Belt and Road Initiative

Opportunities and Challenges for Malaysian SMEs

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I. Belt and Road Initiative and Background

(I) Brief introduction to the Ancient Silk Road. The Ancient Silk Road, which was officially launched during the Han Dynasty (207 BC – 220 AD), is a concept which refers to both the terrestrial and maritime trade routes connecting China with countries in Asia and Europe, or countries between in the East and West. Meanwhile, the Ancient Maritime Silk Road was a network of trade route that was central to the economic and cultural interactions among countries across the large portion of Asia-Africa-Europe landmass which stretched from the Korean peninsula, Japan, countries in today's Southeast Asia，and South Asia , further down to the Mediterranean Sea, eventually winding up its way in countries in Europe.

In short, the above ancient East and West trade enriched the lives of the peoples in many countries along the Ancient Silk Road, and played a significant role in enhancing the development of the civilizations of China and those of the partner countries and in boosting the political and economic relations among the relevant civilizations, due to the fact that silk, tea, porcelain and many other goods as well as cultures, religions, philosophies and technologies were traded and flourished.

(II) Brief introduction of the Belt and Road Initiative. The Belt and Road Initiative, was the brain child by President Xi Jinping when was visiting Kazakstan and Indonesia respectively in 2013. The BRI is a twin engine platform for common development between China and the partner countries around the world. The "Silk Road Economic Belt" focuses on the overland infrastructure and industrial development across Eurasia landmass, while the "Maritime Silk Road"will expand the maritime shipping routes and post-telecommunication lines, after which countries along the road will carry out further cooperation in the field of trade, investment, industry and culture, which are to facilitate conditions for partner countries to tap into the Chinese market, in order to increase their export to China, to receive vertical and horizontal industrial transfers from the Chinese enterprises, in order to up-grade or improve industrial structures, to tap into the Chinese investment in order to expedite their own economic development. In addition, the BRI is set to provide ways and means for the peoples along the Silk Road to know one another, emulate from one another, which would lay human resource foundation for the common development and common prosperity.

II. Opportunities for Malaysian SMEs

(I) It is the geographic advantage. China and ASEAN established Free Trade Area since a decade ago and is set to up grade it into a common market. As Malaysia is one major economy in the ASEAN, small and medium enterprises in Malaysia could take full advantage of the near-zero tariff to expand the two way trade and investment with China. The BRI will open up more opportunities for Malaysia business communities mainly as the Maritime Silk Road will outreach from China down to the ASEAN and has literally turned Malaysia as the gateway between China and Europe, which are the two economic centers giving the Malaysian SMEs the best opportunity to generate trade and investment.

(II) It is the institutional advantage. In 2013, China and Malaysia upgraded the bilateral relations to that of “Comprehensive Strategic Partnership Relations,” which already serves the foundation for the Malaysian business communities to tap into the ever growing Chinese market and its economic growth. Indeed, Malaysia is already the 23rd largest exporter in the world out of 168 countries in the WTO, and China is Malaysia’s largest trading partner and Malaysia is China’s largest trading partner in Southeast Asia, with the bilateral annual trading volume surpassing US$100 billion in 2016, and is projected to reach US$160 billion by 2017. The Malacca Gateway Project that China and Malaysia launched last year would include three reclaimed islands and would develop a fourth natural island. The above mega project will cater to tourism, commercial and housing needs, with ***Pulau Melaka*** being earmarked for exclusive maritime activities i.e. container and bulk terminal, shipbuilding and ship repair services, and for a maritime industrial park, the Malacca Industrial Park.

(III) It is the government policy support. According to the action plan of the BRI, the Maritime Silk Road will start with the transportation and telecommunication networks, and follow up by the industrial cooperation among businesses communities both from China and the partner countries across the world. It is true that, at the initial stage, major companies from China and the partner countries will be the main stake holders for mega connectivity projects. However, SMEs from Malaysia and other partner countries will definitely have many opportunities during the century-long period of industrial cooperation. It is fortunate that Malaysia has more people who can speak Mandarin than any other countries around the world. And, more and more Malaysians are learning Mandarin now. It is certainly a strategic decision by the government to include Mandarin in the syllabus. With the increase of Mandarin speakers in Malaysia, it would be much easier for the business communities of both countries, especially SMEs, to employ bilingual young people in order to expand the two way trade, investment and to carry out effective industrial cooperation.

(IV)It is the structural readjustment opportunity. From the geographic perspective, Malaysia can take full stock from both the Maritime Silk Road and the China-ASIAN Free Trade Area to further promote the economic and trade cooperation with China. Consider the huge scale of the Chinese market, it would be the best way for Malaysian SMEs to focus their trade and investment expansion to a selected number of provinces and municipalities across China. More importantly, they can take the full advantage of the cultural linkage between the two countries, which boasts a population with Chinese origin of about 7 million.

(V) It is the the new industrial platform. International experience shows that bilateral economic trade and economic relations would be sustainable unless the two countries would identify and establish the right channels and select the right business connections. In this regard, Malaysian government has come with the right choice. On 4th November 2016, Jack Ma, the founder of Alibaba group agreed to act as an adviser to the Malaysian Government on its digital economy aspirations. For that matter, Alibaba would set up a logistics hub in Malaysia, which would include infrastructure and real estate projects.The Malaysian government has agreed to allocate the land for Alibaba to set up this e-hub, which would make it easier for SMEs in Malaysia to expand their production scales and more effectively participate in regional and international trade. The hub, which is set to be in operation by the end of 2019, will be part of a digital free trade zone. Accordingly, the hub will offer services such as centralized customs clearance, warehousing and fulfillment facility for business enterprises both from Malaysia and the partner countries, in order to generate more trade and investment.. In addition, Alibaba will also explore ***e-payment*** and financing opportunities to facilitate business-to-business trade, which would be an ideal platform for the Malaysian SMEs. Jack Ma has promised the Malaysian government that he is to launch ***Alipay*** in Malaysia soon, which would boost Malaysian domestic market and for the Malaysian SMEs to more effectively tap into the Chinese market as well as other markets around the world.

(VI)It is the financial vehicle opportunity.In order to effectively promote the joint construction of the Maritime Silk Road, the Chinese government has joint hands with partner countries to establish the Asian Development Bank, to which Malaysia is a member, in order to provide financial support for the business communities with preferential packages to boost the two way trade, two way investment and industrial cooperation among enterprises between China and relevant partner countries. And, the Silk Road Fund is also to come up with fund for SMEs in the above regard.

(VII) It is the manufacturing opportunities. Malaysian SMEs have contributed greatly to the national economy and have been collectively contributing to more than half of the annual national GDP. It is an open secret that when the construction of the maritime Silk Road connectivity networks is fully completed and when the Malacca industrial park is in full operation, the local manufacturing enterprises can have more market access to plan their future production chains or to expand their positions in the regional and international supply chains with partnership relations with the Chinese counterparts.

(VIII) It is the employment opportunities. In essence, the ultimate goal of economic development for any country or any bilateral economic cooperation is to satisfy the material need and spiritual aspiration of the peoples, whose success is earmarked by the rate of job creation. In this regard, Malaysian SMEs are to become the major job providers for the young people, who come into the labor market by increasing numbers, with the joint construction the BRI related projects in and around Malaysia. In this regard, too, Malaysian SMEs would enjoy more policy guidance and economic support by the governments of both countries in expanding the production and business operation scales in partnership with the Chinese partners.

III. Pending Issues for Malaysian SMEs

(I)IT is difficult to promote bilateral trade without having to manage the trade deficit. Malaysia has been facing trade deficit with

China since 2012. In order for the bilateral economic relations to be sustainable, and in order for the smooth implementation of the Belt and Road joint construction, both China and Malaysia have yet to join hands in identify ways and means to address the issue of trade imbalance. Take the bilateral trade of 2016 for example, the total trade increased by 4.4% over the previous year. Malaysia export stood at RM98.6 billion and import stood at RM142 billion, which resulted a trade deficit of about RM43 billion.

(II) It is difficult to receive equal treatment in finance and policy support.It is true that, right at the moment, China and the partner countries are concentrating their capital, human resources and technologies on the joint construction of the mega connectivity projects. Therefore, SMEs of all the partner countries have to be a bit more patient for Stage II joint construction. This is the stage where the SMEs of the partner countries will become the major players. The key question is Malaysian SMEs will have to carry out more feasibility studies, in order to spot the "early bird" opportunities, rather than waiting for the "moon cakes to drop from the sky".

(III) It is difficult to cope with the changing market dynamics at the Chinese market. It is true that China has been increasing imports and exports by as much as $1 trillion per year since some years ago. With the BRI in full swing, China will nurture an ever larger appetite for foreign goods and services. However, Chinese market has been dominated mostly by brand products or products produced by transnational corporations in China. Meanwhile, Chinese consumers have been used to their favorite brand products and services. Therefore, Malaysian producers would have to produce the quality products that would meet the market requirements and be accepted and appreciated by the Chinese consumers, in order to get a fair share of the market.

(IV) It is difficult to compete with SMEs from other partner countries. Since China launched the historical agenda for economic reform and opening up, more than one and half million FDI related enterprises have shifted their production lines or production links across China. And many SMEs have also taken the opportunity to shift their production lines to China, in order to stay close to the relevant transnational corporations. In short, Chinese market is huge but the competition is also becoming intense. Therefore, Malaysian SMEs will have to devise ways and means to compete with the existing Chinese and foreign SMEs.

(V) It is difficult to learn and master the game rules at the Chinese market. Since China joint the WTO, she has been shifting to the market economy. Meanwhile, as the Chinese economy has been competing with other mainstream market economies, Chinese enterprises have been accustomed to the international game rules. However, like

Malaysia, Chinese market has also developed certain rules and customs which are different from other markets. Therefore, it is up for the Malaysian SMEs to find the ways and means to adapt to those rules and customs in order to effectively chip into the growing Chinese market.

(VI) It is a challenge to switch to new production chains and supply chains. Malaysian enterprises used to provide the transnational corporations in China with components parts by large volumes. However, as the fourth industrial revolution is evolving, transnational corporations in China, with Internet technologies and 3D printing technologies, will not have to place their lower end manufacturing and assembling link in China alone, and market their end-products around the world. Rather, they would set up branch production lines where the potential customers are. Therefore, Malaysian SMEs would have to adapt to the above new normals. And as more and more Chinese companies have been outsourcing their production lines and production chains overseas, it up for the Malaysian SMEs to grab the opportunity and form the joint ventures with them, in order to ride along with the on-going Chinese industrial transformation.

IV. Policy Thought for Malaysian SMEs

(I) Readjust market development Strategy. As China has joint the rank of middle and high income countries, and as both our economies are at the cross road, both governments have been readjusting their trade and industrial strategies and policies. In this regard, the BRI will definitely provide the steam to the above process. Therefore, the SMEs of both countries should modify their market entry strategies, in order to seek the early market entry advantages.

(II) Make full use of the institutional arrangement between China and ASEAN. For political, economic and cultural reasons, ASEAN has been earmarked as the key area for the Maritime Silk Road construction, which would generate more opportunities for Malaysian SMEs in particular. As more and more BRI related projects will be built in and around Malaysia, the relevant SMEs should fully tap into the opportunities to expand trade, investment and industrial cooperation with Chinese counterparts.

(IIII) Take full stock from China-related economic policies by the Malaysian government. In short, Malaysian SMEs should lobby the government to sign new agreement in terms of closer cooperation among SMEs between the two countries, which would facilitate legal foundation for the SMEs of both countries to plan their market entry strategies.

(IV) Follow closely trade and investment policies by the Chinese government.There is no way to bypass bureaucracy and administrative procedures either in terms of bilateral trade or bilateral investment. The Chinese government has been abolishing or updating redundant trade and investment related policies and regulations or in line with the implementation of the BRI construction. For that matter, Malaysian SMEs should follow the policy trend in China and carry out more study into the new policies and regulations. As one saying goes well, it pays to sharpen the hatchet before going to chop the firewood. And in the mordent business, the best way to success is to best utilize the policy tools.

(V) Formulate business alliance in order to fully tap into the Chinese market. There is a saying that market opportunities do not wait for anybody and they are only going to anybody who is prepared. Malaysian SMES should quickly find the suitable business partners in order to expedite the cooperation in the two way trade or two way investment.

(VI) Establish national trade mark products.The Chinese market has become more mature in line with the WTO rules and the international benchmarks. As the national market is too large for any individual companies to develop on their own capability, Malaysian SMEs should be advised to concentrate their business venture into selected provinces and municipalities. They should form a “consortium” which would allow them to market their products more efficiently. Furthermore, they should nurture brand products on the item basis, rather than marketing their products on the company basis.

(VII)Carry out road shows on trademark products. As mentioned above, Chinese market and the Chinese consumers have been “spoilt” by the foreign products and foreign brands. Therefore, Malaysian SMEs should expedite the process to do more road shows and participate in more commercial exhibitions in order for the Malaysian trademark products to be accepted and appreciated by the Chinese market and the consumers .

(VIII) Find partners with good reputation in China.International practice and experience show that the most outstanding “road blocks” for foreign enterprises to enter into foreign markets are the “invisible barriers” in terms of administrative procedures, and the “cultural shocks”in terms of customs and traditions. Therefore, Malaysian SMEs should identify and establish partnership with Chinese counterparts, and vice verse, in order to get around or overcome the above scenarios.

(IX) Form production chains with Chinese counterparts.It pays for the Malaysian SMEs to either join the production chains by the Chinese enterprises, or those from the partner countries, or form joint production chains with the Chinese counterparts, in order to produce the agreed trade mark products and market them both in China and other partner countries, which would facilitate conditions for the former to help balance out the Malaysian trade deficit indirectly.

(X) Form supply chains with Chinese counterparts. In accordance with research findings, Malaysia and China have been carrying out both horizontal and vertical industrial cooperation since thirty years ago. As China has been readjust it position in the international production chains and supply chains, while establishing its own production chains and supply chains under the framework of Belt and Road Initiative, the Malaysian SMEs should also readjust their strategies and try to follow the Chinese manufacturers in the new market along the new silk road.