

DETERMINANTS OF MALAYSIA'S BILATERAL TRADE IN THE MANUFACTURING SECTOR: A COMPARISON BETWEEN CHINA AND ASEAN

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ABSTRACT

Malaysia relies heavily on international trade to drive its economic growth. Thus, this study aims to identify the determinants of bilateral trade between Malaysia and its major trading partners, namely, ASEAN-4 (Indonesia, the Philippines, Singapore and Thailand) and China. Both time series and panel models are utilised in this study for the period of 1980-2013. Empirical results show that the determinants for the countries under study are similar. The study finds that the development of human capital in Malaysia plays a pivotal role in enhancing and sustaining the trade ties between Malaysia and its major trading partners.

Keywords: *Bilateral Trade, Economic Growth, Sustainability*

1. INTRODUCTION

Malaysia possesses a strong trade orientation history (Khalid & Webb, 2011); since its independence, it has practised liberal policies for trade and foreign capital (Tang, 2013). Hence, Malaysia is involved in trade with many countries. According to Kennedy and Peter (1990), Malaysia's trade openness policy has transformed it into a trade dependence country and one of the "Asian Tigers". It has a sizable amount of both exports and imports and, therefore, its economic growth is mainly contributed by the external sector (Kennedy & Peter, 1990). Export emerges as the main catalyst to stimulate economic growth in the short run (Yousif, 1999). Thus, with rapid expansion of globalisation in this era, international trade plays a pivotal role in further accelerating Malaysia's economic growth.

As Authukorala and Menon (1996) noted, manufacturing has emerged as the most important sector for the Malaysian economy. Based on the Economic Report (2014/15), the manufacturing sector contributed 76.2% and 58.5% to total exports and total imports, respectively, in 2013. In addition, exports for most of the manufactured goods in Malaysia registered a surge which resulted in the said exports rising by 7.1% in 2014 from a year earlier (MITI, 2015). It is apparent that the manufacturing sector is crucial in Malaysia's external sector and, thus, this study will focus on the manufacturing sector.

China has emerged as Malaysia's top trading partner since 2009. In 2014, 14.3% of Malaysia's total trade was contributed by bilateral trade with China (MITI, 2015). China's open door policies since 1979 have transformed it into one of the world's fastest growing economies. Indeed, China has dominated the East and Southeast Asian production network (Tong & Lim, 2009). Hence, it has actively participated in free trade agreements with the Association of Southeast Asian Nations (ASEAN), such as the Regional Comprehensive Economic Partnership (RCEP) and China ASEAN Free Trade Area (CAFTA), which were established in 2012 and 2010, respectively. As Malaysia is an ASEAN member, it is believed that Malaysia can reap benefits from China's rise.

Nevertheless, ASEAN aims to forge closer economic integration among its member countries (Tan & Santhapparaj, 2006). According to ASEAN (2014a), intra-ASEAN trade has grown at a fast pace, with an average growth rate of 10.5% annually during the period 1993-2013. As a result, total intra-ASEAN trade posted an increase of more than sevenfold from US\$82 billion after the establishment of the ASEAN Free Trade Area (AFTA) in 1993 to US\$609 billion in 2013. Furthermore, the full establishment of the ASEAN Economic Community (AEC) in 2015, which transformed ASEAN into one single market and production