



# U.S.-Malaysia Relations: Implications of the 2008 Elections

(name redacted)

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## Summary

This report discusses key aspects of the U.S.-Malaysia relationship (including economics and trade, counterterrorism cooperation, and defense ties) and the possible impact of Malaysia's 2008 elections on the future of the relationship.

In parliamentary elections held on March 8, 2008, the Barisan Nasional (BN), which has ruled Malaysia since independence in 1957, was struck by a "political tsunami" that saw it lose its two-thirds "supermajority" for the first time since 1969. Malaysia's major opposition parties won 82 of the 222 parliamentary seats up for election. In addition, the opposition parties won control of five of Malaysia's 13 state governments. The election results are widely seen as a vote against the current policies of the Malaysian government, which could have implications for relations with the United States.

Prior to the elections, the bilateral relationship has been generally positive and constructive, particularly in the area of trade. Malaysia is a key trading partner of the United States and is regarded as an effective and cooperative regional player in the war against terror. The United States and Malaysia also have informal defense ties including commercial access to Malaysian ports and repair facilities. Despite these positive dynamics, the bilateral relationship has at times been strained. Past differences have stemmed from disagreements between Malaysia's former Prime Minister Mahathir Mohamad and the United States over such issues as the internal suppression of dissent in Malaysia, the Israeli-Palestinian conflict, Iraq, globalization, Western values, and world trade policy. Relations are perceived as having improved since Abdullah Badawi became prime minister in 2003.

After years of strong economic growth, Malaysia has become a middle income country. Much of its gain in economic prosperity has come from the export of electronics and electrical products, with the United States as its top export market. According to U.S. trade figures, Malaysia exports over \$30 billion of goods each year to the United States and imports over \$11 billion from the United States.

The United States and Malaysia have enjoyed a positive trade relationship over the last few years, in part because both nations favor trade and investment liberalization in Asia. Malaysia is the United States' 10<sup>th</sup> largest trading partner. Building on their common perspective of international trade, Malaysia and the United States concluded a trade and investment framework agreement in 2004 and are currently negotiating a bilateral free trade agreement. Key issues still to be resolved in the negotiations principally revolve around market access for key goods and services in both the United States and Malaysia, and intellectual property rights protection in Malaysia. In addition, the dismissal of Malaysia's chief negotiator, Trade Minister Datuk Seri Rafidah Aziz, may complicate future talks.

This report will be updated as circumstances warrant.

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U.S. relations with Malaysia have been generally positive over the last few years. Both countries share interests in maintaining regional stability, dealing with militant Islamists and separatists, developing close trade and investment relationships, securing the safety of ships passing through the strategically important Strait of Malacca, and establishing mutually beneficial military cooperation. However, efforts to negotiate a bilateral free trade agreement (FTA) appear to be stalled. In addition, Malaysia and the United States appear to have conflicting views of the future of regional economic integration in East Asia.

U.S.-Malaysia relations improved after former Prime Minister Mahathir Mohamad turned over power to his former Deputy Prime Minister Datuk Seri Abdullah Badawi on October 31, 2003, ending 22 years of rule by Mahathir. However, an unexpectedly weak showing for Badawi's political party, the United Malays National Organization (UMNO), and its Barisan Nasional (BN) coalition partners in the March 8, 2008 parliamentary elections may have implications for U.S.-Malaysian relations.

This report provides an overview of recent political and economic developments in Malaysia, and examines implications for U.S. policy.

### Malaysia In Brief

**Area:** 127,316 sq. miles (about the size of New Mexico)  
**Capital:** Kuala Lumpur  
**Population:** 27.5 million (2007)  
**Ethnic Groups:** Bumiputeras 58% [Malay 47%, Indigenous 11%], Chinese 24%, Indian 7%, Non-citizens 7%, others 4%  
**Religion:** Muslim, Buddhist, Confucian, Taoist, Christian, Hindu, Sikh, Baha'i  
**Literacy Rate:** 92.5% (2006)  
**Life Expectancy:** Female - 76.3 years; Male - 71.8 years (2006)  
**Sources:** Malaysia Ministry of Finance, *Economic Report 2007/2008*.

## Malaysia's 2008 Elections

UMNO and its coalition partners have been in power since Malaysia's independence in 1957. In the first general election in 1959, UMNO and its coalition partners<sup>1</sup> received just over half the votes, but won 74 out of the 104 seats in the *Dewan Rakyat* (People's Hall), the more powerful lower house of Malaysia's parliament.<sup>2</sup> In every parliamentary election from 1959 to 2004,<sup>3</sup> an UMNO-led coalition has won at least two-thirds of the seats in parliament—with the exception of 1969, when the coalition won 95 out of 144 seats (66.0%). A two-thirds "supermajority" is important because it allows the BN to amend Malaysia's constitution without support from opposition parties. In the election of 2004, the BN won 198 out of 219, or 90.4%, of the seats.

### Political "Tsunami"

The outcome of the parliamentary elections of March 8, 2008, surprised many people. A major Malaysian newspaper, *The Star*, quoted one opposition leader who compared the results to a

<sup>1</sup> At that time, UMNO was part of a political coalition known as the Alliance Party, a predecessor to the BN.

<sup>2</sup> Malaysia has a bicameral parliament consisting of the elected *Dewan Rakyat*, the lower house, and the largely-appointed *Dewan Negara* (National Hall), the upper house.

<sup>3</sup> Under Malaysian law, a parliamentary election must be held at least every five years. However, in many cases, early elections were held after about four years.

tsunami.<sup>4</sup> The BN barely received half of the popular vote, and won just 140 of the 222 seats in the *Dewan Rakyat*—eight seats less than it needed to retain a “supermajority.” The biggest losers among the BN members were:

- UMNO, which saw its seats decline from 109 to 79;
- The Malaysian Chinese Association (MCA), which dropped from 31 to 15 seats; and
- The Malaysian People’s Movement Party (*Parti Gerakan Rakyat Malaysia*, or Gerakan), which held onto only 2 of its 10 seats in the *Dewan Rakyat*.

Most commentators stated the 2008 elections were the BN’s worst results since 1959.

The main opposition parties—the Democratic Action Party (DAP), the Islamic Party of Malaysia (*Parti Islam SeMalaysia*, or PAS), and the People’s Justice Party (*Parti Keadilan Rakyat*, or PKR)—all increased their number of seats in the parliament. The PKR experienced the greatest rise—jumping from just one to 31 seats. The DAP and PAS both increased their seats on the *Dewan Rakyat* by 16 seats, for a total of 28 and 23, respectively. Altogether, Malaysia’s opposition parties received 46.8% of the popular vote, and won 82 out of the 222 seats on the *Dewan Rakyat*.

The BN’s weakness was also reflected in the results of the 12 concurrent state elections.<sup>5</sup> Opposition parties took control of five of the 13 Malaysian states, including surprise victories in Kedah, Penang, and Selangor. The PAS retained its control over the state of Kelantan and the DAP leads a small opposition majority in the state of Perak. Among the seven contested states in which the BN retained control, the opposition gained seats in all but two states—Perlis and Sabah.

There are differing opinions on why the BN lost so much of its support, and the opposition parties gained so much support. Some commentators maintain that Badawi was responsible because he had failed to make adequate reforms within the BN and the government. Others stated that economic factors, and in particular rising income disparities and inflation, had led voters to switch from the BN to the opposition parties. Another group of political observers saw the election results as evidence that Malaysia’s ethnicity-based political system was obsolete and no longer a reliable base of power for the BN.

## Implications of the Elections

In the immediate aftermath of the elections, ex-prime minister Mahathir suggested Badawi should consider resigning.<sup>6</sup> While Badawi did not resign, he did reorganize his cabinet, reducing the number of ministers (from 90 to 70) and removing several long-standing members. According to Badawi, half of the members of the cabinet announced on March 18, 2008, were “new faces.”<sup>7</sup> Among the people removed from the cabinet was Datuk Seri Rafidah Aziz, who had held the position of Minister of International Trade and Industry for over 20 years. Aziz has been an

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<sup>4</sup> “Nik Aziz Likens Big Win to a Tsunami,” *The Star*, March 9, 2008.

<sup>5</sup> The State of Sarawak did not hold concurrent elections.

<sup>6</sup> Jane Ritikos, “Examine Losses, Says Dr. M,” *The Star*, March 10, 2008.

<sup>7</sup> “Abdullah Announces Cabinet Line-Up, Half of Administration New Faces,” *Bernama*, March 18, 2008.

important figure in U.S.-Malaysian trade relations. It is unclear what impact, if any, the new cabinet will have on Malaysia's policies.

The dramatic drop in support for two of Malaysia's ethnically-based political parties—the MCA and the Malaysian Indian Congress (MIC)—has also led to calls for political changes. Gerakan party chief Datuk Chang Ko Youn, who lost his seat in the parliament to a DAP candidate, has suggested that BN member parties should consider eliminating ethnic restrictions on party membership as a first step to the formation of a single party.<sup>8</sup> However, MIC president Seri S. Samy Vellu, who also lost his bid for reelection to the parliament to an opposition candidate, rejected Chang's suggestion, saying "such an action will dilute the rights of the Indian community."<sup>9</sup> Some commentators have suggested that the shift in Chinese and Indian support to opposition party candidates reflects a growing sense among Malaysia's influential ethnic minorities that the BN no longer adequately reflects their interests. Others attribute the desertion of the BN by Malaysia's Chinese and Indian to economic issues, such as food price inflation and rising income disparities.

The strengthening of opposition party power in the *Dewan Rakyat* and in state governments is also expected to restrict the power of Badawi and the BN to implement changes in policy. The loss of a supermajority in the *Dewan Rakyat* is considered by some a psychological and political blow to the BN, which has ruled virtually unchallenged in Malaysia since independence. There is discussion that the election results may be the first sign that politics in Malaysia are starting the process of transformation into a two-party, non-ethnic system, and possibly a more truly democratic process.

In addition, opposition control of five of Malaysia's 13 states may also curtail Badawi's power. For example, the new state government in Penang has already announced that it will no longer abide by the BN's long-standing "New Economic Policy" that grants preferential treatment to Malaysia's *bumiputera*.<sup>10</sup> However, a past judicial tradition of broadly interpreting the federal government's power under Malaysia's constitution may mitigate the opposition's ability to use the state governments to exert power or influence.

A final concern raised by the BN's weak showing in the 2008 is the potential for social unrest and governmental policy change. The last time the BN (or its predecessors) did as poorly in a parliamentary election was in 1969. Following the 1969 elections, there were violent ethnic riots in Malaysia between May and July (precipitated by the "May 13 Incident" in Kuala Lumpur) during which approximately 200 people were killed. Following the riots of 1969, the BN announced a series of economic reforms, known as the "New Economic Policy" (NEP). The events of 1969 are discussed in more detail below. However, in the weeks following the election, there has been virtually no violence or ethnic unrest in Malaysia.

For U.S.-Malaysia relations, the 2008 elections will have little direct or immediate impact, with the possible exception of the removal of Aziz as Minister of International Trade and Industry. Aziz has been Malaysia's chief negotiator during the U.S.-Malaysia free trade agreement (FTA) talks. Her departure implies a loss of "institutional knowledge" for the Malaysian negotiation

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<sup>8</sup> "Samy: Time Not Ripe for Barisan to be a Single Party," *The Star*, March 17, 2008.

<sup>9</sup> *Ibid.*

<sup>10</sup> Claudia Theophilus, "Malaysia PM: Lessons to be Learnt," *Al Jazeera*, March 11, 2008. Malays and other indigenous groups are known as *bumiputeras*, or "sons of the soil."



team. Her replacement, Tan Sri Muhyiddin Yassin, was Minister of Agriculture and Agro-based Industry in the previous cabinet.

## Malaysia's Political Dynamics

Many of the political cleavages of Malaysian society, which continue to have relevance to today's political dynamics, find their root in Malaysia's colonial past. Malaysia inherited a diverse demographic mix from the British. Through the importation of labor, the British added ethnic Chinese and Indians to the Malay and other indigenous populations of peninsular Malaya, Sabah, and Sarawak. The demographic composition of Sabah and Sarawak includes a higher percentage of indigenous groups, such as the Iban. Together the Malay and indigenous population—collectively known as the *bumiputeras*—comprise about 58% of the population compared to 24% for the Chinese and 7% for the Indians. Traditionally, ethnic Chinese and Indians have controlled a disproportionately greater share of the nation's wealth than bumiputeras.

Malaysia has a complex history of inter-communal politics. A British plan after World War II to create the Malaysian Union that incorporated all of the Malayan territories except Singapore would have provided for common citizenship regardless of ethnicity. Concerns among the Malays that they could not compete with the more commercially-minded Chinese led to the creation of UMNO—a conservative, Malay nationalist organization that later reformed itself into a political party. Negotiations between the British and UMNO led to the creation of the Federation of Malaya in 1948, which included Singapore and provided special rights for the bumiputeras and Malaysia's sultans. Sabah and Sarawak joined the Federation to form Malaysia later in 1963, while Singapore left the Federation in 1965. At independence in 1957, there was an understanding that Malays would exert a dominant position in political life in Malaya, while ethnic Chinese and Indians would be given citizenship and allowed to continue their role in the economy.<sup>11</sup>

This accommodation between Malaysia's ethnic groups has not always been tranquil. Between 1948 and 1960, the Communist Party of Malaysia, which was largely comprised of ethnic Chinese, waged a guerilla war against the British. This came to be known as the "Malayan Emergency."<sup>12</sup> The Internal Security Act (ISA), which continues to be used to suppress groups that threaten the regime, originally was put in place by the British to combat "communist subversion." The Special Branch, which Malaysia inherited from the British, continues to act as the primary intelligence and security unit under the Royal Malaysian Police. During the "Emergency," Malays generally sided with the British against the communists whose ranks were drawn largely from the Chinese community. By the mid-1950s, the insurrection had collapsed.

Added to this history of inter-communal strife were the riots of May to July 1969 in which reportedly 196 were killed. Most of those killed were ethnic Chinese. Rioting began on May 13, three days after the Alliance Party, a predecessor to the BN, failed to win two-thirds of the seats in the *Dewan Rakyat*, and lost control of Selangor and Perak. Much like the results of the 2008 elections, one of the main losers in the 1969 elections was MCA, which lost 14 of its 27 seats in

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<sup>11</sup> Barbara Watson Andaya and Leonard Y. Andaya, *A Brief History of Malaysia*, University of Hawaii Press, 2001; Harold Crouch, *Government and Society in Malaysia*, Cornell University Press, 1996.

<sup>12</sup> Lt. General David Patraeus has reportedly studied the Malaya Emergency, among other counterinsurgency operations, as he has prepared himself for operations in Iraq. Dan Murphy, "New Commander, New Plan in Iraq," *Christian Science Monitor*, February 9, 2007.



the *Dewan Rakyat*. Because of the rioting, elections to be held in Sabah and Sarawak were suspended and a state of emergency was declared.<sup>13</sup>

Partly in response to the 1969 riots, the New Economic Policy (NEP) was instituted in 1971. NEP provided preferential treatment for the bumiputera majority via a kind of quota system in order to increase their share of the economic wealth of the country. The New Development Policy (NDP) replaced the NEP in 1990. The NDP retained NEP goals, such as 30% bumiputera control of corporate assets. Prime Minister Mahathir's subsequent *Vision 2020* policy had similar elements, but was more inclusive and attempted to do more to foster national ethnic unity.<sup>14</sup>

The BN appears to be relying on an expanding economy to be able to disproportionately favor bumiputeras, while not undermining its economic appeal to Malaysia's Chinese and Indian population. In this way, Malaysia's social harmony—and support for the BN—may be linked to economic growth. For this reason, periods of economic stagnation could carry the prospect of eroding the delicate balance between ethnic groups in Malaysia and undermining support for the BN.

## **Internal Politics**

Malaysia is a Constitutional Monarchy, but of an unusual kind, whose structure includes 13 states and three federal territories. Every five years, the nine hereditary Sultans elect one from among their group to be the Yang di Pertuan Agong, a traditional title equating to a King. The Agong exercises limited authority and acts on the advice of the Prime Minister, Parliament and the Cabinet. The Prime Minister is the head of the Federal Government, which has 25 ministries. Out of a total of 13 states four are ruled by State Governors appointed by the Federal Government. In the nine other states, the hereditary Sultan fulfills this function. Each state has a state legislature. The lower house of Malaysia's Parliament, the *Dewan Rakyat*, has 222 members elected for terms not to exceed five years. The upper house, the *Dewan Negara*, has 70 members—44 members appointed by the King and 26 elected members with two from each state.

Malaysia is an “ambiguous, mixed”<sup>15</sup> or “semi”<sup>16</sup> democracy that has both democratic and authoritarian elements. The constitution is largely democratic and provides for regular elections that are responsive to the electorate. The government is based on a parliamentary system and the judiciary is designed to be independent. Despite this democratic structure, authoritarian control limits the ability of the opposition to defeat the ruling coalition at the polls.<sup>17</sup>

Prime Minister Badawi heads the United Malays National Organization (UMNO), the key party in the BN. The BN also includes the Malaysian Chinese Association (MCA), the Malaysian Indian Congress (MIC), the *Parti Gerakan Rakyat Malaysia* (Malaysian People's Movement Party, or Gerakan), and a number of smaller political parties. The opposition is led by the Pan-

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<sup>13</sup> Stuart Drummond and David Hawkins, “The Malaysian Elections of 1969: An Analysis of the Campaign and the Results,” *Asian Survey*, Vol. 10, No. 4 (April 1970), pp. 320-335.

<sup>14</sup> YAB Dato' Seri Dr. Mahathir Mohamad, *Vision 2020*, (Kuala Lumpur: Institute of Strategic and International Studies, 1991).

<sup>15</sup> Crouch, pp. 4-5.

<sup>16</sup> William Case, “Malaysia's General Elections in 1999: A Consolidated and High-Quality Semi-Democracy,” *Asian Studies Review*, March, 2001.

<sup>17</sup> Crouch, p. 5.

Malaysian Islamic Party (*Parti Islam Se-Malaysia*, or PAS), the People's Justice Party (Parti Keadilan Rakyat, or PKR), and the Democratic Action Party (DAP). In 1999, PAS, DAP, PKR, and Malaysian People's Party (*Parti Rakyat Malaysia*, or PRM) formed an opposition alliance known as the *Barisan Alternatif* (Alternative Front), but the alliance fragmented in 2001 following the withdrawal of the DAP. For the 2008 elections, DAP, PAS, and the PKR formed an alliance called the *Barisan Rakyat* (People's Front) with a number of smaller parties.

UMNO is the most influential party in Malaysia today and represents the interests of the mostly Sunni Malays. The Malaysian administration, under both Mahathir and Badawi, has promoted a moderate form of Islam—*Islam Hadhari* (see below)—under a secular polity while opposing the rise of Islamic extremists whose policies are more closely associated with PAS.<sup>18</sup> The ruling BN, under Mahathir's leadership, used the power of the state, including the ISA, to thwart political gains by PAS, which advocates a more conservative view of Islam. PAS's influence is traditionally found in the northeast states of Kelantan and Terengganu.<sup>19</sup>

The transition from Mahathir to Badawi was consolidated in the March 21, 2004 elections that expanded the ruling BN's hold on parliament from 77% to 90% of the seats. The BN also increased its share of votes from 57% to 64%.<sup>20</sup> Following the 2004 elections, the government's coalition controlled 11 of 12 state governments. The election was viewed by observers as a vote of confidence by Malaysians in Badawi's relatively moderate form of Islamic practice as opposed to the hard-line approach of PAS.<sup>21</sup> The PAS, which offered a more Islamist agenda, lost voter confidence, including in its area of traditional support in northeast peninsular Malaya.<sup>22</sup>

The political transition from Mahathir to Badawi led to an improvement of U.S.-Malaysian relations. Some think Badawi, who was first elected to Parliament in 1978, is attempting to strike a balance between providing continuity of leadership to produce stability, and meeting expectations for a more open and consultative style of government. Badawi pledged to work with the BN to realize the policy goals articulated in *Vision 2020*.<sup>23</sup> It is thought that Badawi's political legitimacy will at least in part be dependent on his ability to deliver sound economic growth and to counter the perceived rise of Islamic extremism in Malaysia.<sup>24</sup> Badawi's respected religious background<sup>25</sup> has helped him counter the rising popularity of PAS and the forces of Islamic extremism.

However, Badawi's government has been beset by division within UMNO. In part, these are based on differences between former Prime Minister Mahathir Muhammad and Prime Minister Badawi. More recently, now ex-Minister Aziz has supposedly used her leadership of the Wanita

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<sup>18</sup> For a more detailed discussion of these dynamics see William Case, "Deep Insecurity and Political Stability: Inside Mahathir's Malaysia," in (name redacted) ed*The Unraveling of Island Asia?* (Westport: Praeger Publishers, 2002).

<sup>19</sup> S. Jayasankaran, "Lost Ground," *Far Eastern Economic Review*, March 21, 2002.

<sup>20</sup> "Malaysia's Election: Bravo Badawi," *The Economist*, March 27, 2004.

<sup>21</sup> See Anthony Smith, "Malaysia's 2004 Elections: Mahathir's Successor Succeeds," *Asia Pacific Security Studies*, April 5, 2004 and "So Much for the New Broom," *The Economist*, April 3, 2004.

<sup>22</sup> The term "Islamist" is used to identify those who would affiliate themselves with more extreme interpretations of Islam.

<sup>23</sup> "Abdullah Pledges to Work Hard to Make Vision 2020 a Reality," *New Straits Times*, September 8, 2003.

<sup>24</sup> Bridget Welsh, "Elite Contestation, Political Dilemmas and Incremental Change," Woodrow Wilson Center, July 24, 2003.

<sup>25</sup> Badawi's father and grandfather were Islamic religious scholars. Badawi himself has a degree in Islamic Studies.

Umno, UMNO's main women's organization, in an attempt to influence government and party policies. It is thought that party divisions led Badawi to call for the early general elections of 2008 in hopes of securing a fresh mandate and reinforcing his position within his party.<sup>26</sup> The outcome of the elections was clearly contrary to his hopes.

## Islam Hadhari

Under Badawi's leadership, Malaysia has been developing a concept, *Islam Hadhari*, that seeks to promote a moderate or progressive view of Islamic civilization.<sup>27</sup> Badawi has stated that "we are responsible for ensuring that the culture of extremism and violent acts in the name of Islam does not happen in Malaysia."<sup>28</sup> Some observers believe that *Islam Hadhari* could promote a view of Islam that encourages and emphasizes development, social justice and tolerance.<sup>29</sup> Increasing attention appears to be focused on the role that moderate Islamic ideology and moderate Islamic states can play in countering the forces of Islamic extremism within the region and beyond. However, some analysts are concerned about what they see as an "increasing Islamisation trend in Malaysia" and that "a more conservative form of Islam is emerging" in Malaysia despite government efforts through *Islam Hadhari* to "pave the way for the development of Malaysia as a bastion of Islamic moderation."<sup>30</sup>

## Malaysia's International Relations

Malaysia has been playing an active role in international organizations both in its region and beyond. Besides Asia Pacific Economic Cooperation (APEC), ASEAN, and the World Trade organization (WTO), Malaysia is also a member of the Asian Development Bank (ADB), the Islamic Development Bank, the Non-Aligned Movement (NAM), Organization of Islamic Conference (OIC), the United Nations, and the World Bank. In 2006, Malaysia chaired ASEAN, the Organization of Islamic Conference (OIC), and the Non-Aligned Movement (NAM). Malaysia has been an active contributor to international peacekeeping, including most recently in East Timor. It also sent personnel to assist the Aceh Monitoring Mission in Indonesia in 2005 and 2006. Malaysia has also been seeking to facilitate negotiations between the government of the Philippines and the Moro Islamic Liberation Front.<sup>31</sup>

## Regional Relations

Malaysia has placed much emphasis on regional cooperation despite its differences with certain regional states. In the past, Malaysia and the Philippines have differed over the Philippines' claim to parts of Sabah. Indonesia and Malaysia came into conflict as a result of Indonesian military

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<sup>26</sup> "Malaysia: Country Report," *The Economist Intelligence Unit*, February 2007.

<sup>27</sup> Transcript of Interview with the Prime Minister of Malaysia," *Bernama*, February 17, 2005.

<sup>28</sup> "Malaysian Premier calls on Muslims to Defy Militants," *Agence France Presse*, July 20, 2005.

<sup>29</sup> Paul Wiseman, "In Malaysia Islamic Civilization is Promoted," *USA Today*, November 4, 2004. Evelyn Goh, "Keeping Southeast Asia on the U.S. Radar Screen," *PacNet Newsletter*, May 26, 2005.

<sup>30</sup> Mohamad Nawab Mohd Osman, "Where to Islam Hadhari?" *IDSS Commentaries*, November 28, 2006.

<sup>31</sup> "The United States and Malaysia: A Diverse and Expanding Partnership," U.S. Department of State, Bureau of Public Affairs, July 26, 2006.

raids over the border in Borneo in 1963. These were part of its policy of *confrontasi* and repelled by Malaysian and Commonwealth forces. Malaysia remains a member in the Five Power Defense Arrangements along with Australia, New Zealand, the United Kingdom, and Singapore, which has its roots in Malaysia's colonial past.

Malaysia has significant interest in the hydrocarbon potential of the South China Sea. In the past, this has put Malaysia in conflict with Brunei over the Baram Delta off the coast of Sabah and Sarawak. In July 2002, independent U.S. contractor Murphy Oil, working for Malaysia's state oil company Petronas, discovered the Kikeh field, which is estimated to hold 700 million barrels of oil.<sup>32</sup> This represents 21% of Malaysia's current reserves, which are projected to run out in 15 years.<sup>33</sup> Malaysia, China, the Philippines, and Vietnam have conflicting claims over the Spratly Islands and the South China Sea. Though continuing, this conflict has been less contentious in recent years than it was in the 1990s.

Malaysia was a founding member of ASEAN in 1967 and in the 1990s was a strong advocate for expanding ASEAN to include Burma, Laos, and Vietnam. More recently, Malaysia has sought a more influential role in ASEAN and Southeast Asia, particularly with respect to trade issues. Malaysia hosted the East Asian Summit in Kuala Lumpur in December 2005 as part of its efforts to transform ASEAN into a more integrated regional association.<sup>34</sup> Malaysia also promoted the drafting of the new ASEAN Charter and is one of the five members to ratify the new agreement.<sup>35</sup> In addition, Malaysia has supported efforts to form closer trade relations with nations outside of ASEAN via the "ASEAN+3" and "ASEAN+6" models. However, Malaysia's relatively small size and a lack of consensus in ASEAN to follow a Malaysian lead place limits on the extent to which Malaysia can assume a leadership role within ASEAN and the region.

## Malaysia-China Relations

The attitudes of Malaysia (and other ASEAN states) towards China have undergone a significant shift over the past two decades.<sup>36</sup> Relations with China were once characterized by much suspicion. More recently, Malaysia has viewed China as both a major competitor and a major trading partner. There are some indications that Malaysia has attempted to maintain the value of its currency, the ringgit, in line with the value of China's currency, the renminbi, to protect its competitive position in key commodity markets.

Malaysia normalized relations with China in 1974, but has maintained close economic and trade relations with Taiwan. Over 2,000 Taiwanese companies have invested in Malaysia. In 2007, while China was Malaysia's 4<sup>th</sup> largest trading partner, Taiwan was its 7<sup>th</sup> largest trading partner. Hong Kong, a special administrative region of China, was Malaysia's 8<sup>th</sup> largest trading partner in 2007.

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<sup>32</sup> S. Jayasankaran, "Well-Oiled," *Far Eastern Economic Review*, August 28, 2003.

<sup>33</sup> S. Jayasankaran, "Oil and Water," *Far Eastern Economic Review*, July 3, 2003.

<sup>34</sup> For additional information see CRS Report RL33242, *East Asia Summit (EAS): Issues for Congress*, by (name redacted).

<sup>35</sup> Singapore was the first member to ratify the new charter on December 18, 2007. Since then, Brunei, Laos, Malaysia, and Vietnam have ratified the charter. Burma (Myanmar), Cambodia, Indonesia, the Philippines, and Thailand have not ratified the new charter.

<sup>36</sup> Jane Perlez, "Asian Leaders Find China a More Cordial Neighbor," *The New York Times*, 18 October, 2003.

In recent years, issues of economic competition and cooperation have been more of a concern to ASEAN states than security concerns.<sup>37</sup> China currently is said to be thought of “as more of an opportunity with concomitant challenges, rather than as a threat” as it was as recently as 1999, when China fortified Mischief Reef in the South China Sea which it had occupied in 1994.<sup>38</sup> To assert its claims to the South China Sea, Malaysia constructed a concrete building on Investigator Shoal in the Spratlys in 1998. ASEAN states’ perceptions could change again should China more actively reassert its claims in the South China Sea or go to war over Taiwan.<sup>39</sup>

## Malaysia-Indonesia Relations

Relations between Malaysia and Indonesia have at times been tense. Among the top issues between the two nations are differences over Malaysian policies towards illegal Indonesian workers and a maritime dispute off Borneo which has implications for control of valuable energy resources. The presence of thousands of illegal Indonesian workers in Malaysia that have supposedly displaced many of Malaysia’s Indian workers may have contributed to Malaysia’s Indian population deserting UMNO and the BN in the 2008 elections.<sup>40</sup> Many undocumented Indonesians working in Malaysia were pressed to leave Malaysia in late 2004 and early 2005.<sup>41</sup> There are also allegations of the human trafficking of Indonesian women and children to Malaysia for commercial sexual exploitation.<sup>42</sup>

Malaysia also awarded an oil concession to Royal Dutch Shell in 2005 in the waters off Sabah in northeastern Borneo that are also claimed by Indonesia. The conflict escalated to the point that both nations sent naval ships to assert their claims before diplomacy eased tensions.<sup>43</sup> Malaysia agreed to participate in the monitoring of the peace treaty signed in August 2005 between Indonesia and Gerakan Aceh Merdeka (GAM) along with the international monitoring team led by the European Union.<sup>44</sup> Malaysia has also called for ASEAN states to discuss defense issues as well as foreign and economic policy.<sup>45</sup>

Illegal forest fires in Sumatra in August 2005 led Malaysia to close schools, as well as Malaysia’s largest seaport, and declare a state of emergency in Kuala Selangor and Port Kelang as smoke severely limited visibility and created a significant health risk.<sup>46</sup> The Indonesian government reportedly placed the blame for the fires on 10 logging companies, of which 8 were Malaysian-owned.<sup>47</sup> Given that illegal burning of forests in Indonesia has led to dangerous smoke pollution

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<sup>37</sup> Alice D. Ba, “China and ASEAN: Re-navigating Relations for a 21<sup>st</sup> Century Asia,” *Asia Survey*, August, 2003.

<sup>38</sup> Rommel Banlaoi, “Southeast Asian Perspectives on the Rise of China: Regional Security After 9/11,” *Parameters*, Summer, 2003.

<sup>39</sup> J. Wong and S. Chan, “China-ASEAN Free Trade Agreement,” *Asian Survey*, June, 2003.

<sup>40</sup> Vijay Joshi, “Ethnic Tensions in Malaysian Election,” *Associated Press*, March 6, 2008.

<sup>41</sup> “Crackdown on Undocumented Workers Ends ... for Now,” *Asia News*, February 2, 2005.

<sup>42</sup> For more information on human trafficking between Indonesia and Malaysia, see the U.S. State Department’s *Trafficking in Persons Report*, June 2007.

<sup>43</sup> “Malaysia at a Glance: 2005-06,” Economist Intelligence Unit, June 2005.

<sup>44</sup> “M’sia to Send Peace Monitors to Aceh,” *Bernama Daily*, August 6, 2005.

<sup>45</sup> “Malaysia Says Southeast Asian Grouping Should Tackle Defence Issues,” *Agence France Presse*, August 7, 2005.

<sup>46</sup> “Indonesian Fires Blanket Central Malaysia,” *The New York Times*, August 12, 2005.

<sup>47</sup> “Malaysia Must Prosecute Cos for Haze-Indonesia,” *Dow Jones*, August 14, 2005, and “Govt Vows to Prosecute 10 Firms Over Forest Fires,” *The Jakarta Post*, August 16, 2005.



in Malaysia before, some observers have speculated that more must be done to put in place legal frameworks to control trans-border pollution.<sup>48</sup> An estimated 70% of all logging in Indonesia is illegal.<sup>49</sup>

Badawi met with his Indonesian counterpart, President H. Susilo Bambang Yudhoyono, on January 11, 2008, in Putrajaya, Malaysia, as part of the “annual consultations” between the two countries. Their discussions focused on the land and maritime border issues, bilateral defense cooperation, Indonesian migrant workers in Malaysia, illegal logging, and bilateral economic cooperation.

## **Other Bilateral Relations**

Malaysia’s border with Thailand has been a source of friction in their bilateral relationship. Thailand’s southern provinces are Muslim majority areas where separatist violence has been increasing. Malaysia agreed to work with Thailand under a Joint Development Strategy for border areas to develop the economy and living conditions of people in the border region. Badawi has highlighted the need to address poverty as a means of alleviating the conflict in Southern Thailand.<sup>50</sup>

Malaysia’s relations with neighboring Singapore have been termed “bumpy” since Singapore’s independence in 1965. The “bumpiness” of the relationship emerges from several factors, including ethnic tensions, economic and trade interdependency, and common security concerns.<sup>51</sup> Singapore is a largely Chinese city-state with a large Malay minority; Malaysia is a largely Malay nation with a large Chinese minority. Economic conditions force Singapore to rely on Malaysia for many resources, including water and labor. At the same time, Malaysia relies on Singapore for capital investments and trade-related business opportunities, including the re-export of many Malaysian goods. Finally, both nations are reliant on the flow of shipments through the Strait of Malacca. In addition to the Five Power Defense Arrangement, Malaysia and Singapore also have established coordinated naval patrols with Indonesia to protect freight shipments in the region. According to Singapore’s minister of foreign affairs, George Yeo, the results of the 2008 elections should not affect bilateral relations.<sup>52</sup>

## **Malaysia’s Economy and Foreign Trade**

Malaysia is a relatively mature industrialized nation, whose economy relies on both domestic forces (personal consumption and private investment) and external trade for its growth and development. Following a short, severe recession in 1998 and a mild turndown in 2001,<sup>53</sup>

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<sup>48</sup> “Malaysia: Pollution Levels Close Schools,” *Asia Pacific Radio*, August 11, 2005.

<sup>49</sup> Jared Diamond, *Collapse: How Societies Choose to Fail or Succeed* (New York: Viking Publishers, 2005), p. 471.

<sup>50</sup> “Malaysia, Thailand Prepare to Accelerate Development of Border Regions,” BBC News, February 12, 2007.  
“Malaysia Pledges to Aid Thai Government in Ending Violent Unrest on Shared Border,” Global Insight, February 12, 2007.

<sup>51</sup> For an overview of Malaysia-Singapore relations, see K.S. Nathan, “Malaysia-Singapore Relations: Retrospect and Prospect,” *Contemporary Southeast Asia*, vol. 24, no. 2 (August 2002), pp. 385-410.

<sup>52</sup> “Bilateral Ties Not Affected,” *New Strait Times*, March 25, 2008.

<sup>53</sup> The 1998 recession was precipitated by the Asian Financial Crisis (see CRS Report RL30517, *Asian Financial Crisis and Recovery: Status and Implications for U.S. Interests*, by (name redacted) for details). The 2001 downturn is (continued...)

Malaysia’s real gross domestic product (GDP) has grown between 5% and 6% per year for the past five years. The current official government estimate has its real GDP increasing 6.0% in 2007 and projecting 6.0%-6.5% growth in 2008 (see **Table 1**). Malaysia’s central bank, Bank Negara Malaysia, projected 2008 GDP growth of 5.0%-6.0% two weeks after the parliamentary elections, citing “turbulent global financial markets and slowing U.S. growth” as reasons for its less optimistic forecast.<sup>54</sup>

Malaysia’s GDP and average per capita income classify it as a middle income country according to the World Bank’s system, comparable to Mexico and Russia.<sup>55</sup> At official exchange rates, the per capita income in 2007 was \$5,740, but its purchasing power parity value was estimated at \$13,289.

**Table 1. Selected Indicators for the Malaysian Economy**

	2006	2007 (est.)	2008 (proj.)
Real GDP Growth	5.9%	6.0%	6.0 - 6.5%
Nominal GDP (billion ringgits)	572.555	641.499	681.7
Nominal GDP (\$ billion)	148.940	161.843	n.a.
Nominal GDP per Capita (\$)	5,383	5,740	n.a.
GDP per Capita - purchasing power parity. <sup>a</sup> (\$)	11,663	13,289	14,206
Inflation Rate - CPI	3.6%	2.0%	2.5 - 3.0%
Inflation Rate - PPI	6.8%	6.8%	n.a.
Unemployment Rate	3.3%	3.3%	n.a.
Exports (\$ billion; fob)	160.845	176.311	188.3
Imports (\$ billion; cif)	131.223	147.065	159.1
Exchange rate (ringgits per U.S. dollar)	3.678	3.447	n.a.

**Source:** Malaysia’s Ministry of Finance; World Trade Atlas; and CRS calculations.

- a. Purchasing power parity estimates of per capita GDP attempt to revalue official GDP figures by comparing the relative costs of a select group of goods in each nation and then recalculating per capita GDP to reflect the relative purchasing power in each nation.

Since the 2001 economic downturn, Malaysia’s economic growth has relied on a combination of strong domestic demand and continued export growth. In 2007, the main sources of real GDP growth were (in order): domestic consumption, public consumption, public investment, and private investment. Because imports grew more rapidly than exports, 6.2% compared to 4.1%, external trade actually lowered economic expansion in 2007. Government forecasts project private investment will play a greater role in economic growth in 2008, surpassing both public investment and public consumption.

(...continued)

generally attributed to the global economic downturn following the attacks on the Pentagon and World Trade Center (see CRS Report RS21937, *9/11 Terrorism: Global Economic Costs*, by (name redacted) for details).

<sup>54</sup> “Bank Negara Lowers 2008 Growth Target,” *New Strait Times*, March 26, 2008.

<sup>55</sup> For a list of the World Bank’s ranking of economies by per capita income, see <http://siteresources.worldbank.org/DATASTATISTICS/Resources/GNIPC.pdf>.



Another indication of the maturation of Malaysia’s economy is its sectoral balance (see **Table 2**). While agriculture and manufacturing continue to play an important role in Malaysia’s economy, the nation’s GDP mainly comes from the service sectors. The sectoral structure of Malaysia’s economy is more akin to those of South Korea and Thailand than Indonesia, the Philippines and Vietnam.

Although agriculture provides a relatively small portion of Malaysia’s GDP, it plays an important role in the nation’s overall economy. One out of every three Malaysians live in rural areas. Approximately one out of every eight workers in Malaysia are employed in agriculture, animal husbandry, fishing, or forestry. Rice and palm oil are two crops of particular importance to Malaysia, the former for political reasons because many Malaysian farmers are reliant on rice for their livelihood and are opposed to the import of rice. The latter is important for economic reasons, as palm oil is a traditional major export crop for Malaysia.

**Table 2. Share of GDP by Sector: 2000, 2006-2008**

<b>Sector</b>	<b>2000</b>	<b>2006</b>	<b>2007 (est.)</b>	<b>2008 (proj.)</b>
Agriculture	9.4%	7.9%	7.7%	7.5%
Construction	3.6%	3.1%	3.0%	3.0%
Manufacturing	30.0%	31.1%	30.3%	29.6%
Mining	7.2%	8.8%	8.6%	8.4%
Services	54.3%	51.8%	53.2%	54.3%
Adjustments	0.0%	-2.7%	-2.8%	-2.8%

**Source:** Department of Statistics, Malaysia

Malaysia’s manufacturing sector accounts for nearly a third of the nation’s GDP, employs about 30% of its workers, and accounts for over 80% of its export earnings. It is dominated by the production of automobiles, and electrical and electronic products.

Malaysia is a regional leader in the production of automobiles, automotive components and parts. Its two major automobile manufacturers, Proton and Perodua, export their vehicles to over 40 countries, and Malaysia’s leading motorcycle manufacturer, Modenas, exports to markets around the world, including Argentina, Greece, Iran, Malta, Mauritius, Singapore, Turkey, and Vietnam. Malaysia’s automotive industry benefits from Malaysia’s tariff and non-tariff trade restrictions on the import of automobiles, motorcycles, and components and parts for automobiles and motorcycles.

The electrical and electronics (E&E) industry of Malaysia is a world-leader in the production of semiconductors and the assembly of E&E products, much of which is done under contract for leading international electronics companies. Approximately half of Malaysia’s export earnings come from the E&E industry. However, over half of Malaysia’s imports are raw materials, components, equipment, and capital goods to be used by its E&E manufacturers. As a result, the nation’s economy is somewhat dependent on the global demand for electrical and electronic products.

Malaysia’s service sector is highly diversified, providing services for both the domestic and external segments of the economy. The service sector provides over 54% of the nation’s GDP and more than half of its employment. Following the Asian financial crisis in 1997, Malaysia placed

severe restriction on foreign participation in some service sectors, including financial services. Over the last five years, Malaysia has gradually loosened those restrictions, but access to Malaysia's financial markets is still very limited to foreign companies.

Foreign trade was a major driver of Malaysia's economic growth in the past and continues to be important for its overall economic health. According to official figures, Malaysia's total trade exceeded 1 trillion ringgits for the first time in 2006. Over the last six years, Malaysia's exports increased 81.0% in value, while its imports rose by 80.2% (see **Table 3**). Malaysia runs a balance of trade surplus of about \$30 billion per year.

**Table 3. Malaysia's Exports, Imports and Merchandise Trade Balance, 2001-2007**

(billion ringgits and U.S. dollars)

<b>Year</b>	<b>Exports</b>	<b>Imports</b>	<b>Trade Balance</b>
2001	334.3 (88.2)	280.2 (73.866)	54.0 (14.336)
2002	357.4 (93.370)	303.1 (79.870)	54.3 (13.500)
2003	397.9 (100.113)	316.5 (80.093)	81.4 (20.020)
2004	480.7 (125.857)	400.1 (105.297)	80.7 (20.560)
2005	533.8 (140.979)	434.0 (114.626)	99.8 (26.353)
2006	589.0 (160.845)	480.8 (131.223)	108.2 (29.622)
2007	605.2 (176.311)	504.8 (147.065)	100.4 (29.246)

**Sources:** Ministry of Statistics, Malaysia and Global Trade Atlas.

According to Malaysia's trade statistics, the United States was and continues to be its largest export market (see **Table 4**). In 2007, 15.6% of Malaysia's exports went to the United States, down from 18.8% in 2006. With the exception of the Netherlands and the United States, all of Malaysia's top 10 export markets are in the Asia-Pacific, indicating a regional export focus.

**Table 4. Malaysia's Top 10 Export Markets**

(billion ringgits)

<b>Partner</b>	<b>2006</b>	<b>2007</b>
Total Exports	589.0	605.2
United States	110.6	94.5
Singapore	90.8	88.5
Japan	52.2	55.2
China	42.7	53.0
Thailand	31.2	30.0
Hong Kong	29.1	28.0
Netherlands	21.4	23.6

Partner	2006	2007
South Korea	21.3	23.0
Australia	16.7	20.4
India	18.8	20.2

Source: Ministry of International Trade and Industry, Malaysia.

Japan is historically the largest supplier of Malaysia’s imports, but the United States was a close second in 2006 (see **Table 5**). Outside of Germany and the United States, all of Malaysia’s leading suppliers of imports are in Asia, more evidence of its regional trade focus.

Of Malaysia’s largest trading partners, China, Japan, South Korea, and Taiwan have a bilateral merchandise trade surplus. Every other nation has a bilateral trade deficit, with the United States running the largest bilateral trade deficit. According to Malaysia’s trade figures, both Malaysia’s exports to the United States and its imports from the United States declined in 2007, by 14.6% and 9.1% respectively.

**Table 5. Malaysia’s Imports by Top 10 Trading Partners**  
(billion ringgits)

Partner	2006	2007
Total Imports	480.8	504.8
Japan	63.6	65.5
China	58.2	64.9
Singapore	56.2	58.0
United States	60.2	54.7
Taiwan	26.2	28.7
Thailand	26.3	27.0
South Korea	25.9	24.9
Germany	21.1	23.4
Indonesia	18.2	21.4
Hong Kong	12.7	14.7

Source: Ministry of International Trade and Industry, Malaysia.

## Malaysia’s Current Economic Policies

The current goals for Malaysia’s economic policies are to continue its strong economic growth, maintain full employment, reduce inflationary pressures, and lower the fiscal deficit. In addition, as part of its larger policy of *Islam Hadhari*, the government seeks to reduce poverty, improve living standards, and reduce income and wealth inequality between the nation’s various ethnic groups. In particular, there is concern about the income and wealth differential between the bumiputera and the ethnic Chinese and Indian of Malaysia.

For the period 2006 to 2010, the Malaysian government has established a set of objectives to achieve its overall economic goals as part of its Ninth Malaysia Plan.<sup>56</sup> First, it will attempt to move its production into higher value-added activities by greater investment in education. Second, Malaysia seeks to improve the quality of the Malaysian work force by promoting the values of *Islam Hadahari* and improving the quality of Malaysia's educational system. Third, the government will address persistent sources of both regional and ethnic economic inequality. Fourth, Malaysia will seek to eliminate poverty by 2010 and continue to improve living standards. Fifth, in order to facilitate the achievement of the preceding objectives, the Malaysia government will strengthen the quality of its government agencies.

The key macroeconomic policies for the Ninth Malaysia Plan emphasize continued growth by increasing the role of Malaysia's private sector and by attracting foreign direct investment (FDI), especially in higher value-added activities. In addition, the government will attempt to keep inflation under control. Also, there is the explicit objective of reducing the federal fiscal deficit from 3.8% of GDP in 2005 to 3.4% of GDP in 2010. Finally, having ended the peg of the ringgit to the U.S. dollar on July 21, 2005, Malaysia's central bank, the Bank Negara Malaysia, has officially adopted a managed float of the ringgit against several foreign currencies.<sup>57</sup> However, there is some evidence that Malaysia's de facto exchange rate policy is to maintain the value of the ringgit relatively constant when compared to the value of China's renminbi.<sup>58</sup>

Malaysia's stated foreign trade policy for the next five years will continue to support trade and investment liberalization. Malaysia had projected the value of total trade (imports plus exports) will exceed 1 trillion ringgits (\$286 billion) by 2010, but achieved that figure in 2006 and 2007. The government sees the formation of the proposed ASEAN Free Trade Area (AFTA), the trade liberalization and facilitation efforts of the Asia-Pacific Economic Cooperation (APEC), and the current efforts by the World Trade Organization (WTO) for greater liberalization of trade in goods and services as being consistent with its overall trade policy. In particular, Malaysia strongly supports ASEAN's discussions with China, Japan, and South Korea—the so-called “ASEAN+3”—about the possibility of forming an East Asian economic community. The successful conclusion of a free trade agreement with the United States would also be viewed as being consistent with its current trade policy.

## **U.S.-Malaysia Bilateral Trade**

In general, trade relations between the United States and Malaysia are dominated by the outsourcing of the production of machinery, and electronic and electrical products by multinational corporations with operations within the United States and Malaysia. This trade pattern is revealed by the cross-shipment of similarly categorized goods to and from Malaysia, as well as the sector structure of U.S. foreign direct investment (FDI) in Malaysia. From 2001 to 2006, Malaysia's exports to the United States grew substantially, regardless of which nation's trade statistics are used, but then noticeably declined in 2007 (see **Table 6**). However, U.S. exports to Malaysia have not experienced similar growth. As a result, the U.S. bilateral trade

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<sup>56</sup> For more details about the Ninth Malaysia Plan, see its webpage, <http://www.epu.jpm.my/rm9/html/overview.htm>.

<sup>57</sup> Following the Asian Financial Crisis of 1997, the value of the ringgit fell from 2.5 ringgits to US\$1, to over 4 ringgits to the US\$1. In September 1998, the Bank Negara Malaysia pegged the exchange rate at 3.5 ringgits to US\$1.

<sup>58</sup> With the exception of the spring of 2007, the value of the ringgit has stayed within 2% of the value of the renminbi since China adopted a crawling peg in July 2005.

deficit with Malaysia increased between 2001 and 2007—up \$9.2 billion according to the United States and \$5.6 billion according to Malaysia.

**Table 6. U.S.-Malaysia Bilateral Trade Flows, 2001-2006**  
(Billion dollars)

	2001	2002	2003	2004	2005	2006	2007
<b>U.S. Figures</b>							
Exports to Malaysia	9.4	10.3	10.9	10.9	10.5	12.6	11.7
% of Total Exports	1.3	1.5	1.5	1.3	1.2	1.2	1.0
Imports from Malaysia	22.3	24.0	25.4	28.2	33.7	36.5	32.8
% of Total Imports	2.0	2.1	2.0	1.9	2.0	2.0	1.7
<b>Malaysian Figures</b>							
Exports to U.S.	17.8	18.8	17.8	23.6	27.7	30.2	27.5
% of Total Exports	20.2	20.2	17.8	18.7	19.7	18.8	15.6
Imports from U.S.	11.8	13.1	12.2	15.2	14.8	16.4	15.9
% of Total Imports	16.0	16.4	15.2	14.5	12.9	12.5	10.8

Source: Global Trade Atlas

In addition, the relative importance of each other as a trading partner has declined since 2001. From Malaysia's perspective, the United States purchased 20.2% of its exports in 2001, but only 15.6 of its exports in 2007. Similarly, the United States provided Malaysia with 16.0% of its imports in 2001, but just 10.8% of its imports in 2007. For the United States, Malaysia was the supplier of 2.0% of its imports in 2001 and 1.7% in 2007, and was the buyer of 1.3% of its exports in 2001 and 1.0% of its exports in 2007.

**Table 7** lists the top by categories of goods traded between Malaysia and the United States in 2007, according to U.S. trade data. The data reveals considerable reciprocal trade in machinery (HS84), electrical machinery (HS85); over three-quarters of bilateral trade in 2007 was in these two types of commodities. Much of this cross trade was due to outward processing of electronic and electrical products in Malaysia by major U.S. companies.

**Table 7. Top Five U.S. Exports to and Imports from Malaysia, 2007**  
(in million dollars)

Exports		Imports	
Commodity	Value	Commodity	Value
Electrical Machinery (85)	6,320.6	Machinery (84)	14,500.4
Machinery (84)	1,709.7	Electrical Machinery (85)	10,941.4
Optical & Medical Instruments (90)	691.4	Optical & Medical Instruments (90)	957.0
Iron & Steel	411.7	Rubber (40)	839.5
Aircraft (98)	320.2	Furniture & Bedding	829.7

In the bilateral exchange of machinery in 2007, the United States and Malaysia were shipping back and forth mostly computers and related equipment (HS8471) and parts and accessories for office equipment (HS8473). In the exchange of electronics and electrical products, the United States exports were mostly integrated circuits and microassemblies (HS8542) and its imports were primarily telephones and telephone parts (HS8517), as well as a significant amount of integrated circuits and microassemblies (HS8542).

Since 2000, the United States has consistently been among the leading sources of foreign direct investment (FDI) in Malaysia, along with Hong Kong, Japan, and Singapore. In 2007, the United States invested 3.0 billion ringgits (\$870 million) in Malaysia, which was 17.3% of Malaysia's total inward FDI for the year.<sup>59</sup> The United States was Malaysia's fourth largest source of FDI in 2007, after (in order): Japan (6.5 billion ringgits), Germany (3.7 billion ringgits), and Iran (3.1 billion ringgits). The cumulative value of U.S. FDI in Malaysia is over \$20 billion, with much of it being invested in electronics and electrical manufacturing, as well as the petrochemical industry.

## Malaysia and U.S. Trade Relations

Malaysia and the United States currently hold similar positions on international trade relations in general, but occasionally differ on specific issues. Both nations support the general concept of trade and investment liberalization and facilitation. Also, both are actively pursuing trade and investment liberalization via multilateral and bilateral fora. However, on specific issues, there are differences between the United States and Malaysia on the goals and means of obtaining those goals. As a result, the two nations sometimes share the same view on trade issues, and sometimes have different, and even, opposing views.

Since Malaysia and the United States are members of the World Trade Organization (WTO), there is a shared "baseline" for their bilateral trade relations. For example, both nations grant the other nation "normal trade relations," or NTR, status as required under the WTO. Also, since Malaysia and the United States are both members of the Asia-Pacific Economic Cooperation (APEC), they are both committed to APEC's Bogor Goals of open trade and investment in Asia by 2020.<sup>60</sup> In addition, the United States and Malaysia concluded a trade and investment framework agreement (TIFA) in May 2004, are currently negotiating a free trade agreement (FTA), and are parties to various regional trade associations that are considering multilateral trade and investment agreements.

### U.S.-Malaysia FTA

On March 8, 2006, the United States and Malaysia announced they would begin negotiating a bilateral free trade agreement (FTA).<sup>61</sup> The announcement was made by ex-U.S. Trade

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<sup>59</sup> Source of FDI data: Malaysian Industrial Development Authority, or MIDA <http://www.mida.gov.my/>.

<sup>60</sup> For more information about APEC and its Bogor Goals, see CRS Report RL31038, *Asia Pacific Economic Cooperation (APEC) and the 2007 Meetings in Sydney, Australia*, by (name redacted).

<sup>61</sup> "United States, Malaysia Announce Intention to Negotiate Free Trade Agreement," U.S. Trade Representative's website: [http://www.ustr.gov/Document\\_Library/Press\\_Releases/2006/March/United\\_States,\\_Malaysia\\_Announce\\_Intention\\_to\\_Negotiate\\_Free\\_Trade\\_Agreement.html](http://www.ustr.gov/Document_Library/Press_Releases/2006/March/United_States,_Malaysia_Announce_Intention_to_Negotiate_Free_Trade_Agreement.html).



Representative Rob Portman and Malaysia's then-Minister of International Trade and Industry Rafidah Aziz on Capitol Hill with a bipartisan group of Members of Congress in attendance. The stated goals for the proposed FTA were to remove tariff and non-tariff trade barriers, and expand bilateral trade.

Since the announcement, The United States and Malaysia have held six rounds of negotiations concerning the terms of the proposed FTA.<sup>62</sup> The sixth round of talks were held in Kuala Lumpur on January 14-17, 2008.<sup>63</sup> Among the outstanding issues in the negotiations are: (1) market access for U.S. exports to Malaysia of agricultural goods, automobiles, and automotive parts and components; (2) market access for Malaysian exports to the United States of agricultural goods; (3) market access for U.S. services, especially financial services, in Malaysia; (4) Malaysia's enforcement of intellectual property rights (IPR) protection; and (5) Malaysia's government procurement system and its preferential treatment for businesses owned and operated by ethnic Malays, or *bumiputera*.

Conditions for the fifth round of talks (held in Malaysia on February 5-8, 2007) were complicated at the end of January with the news of a \$16 billion energy development deal between Malaysia's SKS Group and the National Iranian Oil Company that would develop Iranian gas fields and build liquefied natural gas plants.<sup>64</sup> Over the last six years, trade between Iran and Malaysia has grown rapidly. According to Malaysia's Department of Statistics, total trade between Malaysia and Iran rose from \$224 million in 2000 to over \$1.045 billion in 2007. In addition, Iran was Malaysia's third largest source of inward FDI in 2007 (see above).

During a House Committee on Foreign Affairs Hearing on January 31, 2007, then-Chairman Tom Lantos called the deal "abhorrent," and sent a letter to U.S. Trade Representative Susan Schwab requesting the suspension of negotiations on the proposed FTA until Malaysia renounced the deal with Iran.<sup>65</sup> U.S. Trade Representative Schwab indicated that she intended to continue the negotiations with Malaysia.<sup>66</sup>

Malaysia sharply rejected the call to revoke the energy deal with Iran. Aziz reportedly stated that the United States has no right to block Malaysia trading with any country, even after the conclusion of the proposed FTA.<sup>67</sup> Badawi also was firm on the issue, "We reject the pressure being inflicted upon us.... Do not bring any political matters into trade."<sup>68</sup> In an official statement on February 6, MITI repeated Malaysia's objections to Representative Lantos' comments, stating:

The call by Tom Lantos to suspend the free trade agreement negotiations because of a business deal by a Malaysian company with the National Iranian Oil company does not augur well for the negotiations.... Malaysia reiterates that the FTA negotiations cannot be

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<sup>62</sup> For details about the proposed FTA and its negotiation, see CRS Report RL33445, *The Proposed U.S.-Malaysia Free Trade Agreement*, by (name redacted).

<sup>63</sup> An informal round of talks were held in Washington, DC on April 13, 2007.

<sup>64</sup> "Malaysia Stands by Iranian Gas Deal," *BBC News*, February 2, 2007.

<sup>65</sup> "Remarks by Congressman Tom Lantos, Chairman, House Committee on Foreign Affairs, at Hearing, 'Understanding the Iran Crisis,'" January 31, 2007.

<sup>66</sup> Reported in *Washington Trade Daily*, February 5, 2007.

<sup>67</sup> "Malaysia Defends State Despite U.S. Threat to Halt FTA Talks," *Bernama - Malaysian National News Agency*, February 2, 2007.

<sup>68</sup> "Malaysia Stands by Iranian Gas Deal," *BBC News*, February 2, 2007.



held hostage to any political demand, and cannot be conducted under such threats. Malaysia is also ready to suspend negotiations if the situation warrants it.<sup>69</sup>

Further complicating the negotiations was the passing of the April 2, 2007 deadline for consideration under Trade Promotion Authority.<sup>70</sup> Because President Bush did not notify Congress by the deadline, there are several scenarios under which Congress could consider the implementation bill for the proposed U.S.-Malaysia FTA.<sup>71</sup>

## **U.S.-Malaysia TIFA**

On May 10, 2004, Malaysia and the United States signed a bilateral trade and investment framework agreement.<sup>72</sup> The U.S.-Malaysia TIFA states that both parties desire to develop trade and investment between the two countries, ensure that trade and environmental policies are supportive of sustainable development, and strengthen private sector contacts. To achieve these goals, the TIFA established a Joint Council on Trade and Investment, jointly chaired by Malaysia's Minister of International Trade and Industry and the U.S. Trade Representative, that is to meet at least once a year for the purpose of implementing the TIFA.

The U.S.-Malaysia TIFA also set out a two-part work program. The first part committed both nations to consultation on trade and investment liberalization and facilitation, with explicit consideration to trade in services, information and communications technology, biotechnology, and tourism. The second part stipulated that the United States and Malaysia will "examine the most effective means of reducing trade and investment barriers between them, including examination and consultations on the elements of a possible free trade agreement."

## **World Trade Organization (WTO)**

Both the United States and Malaysia have been members of the World Trade Organization, or WTO, since its creation on January 1, 1995. While the United States is generally seen as being a consistent supporter of trade and investment liberalization, Malaysia's trade policy has undergone significant changes over the last 12 years. However, under the Bawadi Administration, Malaysia has generally been supportive of trade and investment liberalization.

For the current Doha Round, the United States and Malaysia are in general agreement on the overall goals of the talks, but have differed on some of the specifics. In particular, Malaysia joined its fellow ASEAN members in pushing the United States and the European Union to improve their market access offers for agricultural goods, including "making substantial reductions in trade distorting domestic support by the major players."<sup>73</sup>

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<sup>69</sup> "Statement by the Ministry of International Trade and Industry on US Congressman Tom Lantos Request to Suspend Malaysia-US FTA Negotiations," February 6, 2007.

<sup>70</sup> For a more detailed discussion of Trade Promotion Authority, see CRS Report RL33743, *Trade Promotion Authority (TPA): Issues, Options, and Prospects for Renewal*, by (name redacted) and (name redacted).

<sup>71</sup> For a discussion of those scenarios, see CRS Report RL33445, *The Proposed U.S.-Malaysia Free Trade Agreement*, by (name redacted).

<sup>72</sup> The full text of the TIFA is available at the U.S. Trade Representative's website at [http://www.ustr.gov/assets/Trade\\_Agreements/TIFA/asset\\_upload\\_file922\\_10023.pdf](http://www.ustr.gov/assets/Trade_Agreements/TIFA/asset_upload_file922_10023.pdf).

<sup>73</sup> "Statement on the Doha Development Agenda of the WTO," January 13, 2007.

## Asia-Pacific Economic Cooperation (APEC)

The Asia-Pacific Economic Cooperation (APEC) group is another multilateral forum where the United States and Malaysia are both founding members. While Malaysia and the United States accept APEC's Bogor Goals for trade and investment liberalization by 2020, as well as APEC's "open regionalism" approach, there have been some differences of opinion on the future of APEC.<sup>74</sup> During the 2006 APEC meetings, The United States proposed the transformation of APEC into a Free Trade Area of the Asia-Pacific, or FTAAP. This proposal received a mixed response from other APEC members. Many observers believe that Malaysia prefers the formation of an all-Asian free trade area that would exclude the United States (see below).

## Association of Southeast Asian Nations (ASEAN)

During its January 2007 summit in Cebu, ASEAN invited Australia, India, Japan, New Zealand, the People's Republic of China, and South Korea—the so-called "ASEAN+6"—to attend as part of the second East Asia Summit (EAS). The first EAS was held in Kuala Lumpur in December 2005.<sup>75</sup> ASEAN has also held talks about greater regional cooperation with just Japan, China, and South Korea—the ASEAN+3. ASEAN+3 met after ASEAN's last summit in Singapore in November 2007. Malaysia is a founding member of the Association of Southeast Asian Nations (ASEAN). ASEAN currently has 10 members; the United States is not a member.<sup>76</sup> East Timor has applied to become ASEAN member.

Malaysia is widely seen as a major supporter of the formation of an all-Asian free trade area that would exclude the United States. To some observers, Malaysia's support for the EAS is a continuation of Mahatir's East Asian Economic Caucus and its predecessor, the East Asian Economic Group. According to one source, the goal of forming an all-Asian free trade area was endorsed after the second EAS by China after overcoming its reluctance to include Australia and India.<sup>77</sup> An attempt to forge a similar agreement during the 2005 East Asia Summit was unsuccessful.

The possible creation of an all-Asian free trade area is seen by some observers as a response to the growing influence of the European Union and the United States in international trade relations. For the United States, the proposed all-Asian free trade area is a rival model to its proposed FTAAP.

Malaysia is one of the five members of ASEAN that have ratified the new ASEAN Charter.<sup>78</sup> One of the main outcomes of the November summit in Singapore was the signing of a new charter on November 20, 2007. To be officially adopted, the new charter must be ratified by all 10 members of ASEAN. Even before the charter was signed, the Philippines indicated that it was unlikely to

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<sup>74</sup> For more information on APEC, see CRS Report RL31038, *Asia Pacific Economic Cooperation (APEC) and the 2007 Meetings in Sydney, Australia*, by (name redacted).

<sup>75</sup> For more information about the first EAS Summit, see CRS Report RL33242, *East Asia Summit (EAS): Issues for Congress*, by (name redacted).

<sup>76</sup> The current ASEAN members are: Brunei Darussalam, Cambodia, Indonesia, Laos, Malaysia, Myanmar (Burma), Philippines, Singapore, Thailand, and Vietnam.

<sup>77</sup> "Asian Leaders Plan Free-Trade Area from India to New Zealand," by Arijit Ghosh and Francisco Alcuaz, Jr. *Bloomberg*, January 15, 2007.

<sup>78</sup> The other four members to have ratified the new charter are Brunei, Laos, Singapore, and Vietnam.

ratify the charter unless Burma (Myanmar) upheld the document's provisions on democracy and human rights.

Among its key provisions, the new charter commits the organization to its transformation into a regional economic community similar to the European Union by 2015. Included in its provisions are a collective commitment to the creation of an ASEAN Community "in which there is free flow of goods, services and investment; facilitated movement of business persons, professionals, talents and labour; and freer flow of capital." However, the charter also contains an "ASEAN minus X" provision that effectively allows any ASEAN member to opt out of economic commitments if it so chooses. It is unclear at this time how the creation of an ASEAN Community will affect U.S. policies in Southeast Asia.

## Other Aspects of U.S.-Malaysia Relations

Bilateral relations between the United States and Malaysia are viewed as having improved since Badawi came to power. In the past, the relationship suffered from what a U.S. official called "blunt and intemperate public remarks"<sup>79</sup> critical of the United States by former Prime Minister Mahathir, who generally subscribed to a view of the United States as a neo-colonial power strongly under the influence of a coterie of Zionist Jews.<sup>80</sup> However, Mahathir's strong expression of sympathy and support following the attacks on September 11, 2001, apparently led to a thawing of a previously cool relationship that culminated with an official state visit to the White House by Mahathir in May 2002.<sup>81</sup> The more cordial relationship between Malaysia and the United States has seemingly continued into the Badawi administration.

However, there are aspects of U.S.-Malaysia relations that periodically raise tensions between the two nations. In particular, Malaysia was and continues to be opposed to the U.S.-led invasion of Iraq, and frequently critiques the U.S. approach to counterterrorism as lacking balance. In addition, the United States has expressed misgivings about Malaysia's relationships with certain nations (in particular, Iran and Sudan) and continues to include Malaysia in the State Department's annual *Country Reports on Human Rights Practices*.

Prime Minister Badawi met with President Bush at the White House on July 19, 2004, during a three-day visit to the United States.<sup>82</sup> Badawi's visit sought to further strengthen the bilateral relationship between Malaysia and the United States following this important transfer of political leadership.<sup>83</sup> Malaysian Foreign Minister Syed Hamid Albar reportedly stated that Badawi would "exchange views on how we can deal with Islamic issues, how we can avoid the perception of prejudice, [and the] perception of marginalization of Muslims."<sup>84</sup> Badawi has also focused on

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<sup>79</sup> Prepared Statement of Matthew Daley, Deputy Assistant Secretary, Bureau of East Asian and Pacific Affairs, U.S. Department of State, As submitted to the Committee on International Relations House of Representatives, Subcommittee on Asia and the Pacific, March 26, 2003.

<sup>80</sup> Alan Sipress, "Malaysia Calls on Muslims to resist Jewish Influence," *Washington Post*, October 17, 2003.

<sup>81</sup> Pamela Sodhy, "U.S.-Malaysian Relations during the Bush Administration: The Political, Economic, and Security Aspects," *Contemporary Southeast Asia*, vol. 25, no. 3 (2003), pp. 363-86.

<sup>82</sup> The two heads of state have met on other occasions, but the 2004 visit has been the only official state visit to the White House.

<sup>83</sup> Malaysian Prime Minister to Meet with U.S. President 19 July," *BBC Monitoring Asia Pacific*, July 6, 2004.

<sup>84</sup> "Malaysian Leader to Tell Bush Terrorism Has Increased," *Associated Press*, July 9, 2004.

strengthening already strong bilateral trade and investment ties between the United States and Malaysia.<sup>85</sup>

During his 2004 visit to Washington, Prime Minister Abdullah Badawi and President Bush reportedly discussed the need to move the bilateral relationship forward and rebuild confidence. Prime Minister Badawi reportedly told the president that “we need to find the moderate center, we must not be driven by extremist impulses or extremist elements ... we need to bridge the great divide that has been created between the Muslim world and the West.”<sup>86</sup> During Badawi’s visit, President Bush expressed his opinion that “the United States and Malaysia enjoy strong bilateral ties, ranging from trade and investment relationships to defense partnerships and active cooperation in the global war on terrorism. As a moderate Muslim nation, Malaysia offers the world an example of a modern, prosperous, multi-racial, and multi-religious society.”<sup>87</sup>

## **U.S. Invasion of Iraq**

Even before the invasion began, Malaysia was a vocal critic of a possible U.S.-led war against Saddam Hussain’s government in Iraq. At an Extraordinary Islamic Summit Session of the OIC held in Doha on March 5, 2003—two weeks before the war began—then-Prime Minister Mahathir stated Malaysia’s opposition to war against Iraq.<sup>88</sup> In his speech to UMNO’s 54<sup>th</sup> General Assembly on June 19, 2003, Mahathir said, “The hunt for the terrorists has made the world tense and unsafe. Bombs explode in many parts of the world. Afghanistan and Iraq were attacked and Syria and Iran were similarly threatened unless they changed their governments.”<sup>89</sup>

Malaysia’s opposition to the Iraq war and the continued U.S. presence in Iraq continued after Badawi became prime minister. In a speech at the Oxford Centre for Islamic Studies in January 2004, Badawi said, “The world must never forget that Iraq was illegally invaded. The world was told before the fact that the invasion was necessary because of an imminent threat posed by weapons of mass destruction. We know today that this reason was baseless.”<sup>90</sup> During an UMNO party meeting in September 2004, Badawi reportedly said that Western countries had fueled international terrorism through the invasion of Iraq and their pro-Israel stance on the conflict between Israel and the Palestinians.<sup>91</sup> Later on that same month, in his speech before the United Nations General Assembly, Badawi stated, “Malaysia is convinced that the fight against terrorism cannot succeed through force of arms alone.”<sup>92</sup> He went on to denounce “the increasing tendency to attribute linkages between international terrorism and Islam.”<sup>93</sup> Badawi also indicated that he

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<sup>85</sup> “Abdullah’s Leadership Style Gets Positive Response From Leaders,” *Bernama Daily*, July 9, 2004.

<sup>86</sup> Speech by The Honourable Abdullah Ahmad Badawi, Prime Minister of Malaysia, Dinner Hosted by the U.S.-ASEAN Business Council, Washington, DC July 19, 2004.

<sup>87</sup> President Bush, *Written Remarks to the U.S. ASEAN Business Council Dinner Honoring Prime Minister Badawi*, July 19, 2004.

<sup>88</sup> Speech by Prime Minister Mahathir, Extraordinary Islamic Summit Session of the OIC, March 5, 2003.

<sup>89</sup> Speech by Prime Minister Mahathir, 54<sup>th</sup> UMNO National Assembly, June 19, 2003.

<sup>90</sup> Speech by Prime Minister Badawi, Oxford Centre for Islamic Studies, January 20, 2004.

<sup>91</sup> “Malaysia Accuses West of Fueling Terrorism,” AFP, September 23, 2004.

<sup>92</sup> Address of Prime Minister Badawi, United Nations General Assembly, September 27, 2004.

<sup>93</sup> *Ibid.*

believed that the United Nations should be “given the lead role” in returning Iraq to a peaceful, stable nation.<sup>94</sup>

Although the rhetoric has changed in tone and tenor over the last four years, Malaysia opposition to the U.S. military presence in Iraq remains strong, and its disagreement with U.S. approach to terrorism continues. On January 15, 2008, Badawi stated:

The fundamental point I am making is that religion in general, and the teachings of Islam in particular, cannot be faulted as either the reason for economic deprivation in the Muslim world or the source of the discord which persists between the Muslim world and the West. The problems which continue to fester in Afghanistan, Iraq, the Golan Heights, Lebanon and Palestine are vestiges of the projections of power by the centres of world power. The resulting humiliation being felt by Muslims is the real cause of their loss of trust and confidence towards the West.<sup>95</sup>

## Counterterrorism

Though Malaysia opposed the U.S.-led invasion of Iraq, the United States considers Malaysia a valuable ally in the war against militant Islam in Southeast Asia. Southeast Asian Islamic populations in Brunei, Indonesia, and Malaysia (and to a lesser extent in Burma, the Philippines, Singapore, and Thailand) constitute a third of the world’s Islamic population and are experiencing a spiritual, social, and cultural revival at a time when there is also increased radicalization among some groups in the region as demonstrated by the terrorist group Jemaah Islamiya (JI) and Abu Sayyaf.<sup>96</sup>

Malaysia reportedly estimated that there were 465 members of JI in Malaysia in 2003.<sup>97</sup> Malaysia has detained over 110 suspected terrorists since May 2001.<sup>98</sup> The Malaysian government believes that it has effectively crippled the Kumpulan Mujahedin Malaysia (KMM), which is thought to have had close ties with the Jemaah Islamiya (JI) terrorist group. The KMM sought the overthrow of the Malaysian government and the establishment of an Islamic state over Malaysia, Indonesia and Muslim parts of Southern Thailand and Southern Philippines. Two of JI’s leaders, Noordin Mohammad Top and Azahari Husin, the later now captured, are Malaysian, though Top is thought to be a fugitive in Indonesia.<sup>99</sup>

The increasingly perceived comity of interests after September 11, 2001, improved the bilateral relationship. Foreign Minister Syed Hamid Albar stated in January of 2001 that Malaysia was looking forward to closer ties with the United States when President Bush assumed office.<sup>100</sup> The

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<sup>94</sup> Ibid.

<sup>95</sup> Statement by the Honourable Abdullah Ahmad Badawi Prime Minister of Malaysia on the Occasion of the First Alliance of Civilizations Annual Forum, January 15, 2008.

<sup>96</sup> S. MacDonald and J. Lemco, “Political Islam in Southeast Asia,” *Current History*, November, 2002. For additional information, see CRS Report RL31672, *Terrorism in Southeast Asia*, by (name redacted) et al.

<sup>97</sup> Bridget Welsh, “Malaysia: Security Begins at Home,” in David Wiencek and William Carpenter, *Asian Security Handbook: Terrorism and the New Security Environment*, (Armonk: M.E. Sharpe, 2005).

<sup>98</sup> Country Reports on Terrorism, 2005, United States Department of State, Released April 2006 and J. Chao, “Malaysia’s War on Terror Worries Rights Advocates,” *American Statesman*, November 10, 2002.

<sup>99</sup> Country Reports on Terrorism, 2005, United States Department of State, Released April 2006.

<sup>100</sup> “Looking Forward to Warmer Ties in Post-Clinton Era,” *New Straits Times*, January 10, 2001.



September 11, 2001 attacks against the United States were strongly criticized by former Prime Minister Mahathir, and the two nations subsequently began to work closely on counter-terror cooperation. Mahathir met with President Bush in Washington in May 2002, where they signed a memorandum of understanding on counterterrorism. Some Malaysian officials have, in general terms, equated the ISA with the USA Patriot Act. It has been argued that U.S. criticism of the ISA became muted following the passage of the USA Patriot Act.<sup>101</sup>

In May of 2002, the United States and Malaysia signed a declaration that provides a framework for counterterrorism cooperation.<sup>102</sup> Malaysia has taken a leading regional role in the war against terror by establishing a regional counterterrorism center in Kuala Lumpur that facilitates access to counterterror technology, information and training.<sup>103</sup> The concept for the center was announced in October 2002 following a meeting between President Bush and then-Deputy Prime Minister Badawi at the APEC meetings in Mexico.<sup>104</sup> Malaysia hosted the ASEAN Regional Forum Inter-Sessional Meeting on Counter-Terrorism in March of 2003.<sup>105</sup>

U.S. Coordinator for Counter-terrorism Ambassador Cofer Black emphasized the need to develop “sustained international political will and effective capacity building” to more effectively fight terrorism.<sup>106</sup> Within this context Ambassador Black made special reference to Malaysia’s contribution to the war against terror in Asia. He identified Malaysia’s opening of the Southeast Asia Regional Center for Counter-terrorism in August 2003 as a key example of counterterrorism capacity building in Asia. Other observers have questioned the degree to which the center has established its effectiveness. Since becoming Prime Minister, Badawi has continued Malaysia’s commitment to fight terrorism.<sup>107</sup> While attending a regional counter-terror conference in Bali, Indonesia in February 2004, then-U.S. Attorney General Ashcroft reportedly stated that the United States is very satisfied with the role that Malaysia has played in fighting terrorism and that Malaysia has provided a good example to countries in the region.<sup>108</sup>

However, during an address to a regional defense conference in Singapore in June 2004, Malaysian Defense Minister Najib Tun Razak admonished the West when he stated, “Let there be no doubt, there is more (terrorism) to come if we continue to ignore the need for a balanced approach to this campaign against terror... We are concerned that powerful states may not be going about this campaign in ways that will win the hearts and minds of millions of ordinary people worldwide.”<sup>109</sup> Some observers view this exchange as highlighting differences in regional Southeast Asian states’ desires to include more “soft power” approaches to the war against terror as opposed to what they feel is an over reliance on “hard power” by the United States.

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<sup>101</sup> Sodhy, op. cit.

<sup>102</sup> “Malaysia, USA Sign Anti-terror Declaration,” *BBC Monitoring Service*, May 15, 2002.

<sup>103</sup> R. Hamsawi, “Local Funding for Anti-Terror Center,” *New Straits Times*, April 3, 2003.

<sup>104</sup> “Malaysia: Minister Gives Details of ASEAN Anti-terror Centre Project,” *BBC Monitoring Service*, April 2, 2003.

<sup>105</sup> See CRS Report RL31672, *Terrorism in Southeast Asia*, for further information on terrorism in Southeast Asia.

<sup>106</sup> United States Department of State, *Patterns of Global Terrorism, 2003*, April, 2004.

<sup>107</sup> “Malaysia Pledges Terror Fight,” *The Wall Street Journal*, November 4, 2003.

<sup>108</sup> “U.S. Compliments Malaysia for Role in Anti-terrorism Efforts,” *Bernama Daily*, February 5, 2004.

<sup>109</sup> “Malaysia Says U.S. Needs to be More Balanced in Its War Against Terrorism,” *International Customwire*, June 6, 2004.

## Military Cooperation

Military cooperation between the United States and Malaysia includes high-level defense visits, training exchanges, military equipment sales, expert exchanges and combined exercises. The 2007 Congressional Budget Justification for Foreign Operations states that “exposure to U.S. ideals promotes respect for human rights.” It goes on to state that “the Malaysian military has not been involved in systemic violations of human rights.”

In mid-2005, Deputy Secretary of State Zoellick and Malaysian Deputy Prime Minister Najib witnessed the renewal of an Acquisition and Cross Servicing Agreement that provides a framework for bilateral military cooperation.<sup>110</sup> Malaysian officers train in the United States under the International Military Education and Training (IMET) program and there is a student exchange program between the Malaysian Armed Forces Staff College and the U.S. Army Staff College at Fort Leavenworth. United States troops also travel to the Malaysian Army’s Jungle Warfare Training Center in Pulada. Humanitarian assistance, disaster relief, anti-piracy, and counterterrorism are areas that have been identified as areas of mutual interest. Between 15 and 20 U.S. Navy ships visit Malaysia annually. Bilateral military exercises include all branches of the service.<sup>111</sup> Malaysia has also bought significant military equipment from the United States, including F-18/D aircraft. Recent military procurement is reportedly seeking to narrow the technology gap with small, but well armed, Singapore.<sup>112</sup> Such purchases will also likely help Malaysia secure its maritime interests in the Strait of Malacca and the South China Sea.

United States warships and U.S. military personnel go to Malaysia to participate in joint Cooperation Afloat Readiness and Training exercises with Malaysia in the South China Sea. The exercise is aimed at bolstering bilateral military ties and improving the ability of the United States Navy to operate in regional waters.<sup>113</sup> In an address in Malaysia in June 2004, Admiral Fargo pointed to shared concerns over “transnational problems,” including “terrorism and proliferation, trafficking in humans and drugs and piracy” and emphasized that “we have tremendous respect for sovereignty.”<sup>114</sup> The United States has sent Coast Guard officers to the Marine Patrol training Center in Johor Baharu to help train Malaysian officers in maritime enforcement. Malaysia established a Maritime Enforcement Agency in 2005 to increase maritime patrols.<sup>115</sup> Over 50,000 ships a year pass through the Straits of Malacca. Some ships have been vulnerable to piracy in the 600 mile long strait. There is also concern that terrorists could seek to mount an attack against shipping in the strategically vital strait.<sup>116</sup>

After some apparent miscommunication, Malaysia and the United States reportedly have come to a mutual understanding on how best to secure the Straits of Malacca, which are territorial waters from possible terrorist acts.<sup>117</sup> An estimated 30% of world trade and half of the world’s oil transits

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<sup>110</sup> “Malaysia’s Efforts Against Terror,” *Bernama*, June 8, 2005.

<sup>111</sup> Huhtala, April 14, 2003.

<sup>112</sup> S. Jayasankaran, “Malaysia: Call for Arms,” *Far Eastern Economic Review*, May 16, 2003.

<sup>113</sup> “U.S. Navy Task Force to Head for RP,” *Manila Times*, July 14, 2004.

<sup>114</sup> Admiral Thomas Fargo, Commander, U.S. Pacific Command, Malaysia Media Roundtable, June 23, 2004.

<sup>115</sup> “24 Hour Surveillance for the Malacca Strait,” *Bernama*, March 11, 2005.

<sup>116</sup> “Malaysia to Beef Up Malacca Patrols,” *Agence France Presse*, February 6, 2007.

<sup>117</sup> For a discussion of threats to shipping in the strait and regional responses see Bronson Percival, *Indonesia and the United States: Shared Interest in Maritime Security*, U.S.-Indonesia Society, June 2005.



through the Straits of Malacca.<sup>118</sup> Testifying before the House Armed Services Committee on March 31, 2004, Admiral Thomas Fargo, Commander of the U.S. Pacific Command, identified the Straits of Malacca off Malaysia's coast as an area where there is concern that international terrorists might seek to attack shipping or seize a ship to use as a weapon. Fargo also reportedly suggested the idea that U.S. counterterrorism forces be positioned in the area to be able to deal with such a threat. This idea reportedly was announced without prior consultation with Malaysia, which reportedly responded "coolly" to the suggestion.<sup>119</sup> Malaysia reportedly prefers an arrangement, in the words of Defense Minister Najib, where "the actual interdiction will be done by the littoral states."<sup>120</sup> This approach was subsequently supported by Fargo during a visit to Malaysia, where he reportedly stated that U.S. cooperation would focus on intelligence sharing and capacity building to assist regional states in addressing the potential threat.<sup>121</sup> On July 20, 2004, Malaysia, Indonesia, and Singapore began coordinated naval patrols of the Straits of Malacca.<sup>122</sup>

## Human Rights

The State Department report on human rights practices in Malaysia stated that the Malaysian government "generally respected the human rights of its citizens; however, there were problems in some areas."<sup>123</sup> Among the problems remaining are: abridgement of citizens' right to change their government, detentions of persons without trial, restrictions on freedom of the press, restrictions on freedom of assembly and association, ethnic discrimination, and incomplete investigation of detainee deaths. The report also mentioned that "the civilian authorities generally maintained effective control of the security forces."<sup>124</sup>

## Relations with Sudan

Although official bilateral trade in 2007 was small (less than \$53 million in exports and only \$42 million in imports), Prime Minister Badawi has publically stated that Malaysia hopes to increase trade and investment relations with Sudan. Malaysia already plays an important role in Sudan's trade with other nations. Malaysian companies—along with companies from China, France, India, Kuwait, and the United Kingdom—are reportedly major investors in Sudan's petroleum industry. In 2005, the Sudanese government received \$2.3 billion in revenues from petroleum exports.<sup>125</sup> The Malaysian newspaper, *The New Straits Times*, reports that Malaysia is the second largest investor in Sudan, after China.<sup>126</sup> Malaysian companies reportedly provide substantial

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<sup>118</sup> "Malaysia Accepts U.S. Aid, But Not Patrol, In Strait," *International Herald Tribune*, June 22, 2004 and Prime Minister of Singapore Lee Hsien Loong, "Engaging a New Asia," Washington, July 12, 2005.

<sup>119</sup> "Indonesia, Malaysia Give Cool Response to Suggestion of U.S. Troops in Malacca Strait," *Voice of America Press Release*, April 7, 2004.

<sup>120</sup> "Malaysia, United States to Discuss Security in the Straits of Malacca," *International Custom Wire*, June 6, 2004.

<sup>121</sup> See "U.S. to Render Assistance to Littoral States of Malacca Strait," *International Customwire*, June 23, 2004 and "U.S. Navy Task Force to Head for RP," *Manila Times*, July 14, 2004.

<sup>122</sup> "Indonesia: Three Nations Patrol Straits," *Stratfor*, July 20, 2004.

<sup>123</sup> U.S. Department of State, *Country Reports on Human Rights Practices - 2007*.

<sup>124</sup> *Ibid.*

<sup>125</sup> "Divestment Campaign Targeting Sudan over Darfur Goes Global," *Associated Press*, May 1, 2007.

<sup>126</sup> "Malaysia to Help Sudan with More Investments," *The New Straits Times*, April 17, 2007.

construction and transportation services to Sudan's oil industry. Petronas, Malaysia's state oil company, has interests in nine oil fields in Sudan, plus a refinery project on Port Sudan.<sup>127</sup>

Malaysia is the current chair of the Organization of the Islamic Conference (OIC); Sudan is also a member. During an April 2007 trip to Sudan, Prime Minister Badawi expressed some support for its fellow OIC member, saying the situation in Darfur was being exaggerated by the media.<sup>128</sup> In addition, Malaysia would "approach the leaders of the Organization of the Islamic Conference and Islamic Development Bank to extend whatever help that can be given to the government of Sudan."<sup>129</sup>

Malaysia also opposes proposed U.N. sanctions on Sudan. In the opinion of Prime Minister Badawi, the sanctions would hurt the people of Malaysia.<sup>130</sup> Instead, Malaysia prefers to allow more time for talks between the United Nations and Sudan. The United States has so far held off on unilateral sanctions on Sudan to give the United Nations time to convince Sudan to permit U.N. peacekeepers into Darfur. However, during Prime Minister Badawi's visit to Sudan, Sudan's President Omer Hassan Ahmed Al-Bashir told reporters he hoped Malaysia would help Sudan "confront Western pressure to accept international forces in Darfur."<sup>131</sup>

## **U.S. Assistance**

U.S. assistance to Malaysia is relatively modest in size, and has been declining in value over the last four years. United States foreign assistance to Malaysia has included International Military Education and Training (IMET), Non-Proliferation Anti-Terrorist Demining and Related Programs (NADR), Anti-Terrorism Assistance (ATA), and Export Control and Related Border Security Assistance (EXBS). For FY2009, the Bush Administration has requested funding for International Narcotics Control and Law Enforcement.

IMET programs with Malaysia seek to contribute to regional stability by strengthening military-to-military ties and familiarizing the Malaysian military with U.S. military doctrine, equipment, and management that promotes interoperability. The U.S. is a leading training partner with Malaysia at its Southeast Asia Regional Counter-terrorism Center.

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<sup>127</sup> "Malaysia PM Visits Darfur, Seeks Firmer Sudan Ties," *Reuters*, April 18, 2007.

<sup>128</sup> "No Sanctions on Sudan: Malaysia," *Bernama*, April 17, 2007.

<sup>129</sup> "Malaysia PM Visits Darfur, Seeks Firmer Sudan Ties," *Reuters*, April 18, 2007.

<sup>130</sup> "No Sanctions on Sudan: Malaysia," *Bernama*, April 17, 2007.

<sup>131</sup> "Malaysia to Help Sudan with More Investments," *The New Straits Times*, April 17, 2007.

**Table 8. Bilateral Assistance**  
(in millions of dollars)

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<b>Account</b>	<b>FY2007 actual</b>	<b>FY2008 estimate</b>	<b>FY2009 request</b>
International Military Education and Training (IMET)	0.871	0.876	0.750
International Narcotics Control and Law Enforcement	—	—	0.400
Non-Proliferation Anti-Terrorist Demining and Related Programs (NADR)	2.401	1.998	1.540
Totals	3.272	2.874	2.690

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**Source:** State Department, FY 2007 Congressional Budget Justification for Foreign Operations, Released March 11, 2008. See also CRS Report RL31362, *U.S. Foreign Aid to East and South Asia: Selected Recipients*, by (name redacted).

Figure 1. Map of Malaysia



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