supply chains that end in China which undertakes final assembly. Neither Malaysia nor China controls

these chains; control is vested in transnational corporations from the US, Europe and Japan. The volume of these exports depends on the demand for the final products which are not only for China's domestic consumption but also for the global market, and hence are not solely dependent on the health of China's economy.

Besides SITC77, exports of office machines (SITC75), petroleum and petroleum products (SITC33) and vegetable oils and fats (SITC42), each accounting for less than half, and often just a third of the value of SITC77, make up the second, third and fourth largest exports by value. Of these, export revenue from petroleum and petroleum products (SITC33) is expectedly the most volatile. Exports of vegetable oils and fats (SITC42) fell sharply in 2015 and was no longer in the top 5 in 2016 while exports of office machines (SITC75) have fallen considerably from the levels it attained in 2010 and 2011.

As for Malaysia's palm oil exports, these fall under SITC42. Since 2011, when these exports were ranked second, their proceeds had indeed been falling, from accounting for 10 % of the top 5 exports in 2012 to just below 5% in 2015. Thus, from the perspective of exports, the fall in exports of vegetable oils and fats (mainly palm oil) has been compensated by increases in the exports of other products, especially those related to process trade, discussed above. Rubber, once the mainstay of Malaysian exports, did not make even the top five with 2011 being the singular exception. Second, those primary commodities impacted form just a small share of total exports to China. As an illustration, using the broader SITC 1-digit classification, exports of animal and vegetable oils and fats (SITC4) are valued at no more than a third of the exports of mineral fuels and lubricants (SITC3) during the period covered in Table 2.

Unlike exports, Malaysia's imports from China have little to do with China's economic performance; instead, it is closely related to Malaysia's growth and development needs. Like exports to China, imports from China have more than doubled between 2009 and 2016. But compared to exports, imports from China are less concentrated. The top 5 imports are all industrial products – equipment, parts and iron and steel. While the top import in value terms is also SITC 77, its share of the top 5 imports stood at 35% in 2009, and despite a more than doubling in value, at only 45% in 2015. These imports have been increasing monotonically during the entire period.

With the exception of SITC75 – office machines and equipment – all top 4 import categories have seen significant increases between 2009 and 2016. Imports of iron and steel (SITC67) more than quadrupled over the period, industrial machinery and equipment (SITC74) doubled, and telecommunications equipment (SITC76) by 67%. These increases reflect Malaysia's growing use of Chinese equipment and iron and steel for its

Table 3 Malaysia's Trade with China, Top 5 Items, 2010-2016**A. Exports to China (RM million)**

<i>Item by 2-Digit SITC</i>	<i>2010</i>	<i>2011</i>	<i>2012</i>	<i>2013</i>	<i>2014</i>	<i>2015</i>	<i>2016</i>
23 Crude rubber		5,981					
33 Petroleum & petroleum products	3,918		4,515	6,775	6,538	10,558	7,695
42 Vegetable oils & fats	7,656	11,632	8,870	7,610	6,054	4,688	
51 Organic chemicals					4,374	4,374	5,354
57 Plastics in primary forms							4,262
62 Rubber manufactures	3,908	4,553	5,804				
68 Non-ferrous metals				6,714			
75 Office machines	15,839	11,261	9,681	7,273	6,753	6,871	7,415
77 Electrical machines, appliances & parts	23,243	28,252	29,100	31,698	34,660	35,059	34,192
Total Top 5 exports	54,240	61,679	56,589	54,703	53,036	51,504	58,918
Total exports to China	80,105	91,551	88,792	97,043	92,286	101,531	98,559
SITC77 as % of Top 5 Exports	42.8	45.8	51.4	57.9	65.4	68.1	58.0
Top 5 as % of Total Exports	67.7	67.4	63.7	56.3	57.5	50.7	59.8

B. Imports from China (RM million)

67 Iron & steel	2,821	3,451	4,375	5,107	6,665	7,319	7,400
74 Industrial machinery & equipment	3,237	4,324	5,853	6,099	6,699	8,263	8,690
75 Office machines & equipment	9,821	9,086	9,425	8,766	7,953	9,395	9,083
76 Telecommunications equipment	8,106	8,416	8,570	9,813	10,181	10,644	12,671
77 Electrical machinery, equipment & parts	12,905	15,255	23,985	27,809	29,902	28,704	29,153
Total Top 5 imports	36,890	40,532	52,208	57,594	61,400	64,325	66,997
Total imports from China	66,430	75,706	91,864	106,265	115,513	129,360	142,346
SITC77 as % of Top 5 Imports	35.0	37.6	45.9	48.3	48.7	44.6	43.5
Top 5 as % of Total Imports	55.5	53.5	56.8	54.2	48.7	49.7	47.1

Source: Malaysian External Trade Database <http://trade.stats.gov.my/tradeV2/>

projects. For example, imports of telecommunications equipment emanate from contracts signed between Malaysian telecommunications companies with China's Huawei and ZTE (Li and Cheong, 2017).

The significance of imports with respect to Malaysia's trade with China lies in data for the category SITC77, the largest with respect to both exports and imports. The difference between this group's exports and imports for this category is the value added Malaysia gains from participating in electronics supply chains.³ As the table shows, this value addition after the Global Crisis in 2009 was a respectable 50% of this group's export value in 2009, but fell to only 18% in 2015. At barely RM5.04 billion (exports of RM34.19 billion against imports of RM29.15 billion) in 2015, this category's ability to offset the decline in commodity exports to China is no longer as impressive as viewed from the perspective of gross exports alone. Nevertheless, the value added for electronics appliances, etc. (SITC77) in 2016 (RM5.04 billion) still more than offsets the fall in value of vegetable oils (SITC42) between 2015 and 2016 (RM567 million).

What are the takeaways from this review of bilateral trade? First, the trade impact of China's economic slowdown is not as important as many believe. Second, this is because primary commodity exports to China represent just a small fraction of Malaysia's total exports of primary commodities.⁴ And third, Malaysia's most important exports to China in the form of electronics parts and components are not all destined for the China market.

3. China's Investment in Malaysia

Chinese outward foreign direct investment is of relatively recent extraction, with impetus coming from the state's "Going Out" policy announced in 1999 (China State Council, 2006). Since then, a number of Chinese firms, led by state enterprises and followed by non-state enterprises, had invested overseas. These enterprises have initially concentrated their investments in resources (in developing countries and Australia) and technology (in advanced countries). With neither in plentiful supply, Malaysia was not on the radar of resource- or technology-seeking Chinese investment in the early years of this century.

Over the first decade of the "Going Out" Policy, Chinese enterprises' outward investment began also to include other motives like seeking markets. This motive is partly driven by intense competition in the home market in China. The expertise Chinese enterprises have developed in construction and transport infrastructure has also spurred these firms to seek opportunities abroad.

China did not figure prominently in Malaysia's FDI even as recently as 2008, when its first FDI project of over US\$100 million was made. As Table 4 shows, China's FDI, measured in terms of actual flows, was a paltry US\$372

Table 4 Foreign Direct Investment Flow into Malaysia by Selected Country of Origin, 2008-2013 (US\$ mil.)

<i>Year</i>	<i>Total</i>	<i>Singapore</i>	<i>Japan</i>	<i>US</i>	<i>Netherlands</i>	<i>Hong Kong</i>	<i>China</i>
2008	13,323	4,723	2,637	3,823	2,375	1,867	372
2009	6,475	4,093	2,519	1,277	2,134	2,357	264
2010	9,434	3,814	3,311	5,382	4,066	1,278	343
2011	10,772	5,748	5,584	3,966	2,784	2,377	313
2012	6,933	5,659	4,520	3,819	2,673	3,197	773
2013	10,166	5,239	4,984	2,886	4,153	3,722	779

Source: US Department of State: Investment Climate Statement, 2014, citing Bank Negara and Department of Statistics.

million, just 3% of a total inflow of US\$13,323 million. This level of inflow was maintained until 2011, after which it doubled in value, but more than doubled its share of the total, since total investment never reached the level achieved in 2008. Significantly, total investment was halved with the impact of the Global Financial Crisis, declining a little less with respect to investment from China.

That China's FDI in Malaysia has moved beyond the search for resources is revealed by the statistics on Chinese FDI in Malaysia's manufacturing sector (Table 5). China became a significant player only in 2012, well after the onset of the Global Financial Crisis in 2008, but coinciding with the start of China's economic slowdown. Between 2012 and 2015, China accounted for around 10% of total FDI in manufacturing. That share surged to 17% in 2016, reflecting not only the fall in total FDI to Malaysia but also increased Chinese investment, a part of which is related to developments emanating from China's One Belt One Road (OBOR) initiatives. This investment surge in 2016, during which there is much debate about growth dipping below the 7% target, is also confirmation that Chinese FDI bears little if any relationship with its economic growth. Indeed, if a link between Chinese outward FDI and economic growth is to be hypothesized, it should be that slower growth would lead to more outward FDI – Chinese enterprises, facing poorer market prospects at home, might be pressured to look for markets overseas.

Table 6, from the *China Global Investment Tracker*,⁵ shows the sectoral composition of Chinese direct investment. Because these figures refer to commitments rather than disbursements they cannot be compared to the figures in Tables 4 and 5. China's first major investments in Malaysia were in the energy sector, with Sinomach committing US\$120 million in July 2008 and Three Gorges Construction investing US\$880 million in a hydroelectric

Table 5 Approved Foreign Direct Investment in Manufacturing in Malaysia by Selected Country of Origin, 2006-2016 (US\$ mil.)

<i>Year</i>	<i>Total</i>	<i>Singapore</i>	<i>Japan</i>	<i>US</i>	<i>Netherlands</i>	<i>Germany</i>	<i>Hong Kong</i>	<i>China</i>
2006	5,512	514	1,202	675	895	63	n.a.	n.a.
2007	9,717	858	1,896	878	491	1,092	n.a.	n.a.
2008	13,323	565	1,637	2,544	526	1,287	24	10
2009	6,475	585	2,047	672	140	124	1550	47
2010	9,434	700	1,308	3,811	303	629	898	n.a.
2011	11,382	825	3,367	836	336	650	131	398
2012	6,948	738	930	985	276	231	30	659
2013	10,178	1,507	1,197	2,106	794	572	151	1,005
2014	11,312	2,235	3,106	386	233	1,262	n.a.	1,358
2015	5,103	324	932	965	204	270	740	435
2016	6,161	481	418	318	723	594	60	1,073

Source: For 2006-2013, US Department of State: Investment Climate Statement, 2014, citing Bank Negara and Department of Statistics. For 2014-2016, Malaysian Industrial Development Authority: Malaysian Investment Performance Reports, with US\$1 to MYR3.50 in 2014, MYR4.30 in 2015 and MYR4.45 in 2016.

Table 6 China's Investments in Malaysia of US\$100 million and above, 2008-2015

<i>Year</i>	<i>Real Estate</i>	<i>Non-energy Resources</i>	<i>Energy</i>	<i>Transport</i>	<i>Other</i>	<i>Total</i>
2008			1,000	680		1,680
2010	140		570		1,250	1,960
2011			830		1,040	1,870
2012	1,750	1,480	200			3,430
2013	1,770		2,970	580	950	6,270
2014	180		1,570	1,300	200	3,250
2015	1,890		3,340	830	600	6,660
2016	410	n.a.	n.a.	2,010	n.a.	n.a.

Source: *China Global Investment Tracker*.

project (see Annex 1). There was also an investment of US\$680 million by the China Communications Construction Company in automobiles that year, signifying the rise of market-seeking Chinese FDI. Chinese FDI in Malaysia remained at about the 2008 level until 2012, when large investments of well over a billion were made in real estate and in timber boosted total Chinese

FDI by nearly 80% compared to 2011. Chinese FDI nearly doubled again in 2013, dominated by energy and real estate, fell by half in 2014, and again doubled to a record US\$6.6 billion in 2015. Thanks to purchase of assets of Malaysia's heavily indebted 1Malaysia Development Berhad (1MDB), China was reported to have vaulted to the top of Malaysia's FDI league (Chew, 2016a).

Regardless of whether FDI to Malaysia revives, China is set to remain among the top of the FDI league. It is likely that its timely assistance to 1MDB would have put it in the good books of the Malaysian government when it comes to upcoming major infrastructure projects, of which the Kuala Lumpur – Singapore high-speed rail project, estimated to cost above US\$10 billion, is the largest (Hafiz, 2016).⁶ Despite the official stance that the project will be openly bid, China's presence in a string of infrastructure projects⁷ will certainly help its cause. The Chinese government has also been adept at demonstrating in concrete terms its intention of being a benefactor of Malaysia. In November 2015, Chinese premier Li Keqiang pledged to buy Malaysian bonds in support of the sliding Ringgit, while the China Construction Bank announced the listing of the world's first 21st Century Maritime Silk Road bond worth RMB1 billion (RM667.1 million) on Bursa Malaysia (Khuo, 2016). It is therefore not surprising that Malaysia itself is gearing up for Chinese FDI (ASEAN Economist, 2016). The most concrete evidence of this increased China dependence is the November 2016 visit of Malaysian Prime Minister Najib to Beijing that produced pledges of US\$33 billion in FDI from China (Chew, 2016b).

Although energy remains a major area for Chinese FDI, real estate and transport equipment have also been important areas, the latter clearly representing a degree of market-seeking by Chinese enterprises. As the Chinese economy slows, Chinese enterprises are likely to look increasing to overseas markets to expand. This may prove a boon to Malaysia, where FDI has stalled for a variety of reasons to be discussed later.

China's FDI is driven not just by commercial considerations but also by strategic imperatives, as the Guangxi Beibu Gulf International Port Group's investment in Kuantan port and the Malaysia-China Kuantan Industrial Park suggests. Malaysia appears also to be aware of the potential to capture more Chinese FDI through the latter's One Belt One Road (OBOR) grand strategy, into which the establishment of financial institutions like the Asian Infrastructure Investment Bank fit (Tan, 2015). This ambitious strategy, although primarily serving China's geopolitical imperatives (reduced dependence on traditional sea lanes for the resources it needs and greater voice in international affairs) also fits well with substantial infrastructure needs in the countries along the OBOR, Malaysia among them (Cheung and Lee, 2015).

Thus, not only is Chinese FDI in Malaysia delinked from its economic growth, the former is likely to increase even as China's economy slows. Driven by the need to meet debt obligations and also standing to benefit from China's OBOR, Malaysia is becoming increasingly dependent on Chinese FDI. At the same time, the outward expansion plans of its growing number of Chinese transnational corporations should accelerate with their domestic market not growing at the same pace as before.

4. Malaysia's Investment in China

Outward FDI (OFDI) from Malaysia had increased significantly. Table 7 shows that despite some fluctuation, OFDI from Malaysia has been in excess of US\$15 billion since 2008, the exception in 2009 reflecting the impact of the Global Financial Crisis. Contrary to expectations, developed countries have not been the centre of attention – in 2011 and 2012 they account for less than half of Malaysia's OFDI, and in 2008-2010 for a third or less. Most Malaysian OFDI has gone to Asia, with Singapore a major destination. Direct flows to China have been unimportant; even including investments routed through Hong Kong. Information on the major activities in which Malaysian OFDI are involved in China is not readily available, but an analysis of Malaysian Chinese investment in China shows this to be largely

Table 7 Host Region and Country FDI Flows from Malaysia, 2001-2012 (US\$ million)

<i>Region/Country</i>	<i>2008</i>	<i>2009</i>	<i>2010</i>	<i>2011</i>	<i>2012</i>
World*	15,120	6,505	15,263	18,080	16,806
Developed countries	3,593	899	3,233	6,300	7,093
Europe	1,327	142	1,370	3,171	-1,574
North America	-549	429	-3	676	7,168
Other (Australia)	2,815	329	1,865	2,452	1,499
Developing countries	9,845	4,645	9,815	10,299	9,146
Asia	7,385	2,909	7,916	4,326	7,954
China	198	281	87	296	73
Hong Kong SAR	340	-616	493	161	1,260
Singapore	1,772	632	4,384	2,574	2,952

Note: * The numbers do not add up because some categories have been omitted from this table.

Source: UNCTAD FDI/TNC database, based on data from Bank Negara Malaysia and the Department of Statistics Malaysia.

engaged in manufacturing for the China market (Cheong et al., 2017). China's "new normal" is likely to affect Malaysian businesses in China both positively and negatively. On the one hand, economic slowdown will impact these businesses negatively. On the other, the switch to consumption-driven growth should have salutary effects. Overall, however, given their modest scale in relation to total investments, the impact on Malaysia is not likely to be material.

5. Malaysia–China Exchange Rates

A third area in which Malaysia–China economic relations can be impacted is the Ringgit–Yuan exchange rate. After a protracted period of appreciation to reach a point where the US could no longer argue that China is a currency manipulator (Crutsinger, 2015) and the IMF said its currency was no longer undervalued (IMF, 2015), China devalued the Yuan by 1.87% on August 11, 2015, followed by a series of further downward adjustments (Inman et al., 2015). This triggered almost immediate commentary about its adverse impact on Southeast Asian exports (Jennings, 2015), on their currencies (Deng, 2015) and on financial markets (El-Erian, 2016).

What is to be made of all these narratives? First, it should be remembered that the Chinese Yuan has undergone a period of appreciation that should theoretically have made ASEAN's exports much more competitive. The devaluation has not caused a complete reversal of this, so why should the loss of competitiveness cause such an alarm for ASEAN's exports? Second, the effect of quantitative easing, which the US, Europe and Japan have undertaken repeatedly since the Global Financial Crisis of 2008, has been similar to direct devaluation – money supply in the economy is increased, thus lowering the exchange rate of the national currency. It seems odd that these have not received the same attention as China's devaluation when it comes to exchange rate impact. Also, apart from the need to distinguish between short-term and longer-run impact, the above general diagnoses are less than helpful given that ASEAN countries are not all alike.

When it comes to Malaysia, the same questions discussed above may be asked. First, how has it affected the competitiveness of Malaysian exports? Table 8 shows the exchange rate between the Malaysian Ringgit (MYR) and the Chinese Yuan as well as several ASEAN currencies. The figures show how much MYR is needed to exchange for one Chinese Yuan (CNY), one Singapore dollar (SGD), 100 Thai Baht (RHB) and 100 Philippine Peso (PHP), with a rising number signifying a depreciation of the MYR. As Table 8 shows, the MYR remained stable against the CNY until mid-2015, and depreciated thereafter. The depreciation of the Malaysian Ringgit was precipitated by numerous factors affecting the economy, of which China's

Table 8 Exchange Rates between the Malaysian Ringgit (MYR) and Selected Foreign Currencies, 2012-2016

<i>Year/Month</i>	<i>Chinese Yuan (MYR:CNY1)</i>	<i>Singapore \$ (MYR:SGD1)</i>	<i>Thai Baht (MYR:THB100)</i>	<i>Philippine Peso (MYR:PHP100)</i>
2012 Jan	0.50	2.44	10.00	7.20
Jun	0.50	2.47	10.01	7.32
2013 Jan	0.49	2.49	9.95	7.43
Jun	0.50	2.45	10.14	7.31
2014 Jan	0.54	2.59	9.96	7.40
Jun	0.57	2.57	9.81	7.35
2015 Jan	0.57	2.64	10.67	7.84
Jun	0.59	2.72	10.92	8.24
2016 Jan	0.66	3.03	11.95	9.18
Jun	0.63	2.99	11.58	8.86
Dec	0.64	3.10	12.52	9.05

Source: Bank Negara Malaysia. Available online at <http://www.bnm.gov.my/index.php?ch=statistic&pg=stats_exchangerates&lang=en&StartMth=1&StartYr=2016&EndMth=12&EndYr=2016&sess_time=1200&pricetype=Mid&unit=rm>

slowdown was arguably not the most important (Saleem, 2015).⁸ It was not just against the CNY that the MYR depreciated; it depreciated as much against the Singapore dollar (SGD) (by about 20% between January 2012 and December 2016) and also against the THB and PHP. Thanks to this substantial depreciation, the worst in Asia, Malaysian exports should remain highly competitive from an exchange rate perspective despite China's devaluation.

Beyond the above generalization about competitiveness, the extent to which two countries' exports compete depends on whether the same products are exported by both. This can be measured by the export similarity index.⁹ Loke (2009: 11) found similarity between Malaysia's and China's exports to be rising to a moderate level (40%) before it was reversed (to 30%) in 2008. A more recent study by Nasrudin et al (2014: 28) found moderate similarity of around 40% between Malaysia and the China-ASEAN Free Trade Area as a region while China's is somewhat higher at above 50%. The greater the similarity, the larger the competitive edge afforded by currency depreciation.

Thus, reviewing the Ringgit–Yuan exchange rate trajectory in combination with the degree of export similarity suggests that the devaluation of the Yuan should be less of a worry than the need to arrest the slide in the Ringgit.

It should also be remembered that because of both countries' participation in production networks in which parties are tied to fixed term contracts, free market exchange rates are not as material as it appears.

6. Conclusion – Malaysia's Woes and China's New Normal

There is no doubt that Malaysia has been experiencing bad times of late. With growing economic ties with China, it is also easy for commentators to point a finger at China's slowdown as a major contributor to the country's woes. Policy-makers would likewise find it convenient to blame external forces rather than domestic issues for which they are to an extent accountable. The horde of commentary in the international media has made it easy for both groups to ride the bandwagon of "public opinion".

But what does more careful examination of data reveal? First, the impact on trade with China is not as important as it is often believed. While Malaysia's exports of palm oil are adversely impacted by virtue of lower prices and reduced volume, the value of palm oil exports represent only a small proportion of exports destined for China and an even smaller proportion of total exports. This is also the case with petroleum exports to China, the share of which in total exports to China (7.6% in 2016) is smaller than petroleum's share in total exports (9.6%). Second, Chinese FDI did not follow the deceleration of Chinese economic growth; instead it has moved in the opposite direction. And as total FDI in Malaysia has stagnated, China's share has grown even more. Chinese FDI has been driven by both strategic and commercial imperatives. While China's OBOR strategy has the potential for Malaysia to increase FDI from China, China's slowdown may spur Chinese enterprises to invest overseas, including in Malaysia. Thirdly, Malaysia's currency has depreciated substantially well before China's Yuan devaluation, so that any loss of export competitiveness would have been more than offset.

Overall, then Malaysia's "new normal" of uneven growth cannot be blamed on China's growth deceleration. Malaysia's growth post-1997-99 Asian Financial Crisis that never recovered to the level of the 1980s and early 1990s clearly preceded China's growth slowdown from about 2012. The explanation for this slowdown has to be found elsewhere. However, "elsewhere" does not mean that external factors are not to blame. Indeed, the collapse of oil prices in 2015 struck a particularly harsh blow to an economy that has come to depend on oil export revenues and was already beset by challenges.

This dependence, as well as the still significant contribution of oil palm in net exports to China, raises questions as to why a country that has been

touted by the government as being well on the way to becoming a developed country was so dependent on primary commodity exports. That, as has been noted, so little value-added has accrued to Malaysia's electronics exports only strengthens arguments of structural problems in the domestic economy. Of direct relevance is Malaysia's failure to develop its human capital to its full potential (Cheong et al, 2016). Amid the current economic gloom, Malaysia is also rocked by political scandals that have been addressed by measures that undermined rather than restore confidence (Chander and Welsh, 2015). The upshot of this and other adverse developments has been stagnation in private investment, while a net outflow of FDI to the tune of US\$6 billion was reported for 2014, amounting to 6.5% of Malaysia's GDP (UNCTAD, 2015).¹⁰

Although this paper is not the place to address these domestic issues, making them explicit is important to show that China's New Normal is the least of the many challenges Malaysia faces. Malaysia must deal with its own demons first.

Finally, what does China's New Normal really portend for Malaysia? On the positive side, as has been concluded, China's growth deceleration, coupled with its implementation of OBOR can actually yield benefits for its economic relations with Malaysia. Malaysia may also benefit from China's shift towards consumption, for instance, in the form of tourist arrivals. However, China's rapidly advancing technological prowess, also part of its "new normal" only now garnering attention, should see more Malaysian imports of Chinese high-tech equipment such as telecommunications equipment that will tilt the China-Malaysia trade balance in the former's favour. Adding to this imbalance will be Malaysia's implementation of mega-projects with Chinese participation seeing more imports of Chinese steel. Over the longer term, Malaysia is also likely to lose out in process trade as China progressively takes over upstream segments of the supply chains in which Malaysia currently participates. Finally, a potential benefit of a China slowdown for Malaysia may be to force the latter to rethink the many vulnerabilities of its own making – reliance on primary commodity exports and on a cheap labour model that adds little value to production in supply chains, born of the failure to develop and retain the quantity and quality of human capital needed to move the country up to advanced economy status, and to capture the opportunities arising from China's rebalancing. Will this occur? The ball is entirely in Malaysia's court.

Annex 1: China's Investment to Malaysia since 2008

<i>Year</i>	<i>Chinese Entity</i>	<i>US\$ Million</i>	<i>% Share</i>	<i>Transaction Party</i>	<i>Sector</i>	<i>Subsector</i>
2008	Sinomach	120			Energy	Hydro
2008	Three Gorges led consortium	880			Energy	Hydro
2008	China Communications Construction	680			Transport	Autos
2010	Chinalco*	350	35	GIIG	Metals	Aluminum
2010	Sinomach	310			Energy	Coal
2010	Sinoma	140		Hume Cement	Real estate	Construction
2010	Sinohydro	260		Tenaga	Energy	Hydro
2010	Sinomach	900		Lion Group	Metals	Steel
2011	Chinalco*	800		Smelter Asia	Metals	Aluminum
2011	Genertec	830	50	Alstom	Energy	Coal
2011	Shougang Group*	240	40	Hiap Teck Venture Berhad	Metals	Steel
2012	Power Construction Corp	1,420			Real estate	Construction
2012	Three Gorges	200			Energy	Hydro
2012	Country Garden Holdings*	330			Real estate	Property
2012	MCC	1,480			Other	Timber
2013	Guangxi Beibu*	400	49	Malaysia-China Kuantan Industrial Park	Real estate	Property
2013	Guangxi Beibu	480	40	IJM Corporation	Transport	Shipping
2013	Guangxi Beibu"	650			Metals	Metals
2013	Power Construction Corp	300		OM Holdings	Metals	Metals
2013	Power Construction Corp	2,400		Tenaga	Energy	Gas
2013	Comtec Solar*	380			Energy	Alternative

Annex 1: (continued)

<i>Year</i>	<i>Chinese Entity</i>	<i>US\$ Million</i>	<i>% Share</i>	<i>Transaction Party</i>	<i>Sector</i>	<i>Subsector</i>
2013	China Communications Construction	100			Transport	Shipping
2013	Power Construction Corp	190		Sarawak Cable	Energy	Property
2013	Guangzhou R&F	1,370			Real estate	Autos
2014	Beijing Urban Construction	1,300	50	Zenith Sdn.	Transport	Property
2014	Shanghai Greenland	\$180			Real estate	Textiles
2014	Shandong Daiyin*	\$200			Other	Oil
2014	Sinopec	1,330		Petronas	Energy	Coal
2014	Shanghai Electric	240		Sarawak Energy	Energy	Construction
2015	State Construction Engineering	430			Real estate	Property
2015	Shanghai Greenland	660			Real estate	Alternative
2015	Jinkosolar*	100			Energy	Autos
2015	SAIC	280	49	Weststar Maxus	Transport	Industry
2015	State Construction Engineering	600			Other	Coal
2015	China Energy Engineering*	940	50	JAKS Resources	Energy	Construction
2015	State Construction Engineering	100			Real estate	Shipping
2015	China Communications Construction	550			Transport	
2015	China General Nuclear	2,300	100	Edra	Energy	Property
2015	China Railway Engineering	700	40	IMDB	Real estate	

Note: * Refers to greenfield investment.

Source: China Global Investment Tracker.

Notes

- * Dr. Cheong Kee Cheok is currently an Associate Member of the Institute of China Studies, University of Malaya. As a graduate of the University of Malaya (UM), he obtained his PhD at the London School of Economics. Upon returning to Malaysia, he joined the Faculty of Economics and Administration, UM, and was appointed first as Deputy Dean, then the Dean of Faculty. After a decade at UM, he spent 16 years overseas at the World Bank as an Economist and subsequently Senior Economist. He was Acting Coordinator for China and Vietnam in the Economic Development Institute (now known as the World Bank Institute). After returning to Malaysia in 1997, he continued to work as consultant for the Bank and UN agencies. His work has taken him to China, Vietnam, Cambodia, Laos, Mongolia and North Korea and other Asian countries. His research interests include economic development, transition economies, employment and poverty and international economic relations. He can be reached at <keecheok1@yahoo.com>.
- ** Ms. Wang is currently a PhD candidate at the Faculty of Economics and Administration, University of Malaya (FEA, UM). She graduated from Troy University with a bachelor's degree in Business Administration. She then studied at the University of Malaya for postgraduate studies. She is now working on her PhD thesis. She has published several papers in international journals such as *Cities*, *Habitat International* and others. She can be reached at <qianyiyouyou@sina.com>
1. According to the World Bank database (data.worldbank.org), trade (the sum of exports and imports of goods and services) accounted for 140% of Malaysia's GDP in 2014.
 2. In SITC group 77 for 2015, out of a total export value of RM35 billion, nearly RM31 billion were from SITC776 – “thermionic valves and tubes, photocells, etc. and parts thereof NEC”.
 3. As proof that imports and exports of SITC77 relate to electronics industry supply chains, about RM17 billion (60% of SITC77) consists of items under SITC776, which dominates the items exported, in 2015. An additional RM4.5 billion (16% of SITC77) are imports of SITC772 – “Electrical apparatus, resistors other than heating resistors, printed circuits, switchboards and control panels”.
 4. In 2016, Malaysian exports of petroleum and petroleum products (SITC33) to China amounted to 10.2% of its total exports of this item. For vegetable oils and fats, the share was 9.5%.
 5. The China Global Investment Tracker, launched in 2005, is co-published by the American Enterprise Institute and the Heritage Foundation. It tracks all Chinese investments overseas that are valued at US\$100 million and above.
 6. In March 2016, the China Global Investment Tracker showed the China Railway Engineering Corp. investing US\$2,010 million in Malaysia's transport sector and US\$410 million in the real estate sector, the vendor of the real estate being 1MDB.
 7. The second Penang Bridge, with the China Engineering Harbor Company as main contractor, was completed in 2014. The 944 MW Murun Dam, constructed

- by China's Three Gorges Development Company, was completed in 2015. The Gemas – Johor Bahru electric double-track rail project, with China Railway Construction Corporation as main contractor, is scheduled for completion in 2019 (Hafiz, 2016).
8. From MYR3.16 to US\$1 on 31 August 2014, the rate went to MYR4.19 exactly a year later, peaking at MYR4.41 on 27 September 2015.
 9. This index is defined as the sum over all products of the smaller of the share of a particular export to total exports in two countries, expressed as a percentage (Finger and Kreinin, 1979). Sometimes, net rather than gross exports is used for estimation.
 10. Malaysia also ranks fifth globally in terms of illicit financial outflows in 2013, with an accumulated outflow of US\$419 billion since 2004, US\$48 billion leaving in 2013 alone (Kar and Spanjers, 2015).

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