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THE DEVELOPMENT OF MEASURES AND INSTITUTIONAL OPERATIONS TO SUPPORT DIRECT INVESTMENT IN ASEAN ECONOMIC COMMUNITY OF SMES

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Abstract

The aim of this study is to examine the current Outward Foreign Direct Investment (OFDI) policy that promotes outbound investment of the Thai Small and Medium Enterprises (SMEs). By learning from the OFDI policy for SMEs in countries in which the role of SMEs and its economic structure are similar to Thailand, we can compare, formulate and improve our OFDI policy for SMEs. By doing so, we hope that the improved policy will stimulate more outbound investment that is consistent with the current changes in economic structure of Thailand. Four countries are used for our analysis - Singapore, Malaysia, Korea, and Italy. We find that the OFDI promoting and supporting policies in these countries are similar in nature and are not much different from investment theory. However, the largest differences are in the priority and the main focal point of each policy, depending on the country's institutional and organizational structures. Hence, it reflects the importance of how an appropriate policy is designed for a specific use.

Keywords: ASEAN, Thailand, SMEs, Outward Foreign Direct Investment

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Introduction

Thailand is facing an important structural change in its economic system from both domestic factors and regional forces. The domestic factors include a lack of operational workers, a wage rise policy, aging society, a lack of production factors and a transition to a middle-income country. All mentioned factors drive Thailand to move away from labor-intensive industries to skilled labor-intensive industries, technology-oriented industries and the service sector. At the same time, firms in labor-intensive and resource-intensive industries have to invest abroad to seek for necessary resources.

Furthermore, there are external driving forces resulting from several changes in regional policies. The crucial regional policies worth mentioning are trade liberalization and economic reforms in the Greater Mekong Subregion (GMS) countries, several trade agreements and economic cooperation programs in the region such as ASEAN Economic Community (AEC), and the transition in Myanmar which increase intra-regional connectivity together with trade and investment facilitation. Such changes bring about the creation of co-production bases in the region and the relocation of labor-intensive process to developing ASEAN countries which force Thai enterprises to move out accordingly.

The above mentioned domestic and regional driving forces push Thailand to become a source of investment instead of an investment recipient country. However, Boonprakaikaw and Cheewatrakoolpong (2014) point out that Thailand still has lower outward FDI performance than many ASEAN counterparts due to a lack of outward FDI promotion policy. Thailand just appointed the Board of Investment of Thailand (BOI) to be a responsible agent for outbound investment in 2013.

Moreover, Cheewatrakoolpong et.al. (2013) found that the Thai SMEs face more obstacles when investing abroad than the large enterprises due to a lack of information regarding investment law and regulations in the host countries, financial inaccessibility, insufficient infrastructure and facilities and a lack of investment promotion and facilitation policies.

Even though Thailand has appointed the BOI as a responsible agent for outbound investment, the role of the BOI is limited to provide investment information and facilitation to Thai investors. There are no promotion policies such as tax incentives which are implemented by most developed countries. Also, the BOI does not have outward FDI promotion and facilitation policies that specifically aim to help SMEs.

As a result, this paper aims to study the outward FDI promotion policies for SMEs. We will start to consider the outward FDI promotion policies for SMEs in the selected countries and compare their policies with the Thai ones. We will also consider the demand for outward FDI promotion policies of Thai SMEs. Finally, we will propose the suitable outward FDI promotion policies for SMEs in Thailand to increase outward FDI performance of Thai firms and stimulate outbound investments in line with Thailand's structural changes.

Objective of the Study

The main objective of this study is to examine the current outward foreign direct investment (OFDI) policy that promotes outbound investment of Thai small and medium enterprises (SMEs)

Methodology

Our methodology can be divided into 3 parts as follows.

1. Data Collection

1.1 *Secondary Data*: We collected related secondary data including statistics, previous literature, outward FDI related policies from relevant government agencies of Thailand and outward FDI promotion policies of selected countries.

1.2 *Primary Data*: We collected primary data from the two following sources: (1) interviews with relevant stakeholders in Thailand, and (2) interviews with relevant stakeholders in the target areas including Yangon, Myanmar and Ho Chi Minh city, Vietnam.

1.3 *Focus Group*: We organized the focus group of 15 people with relevant stakeholders including representatives from the government agencies, private sector, related organizations and researchers to design outward FDI promotion policies for SMEs of Thailand.

2. Data Analysis

2.1 *Analysis of the demand for Thailand's outward FDI promotion policies for SMEs*: We employ the push-pull factor framework to analyze the demand for Thailand's outward FDI promotion policies for SMEs using primary and secondary data collected in Section 3.1.

2.2 Analysis of the supply of Thailand's outward FDI promotion policies for SMEs: We employ the supply chain framework that considers outward investment as a main product/service in the supply chain. We will analyze each stage of the services to support outward investment and related government agencies. We also consider frictions that occur, related rules and regulations and lacking policies or authorities.

2.3 Gap analysis between Thailand's current outward FDI promotion policies and the selected countries' policies: We will use the gap analysis to compare Thailand's outward FDI promotion policies for SMEs with those policies implemented by the selected countries.

3. Policy Recommendation

From our analysis of the demand for and supply of Thailand's outward FDI promotion policies for SMEs together with the gap analysis between Thailand's current outward FDI promotion policies and the selected countries' policies, we propose recommendations for the suitable Thailand's outward FDI promotion policies for SMEs and the responsible government agencies for each task.

The Roles of SMEs in Thailand's Economy

SMEs have played an important role in Thailand's economy. In 2014, there were 10.49 million workers employed SMEs or 80.63% of overall labor force. SMEs produced output of 2.06 trillion baht or 45.88% of GDP. SMEs consisted of 2,722,854 firms, of which 99.28% were classified as small-sized enterprise and only 12,778 firms were classified as medium-sized enterprise (Table 1).

Table 1: Number of Employment and Enterprises in Thailand in 2014

Size of Enterprises	Number of Employment (person)	Percentage of Employment	Number of Enterprises (firm)	Percentage of Enterprises
Small and Medium-sized Enterprises (SMEs)	10,496,177	80.63	2,735,632	99.74
Small-sized Enterprises (S)	9,523,770	73.16	2,722,854	99.28
Medium-sized Enterprises (M)	972,407	7.47	12,778	0.47
Large-sized Enterprises (L)	2,521,642	19.37	7,009	0.26
Total (S+M+L)	13,017,819	100.00	2,742,641	100.00

Source: The Office of Small and Medium Enterprises Promotion (OSMEP)

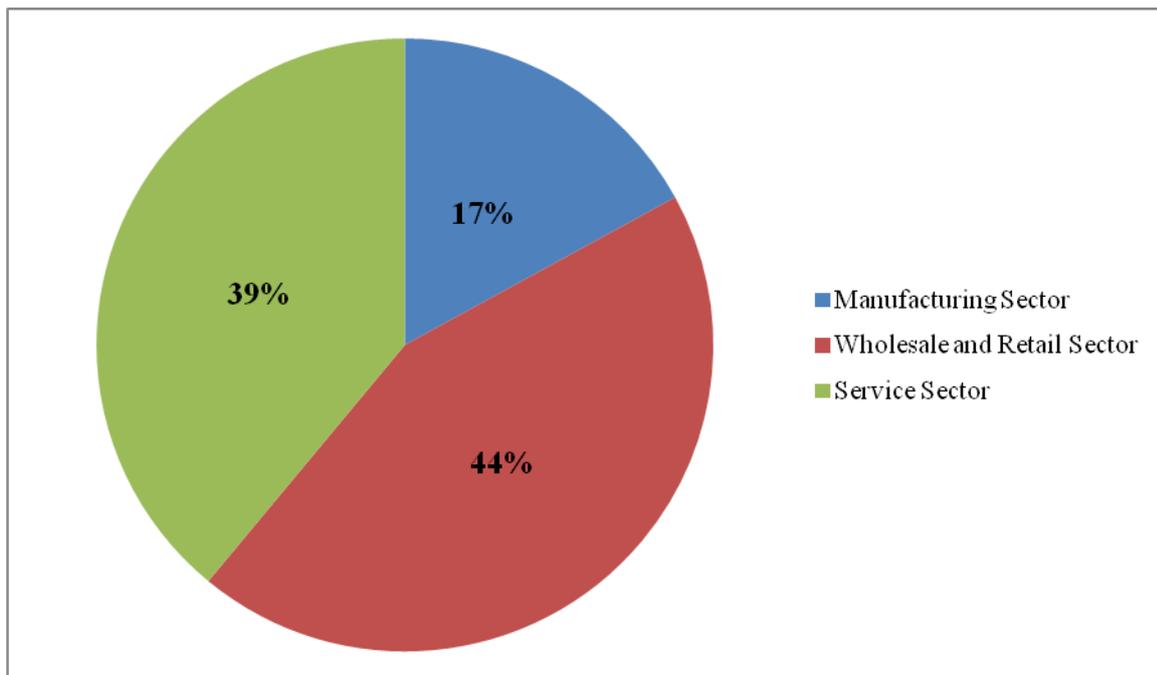


Figure 1: Percentage of Business Sector in Thailand

In addition, 17%, 44% and 39% of SMEs were in manufacturing, wholesale and retail, and service sector respectively (Figure 1). According to the Office of Small and Medium Enterprises Promotion (OSMEP), SMEs' output has grown faster than the overall GDP and will play larger role in Thailand's economy. SMEs in Thailand are highly competitive in food, automotive and parts, garment, packaging and design, jewelry and agriculture machine.

Analysis of Outward FDI Promotion Policies for SMEs in the Selected Countries

We start with selecting 4 countries, 2 ASEAN countries and 2 non-ASEAN countries, to be our model for designing Thailand's outward FDI promotion policies for SMEs. Our selection criteria are composed of 3 steps. First of all, we use the UNCTAD's outward FDI performance index in 2013 to select countries with good outward investment performance. Second, we consider the countries with outward FDI promotion policies made specifically for SMEs. Lastly, we consider the countries that have a similar economic structure to Thailand, especially before the implementation of outward FDI promotion policies. Using those criteria, we pick Singapore and Malaysia as our selected ASEAN countries and Korea and Italy as our selected non-ASEAN countries.

We found that outward FDI promotion policies in other countries are usually made for large enterprises. The countries that have outward FDI promotion policies specifically for SMEs are the ones that already have had successful multinational enterprises such as Singapore and Korea or the ones that SMEs are very crucial for their economies such as Italy and China. Many countries such as Japan and Malaysia choose to have the policies to strengthen their domestic SMEs without the policies to promote their SMEs to invest abroad.

Most of the countries that have outward FDI promotion policies specifically for SMEs concentrate on financial assistance and information assistance since asymmetric information and financial accessibility are the main obstacles for SMEs to invest abroad compared with large enterprises.

Considering Singapore, outward FDI promotion policies for SMEs are in forms of financial assistance, information assistance, and business matching with foreign partners and Singaporean large enterprises. In case of Malaysia, the policies include encouraging financial institutions to grant loans to the SMEs that invest in ASEAN countries, supporting bilateral joint cooperation of Malaysian SMEs with domestic companies in the host countries, and establishing industrial linkages and trade linkages between Malaysian SMEs and Malaysian large enterprises.

As for Korea, the government assists Korean SMEs to invest abroad by providing special loans, offering capacity building program and assisting selected SMEs to invest in the target host countries by providing offices and supporting services such as law, accounting and marketing.

Finally, Italy's outward FDI promotion policies for SMEs are concentrated on financial assistance such as special loans, venture capital, loan guarantee and financial assistance for related activities such as exporting.

Analysis of the demand for outward FDI promotion policies for Thai SMEs

The "OLI" or "eclectic" approach to the study of foreign direct investment (FDI) was developed by Dunning (1977). "OLI" stands for Ownership, Location, and Internalization, three potential sources of advantage that may underlie a firm's decision to become a multinational. Ownership advantages address the question of why some firms but not others go abroad, and suggest that a successful multinational enterprise (MNE) has some firm-specific advantages which allow it to overcome the costs of operating in a foreign country. Location advantages focus on the question of where an MNE chooses to locate. Finally, internalization advantages influence how a firm chooses to operate in a foreign country, trading off the savings in transactions, holdup and monitoring costs of a wholly-owned subsidiary, against the advantages of other entry modes such as exports, licensing, or joint venture.

Using Dunning's (1993) OLI paradigm and UNCTAD (2006) as the analytical frameworks in our in-depth interview, we divide the determinants of outward FDI into push and pull factors. By grouping the SMEs into two groups – manufacturing-related and services-related, we find that the determinants and obstacles for Thai SMEs' outbound investment are different depending on the types of business. Their needs for outward FDI supporting and promoting policies from the government are also different.

In the manufacturing-related SMEs, the main push factor is the increase in labor wage. The problem is amplified by the severe scarcity of unskilled-labor and the termination of the special trade privilege. Service-related SMEs are not affected by the same problems. The main reasons for outbound investment for this group are the fierce competitive environment in the service sector of the domestic market and the owner advantage of Thai SMEs over neighboring countries.

The outside or pull factors are also different between these two groups. While the larger foreign market and cheaper production cost are the main attractive features for the manufacturing-related SMEs, service-related SMEs are pulled by the demand from their clients to invest in foreign market.

Although both groups have different motives for outbound investment, their problems and obstacles are quite similar. Lagging and scattered investment and in-depth business information in foreign market is a major problem. We find that the lack of coordination between private and government agencies contributes to this problem. The main obstacle for investing in foreign market is the frequent changes in investment laws and regulations in the host country.

From the fore mentioned problems and obstacles, we find that SMEs believe that the government can help facilitate the outbound investment of the Thai SMEs by, first, clearly determining the direction of outward FDI, and forming coherent supporting and promoting policy, as well as specifying which types of business government should support. In terms of the outward FDI promotion policies for Thai SMEs, SMEs need support in gathering consistent investment and in-depth business information, and in finding reliable business investment legal advisor.

For the policy to be effective and beneficial to Thai SMEs, government need to be consistent. The continuity and consistency of the supporting and promoting policies is important for sustainable development of Thai SMEs.

Analysis of Thailand's Outward FDI Promotion Policies for SMEs

In Thailand, the public policies were made underlying the economic competitiveness through stimulating the Outward Foreign Direct Investment for Small and Medium Enterprises, presently. The essential scheme's promoters are composed of (1) The Board of Investment of Thailand (BOI), (2) Export-Import Bank of Thailand (EXIM Bank), and (3) Office of Small and Medium Enterprises Promotion (OSMEP). Particularly, setting the strategic planning is the authority and function of OSMEP.

In accordance with the strategic scheme, OSMEP rounds up all of respecting small and medium enterprises every five-year since 2002. This statistics aforementioned expose various enterprises' dimensions-related operated by specifically developing achievement. In addition, "the fourth-strategy encouraging linkage's capabilities of small and medium enterprises among the international economy" also fosters exportation, mergers and acquisitions along with other treaties or agreements not only the overseas affiliates.

Contemplating upon the fourth of strategy, the performance measure consists of two substantial ingredients; (1) the intellectual augmentation of small and medium businesses in the context of free trade and overseas investment, (2) the increased opportunities of the intercompany transactions. Thus, both of these crucial elements are involved with the foreign shareholding networks.

On the ground of this investigation, regarding to OSMEP's outline with supporting the competencies of small and medium enterprises, the study is compiled by assorted institutions-concerned then it expresses abundant of schemes association scattering in many parts of government services. Seeing that Thai government service's structure is classified through the affairs not the missions, the outward foreign direct investment of small and medium enterprises is not preliminary recognized in bureaucracy, consequently the later expansion resulted in plentiful dispersion. Nonetheless, these platforms widely benefit to policies' operating diffusion and precisely proper to each specialization. In contrast, the more publicized, the harder cooperated and coped with any problems, especially in the case of the state agencies face with their inadequate efficiency.

Considering to the core missions of Thai agencies, almost reveal the commencement of OSMEP's strategy. Provide with the oversea investing information is the first priority followed by the seminars or work shop training led more specific than notifying knowledge. Nevertheless, the administrations still discord with entrepreneurs' requirements as well as the dispersed operation system.

Furthermore, some bureaus' interviews seem not to be harmonizing in the conventional associations by the way the agencies appear the obscure synergy. Notwithstanding, the significant issues, neither the basal manifesto nor business partnerships are demonstrated the forthcoming promotions for their affiliates aboard. Currently, the state agencies administrate only assisting in either SMEs or OFDI, not the both of SMEs and OFDI measure sustenance. In other words, there is none of the state agency simultaneously dominating the both of SMES and OFDI.

Conclusion

This study uses "Gap Analysis," which is frequently used to evaluate government policy. The gap is the difference between the demand for OFDI supporting policy from private sector and the supply of currently implemented OFDI policy from government.

On the demand side, we find that to alleviate problem and obstacle from investing abroad, SMEs in manufacturing and service sectors need different promoting and supporting policies, but both have mentioned in-depth business information as a crucial priority. On the supply side, we find that there is no direct organization or agency taking care of OFDI nor policy focusing on SME's OFDI. Although there are many agencies involved in procedure related to either promoting OFDI or helping SMEs, they are doing the same thing.

The solution that we propose is to promote the cooperation and coordination between existing agencies. We believe that the core agencies responsible for SMEs' OFDI should be the Office of Small and Medium Enterprise Promotion (OSMEP) and the Board of Investment of Thailand (BOI) since their focal obligations are to support and promote SMEs, and provide assistance for investors and facilitate FDI, respectively. While other involved agencies such as the Revenue Department, Commercial Banks, the Neighbouring Countries Economic Development Cooperation Agency (NEDA), the Thai Chamber of Commerce, the Federation of Thai Industries, Ministry of Commerce, and Ministry of Industry should be supporting agencies.

In addition, we also propose the following five SMEs' FDI promoting polices and the authorized agencies involved. The Revenue Department and BOI should be responsible for providing tax incentives. OSMEP, Commercial Banks, SME Bank and EXIM Bank can help the SMEs in terms of funding. Due to their official roles in other countries, government agencies and private sectors can help collecting and clarifying the in-depth business information needed by the SMEs. The BOI and NEDA can give aid to the neighboring countries in terms of building infrastructure needed for our outbound investment.

Policy Recommendations

The policy recommendations for Thailand's outward FDI promotion policies for SMEs and responsible government agents are as follows;

1. Designing Thailand's outward FDI promotion policies for SMEs

We divide the suitable Thailand's outward FDI promotion policies for SMEs into 5 categories, namely, tax incentives, financial assistance, information assistance, infrastructure assistance, and other policies. The recommended policies and corresponding agents can be summarized in Table 2.

Table 2: Policy Recommendations for Thailand’s outward FDI promotion policies for SMEs and responsible government agents

Type of Policies	Recommended Policies	Responsible Agents
Tax Incentives	150-200% tax deductible for eligible expenditures such as oversea project feasibility study expenses and oversea market research expenses.	Revenue Department and BOI
	Exemption of income tax from foreign sourced dividend and foreign branch profits.	Revenue Department
	Improvement of double taxation treaties to cover all related agents.	Revenue Department
Financial Assistance	Increasing financial accessibility of SMEs that invest abroad via new financial products and loan guarantees.	OSMEP and Commercial Bank
	Special loans with privilege interest rate for potential SMEs.	Commercial Bank
	Partial financial support of the eligible costs of selected activities such as market surveys and feasibility studies.	OSMEP and SME Bank
	Partial subsidy of insurance against political risks.	EXIM Bank
Information Assistance	Establishment of a one-stop service to provide related information and synchronization of the online database.	BOI
	Providing in-depth information such as market research by sector, trade and investment laws and regulations in the selected host countries.	BOI, Ministry of Commerce and Ministry of Industry

Type of Policies	Recommended Policies	Responsible Agents
	Establishment of industrial clusters among SMEs that want to invest abroad.	BOI, Thai Chamber of Commerce and Federation of Thai Industry
	Establishment of baby-sitting system using experienced investors in the selected host countries.	Thai Chamber of Commerce and Federation of Thai Industry
Infrastructure Assistance	Assisting selected SMEs to invest in the target host countries by providing offices and supporting services during the first 3-5 years.	BOI and NEDA
Other Policies	Establishment of scoring system to evaluate the SMEs that are strong enough to invest abroad.	OSMEP

Source: Author's policy recommendations

2. Designing responsible agents for outward FDI promotion for SMEs

For the plausible synergy, there has to be divided in three parcels; the major, the major's backup, and the supporter. To beginning with the major, it is comprised of two academies; (1) Office of Small and Medium Enterprises Promotion (OSMEP) handling the strategic planning and cooperating with SMEs developed associations undertaken by the public policy and its executive power, and (2) The Board of Investment of Thailand (BOI) continuing its reputation as a result of the experiences among international collective actions for a period hence negotiation and data achievement belong to the BOI's competencies.

Meanwhile, the other five supporters dealing with the SMEs' measurement; (1) Revenue Department functions as considering the tax incentive and process, efficiently, (2) Commercial Bank performs as SMEs financial booster together with OSMEP electing the high potential SMEs conformed to the country and bank advantages, (3) Neighboring Countries Economic Development Cooperation Agency, Public Organization (NEDA) executes as the fundamental construction's promoter in the neighbor countries responding to SMEs' requests, (4) The Thai Chamber of

Commerce and Board of Trade of Thailand and the Federation of Thai Industries, in the status of entrepreneurship they have to participate in the director of SMEs' outward-investing likewise the important state measures, and the last but not least (5) Ministry of Commerce and Ministry of Industry conduct the entrance of SMEs business-engagement by subsidizing knowledge improvement together with the other agencies related to OSMEP's strategic target.

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