

PERSPECTIVE

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China-Malaysia Relations Back on Track?

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EXECUTIVE SUMMARY

- China-Malaysia relations appear to have gained new momentum with Malaysia re-joining the Belt and Road Initiative after months of uncertainty.
- In the run-up to Mahathir's participation at the Second Belt and Road Forum in Beijing, frantic negotiations took place that led to the resumption of key projects like the East Coast Railway Line and Bandar Malaysia.
- The revival of these projects reaffirms China's approach of looking at its relations with Malaysia from the strategic standpoint of fostering long-term and stable ties. China accorded Mahathir high-level treatment by granting him access to China's top three leaders in his second official visit to China since taking office in May 2018.
- China further secured Mahathir's endorsement of Huawei's role in Malaysia's socio-economic development, in a seeming rebuff of US efforts to thwart Huawei's global expansion.
- While China's presence in Malaysia is set to increase, Beijing may need to pay greater attention to how this can exacerbate the sensitive issues of race, religion and politics in Malaysia.

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INTRODUCTION

China-Malaysia relations appear to be on the mend with the resumption of key projects like the East Coast Railway Line (ECRL) and Bandar Malaysia. After the Pakatan Harapan coalition swept into power in May last year, there were serious doubts on the status of China's megaprojects in Malaysia. And even after Mahathir Mohamad's first visit to China in August 2018 as prime minister, the fate of these projects still hung in the balance.

Yet, in the run-up to and during Mahathir's second visit to China in April 2019, such doubts were erased as China and Malaysia agreed to restart the ECRL and Bandar Malaysia. Malaysia also stands out for its endorsement of Huawei even as the United States seeks to thwart Huawei's global expansion.

In turn, China appears ready to support Mahathir's domestic socio-economic development agenda of building infrastructure, providing jobs, upgrading its industries and improving the lives of its people. Chinese companies like Huawei and SenseTime appear poised to expand their footprint in Malaysia. On its part, the Mahathir administration, faced with increasing domestic pressure to deliver on bread and butter issues that matter to its electorate, is increasingly looking to China to help it meet this objective.

LAYING THE GROUNDWORK

The context surrounding Mahathir's second visit to China in April 2019 was markedly different from that of his first visit in August 2018. In his 2018 visit, the foremost issue that stood out was the uncertainty over the fate of China's mega-projects in Malaysia, such as the ECRL and the Multi-Product Pipeline as well as the Trans-Sabah Gas Pipeline. The indications then were that these projects would either be cancelled or suspended indefinitely. In addition, Mahathir came across as critical of China during a joint press conference with Chinese Premier Li Keqiang in August 2018 when he commented on the topic of free trade and said that "we do not want a situation where there is a new version of colonialism because poor countries could not compete with rich cities".¹

In contrast, during Mahathir's April 2019 visit, the atmospherics had become much more positive. For one thing, Mahathir did not criticise China before and during his visit. In fact, a key message that came out from the visit was that Malaysia was fully behind the Belt and Road Initiative (BRI), the major foreign policy initiative by Chinese President Xi Jinping.

More importantly, before the visit, China and Malaysia made progress on two signature projects under the BRI which had previously hit an impasse. The first project was the ECRL. In January this year, there were still conflicting signals on the status of the ECRL with Malaysian Economic Affairs Minister Azmin Ali first announcing that the Malaysian cabinet had decided to scrap the project², followed by Finance Minister Lim Guan Eng's remarks on the very same day expressing shock over Azmin's announcement.³ Mahathir joined the fray when he called for patience and urged the public not to jump to conclusions but to wait for the official statement.⁴ In a hint that frantic negotiations were going on behind the scenes, China's foreign ministry spokesperson Geng Shuang said that the two sides had always maintained constant communication on this issue.⁵

Talks on the ECRL were not altogether smooth sailing. Malaysia's point man on this issue, Chairman of the Council of Eminent Persons Daim Zainuddin alluded to this when he said in February 2019 that the ECRL was a "complicated" and "sensitive" issue and that it was "better to talk less about it".⁶ Mahathir conveyed a less optimistic tone when he said in March that the future of the ECRL was unlikely to be resolved before his Beijing visit in April for the Belt and Road Forum as the talks not only depended on the Malaysian negotiators but also on the response from China.⁷ It was eventually announced on 12 April 2019, following Daim Zainuddin's visit to Beijing, that the two sides had reached a Supplementary Agreement that paved the way for the resumption of the ECRL at a reduced cost of RM44 billion, down from the initial cost of RM65.5 billion.⁸ This announcement took place less than two weeks before Mahathir's visit to China on 24 April 2019.

The second project that made headway was Bandar Malaysia. China regards Bandar Malaysia in Kuala Lumpur (KL) as the accomplishment of an important transportation hub that would be part of China's ambitious railway network extending southwards from Kunming via Laos and Thailand to KL and thereafter from KL to Singapore via the High Speed Rail. Chinese top leaders, companies and banks had lent their strong support to this project.⁹

In December 2015, a month after Chinese Premier Li Keqiang visited Malaysia and reiterated China's commitment to work with Malaysia on the High Speed Rail,¹⁰ a consortium comprising China Railway Engineering Corporation (CREC), a Chinese state-owned enterprise, and Iskandar Waterfront Holdings (IWH) signed an agreement to acquire a 60% stake in Bandar Malaysia. In June 2016, further progress was made when a consortium of influential Chinese banks including Bank of China, Industrial and Commercial Bank of China, China Construction Bank and HSBC signed an agreement with Malaysian counterparts such as CIMB, Maybank, RHB and Affin Bank, to provide funding for investors in Bandar Malaysia.¹¹

Although the project was suspended by the Najib administration in May 2017 due ostensibly to the failure of the IWH-CREC consortium to fulfill payment obligations related to 60% of its equity share to Malaysia's Ministry of Finance, the Chinese side never completely gave up on the project. What caught observers by surprise was the sudden announcement of the project's revival. On 19 April 2019, five days before Mahathir's visit, the Prime Minister's Office of Malaysia issued a statement announcing the reinstatement of Bandar Malaysia.¹² Before this, there was no clear indication that this would occur.

The ground was therefore "sweetened" for Mahathir's April 2019 visit to China with the revival of the ECRL and Bandar Malaysia. The Chinese side consistently refrained from talking about the specifics of these two projects in public, allowing negotiations to take place in private.

MAHATHIR'S CHINA ITINERARY

Mahathir official trip to China lasted five days, from 24 to 28 April 2019. He made his debut at the Second Belt and Road Forum in Beijing. Apart from delivering a keynote address at the High Level Meeting (on 26 April) and participating at the Leaders' Roundtable of the

Belt and Road Forum (on 27 April), Mahathir's itinerary in China comprised three other components.

The first part of Mahathir's itinerary was his meetings with top Chinese leaders. China accorded Mahathir high-level treatment, signaling its respect for an elder statesman and the importance it attached to relations with Malaysia. Mahathir met with Chinese President Xi Jinping, Premier Li Keqiang and Chairman of the National People's Congress Standing Committee Li Zhanshu on 25 April 2019. These three Chinese leaders are respectively ranked first, second and third on the Political Bureau Standing Committee, China's highest decision-making body.¹³ In addition, during the leaders' photoshoot at the Belt and Road Forum on 27 April 2019, Mahathir was lined up in the front row where President Xi stood, together with Philippines President Rodrigo Duterte, Thailand Prime Minister Prayut Chan-o-cha, Brunei Sultan Hassanal Bolkiah and Cambodian Prime Minister Hun Sen.

The second part of Mahathir's itinerary related to the agreements signed. Three key agreements, witnessed by Mahathir and Premier Li Keqiang, were signed on 25 April 2019. They were:

- (a) A Memorandum of Understanding (MoU) between the Malaysian Palm Oil Council Board (an agency under Malaysia's Primary Industries Ministry) and the China Chamber of Commerce of Import and Export of Foodstuff, Native Products and Animal By-products. (Under this MoU, China will purchase an additional 1.9 million tonnes of Malaysian palm oil at an estimated cost of RM4.56 billion over the next five years, i.e. from 2019 to 2023, and invest at least RM2 billion in a biojet fuel plant and RM200 million to produce unsaturated fats. The two countries further agreed to work together to encourage the use of renminbi for palm oil trade, subject to Bank Negara Malaysia's approval).¹⁴
- (b) An MoU between the Malaysian Investment Development Authority (MIDA) and China Communication Construction Company (CCCC) on the development of industrial parks and logistic hubs pursuant to the Supplementary Agreement that revived the ECRL. (CCCC is a China state-owned company that has entered into a 50:50 joint venture with Malaysia Rail Link to jointly develop the ECRL).
- (c) A framework agreement on the reinstatement of Bandar Malaysia between the original consortium members IWH and CREC on the one hand and the government of Malaysia on the other. (This agreement marks a step forward from the statement by the Prime Minister's Office of Malaysia on 19 April 2019 announcing the reinstatement of Bandar Malaysia).

The third part of Mahathir's itinerary had to do with the enterprises he visited, one of which was Huawei's Beijing Research Centre where he met with Huawei's founder Ren Zhengfei. During the tour, Mahathir was briefed on Huawei's cloud services as well as industrial applications in areas such as smart city, smart manufacturing and smart transportation. Using Huawei's teleconferencing system, Mahathir also had an exchange with students receiving training 4,300 km away at Huawei's Malaysia Office and its Global Training Centre.¹⁵ Another enterprise that Mahathir visited was SenseTime's Beijing Office where he witnessed the company's Artificial Intelligence (AI) technologies and applications in

areas such as autonomous driving, smart city, education and healthcare. An agreement on strategic collaboration was signed between SenseTime, China Harbour Engineering Company and Malaysian technology company G3 Global to establish the first AI Park in Malaysia.¹⁶

CHINA'S OBJECTIVES

China achieved a number of objectives during Mahathir's April 2019 visit. Foremost among them is that relations between the two countries are now on a positive trajectory as they celebrate the 45th anniversary of diplomatic ties this year. The initial doubts about China's mega-projects, especially the ECRL and Bandar Malaysia, are now a thing of the past. From China's perspective, the two countries were able to approach their relations from a long-term, strategic standpoint and build on the earlier foundations laid. President Xi Jinping alluded to this in his meeting with Mahathir when he said that in the 45 years of diplomatic relations, Mahathir had made important contributions to the development of China-Malaysia relations when he was prime minister for half of this period.¹⁷ Xi added that relations between the two countries were now at a new historical standpoint.¹⁸

Secondly, after months of uncertainty, China succeeded in getting Malaysia to rejoin the BRI. In an interview he gave to the Chinese media prior to his 2019 visit, Mahathir said that with the BRI, more ships would pass by Malaysia and other Southeast Asian countries, and this will promote trade between Southeast Asia and China. He added that the Straits of Malacca was an important sea-lane of communication between East and West and that historically Malaysia was a transit hub for goods, given its geographical location between East and West. He expressed the hope that China would choose Malaysia as the trade hub for Southeast Asia.¹⁹ Mahathir made the same point at the High Level Meeting of the Belt and Road Forum on 26 April 2019 when he said that the BRI would encourage more ships to pass by Malaysia and Southeast Asian countries and therefore will increase trade between Southeast Asia and China.²⁰ He was confident that Malaysia will benefit from the BRI and expressed his full support for it.²¹ When Mahathir met with China's top three leaders, China's official media channels highlighted that China and Malaysia will work together to jointly construct the BRI.

Furthermore, two of the three key agreements signed during Mahathir's visit were related to the BRI, namely the framework agreement on the reinstatement of Bandar Malaysia and the MoU on the development of industrial parks and logistics hubs. Although details about this MoU remain sketchy, it appears that the CCCC, the company that is also responsible for the ECRL, can be expected to play a leading role in building industrial parks, logistic hubs and transit-oriented developments in Malaysia. In particular, as mentioned above, the China Harbour Engineering Company, which is actually a subsidiary of CCCC, has entered into an agreement with SenseTime and G3 Global to build the first AI Park in Malaysia. In addition, the China-Malaysia Qinzhou Industrial Park and the Malaysia-China Kuantan Industrial Park, two related sister projects started by the Najib administration, were listed as key connectivity projects in the Joint Communique of the Leaders' Roundtable of the 2nd Belt and Road Forum.²²

In contrast to Mahathir's 2018 visit where China's mega-projects were given short shrift, his 2019 visit saw Malaysia rehashing itself as an "ardent" supporter of the BRI. To China,

Malaysia's support is significant as the latter was the first country in ASEAN to establish diplomatic ties with China. Malaysia's renewed support for BRI thus provides a pillar of endorsement for China's BRI in other countries. Equally important for China, Malaysia's backing for the BRI demonstrates that through negotiations, it is possible to revise and make adjustments to previously unsatisfactory deals to achieve win-win outcomes. This room for improvement is in line with Chinese President Xi Jinping's call to build "high-quality, sustainable, risk-resistant, reasonably priced, and inclusive infrastructure" at the Second Belt and Road Forum. The improved BRI deals are all the more important at a time when China is receiving brickbats from the West for ensnaring other countries in "debt traps".

Thirdly, Beijing is signaling that it is prepared to lend a "helping hand" to countries that support China's BRI. Though not explicitly stated, this is evident from the actions China has taken. China moved to commit to a deal to buy an additional 1.9 million tonnes of Malaysian palm oil over the next five years and for other palm oil-related investments, following the revival of the ECRL and Bandar Malaysia.²³ This deal is timely as Malaysia, which together with Indonesia accounts for about 85% of global palm oil production, is grappling with an EU restriction and eventual ban of its palm oil exports due to environmental concerns. According to the Malaysian Palm Oil Board, the EU is the second largest buyer of Malaysian palm oil (after India), importing 1.9 million tonnes.²⁴ In this regard, China's plans to purchase an additional 1.9 million tonnes seem intended to make up for the potential loss of its EU market share.

China is further keen to step up its investments in Malaysia to support Mahathir's domestic agenda of promoting socio-economic development. Apart from investing for commercial profits, China is now emphasizing that its companies not only transfer and share knowledge but can also make a social contribution. At the sidelines of the Belt and Road Forum, *Global Times*, a publication under China's Communist Party newspaper *People's Daily*, cited the Malaysian Minister of Housing and Local Government Zuraida Kamaruddin as announcing that Malaysia has signed an agreement with six Chinese companies, including CREC that is building Bandar Malaysia, to construct 100,000 houses this year for Malaysia's low-income households. Of this figure, 10% or 10,000 homes will be built for Bandar Malaysia so that those with low income can also benefit from living in this development. It was further reported that Malaysia is considering including Huawei in developing its smart cities.²⁵

Fourthly, China has secured Malaysia's endorsement for Huawei with implications beyond bilateral relations. At a time when the United States is advocating firm and decisive action to exclude Huawei from 5G businesses, Malaysia is bucking the trend by re-affirming Huawei's role in contributing to the growth and upgrade of its economy. In his tour of Huawei's Beijing Research Centre, Mahathir seemed impressed with what he saw when he said that the "achievements of Huawei are very remarkable and we are learning more on how to use artificial intelligence for many different applications. For many of us, this is a good lesson on how progress has been made by China and by Huawei".²⁶ Earlier, in the same month of April 2019, Malaysia's Deputy Minister of International Trade and Industry Ong Kian Ming endorsed Huawei's contribution to job creation and industrial and technological upgrading in Malaysia while touring Huawei's Global Training Centre in Cyberjaya. Huawei itself has highlighted that out of its current 2,500 employees in Malaysia, over two thirds are Malaysians.²⁷ Malaysia's approach is in stark contrast to that of Vietnam which has taken a more guarded position especially on Huawei's participation in its 5G network plan.

CONCLUSION

Mahathir's April 2019 visit to China has injected more predictability to Malaysia-China relations. In particular, the ECRL and Bandar Malaysia which China considers signature projects under the BRI has been revived and given new momentum. To China, this is a welcome development as it underscores the fact that the two countries are approaching their relationship from a long-term and strategic standpoint.

With Malaysia's renewed backing for China's BRI, Beijing in turn appears ready to commit more economic resources to help Mahathir meet his domestic social-economic development agenda. Already, Chinese companies like Huawei and SenseTime are poised to expand their presence in Malaysia. China has also committed to buy more agricultural products from Malaysia such as its palm oil.

However, in expanding its footprint across Malaysia, it may be prudent for China to exercise caution given the sensitive dynamics of race, religion and politics in Malaysia. In the past, anti-Chinese sentiments leading to social unrest and violence have occurred. Going forward, the possibility of an anti-Chinese backlash either arising from factors related to China or purely due to domestic politics should not be entirely discounted.

¹ "Mahathir, China and neo-colonialism", *Nikkei Asian Review*, 30 August 2018. When asked, Mahathir denied that he was referring to any specific country. See "Transcript of Mahathir's press conference" (Beijing), 1Media.My, 21 August 2018.

² "Malaysia cancelling ECRL project with CCCC: Azmin", *New Straits Times*, 26 January 2019.

³ "Lim Guan Eng shocked by Azmin's announcement on status of ECRL", *New Straits Times*, 26 January 2019.

⁴ "Dr M: Be patient and wait for statement on ECRL", *New Straits Times*, 28 January 2019.

⁵ "2019 nian yiyue 29 ri waijiaobu fayan ren Geng Shuang zhuchi lixing jizhe hui (2019, January 29 China's foreign ministry spokesperson Geng Shuang's regular press conference), China's foreign ministry website, 29 January 2019.

⁶ "China ECRL team to visit Malaysia this month, says Daim", *The Star*, 21 February 2019.

⁷ "East Coast Rail Link deal before belt and road forum? Depends on China, Mahathir says", *South China Morning Post*, 20 March 2019.

⁸ Under the Supplementary Agreement, the total cost of Phase 1 and Phase 2 of the project was reduced from the initial RM65.5 billion to RM44 billion (a reduction of RM21.5 billion); a joint venture company comprising Malaysia Rail Link and China Communications Construction Company would be set up with each side holding 50% share; and the percentage of local participation would be increased to 40 percent of civil works (up from the original 30 percent). If the ECRL were to have been cancelled, the Malaysian government would have had to pay termination costs of RM21.78 billion. See "Press Statement by YAB Prime Minister Tun Dr. Mahathir bin Mohamad on East Coast Rail Link (ECRL) Project", Prime Minister's Office of Malaysia, 15 April 2019.

⁹ Bandar Malaysia would also link up to other public transport networks in Malaysia. As an integrated township development project, it would also comprise retail, residential and commercial components as well.

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- ¹⁰ “Li Keqiang tong Malai xiya zhongli Najibu juxing huitan” (Li Keqiang holds talks with Malaysian Prime Minister Najib), *Xinhua*, 23 November 2015.
- ¹¹ “Zhongguo zhongtie Malai xiya ‘damacheng xiangmu’ qianshu sanxiang guanjian xieyi (China Railway Engineering Corporation Malaysia’s ‘Bandar Malaysia’ signs three crucial agreements), *China News Service*, 17 June 2016.
- ¹² “Government to reinstate Bandar Malaysia project”, Prime Minister’s Office of Malaysia, 19 April 2019.
- ¹³ Mahathir had also met the same three leaders in his August 2018 visit to China.
- ¹⁴ “China set to buy an additional RM4.56 billion worth of Malaysian palm oil”, Prime Minister’s Office of Malaysia, 25 April 2019.
- ¹⁵ “Malai xiya shouxiang fangwen Huawei Beijing yanjiu shuo (Malaysian prime minister visits Huawei’s Beijing Research Centre), Huawei press statement, 25 April 2019.
- ¹⁶ “SenseTime Welcomes Malaysian Prime Minister in China Enters into a Strategic Collaboration with G3 Global and CHEC on the 1st AI Park in Malaysia”, SenseTime News, 26 April 2019.
- ¹⁷ Mahathir was prime minister from July 1981 to October 2003, for a period of more than 22 years.
- ¹⁸ “Xi Jinping huijian Malai xiya zongli Maha dier” (Xi Jinping meets with Malaysian Prime Minister Mahathir), *Xinhua*, 25 April 2019.
- ¹⁹ “Gaoduan fangtan: Malai xiya qidai banyan ‘yidai yilu’ shang de maoyi shuniu jue – fang Malai xiya Zhongli Maha dier” (High level interview: Malaysia looks forwards to play a trade hub role in BRI – interview with Malaysia’s Prime Minister Mahathir), *Xinhua*, 21 April 2019.
- ²⁰ “Waiguo lingdao ren dui ‘yidai yilu’ shuqi da muzhi” (Foreign leaders gives ‘One Belt One Road’ the thumbs up), *China Daily*, 26 April 2019.
- ²¹ At the same time, Mahathir stressed the importance of maintaining the freedom of navigation along the trade routes of the BRI and called on non-littoral states to share responsibility to keep pollution at bay in the Straits of Malacca with trade booming under the BRI. See “Malaysia’s Mahathir backs China’s belt and road but insists on open trade routes”, *SCMP*, 26 April 2019.
- ²² “Joint Communique of the Leaders’ Roundtable of the 2nd Belt and Road Forum for International Cooperation”, *Xinhua*, 27 April 2019.
- ²³ The 1.9 million tonnes of palm oil exports over five years would work out to an increase of 380,000 tonnes per year. In 2018, Malaysia exported 3.07 million tonnes of palm oil and palm-oil based products to China valued at RM8.38 billion, a 7.3% increase from the 2.86 million tonnes exported in 2017 valued at RM9.39 billion. See “Malaysia to export US\$891m palm oil to China”, *New Straits Times*, 4 March 2019.
- ²⁴ “Malaysia threatens to freeze out EU over palm oil ban”, *Nikkei Asian Review*, 28 January 2019.
- ²⁵ “Chinese firms to build 100k homes in Malaysia”, *Global Times*, 27 April 2019.
- ²⁶ “Prime Minister of Malaysia Visits Huawei”, Huawei press statement, 25 April 2019. According to this statement, Huawei has been in Malaysia since 2001 and has maintained robust growth. Its regional headquarters is in Malaysia and it has established 11 shared service centres in the country.
- ²⁷ “YB Dr Ong Kian Ming Deputy Minister of International Trade and Industry visits Huawei Malaysia Global Training Centre”, Huawei press statement, 15 April 2019.

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