



# ANALYSIS OF MALAYSIA'S TERMS OF TRADE & TARIFF POLICIES

*WITH SPECIAL RESPECT TO INDIA*

<sup>1</sup> Abhinandan Shrivastava, <sup>2</sup> Dr. Vinita Shrivastava

<sup>1</sup> Student, Bsc. Economics, Third Year, <sup>2</sup> Assistant Professor (Economics), Department of  
Commerce

<sup>1</sup> Gokhale Institute of Politics and Economics Pune, India

<sup>2</sup> Indira College of Commerce and Science, Affiliated with Savitri Bai Phule Pune University,  
Pune, India

**Abstract:** The authors have analyzed the terms of trade of Malaysia, overviewed its trade agreements and tariff policies with other nations, and have analyzed trade relations between Malaysia and India. They found that, in general, Malaysia has had a declining net barter terms of trade, with respect to both, the world and India. This is because Malaysia's exports constitute of high-quantity, low-value goods relative to its import goods. This strategy is working for Malaysia, as its growth in trade has been on an uptrend since the 2000s.

**Key Words:** Malaysia, Terms of Trade, Exports & Imports, India, Trade Agreements

## **I. Introduction**

In 2021, Malaysia's current GDP stood at 372.7 billion dollars, making Malaysia stand at rank 39 according to the size of its GDP, its imports and exports of goods & services stood at 230.4 and 256.8 billion dollars respectively.

Malaysia is a high-middle-income country and is classified as an emerging economy. Malaysia started liberalizing trade since the 1980s, and since then, trade has played an important role in Malaysia's economy.



Source: World Bank, Graph constructed by Author <sup>1</sup>

As we can see in this graph, in 2021, Malaysia's trade as a % of GDP was 130.7%. In comparison, the same statistic for India was 44%. And this 130% is after a continuous decline since the 2000s. This portrays just how much Malaysia partakes in trading activities.

## II. Research Methodology

The relevant points and statistics have all been obtained through secondary data sources. Official websites of India's Department of Commerce, the Department of Statistics of Malaysia, the World Bank, & World Integrated Trade Solution (WITS) were used. Additionally, websites like MacroTrends, and Observatory of Economic Complexity were used in tandem.

Finally, the authors have calculated the commodity and income ToT between Malaysia and India manually. The export and import values and respective quantities were taken from Government of India's commerce website. Then, these values were converted into their absolute values, and the average export and import prices were calculated. Then, these prices were indexed, with the base year as 2012-13. The formula for indexation was the normal one, which is followed for other indexes like the CPI:

$$\text{XMPIS} = \left( \frac{\text{Value in Current Year}}{\text{Value in Base Year}} \right) * 100$$

Once we had the indexed values, we calculated the commodity ToT as follows:

$$\text{Commodity ToT} = \left( \frac{\text{Export Price Index}}{\text{Import Price Index}} \right) * 100$$

Once we had commodity ToT, we multiplied this with the respective export volumes, to obtain the income ToT. Do note that all the policies and statistics have been looked at from the Malaysian perspective.

## III. Literature Review

There is a lot of literature that exists, that showcases the positive links between trade agreements and capital flows, which lead to more trade between countries.

In the North American region, Globerman and Shapiro (2002) found that Canada-USA FTA and North American FTA, both increased FDI flows. Banga (2004) shows that RTAs like ASEAN lead to more investment within the countries and more geographical integration of FDI.

In the OECD regions, Leshier and Miroudot (2006) find that provisions for investments in FTAs have a positive influence on trade and an even stronger influence on foreign investment.

In the Korean context, a study on Korea-US FTA by Kang and Park (2006) found that FTA increased FDI flow by 14-35% from member countries and by 28-35% from nonmember countries. For the European region, the study conducted by Baltagi et al. (2007) concluded that RTAs increase the FDI in European economies by up to 78%.<sup>2</sup>

## IV. Theoretical Introductions

Before the analysis, the authors will be covering the basic theory of the two indicators that are used for analyzing Malaysia. These are Terms of Trade (ToT) and Tariffs.

### 1) Terms of Trade (ToT)

The terms of trade, or more specifically, the *commodity terms of trade*, of a country is the ratio between the export and import prices. In the real world, commodity ToTs are calculated by using XMPs (Export-Import Price Indices).

Commodity ToT measures the situation of the trade according to the prices of imported and exported commodities.

An increase in the commodity ToT means a country will be able to buy more imports from unit exports. Similarly, a deterioration in commodity ToT means a country will have to export more units in order to import commodities.

On the other hand, another very common type of terms of trade measure used is the *income terms of trade*.

*Income Terms of Trade* are the same as commodity terms of trade but also account for the volume of exports.

The formula goes as

$(\text{Index Price of Exports} * \text{Volume of Exports}) / (\text{Index Price of Imports})$

Basically, Income ToT is the commodity ToT, multiplied by export quantity. When it comes to economic growth, many economists consider the income ToT to be more useful than the commodity ToT.

For our analysis, we will be considering both, the commodity, and the income terms of trade.<sup>3</sup>

### 2) Tariffs

Tariffs are any sort of duties or taxes imposed by the government on internationally traded goods. An import tariff will be incorporated into imports, and an export tariff will be incorporated into exports. Generally, most tariffs are *ad-valorem*, which means a fixed percentage will be charged on the traded goods. Another type is the *specific tariff*, which adds a fixed sum according to units traded, but is very rarely observed in the trading world. If countries want to incorporate both these types of tariffs, they employ a *compound tariff*, which is a combination of both.

Tariffs are generally used by countries to restrict foreign intervention in the domestic market, and help give an advantage to domestic producers. Infant and industrializing economies use import tariffs. Even developing countries use some export tariffs on their main export commodities, just to earn some extra easy revenue.

In this case, as tariffs and terms of trade are highly interlinked, and both these aspects are extensively covered by a nation's trade agreements, we will be covering the various trade agreements Malaysia has gotten into, what their tariff policies have been, and will finally analyze the terms of trade of Malaysia.

## V. Analysis

### 1) Trade Policies & Agreements

As we have seen, trade has a heavy influence on the Malaysian economy. For trade to prosper, Malaysia has harnessed the power of Free Trade Policies (FTPs) with many nations. Malaysia is also a strong supporter of Regional Trade Agreements (RTAs) which is evident by how active Malaysia is when it comes to various types of trade agreements through its membership with the Association of South East Asian Nations (ASEAN).

Through ASEAN, Malaysia has made strong trade agreements with other countries. In fact, on top of trade ties through ASEAN, Malaysia and India have another trade agreement, called the Malaysia-India Comprehensive Economic Cooperation Agreement (MICECA), which serves as an added bonus.

## ASEAN Free Trade Agreement (AFTA)

The AFTA is the trade bloc agreement amongst the ASEAN nations, which promotes trade, manufacturing, and capital inflows within the region. Its main objective is to promote economic growth among the ASEAN members and make all the members of ASEAN a bigger world market.<sup>4</sup> The AFTA goes as follows:

### 1) Common Effective Preferential Tariff Scheme

As one of the goals of ASEAN was to promote exports with the global market, the CEPT scheme (introduced in 1992) aimed to increase the productive efficiency of the ASEAN members by facilitating a gradual elimination of intra-regional tariffs. This was done according to the sensitivity of the products to the respective ASEAN Member States (AMS) domestic industry.

### 2) Tariff Elimination

Since January 2010, the 6 countries under ASEAN (Singapore, Thailand, Malaysia, Indonesia, Philippines, and Brunei Darussalam) are a free trade area and have eliminated up to 99 percent of the import duties on traded commodities.<sup>5</sup>

Via its membership in the ASEAN, Malaysia has also gotten into trade agreements with the likes of Japan, Korea, Australia, New Zealand, Pakistan, Chile, and the United States. There also exists an ASEAN-China FTA, called the ACFTA, which defines trade agreements between ASEAN and China.<sup>6</sup>

### - Malaysia-India Cooperative Agreement (MICECA)

The MICECA came into effect in July 2011 and provides additional benefits in the trade of goods, services, capital flows, and movement of persons. These are on top of the ASEAN-India Trade in Goods Agreement (AITIG). The MICECA have the following features:

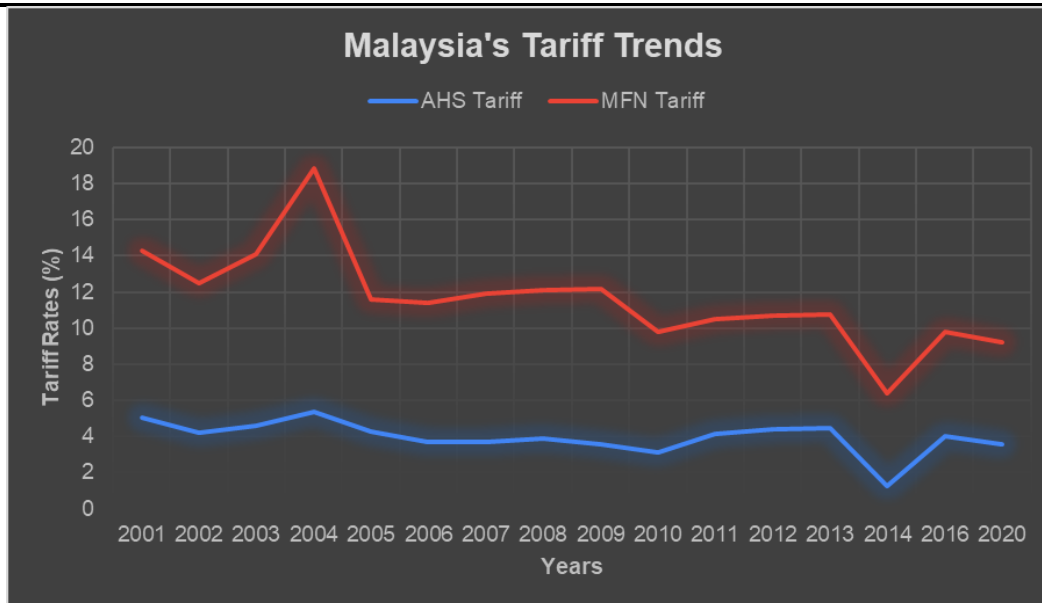
- 1) Both countries will reduce or eliminate tariffs on their industrial and agricultural products.
- 2) India will start to gradually eliminate or reduce the amount of tariff charged on goods.
- 3) This transition will follow a timed approach and has been summarized in the table below:

Commodity Group	Period
Normal Track 1 (NT1)	Eliminate Tariffs by September 2013.
Normal Track 2 (NT2)	Eliminate Tariffs by June 2016.
Sensitive Track (ST)	Reduce Tariffs to 5% by June 2016.

- 4) As Malaysia exports so much palm oil to India, Malaysia has been granted better concessions on palm oil and related products.
- 5) India will bind tariffs on refined palm oil (RPO), and 3 palm oil products at 45% by 31 December 2018.<sup>7</sup>

According to the Asia Pacific Trade & Investment Report 2018, Malaysia had 15 total trade agreements with partners. And a total of 66.8% of its exports are directed toward its trade agreement partners, and 62.5% of total imports come from its trade agreement partners. We can refer to Table A in the annexure to get more details.<sup>8</sup>

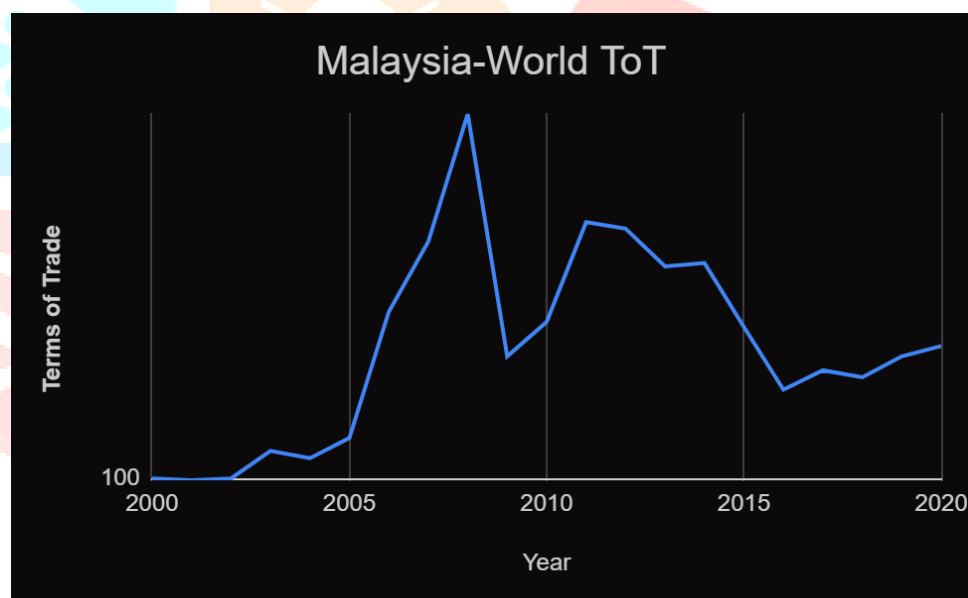
As we can see, these are the average weighted tariffs, and simple mean of MFN tariff charged by Malaysia over the years.<sup>9, 10</sup> More details can be found in Table B in Annexures.



Source: MacroTrends, World Bank. Graph constructed by Author

## 2) Malaysia ToT - The World

Let us now first look at the Terms of Trade Malaysia has with respect to the rest of the world. Exact details are available in Table C in Annexures.

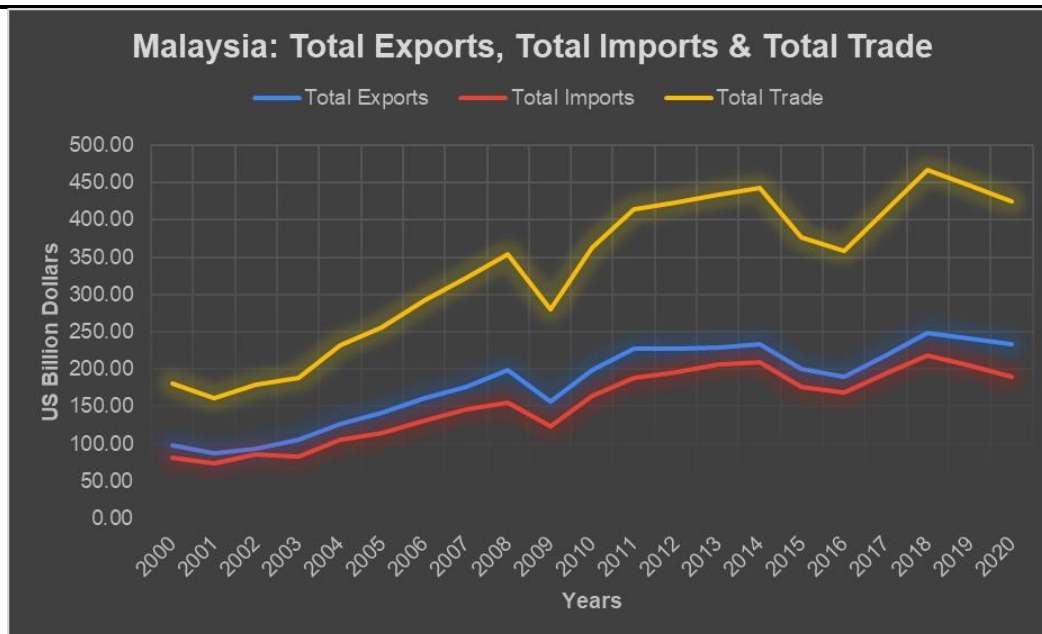


Source: World Bank. Graph constructed by Author (Log Scale)<sup>11</sup>

As we can see, Malaysia's ToT with the world was the highest in 2008, at 121.7. It fell sharply in 2009, recovered a little from 2011-2014, but has been trading around the 105-108 area since then. The fall in 2009 is attributable to the Global Financial Crisis.

Looking at the overall trend, we can see that the ratio of export to import prices for Malaysia has been falling. However, a falling net barter term of trade is not a bad thing, and it may very well mean that Malaysia has transitioned into exporting more low-value, high-quantity goods.



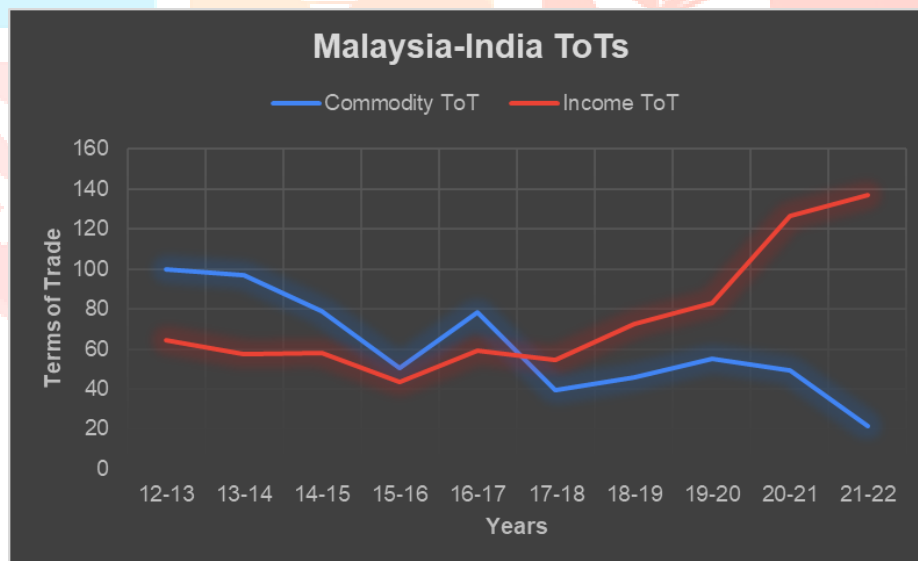


Source: WITS Data. Graph constructed by Author. <sup>12</sup>

As we can see, the total exports, total imports, and total trade of Malaysia have been on an increasing trajectory, implying that even though Malaysia's ToT has deteriorated, trade has prospered, and what we state above as a possible reason is more plausible.

### 3) Malaysia ToT - India

Let us now look at Malaysia's ToT concerning India. Exact details and calculations are mentioned in tables E, F, and G.



Source: Calculated by the Author

Now, looking at the ToT between Malaysia and India, a lot of interesting things can be observed.

- 1) If we glance at the tables which calculate the average import and export prices between the nations, it is evident that Malaysia's exports to India are of low-price but high-quantity goods.
- 2) Similarly, its imports from India are relatively costlier.
- 3) The commodity ToT for Malaysia has deteriorated *a lot* since 2012-13, but the income ToT has gotten better over the years.

This implies that Malaysia's *value* of exports has increased, and it results not from Malaysia getting more export prices, but it getting more export volumes from its trade.

## VI. Conclusions

As we have seen, Malaysia has strong linkages with the world, and it undertakes trade agreements very aggressively.

Major exports of Malaysia to the world have been integrated circuits and related electrical equipment, Mineral fuels and oils like refined petroleum and palm oil, and articles of plastic and rubber. Consequently, Malaysia also imports these similar products.

As we have also seen previously, Malaysia used to have high tariff rates in the early 2000s, but since then, due to their perusal of FTAs, they have strived towards reducing their tariff on commodities. This has helped it import more products, and has consequently led to more exports as well.

In the case of India, we have observed deteriorating commodity terms of trade, but appreciating income terms of trade. This, with the fact that Malaysia shares a trade surplus with India, shows that Malaysia imports high-value commodities from India, and exports relatively lower-valued commodities to India.

This can be proved, as major imports from India include petroleum oils, cyclic hydrocarbons, unwrought aluminum, the meat of animals, vessels, boats, ships & related equipment, etc. And on the other hand, the exports from Malaysia mostly include palm oils, petroleum and crude oils, and some electronic equipment. As oils make up a significant portion of Malaysia's exports to India, the average price of exports is driven down. Hence, there is such a decline in Malaysia's commodity ToT. But, as the trade surplus indicates, Malaysia's value of exports to India has been growing, and such a change is captured by the income ToT.

By looking at all this, we can conclude that Malaysia has a clear advantage in some commodities, and it should pursue economic growth and other objectives in this fashion, as these trade policies are proving to be very beneficial for Malaysia.

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## VIII. Annexures

Table A: Malaysia's Total Trade Agreements <sup>8</sup>

Title	Status	Year in force	Share of total exports (%)	Share of total imports (%)
Global System of Trade Preferences (GSTP)	in force	1989	39.94	33.79
ASEAN Economic Community	in force	1992	28.86	24.01
ASEAN-China	in force	2005	42.29	42.41
Japan-Malaysia	in force	2006	7.96	7.11
ASEAN-Japan	in force	2008	36.82	31.12
Malaysia-Pakistan	in force	2008	0.54	0.08
ASEAN-Australia-New Zealand	in force	2010	32.79	26.64
ASEAN-India	in force	2010	32.54	27.02
ASEAN-Republic of Korea	in force	2010	31.90	28.09
Malaysia-New Zealand	in force	2010	0.48	0.38
Group of 8 Preferential Trade Agreement (D-8 PTA)	in force	2011	6.80	4.90
India-Malaysia	in force	2011	3.68	3.01
Malaysia-Chile	in force	2012	0.08	0.09
Australia-Malaysia	in force	2013	3.45	2.25
Malaysia-Turkey	in force	2015	1.12	0.17
Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP)	signed	NA	30.85	23.58
ASEAN-European Union (EU)	under neg.	NA	39.02	33.02
ASEAN-Hong Kong,China	under neg.	NA	33.94	25.58
Malaysia-European Free Trade Association (EFTA)	under neg.	NA	0.60	1.55
Malaysia-European Union (EU)	under neg.	NA	10.16	9.01
Regional Comprehensive Economic Partnership (RCEP)	under neg.	NA	60.89	59.23
Trade Preferential System among the Organisation of the Islamic Conference (TPS/OIC)	under neg.	NA	4.87	3.79

**Table B: Trends in Malaysia's Tariffs** <sup>9,10</sup>

(Values in %)

Weighted Mean Applied Tariff		MFN Tariff (Simple Mean)	
Year	AHS Tariff	Year	MFN Tariff
2001	5.06	2001	9.2
2002	4.2	2002	8.3
2003	4.57	2003	9.5
2004	5.37	2004	13.5
2005	4.27	2005	7.3
2006	3.68	2006	7.7
2007	3.71	2007	8.2
2008	3.89	2008	8.2
2009	3.55	2009	8.6
2010	3.12	2010	6.7
2011	4.17	2011	6.3
2012	4.41	2012	6.3
2013	4.44	2013	6.3
2014	1.28	2014	5.1
2016	4.02	2016	5.8
2020	3.6	2020	5.6

Data for the years 2015, 2017, 2018, &amp; 2019 was not available.

**Table C: Malaysia's Terms of Trade with The World** <sup>11</sup>

Year	ToT	Year	ToT
2000	100	2011	114.8
2001	99.9	2012	114.4
2002	100	2013	112.1
2003	101.5	2014	112.3
2004	101.1	2015	108.5
2005	102.2	2016	104.9
2006	109.4	2017	106
2007	113.6	2018	105.6
2008	121.7	2019	106.8
2009	106.8	2020	107.4
2010	108.8		

**Table D: Malaysia's Total Exports, Total Imports, and Total Trade<sup>12</sup>**

(Figures in US Billion Dollars)

Year	Total Exports	Total Imports	Total Trade
2000	98.23	81.96	180.19
2001	88.00	73.85	161.85
2002	93.28	86.14	179.42
2003	104.97	83.61	188.58
2004	126.64	105.16	231.80
2005	141.62	114.29	255.91
2006	160.67	131.13	291.80
2007	175.96	146.10	322.07
2008	198.70	155.66	354.36
2009	157.19	123.58	280.77
2010	198.79	164.59	363.38
2011	226.99	187.57	414.57
2012	227.45	196.20	423.65
2013	228.32	205.81	434.13
2014	234.13	208.82	442.96
2015	200.21	176.17	376.39
2016	189.41	168.38	357.79
2017	217.72	194.72	412.44
2018	248.71	218.02	466.73
2019	240.21	205.03	445.24
2020	234.05	190.40	424.45

**Table E: Value of Exports, Quantity of Exports & Average Export Price (Malaysia-India)<sup>13</sup>**

Years	Value of Exports (Rupees)	Quantity of Exports	Average Export Price (Rupees)
12-13	541,987,633,000	6,448,273,970	84.052
13-14	559,021,137,000	5,922,804,410	94.385
14-15	679,188,378,000	7,381,886,120	92.007
15-16	593,731,699,000	8,596,489,100	69.067
16-17	598,814,501,000	7,590,358,780	78.891
17-18	580,812,886,000	13,762,342,270	42.203
18-19	754,916,712,000	15,773,791,470	47.859
19-20	691,666,295,000	15,114,219,200	45.763
20-21	617,912,170,000	25,479,873,440	24.251

21-22	926,306,476,000	63,933,578,200	14.489
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**Table F: Value of Imports, Quantity of Imports & Average Import Price (Malaysia-India) <sup>13</sup>**

Years	Value of Imports (Rupees)	Quantity of Imports	Average Import Price (Rupees)
12-13	16,343,182,896,000	3,482,889,940	4692.420
13-14	19,050,110,886,000	3,503,107,870	5438.060
14-15	18,963,484,176,000	2,904,086,020	6529.932
15-16	17,163,844,044,000	2,257,213,030	7603.998
16-17	18,494,335,534,000	3,288,705,750	5623.591
17-18	19,565,145,280,000	3,295,041,620	5937.754
18-19	23,077,261,938,000	3,958,823,710	5829.323
19-20	22,198,541,810,000	4,775,486,670	4648.436
20-21	21,590,432,213,000	7,910,677,580	2729.277
21-22	31,470,214,928,000	8,337,650,060	3774.471

**Table G: Calculating Export & Import Price Indexes, and then Commodity & Income ToT**

Years	Export Price Index	Import Price Index	Net Barter ToT	Income ToT
12-13	100.00	100.00	100.00	64.48
13-14	112.29	115.89	96.90	57.39
14-15	109.47	139.16	78.66	58.07
15-16	82.17	162.05	50.71	43.59
16-17	93.86	119.84	78.32	59.45
17-18	50.21	126.54	39.68	54.61
18-19	56.94	124.23	45.83	72.30
19-20	54.45	99.06	54.96	83.07
20-21	28.85	58.16	49.61	126.40
21-22	17.24	80.44	21.43	137.01