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Navigating the Samurai Bond and 'Look East Policy 2.0': A Deeper Malaysia-Japan Economic Partnership?

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Upon his return to the premiership in May 2018, Tun Mahathir Mohamad has made six official visits to Japan to further strengthen bilateral relations. In one of the visits, the Japanese Prime Minister, Shinzo Abe, has reciprocated Malaysia's wishes to reinforce economic partnership, particularly on exchanges in technical education, human resource competency, and technology transfers.[1] Consequently, the Japanese Government had offered financial assistance to Malaysia in the form of a low-interest, Tokyo-based, yen-denominated bond, or the Samurai bond, in November 2018. The bond, eventually issued in March 2019, was offered at an ultra-low interest rate of 0.65%, in which cheap access to capital market can finance infrastructure projects and alleviate Malaysia's public debt concerns.[2] The renewed ties have arguably drawn a parallel with the Look East Policy, first introduced by Tun Mahathir during his first stint as the Prime Minister, given the similarities in motivation (to replicate the Japanese economic model), scope (education, technology, and investments), and leadership. Although this replication of the special bilateral relationship of the yesteryears has already shown swift policy outcomes, lessons learnt from the Look East Policy imply that more must be done within the context of Malaysia-Japan relations. More specifically, considering how Tun Mahathir aspires to make Malaysia a high-income country by 2025, the 'Look East Policy 2.0' should then reflect the complex challenges faced by the global economic structure in the 21st century and beyond. In other words, Putrajaya should ensure that the 'Look East Policy 2.0' is not limited to investment promotions and educational exchanges, but rather sophisticated and permanent technology transfers.

Look East Policy as the cornerstone of Malaysia-Japan

First introduced by Tun Mahathir on 8 February 1982 at the 5th Joint Annual Conference of the Malaysia-Japan Economic Association in Kuala Lumpur, the Look East Policy reflected Malaysia's shifting development model, away from the laissez-fare capitalism propagated by the West to the developmental state policy adopted by Japan and South Korea. That is, the complementary state-business relationship in Japan had inspired him to replicate such an idea in Malaysia, in which the state can direct and facilitate private sector investments to promote socioeconomic growth, especially given his belief that the unrestrained Western capitalism would fail to alleviate the economic gap between the Malays and non-Malays.[3] Essentially, this form of state intervention relies on the establishment of state-owned enterprises to invest in strategic sectors with the profits being reinvested into public domain. However, pursuing the Asian development model posed a challenge to Malaysia as it lacked intensive physical, capital, and human resources to promote an export-oriented, heavy-industry manufacturing. Thus, the Look East Policy was introduced with these two main pillars at its core: 1) replicating Oriental virtues and values, work ethics, and management style through educational and training exchanges and 2) attracting Japanese investments and technology transfers to cover such constraints.[4]

Lessons from Look East Policy

After over three decades of its implementation, the Look East Policy can be evaluated with varying degrees of success. With an uninterrupted period of rapid economic growth averaging almost 8% annually between mid-1980s and prior to the Asian Financial Crisis in 1997, which was mostly aided by extensive foreign direct investments (FDI) from East Asia, the attempt to replicate the export-oriented manufacturing model can be deemed successful. In addition, the Japanese government also allocated USD400 million in loans and grants in 1998 and 1999 for educational scholarships, with almost 2,000 Malaysian students of science and engineering backgrounds in Japanese universities benefitting from the scheme.[5] However, further analysis of the Look East Policy has highlighted policy inefficiencies that should serve as key lessons for future bilateral cooperation:

i. Creating Conducive Economic Incentives

Given the borderless nature of capital movements, attracting constant flows of FDI relies on a conducive and competitive economic environment that provides comparable returns to investment. While Japan has always been the largest source of manufacturing FDI in Malaysia since 1980 – totalling at RM88.5 billion as of 2016[6] – this flow only accelerated after the 1985 Plaza Accord, in which the depreciation of USD against the yen incentivised Japanese firms to scour for investment opportunities abroad due to currency advantages. In fact, there exists a significant disparity in Japanese FDI pre- and post-1985 – the values ranged from RM32.6 million to RM308.7 million between 1970 and 1984 and RM116.3 million to RM4.2 billion between 1985 and 1991.[7] Thus, Malaysia must realise that bilateral economic cooperation is not based solely on altruism or political goodwill, but also encompasses sound and valid domestic macroeconomic principles.

ii. Balancing Idiosyncratic Motivations and Tangible Outcomes

However, the Look East Policy was not limited to Tun Mahathir's economic vision of Malaysia. His deep admiration of the Japanese culture, work ethics, and successes in a Western-dominated world – amplified by his Global South activism and nationalist stances – has illustrated the extent of idiosyncrasy in Malaysian foreign relations. For instance, the Look East Policy was considered an integral part of the two-pillared Malaysian foreign policy in the 1980s, with the other being the 'Buy British Last'. Introduced by Tun Mahathir in 1981 merely months after entering office, the 'Buy British Last' signified the deteriorating relations between the UK and Malaysia that were mostly attributed to the exorbitant tuition hike for Malaysian students at British universities and the hostile reception from the London Metal Exchange to an attempted takeover of Guthrie, a then British company – although other factors such as economic nationalism, perceived lack of reciprocity, and domestic grievances were also identified.[8] Consequently, this approach resulted in rather inefficient outcomes, notably in the procurement process for a sugar company when a Japanese tractor was preferred over that of the British despite the latter being 20% cheaper.[9] While the extent of leaders imprinting their personal influences in policies can often be overstated as the former are usually constrained by global and domestic political-economic norms – including that of Tun Mahathir, whose foreign policies are a manifestation of his personality traits and the need to promote national development, national integration, and regime maintenance[10] – Malaysia must then ensure that future bilateral partnerships are planned to minimise the disparity between idiosyncratic motivations and tangible political-economic outcomes.

Samurai Bond: A Stimulant to the 'Look East Policy 2.0'

The growing internationalisation of bond markets, i.e., the ability to issue foreign-denominated bond by non-residents, has prompted governments to seek for alternative, and often affordable, financing options abroad. For example, Malaysia has requested for yen credit from Japan given how most indicators on the Japanese interest rates – from the overnight Central Bank Rates to the 10-year long-term Government bond yield – have remained below 0.5%, or even negative, since the economic crash in 2008.[11] That is, low interest rates can encourage public and private investments as the cost of borrowing is essentially at its lowest today and would only increase in future (barring the unlikely mainstreaming of negative rates). Therefore, issuing a Samurai bond offers an avenue for Malaysia to not only finance its domestic development at a lower cost, but also free up funds to dispose higher-rated loans issued by the previous administration, such as the RM5 billion, 30-year, government-guaranteed 1MDB bond issued at 5.75% annual rate.[12]

The continuous effort to strengthen bilateral relations was promptly recognised by Japan, in which Malaysia was granted access to the Japanese capital markets to issue its first Samurai bond after a thirty-year absence in March 2019. The 10-year bond that is guaranteed by the Japan Bank for International Cooperation (JBIC) at 0.63% per annum was approximately oversubscribed by 1.6 times at the value of JP¥324.7 billion against the initial offering of JP¥200 billion – with the conditions being much more advantageous relative to those of its ASEAN peers, e.g., Indonesia with JP¥100 billion at 1.27% per annum and Philippines with JP¥40.8 billion at 0.99% per annum.[13] Although economic fundamentals and market confidence have greater weightage in determining the terms of foreign-guaranteed debts, in which Malaysia arguably outperforms most of its neighbours, close diplomatic relations may offer additional reassurance on economic agreements.

'Look East Policy 2.0': Status Quo or a Collaborative Breakthrough?

The issuance of the Samurai bond and the commitment by University of Tsukuba to establish the first ever Japanese university branch abroad in Malaysia[14] – imply that initial outcomes of the 'Look East Policy 2.0' have been rather encouraging, especially in the scope of supporting Malaysia's aspirations of being a high-income nation by 2025. However, given the rapid disruption of conventional economic structures that is upon us – with the breakthrough emergence of Industry 4.0, big data, artificial intelligence, Internet-of-Things, and similar technological-driven changes – the Government should further elevate and expand its idea of bilateral economic relations to ensure that it is not left behind in the digital epoch. Since Japan is listed as the ninth most innovative economy in the world while South Korea retained its first spot for the sixth year running based on the 2019 Bloomberg Innovation Index – an index that measures countries' innovativeness based on their research and development intensity, patent activity, tertiary education efficiency, productivity, value-added manufacturing, high-tech public company density, and researcher density[15] – the 'Look East Policy 2.0' should not then be reduced to mere carbon copies of the first Look East Policy. Despite its prior benefits, Malaysia must be bold to ensure that the approach under the 'Look East Policy 2.0' will be distinct, as to facilitate advanced and sophisticated technological exchanges that are conducive to the invention and development of productive heavy industries. In this context, Malaysia can emulate other advanced nation approach towards innovation and technology transfers: establishing tri-sectoral research sectors (industrial, academic, and government) with specific yet complementary purposes to extract multiplier effects of foreign ventures and minimising the development gap between foreign-based academic knowledge and domestic-based industrial outcomes through institutional collaboration in the commercialisation process.[16]

Conclusion

The prompt financial relief through the issuance of Samurai bond inherently signals the positive reaffirmation of Malaysia-Japan relations under Tun Mahathir's second stint as the Prime

Minister, which is arguably reminiscent of the first Look East Policy. The efforts to resurrect the highs of the special partnership of the past have been evidently expressed by the Malaysian government today. While it might be tempted to replicate the approaches of the Look East Policy – given how it has benefitted from Japanese investments, academic exchanges, and production outsourcing – Malaysia must acknowledge that almost 40 years have elapsed since then. The subsequent drastic changes in global structures of political economy and the practical application of economic conventional wisdoms, mostly attributed to the emergence of disruptive and transformative technologies, have inherently put Malaysia at a crossroads: Putrajaya could maintain the status quo in pursuing its ties with Tokyo – just like Tun Mahathir's first stint in office – or it could be bold by recognising, and hence, incorporating responses to, these complex challenges of the 21st century and beyond. Regardless of the path it chooses, its implications must be carefully dissected to ensure that Malaysia is not blindsided by historical ties to explore other – or even more – beneficial partnerships, or even worse, to avoid falling into lopsided and/or unfair deals.

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