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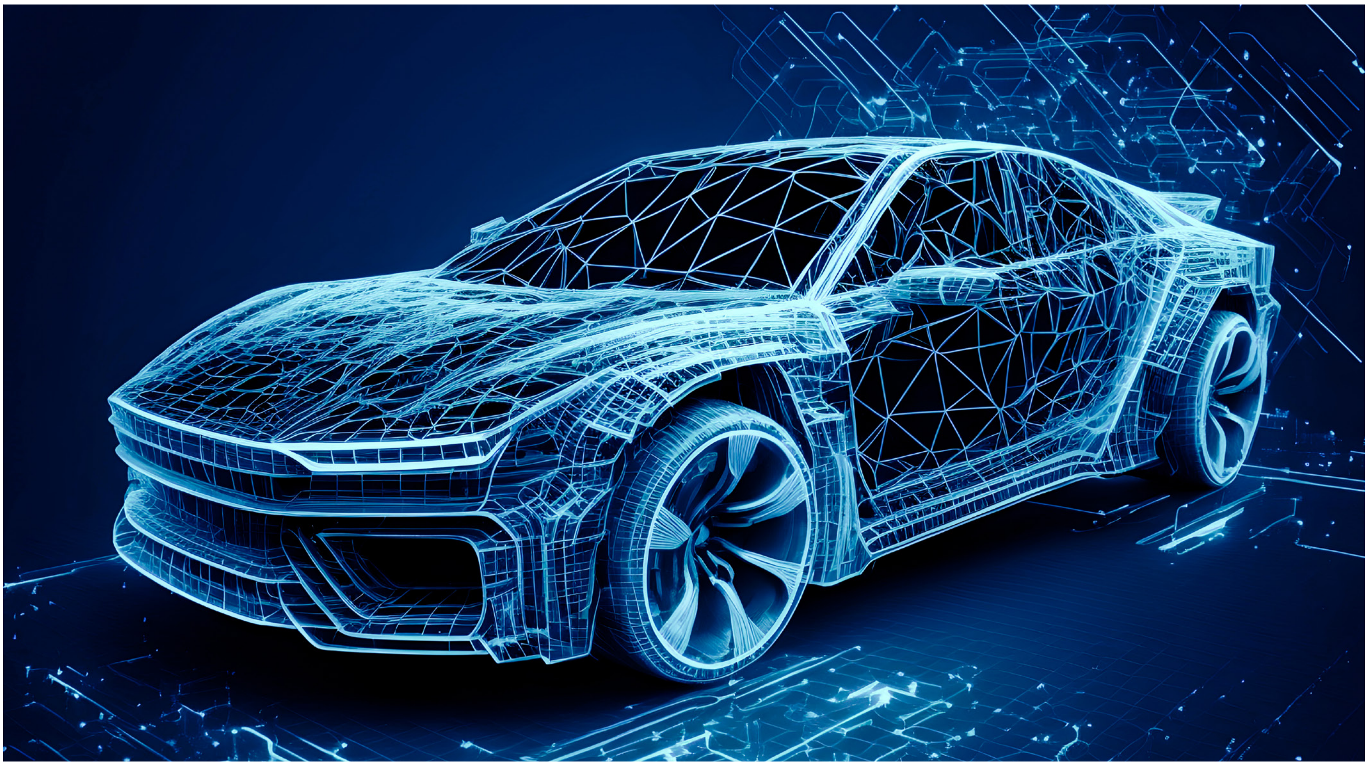
The Automotive Industry of Malaysia – A hidden champion and lucrative investment location



Malaysia is a country of cars. Against the stereotype of chaotic, overcrowded roads in Southeast Asian countries, traffic flows smoothly through Malaysia's extensive and ever-expanding highway system, making the car the preferred mode of transport for most Malaysians and resulting in one of the highest car ownership rates in the region.

Not only does the car play an important role in people's daily lives, it is also central to the Malaysian economy. The automotive sector generates around 4% of the country's GDP and employs some 700,000 people.

Malaysia's attractiveness as an automotive hub and preferred investment location was recently underlined when Tesla announced that it would set up its first office in Southeast Asia and new regional headquarters in Malaysia, choosing the country over several of its neighbours. This announcement came around the same time when also Geely reaffirmed its commitment to Malaysia as its primary hub in the region by pledging a major USD 10 billion investment in the country.

I. Malaysia's primary automotive industry

Malaysia's automotive industry is led by its two national car brands, Proton and Perodua, making it the only country in Southeast Asia to design, engineer, and manufacture cars from the ground up. But Malaysia is also a manufacturing and assembly hub for many more foreign brands. With a total of 27 car brands operating in the country and over 700,000 cars and commercial vehicles sold annually, Malaysia has the third largest automotive industry in Southeast Asia and the 20th largest in the world. Foreign companies such as BMW, Mercedes, Volkswagen, Toyota, Ford, Kia, Mazda, Mitsubishi, Nissan, Renault, Peugeot, and Subaru maintain long-established production activities through trusted contract manufacturers or joint ventures.

Other brands, such as Volvo or Honda, own and operate their own assembly lines in Malaysia as wholly foreign-owned companies and were allowed to directly manufacture passenger cars with engine capacities of less than 1,800 cubic centimetres (cc) from the beginning of 2014. Foreign manufacturers can also obtain production licences for pick-up trucks, hybrid and electric vehicles, and motorcycles with an engine capacity of more than 200 cc.

II. Strong component and supporting industry

Malaysia is not only host to many automotive manufacturers, but also has a strong and sizable component and supporting industry. Over 640 component manufacturers operate in Malaysia, including global brands such as Robert Bosch GmbH, ZF Friedrichshafen AG, Delphi Technologies PLC, Continental AG, Nippon Kayaku, PD Kawamura, Akashi Kikai Industry Co Ltd and Denso Corporation, catering to both local and regional demand.

Original equipment manufacturers and their suppliers can also rely on Malaysia's export-oriented and engineering heavy industries for support. In particular, Malaysia's globally significant electrical and electronics (E&E) industry (including a large and rapidly expanding semiconductor industry) and strong engineering support industries (including mould and die, machining, metal stamping and casting, surface engineering, heat treatment and forging) provide immediate supply and support to the automotive industry via short delivery routes.

III. Global connectivity

Malaysia's various industrial hubs and designated economic zones are well connected to each other and to the world through a modern and efficient highway network, several international and local airports and two major ports along the world's busiest shipping lanes.

Its central location between the South China Sea and the Indian Ocean, and a relative proximity to Australia and the Pacific Ocean, has fostered long and reliable trading relationships with all the major economic regions of the world.

These relationships have materialised in a dense network of free trade and investment agreements such as the ASEAN Free Trade Agreement (AFTA), the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) and the Regional Comprehensive Economic Partnership (RCEP). As a member of the Association of Southeast Asian Nations (ASEAN), Malaysian companies enjoy largely tariff-free and partially harmonised access to its population-rich and fast-growing neighbouring economies.

Malaysia generally maintains good relations with most countries in the world and holds a neutral position between rivalling powers such as the US, China, Russia, and India. This strategic political neutrality, coupled with its own political stability and established trade links, makes Malaysia an ideal location for supply chain diversification and alternative manufacturing hubs in line with supply chain de-risking strategies.

With the fastest median 5G speed in Southeast Asia, seamless and stable data exchange with all parts of the world is guaranteed, enabling remote access tools, advanced infotainment programmes and cloud computing solutions. Data protection regulations are loosely based on EU law and are generally fairly liberal, with no general mandatory data localisation requirements.

The digital industry has also been identified by the Malaysian government as a key industry for the overall development of the country's economy, and is supported by numerous incentives. This is particularly true for the automotive industry, where the government is focusing on research and development of Next Generation Vehicles (NxGV) and Mobility as a Service (MaaS) solutions. The use of Industry 4.0-related technology applications such as artificial intelligence, big data and the Internet of Things in the automotive industry is particularly encouraged and liberally regulated.

IV. Research and development, training, and workforce

The Malaysian government aims to further establish Malaysia as an automotive research and development (R&D) hub and offers several incentives, including special investment vehicles, grants, investment tax incentives and special visa types for R&D facilities.

Malaysia is home to several internationally recognised universities and research institutes with a focus on engineering. Collaboration between industry and universities is common and encouraged by the government. Active collaboration with local universities in exchange for easier access or grants can be part of individual investment agreements between investors and government authorities.

Malaysia's Technical Vocational Education and Training (TVET) system, which combines theoretical education with practical on-the-job training in industry, and special apprenticeship programmes of car manufacturers provides a steady supply of quality skilled workers and technical experts to the automotive industry and other sectors.

University and vocational graduates usually speak English at a professional level, have international and intercultural experience and can easily adapt to the corporate culture of investors. Despite these facts, the overall cost of labour is comparatively low, making Malaysia particularly attractive for investments that require a large number of skilled labour.

However, due to the high demand for engineers in the booming E&E industry, finding qualified staff can be a challenge in certain sectors and areas. Recognising this shortage and potential, the government is actively promoting engineering subjects and training programmes. As graduates and experienced professionals often favour foreign employers over local competitors, foreign investors are less affected by this partial shortage.

In addition, Malaysia does not only offer a strong, multicultural, and multilingual local workforce, but is also an attractive location for international talent. Its modern infrastructure and high standard of living, coupled with a comparatively low cost of living (and a cheap housing market), is a strong incentive for expatriates. Malaysia actively seeks to attract foreign talents with a sophisticated, liberal, and fully digitised immigration system that sets relatively low barriers to work permits for skilled foreigners.

Special visas are offered for investors and even freelancers in the IT and manufacturing (including automotive) industries.

V. Reliable investment climate

The strength of the Malaysian economy and automotive sector is also based on an open and liberal investment regime.

1. No general differentiation between foreign and local businesses, but sector-specific limitations exist

In general, Malaysia does not differentiate between foreign and local companies. No sector is completely closed to foreign investment and there is no general approval process for foreign investments.

Foreigners can easily set up a local company as an investment vehicle (usually a private limited company – a Sendirian Berhad) and are free to hold 100% of the shares.

However, certain restrictions on foreign ownership are imposed through licences and approvals required for specific business activities in order to protect particular parts of the industry, to encourage the participation of the local population (particularly the so-called Bumiputera – ethnic Malays and indigenous tribes) and to steer economic development.

Most activities in the automotive sector, including in particular the manufacturing of components and parts and related services, are not restricted and allow 100% foreign ownership.

However, for example, the import of Completely Built-Up (CBU) cars requires a special licence, which requires full or majority Bumiputera ownership (depending on the type of licence) and is further restricted by import and excise duties. The import of Completely Knocked-Down (CKD) vehicles is also subject to protective measures in the form of duties and some licensing requirements – although the assembly of foreign CKD vehicles was largely liberalised in 2014.

Major direct investment in restricted areas and direct imports at reduced or even no tariffs are still possible and can be negotiated with the relevant authorities. Malaysian investment agencies are supportive of foreign investors and can often broker investment agreements.

The government has recently announced that it will continue to liberalise the automotive sector and gradually remove the remaining protectionist measures to increase the competitiveness of the local industry and attract foreign investment.

2. Legal System

This liberal investment climate is backed by Malaysia's robust common law system, based on English law, which continues to have a strong influence on Malaysian law. English case law is often directly referred to and imported by the Malaysian courts. Malaysia's written laws are usually bilingual, with official English versions readily available.

Technical regulations for the automotive industry are frequently based on EU or UN law and follow international standards and norms.

The Malaysian judiciary is professional, independent, and generally not biased against foreign investors.

3. Full and unrestricted land ownership

Another significant advantage of Malaysia as a manufacturing location for foreign investors is the possibility for foreigners to obtain full and unrestricted ownership of land and buildings. Industrial land can generally be freely purchased and leased by foreign investors, with only certain areas of land reserved for Bumiputera enterprises.

In addition, comparatively low property prices, readily available land in industrial parks and a modern infrastructure are often a decisive factor for investors in land-intensive industries to choose Malaysia over other regional peers.

4. Administration

The legal framework is administered and implemented by a rapidly professionalising and digitising bureaucracy. In particular, the authorities responsible for economic hubs and foreign investment, as well as federal agencies and trade-related authorities, work efficiently and quickly. However, administrative processes in rural and less developed regions can be slower and less predictable.

In many cases, applications can be submitted and processed entirely online within set processing times. However, there are also cases where regulations or guidelines are deliberately opaque, or where authorities have wide discretionary powers, leading to uncertainty.

The most relevant authorities for the automotive industry are the Ministry of Investment, Trade and Industry (MITI), which oversees many general and technical approvals, and its subordinate Malaysian Investment Development Authority (MIDA) as the main investment agency; the Royal Customs Department (RCD), which oversees the importation of all goods and the administration of Malaysia's Sales and Service Tax (which may be due on importation); the Road Transport Department (RTD), which is responsible for, among other things, technical regulations and the homologation process, and the Department of Environment (DoE), which oversees environmental regulations, including emissions, but is also responsible for Malaysia's Low Carbon Mobility Blueprint 2021-2023, which, for example, provides incentives for electric vehicles.

Malaysia's government agencies tend to be interlinked, and redundancies are increasingly being eliminated in an effort to further streamline administration. For example, the importation of most goods can be fully managed through the Dagang Net portal. Applications for permits or import approvals, submission of customs declarations or manifests, applications for certificates of origin and payments to various authorities can all be handled through the same online platform using a single pre-registered account.

VI. The National Automotive Policy 2020

Malaysia's overall strategy for its automotive industry is set out in the National Automotive Policy (NAP). The current NAP 2020 serves as the general policy framework for the development of the sector until 2030. The NAP and its subordinate policies, strategies and roadmaps are regularly updated and amended to adapt to new technological developments and market trends.

The NAP 2020 formulates five key objectives of the automotive industry to be achieved by 2030:

- The establishment of Malaysia as a regional hub for the development and manufacturing of Next Generation Vehicles (NxGV);
- The expansion of the local automotive industry into the Mobility-as-a-Service (MaaS) industry;
- The promotion of the adoption of Industry 4.0 by the automotive industry;
- Ensuring that the entire ecosystem, including the industry and the population, benefits from the implementation of technological advancements; and
- The reduction of carbon emissions.

To achieve these objectives, the government is focusing on attracting foreign investment, local development of critical components and technologies for NxGVs, expanding the export sector for components and related services, increasing the competitiveness of the sector, strengthening the local skilled workforce, and promoting new environmentally friendly technologies.

VII. Incentives

To support the NAP and the general development of the automotive industry, Malaysia offers several incentives to local companies and investors.

Specific promoted activities[1] are supported by the so-called Pioneer Status, offering companies a partial exemption from the payment of income tax over five years, and by an Investment Tax Allowance, entitling companies to off-set a percentage of their qualifying capital expenditure incurred within five years from the investment against their statutory corporate income tax.

Additionally, grants for training and research and development activities and other individual incentives are available for the automotive industry.

Special incentives are also given for investments in specific areas such as Malaysia's Automotive Hi-Tech Valley in Tanjung Malim and for electric vehicles.

VIII. Electric vehicles and alternative fuels

As part of Malaysia's ambitious ESG (Environmental, Social, Governance) strategy, Malaysia has committed to becoming carbon neutral by 2050.

One of the key initiatives to achieve this goal is to develop and support the electric vehicle industry.

The government has therefore set up the Malaysian Electric Vehicle Task Force to facilitate policies and provide incentives for the electric vehicle industry.

These incentives include, for example, the full exemption of imported electric vehicles from excise, sales and import taxes until the end of 2025, while locally assembled electric vehicles and their components will be exempted until 31 December 2027.

The purchase and maintenance of electric vehicles by individuals is incentivised by full road tax exemption of electric vehicles until the end of 2025 and a tax relief for the installation of charging facilities at home.

Special tax incentives are also provided for the development of battery management systems, on-board charging systems, charging infrastructure, battery swapping technology and artificial intelligence. These include, for example, a full tax exemption for Malaysia-based manufacturers of electric vehicle chargers until 2032 and a full investment tax allowance for five years.

The government has also announced plans to install 10,000 charging stations across the country by 2025, as well as significant investment in clean energy to ensure a green power supply for large-scale electric vehicle use and industry growth.

In October 2023, the Malaysian government has announced its new Hydrogen Economy & Technology Roadmap as another element of its ESG strategy and as a first framework for the development of a hydrogen industry in Malaysia banking in the county's existing oil & gas infrastructure. While still at an early state, the initiative underlines Malaysia's interest in new technologies and offers opportunities for early investors to support the built-up of a Malaysian hydrogen industry and the utilisation of hydrogen as an alternative fuel.

IX. Summary

Despite strong regional and global competition, Malaysia offers a lucrative location for automotive investment, supply chain diversification and as a regional distribution and manufacturing hub.

Malaysia's liberal investment climate, strong support industries, established trade links, skilled workforce, low labour costs, availability of land and government support are strong advantages that make Malaysia stand out.

Although some restrictions remain to protect the local automotive industry, the country continues to liberalise its investment regime and is strongly committed to attracting investors, in particular, in all stages of the electric vehicle supply chain.

[1] Including the manufacturing of, inter alia, rubber tyres, petrochemical products, specialised machinery and equipment, semiconductors and related tools and services, ICT, infotainment products, energy equipment, batteries, and engineering plastic products, and industrial design services, research and development and other services.

While not the largest or most populous country in the region, Malaysia has direct and largely unrestricted access to all ASEAN economies and liberalised access to even more key markets through its dense network of free trade agreements.

Malaysia's mature automotive industry, progressive investment policies and world-class connectivity, should definitely put it on the map for investors in the automotive industry.

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