EE551 Selected Topics in International Economics 1 &

EE561 Selected Topics in Development Economics 1

Why do investors shift production base from Thailand to Vietnam?

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ABSTRACT

The purpose of this research is to identify reasons *"Why do investors shift production base from Thailand to Vietnam?"*. In our research provides relevant indicators which involved economic, labor, politic and technology, all indicators were conducted in both Thailand and Vietnam sides. In order to support our information, this research supplied an interview about Toyota Motor Corporation. It appears that Vietnam is significantly better than Thailand in terms of human resource and economic growth. Moreover, this research highlights information that could help investors to make a decision choosing location of production base.

CONTENT

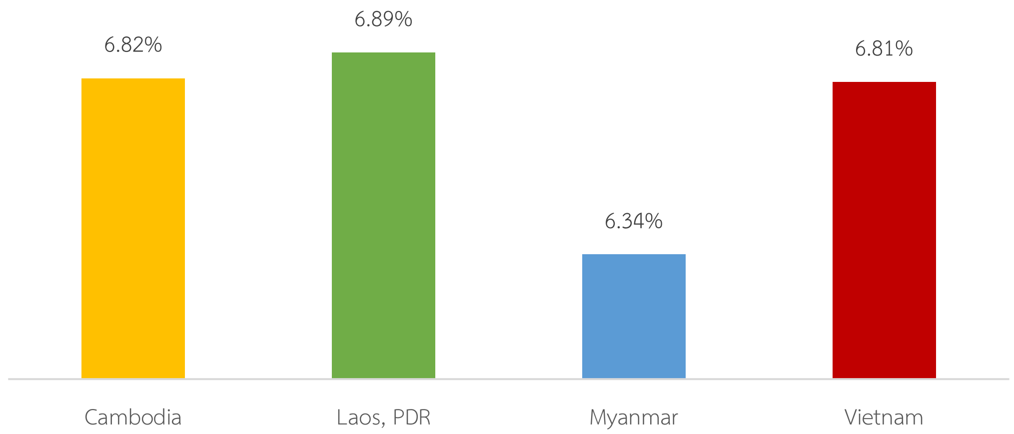
INTRODUCTION

"The business changes. The technology changes. The team changes. The team members change. The problem isn't change, per se, because change is going to happen; the problem, rather, is the inability to cope with change when it comes."

\- *Kent Beck*

The ultimate goal of committing in a business is to maximize profit and stakeholder's interest. However, the business arena is fluctuating. With the growing numbers of competitors and shifting in business environmental, the world of conducting a business becomes brutally. As time passed by, the barrier to entry in each industry became weakened. In order to survive in this aggressive arena, the firms must seek the way to optimize their operation and production base to ensure and smooth their net income. Theoretically, the major factor of production is capital and labor. However, in reality, the complexity of doing a business encounter various of factors for example; regulation, taxes environment etc. The player in the global arena must utilize this factor to effectively and efficiently operating a business. Unsurprisingly, many companies have shifted their production base from a country to another country in order to grip the trend offered by those countries for example; tax heaven and low wages etc. Currently, the rising stars and dark horse country is Vietnam. Vietnam is locating along Mekong river with Cambodia, Laos PDR and Myanmar. The regional economic outlook among CLMV countries will be analyzed in next session.

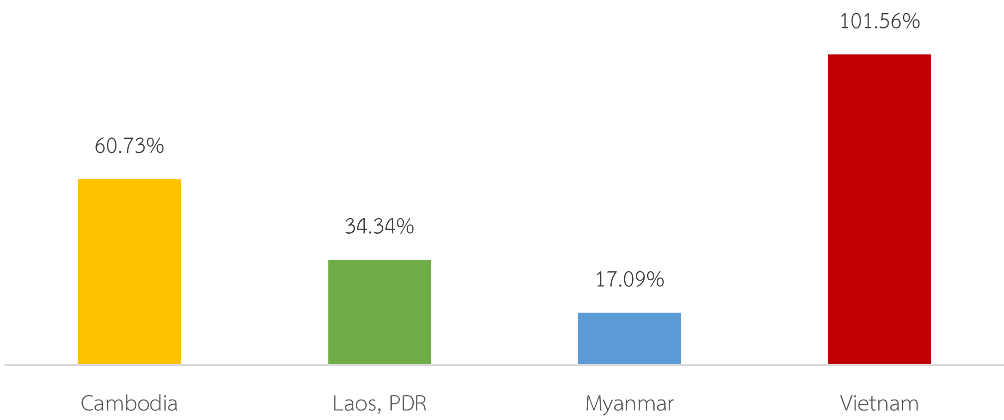
Figure 1: GDP growth (annual%) in 2017



Source: World Bank

The graph presented above indicates Gross Domestic Product growth among CLMV countries as of 2017 (Figure 1). As can be seen, all CLMV countries register strong economic growth. The main driven factors are FDI inflows, infrastructure development and improvement in global demand. As can be seen from the graph presented above, Vietnam's GDP growth was accounted for 6.81% which is slightly lower than LAOS, PDR and Cambodia which yielded 6.89% and 6.82% respectively. However, Vietnam's economic continues to expand in bright area and indicates sustainable economic growth and development due to external and internal demand. The domestic consumption in Vietnam continues to expand boosted by middle class population. Moreover, strong FDI inflows especially mobile phone and electronic segments is the main factor driven strong economic growth in Vietnam. In the other hand, Cambodia's economic growth is driven by export especially garment industry and domestic expenditure. While, Laos PDR is supported by investment in hydropower and transportation sectors.

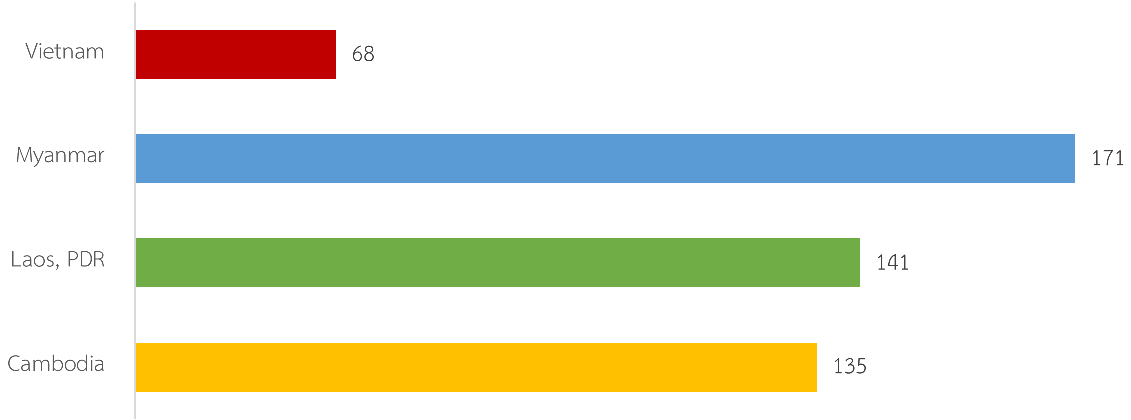
Figure 2: Exports of goods and services (% of GDP) in 2017



Source: World Bank

The figure presented above (Figure 2) indicates export of goods and services as a percentage of GDP among CLMV countries as of 2017. Key takeaway from this indicator is the level of Gross Domestic Product in Vietnam are strongly correlated with the level of export. As can be seen from the chart, the level of export is accounted for 101.56% of GDP. The improving in global market demand and its expansion indicates the positive signal to Vietnam economy. The key success of Vietnam's export sectors which dominates large proportion to GDP are mobile phones, electronic devices and footwear. Moreover, Vietnam status in global market is highly successful. From the fact that, Vietnam's trading attains prosperous in diversifying their market. Its trading is less concentration with one particular countries. From this reason, the risk of declining in export revenue of Vietnam is low from its diversification in global market.

Figure 3: Ease of Doing business index in 2017

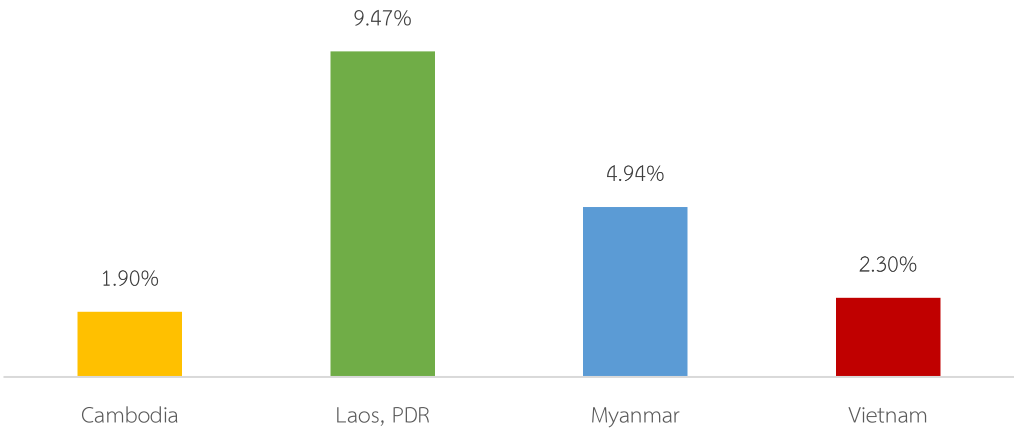


Note: 1=most business-friendly regulations

Source: World Bank

Ease of Doing business is one of the key variables in business decisions in that country. Assessing the level of ease of doing business or conducting business in the country often depends on the ease of starting a business, running business and when business problems. Ease of Doing business will consider the step and duration of services, facility costs, operating costs and how government regulation support business. According to Ease of Doing business index in 2017 (Figure 3), Vietnam was ranked in the top 68 of 190 countries, as a result of improving its business environment throughout the year to increase its business facilities. On the other hand, Cambodia, Laos PDR and Myanmar still have difficulty in doing business. Their rank is around 100 onwards, which also show that they still do not change the measures and structures to attract investors.

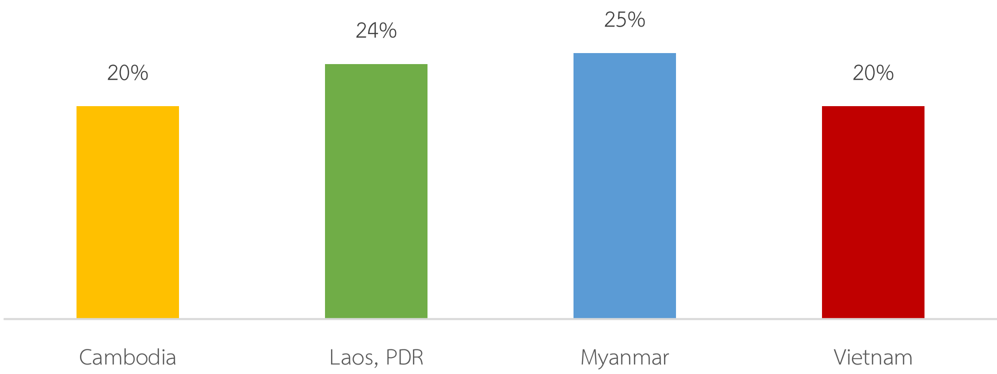
Figure 4: Total natural resource rent (% of GDP) in 2017



Source: World Bank

Natural resources can be viewed as abnormal or supernormal profit theoretically. However, it may reflect the underdeveloped in economic status within economy since practically, the countries cannot utilize and gain the maximum advantages from their given natural resources. The graph presented above (Figure 4) is the proportion of natural resources rent to total GDP. As can be seen, Vietnam obtain 2.30% of GDP as natural resources lower than Laos, PDR and Myanmar which obtain 9.47% and 4.94% respectively.

Figure 5: Corporate Tax Rate (%) in 2017



Source: World Bank

Vietnam's corporate tax in 2017 is 20%, which is equivalent to Cambodia and also Thailand. Due to the graph presented above (Figure 5), Laos PDR and Myanmar have higher percentage of corporate tax rate, which is 24% and 25%, respectively.

LITERATURE REVIEW

With the ultimate goals to achieve sustainable economic growth, the new FDI strategy which will mainly focus on quality rather than quantity of the investment will be implemented in 2018 – 2023. The new era of FDI in Vietnam would be drafted targeting to penetrate manufacturing, services, agriculture and travel industries. The draft will not only focus on medium term but also short-term basis. In short term basis, manufacturing and environmental-friendly technology will be prioritized since its opportunities for competition is limited. In the other hand, medium term basis, skill-development among manufacturing, services and information technologies& intellectual services will be prioritized to ensure stable economic strength. However, massive transformation in Vietnam's labor market is required. Moving from low labor cost economy to skilled labor is inevitable. Moreover, one key success factor in this strategy's implementation is infrastructure. However, the proposal about infrastructure development is not mentioned in new FDI strategies. Lastly, this strategy lured the international firms with exemption or reduction in corporate tax but not domestic firms. Surely, domestic will be suffered by this strategy. Therefore, the government should also seek to balance domestic and international firm's interest. (Dezan Shira, 2017)

FDI has made an important positive contribution to the transition of Vietnam. FDI helps in many aspects of Vietnam such as from a socialist to a market economy and from traditional like agricultural sector to a modern or industrial economy. from this paper, there are still several problems that Vietnam need to solve in order to attract FDI into the country. For example, lack of infrastructure, legal environment and interdependence of foreign investments and foreign investment policy with the large state sector. Since Vietnam has low income level, the infrastructure in Vietnam is not well distributed. Although government try to promote the development of infrastructure like promoting industries in shortage of infrastructure facilities, it creates inefficiencies and unnecessary costs. Next problem is about bureaucratic system. Some still use the same old methods from socialist system. Before, people thought that interdependence is bad thing but actually contacting with other countries brought them many benefits to country for example knowledge and technology which make your country prosperity. As the quote “big fish swallow little fish” is wrong. The objective fact is rise and fall of countries depend on domestic policy of each country as the evidence from Vietnam, Laos and Cambodia so country should improve human resources, sharing factors that rise up the power of development which are national culture, national values and national policy and people need to renovate mindset. (BOI, 2013)

THEORETICAL FRAMEWORK

When one firm has an interest in investing in one country: they will concern about advantages and disadvantages of that country. For the country’s advantages we called it “country-specific advantages”. Some scholars proposed the definition of “country-specific advantages”, Rugman thought it mainly came from the country’s natural resources endowments, labor resources and related cultural factors, including the quality and quantity of the main production factors, but this concept has not been systematically studied and developed. Another scholar, Pei thought that the home country was the cornerstone of a country’s foreign investment enterprises, which provided the basic conditions for national economy. Different conditions of home country created their own trade advantages, scale advantages, location advantages, organizational advantages and other specific advantages, which formed diversified business advantages for domestic enterprises to participate in overseas investment. Broadly speaking, CSAs are the advantages of a variety of country-specific resource allocation or unsynchronized uneven all over the country and forms a national comparative advantage. Country-specific advantages are all kinds of proprietary resources that a country has, and can be freely available to any business; it is a system that all the firms can share the advantages. This is a kind of comparative advantage that formatted by the uneven distribution of resources all over the country, and it plays an important role in the accumulation of corporate resources. (Scientific Research Publishing, 2016)

Country-specific advantages consist of two factors which are called “Push factors” and “Pull factors”. Push factors and pull factors were originated from Globalization, economic crises, political instability, conflicts, civil wars, ethnic cleanings, social inequality, the development of market economy, gender discrimination, the wider processes of transformation, especially this last ten years, made a solid soil for huge wave of migration in the world, and for its mutated form– trafficking in human beings. Globalization has changed the way many people see the world. As people become more aware of living standards and lifestyles in other parts of the world, for example through television or the stories (and sometimes wealth) of returning expatriates, their understanding of their ‘‘relative’’ poverty has increased and their expectations have changed. This motivates people to migrate to secure greater income. There is also evidence that young people in particular consider migration because they want to escape the drudgery of subsistence living and see ‘‘the bright lights of the big city’’. Many poor people tried to find a better life using illegal measures to cross borders with the help of criminal networks. The forces of economic globalization described above foster strong push factors in migrant’s countries of origin, such as economic dislocation and increased absolute and/or relative poverty rates. These hardships motivate millions of persons to seek economic opportunities abroad in order to maintain or regain their economic positions. In addition, high levels of economic and political instability and the experience of economic crises provide an incentive for families to reduce their overall economic risk by diversifying their sources of earnings across multiple countries. At the same time, destination countries exhibit important pull factors, such as significantly higher wages and a demand for migrant workers to perform low-wage (or otherwise undesirable) jobs. This is true in both developed countries and relatively wealthier developing nations, such as Thailand and Mexico, many of which serve as major countries of origin and destination for migration. In addition, the demand for migrant workers is often exacerbated by demographic changes, as declining birth rates in developed countries lead to shrinking populations with a growing ratio of elderly to working-age people. (Belgrade, 2012)

Those factors appeared on both sides, in the countries of origin and in the countries of destination. In the countries of origin those factors are called push factors, and in the countries of destination pull factors.

Push factors are the influences that drive people in one country emigrate or move from their home country to other countries such as abroad investment policies and banking support, lacking of jobs, poverty, low quality life. While pull factors are the circumstances which attract foreigners, outsiders and migrants such as foreign investment policies, natural resources, political stability, economic growth, labor cost and stable exchange rate.

Since we are considered why do investors shift production base from Thailand to Vietnam: company that we interested are Samsung and LG. Samsung and LG originated from South Korea. In this case our countries of origin are South Korea while countries of destination are Thailand and Vietnam.

RESEARCH METHODS

Economic

- ***Gross Domestic product (GDP)***

In year 2017, Thailand's annual GDP growth is 3.915% while Vietnam achieve superior in economic growth accounted for 6.81% in year 2017. The main driven factors affecting Thai economy in 2017 are Trump's trade protectionism, China's slowdown and political uncertainty in Europe. These external risks affect the Thai's level of export to underperform. Furthermore, it direct and indirectly distress Thailand overall economy not only by declining in incomes of exporter, farmer and overall manufacturing production but also sending a negative impact toward domestic consumptions. Meanwhile, Vietnam's economy has been in progressive path. As its domestic consumption is enhancing due to middle class population. Additionally, its overall economy is appreciating with FDI inflows from mobile phone and electronic sectors. Moreover, according to national transportation plan, Vietnam's FDI potential to attract further FDI in hospitality sectors and infrastructure projects is high.

- ***Import and Export***

For the import of goods and services in 2016 using unit of current USD, Vietnam has imported $186.929 Billion where Thailand has imported $220.486 Billion. For export side in 2017 with the same unit, Vietnam has exported $227.245 Billion where Thailand has exported $310.757 Billion. Amount of import and export shows the trade between one country and the rest of the world. From import and export of goods and services data above, it indicates that Thailand has more transactions than Vietnam.

Annual growth of import of goods and services in 2017, Vietnam has grown for 15.285% while Thailand growth was -1.359%. Annual growth of export of goods and services in 2017, Vietnam has grown for 13.863% while Thailand growth was 2.068%. Annual percentage growth of import and export shows the change in amount of transactions comparing the year before (2016) and current year (2017). From the import and export of goods and services annual growth data, surprisingly Vietnam has higher percentage growth than Thailand.

- ***Inflation rate and real interest rate***

According to fisher equations, there are two components within nominal interest rate which are real interest rate and inflation rate. In order to precisely measure the real adjusted returns in each country, the analysis would be conducted based on fisher equations. The equation states that nominal interest rate is equal to the summation of real interest rate with the inflation rate. Theoretically, real interest rate reflects real cost of required fund or real return yield from investors point of view while inflation refers the percentage rising of level of prices of goods and services in a country. According to the graph above which represent comparison of real interest rate and inflation rate between Vietnam and Thailand, Vietnam real interest rate is 3.15% which dramatically higher than Thailand's which accounted for 2.06%. This reflect the superior returns of investing in Vietnam compared to Thailand. In the other hand, Vietnam inflation rate in 2017 is 3.52% while Thailand's inflation rate is 0.67%.

Labor

In labor sector, labor in Vietnam average monthly wage rates in 2017 was 7,270 Baht/month while Thailand average monthly wage rate was 13,721 Baht/ Month.

Labor force in Vietnam in 2017 was 57 million people where Thailand was 39 million people. Moreover, number of working hours in 2017, in Vietnam was 8 hours while Thailand was 7 hours which is 1 hour less than Vietnam.

Vietnam has advantage over Thailand in terms of labor. Vietnam has more human resource, higher population with higher number of working times. Therefore, Vietnam is an ideal destination for labor intensive firm.

Infrastructure

Infrastructure is the term for fundamental facilities and systems serving a country, city, or other area, including the services and facilities necessary for economy to function. By doing business, infrastructure is one of concern too for example logistics. If the logistics within the country is good, it reduces the cost and ease the business.

Vietnam seaports have been invested and built on a large scale to make possible the reception of ships with capacities of over 100,000 tons and 70 international flight paths respectively which are advantages for logistics service development. Moreover, Vietnam is always in trade deficit with materials, machinery and equipment. This is a good market for Vietnam logistics companies. However, in general logistics fees only account for 12-14% of GDP but in Vietnam the fees account for 21-23% of GDP. The Vietnam's logistic fees are high in which the fees for transport, loading, port and other fees are also high. This increases costs for enterprises, increases Vietnamese product prices and reduces the competitiveness of Vietnamese products. (Dezan, 2017)

From looking into data from World Bank, Logistics Performance Index (LPI) which is an interactive benchmarking tool created to help countries identify the challenges and opportunities they face in their performance on trade logistics and what they can do to improve their performance. The index varies from 1 meaning lowest to 5 the highest. Comparing the data of LPI of Thailand and Vietnam in 2017, Thailand's LPI is at 3.26 where Vietnam's is at 2.98. (World Bank, 2017)

Data from world economic forum report 2017-2018 show that global competitiveness index in infrastructure is 4.7 for Thailand and 3.9 for Vietnam as 1 is the lowest and 7 is the highest. (World Economic Forum, 2017)

This implies infrastructure of Thailand is better than Vietnam which contrast with our topic that investor shift production base to Vietnam. Our group opinion is that the LPI differences between two countries is not that large and Vietnam still have opportunity to grow, investors may see the advantage to move into Vietnam now to grow in the future.

Political

- ***Politics***

Thailand and Vietnam are ruled by a different regime. Thailand ruled by democracy, but Vietnam ruled by communist dictatorship. However, in the reality, the regime does not affect much in decision making of investors. In the investors perspective, in term of politics, they will be looking for the interesting policies of each country more than other things else.

For Thailand, after they were trapped in the same regulation for 15 years, finally they declared that they have updated the investment policy. The Thai Board of Investment or BOI has announced a new strategy policy which called seven-year investment promotion strategy. This strategy policy aims to rebuild the Thai economy for sustainable development and emphasized more on the investment promotion. (Aseanbriefing, 2015)

There are six investment key points which BOI try to create the business environment to become more attractive for foreign investors.

- Promote investment that helps enhances national competitiveness.
- Promote activities that are environmental-friendly, save energy, or use alternative energy.
- Promote clusters that create investment concentration based on regional potential and strengthen the value chain.
- Promote investment in border provinces in southern Thailand that develop the local economy.
- Promote special economic zones that create economic connectivity with nearby countries and prepare for entry into the ASEAN Economic Community.
- Promote Thai overseas investment to enhance the competitiveness of Thai businesses and Thailand’s role in the global economy. (Aseanbriefing, 2015)

In the new Investment Promotion Act (B.E. 2520), Thai government provided many incentives and privileges to the foreign investors such as the following examples;

Tax incentives	Non-tax incentives
Exemption or reduction of one-half of import duties on machinery	Permit for foreign nationals to enter the Kingdom for the purpose of studying investment opportunities
Reduction not exceeding 95% of import duties for raw and essential materials	Permit to bring foreign skilled workers, experts, and spouse/dependents that are skilled workers or experts into the Kingdom
Exemption from a juristic person's income tax and dividends on the net profits generated by activities as prescribed by the Board.	Permit to own land to carry on promoted activities
50% reduction of the juristic person's income tax on the profit derived from a promoted activity	Permit to take out or remit abroad money in foreign currency
Double deduction on the costs of transportation, electricity, and water	
Deduction from the net profit, not exceeding 25% of costs of installation or construction of facilities	
Exemption of import duties on raw and essential materials for use in production for export	

Moreover, they also adjusted to the new work permit regulations. In the new Foreign Workers Act (B.E. 2551), they allowed foreign investors to attending a meeting, purchasing goods in goods exhibition or doing business observation without having working permit in some business visa. The incentive given less or more depending on the type of industrial project, they would give you the higher special privileges if you can give a higher beneficial to their country. But, unfortunately, for the foreign shareholder under the List One of the FBA (B.E.2542), the shareholder ratio still needs Thai citizen to be the majority. Thai people must hold at least 51 percent of the total capital. Since, Thai business still cannot compete with foreign firms if we become more open.

The industrial that BOI promoting are activity-based such as agriculture and agricultural products, mineral, ceramics and basic metals, light industrial, metal products, machinery and transport equipment, electronic and electrical appliance industry, chemicals, plastics and paper, and, service and public utilities. And technology-based like biotechnology, nanotechnology and digital technology etc. (Aseanbriefing, 2015)

	Exemption of corporate income tax	Exemption of import duty on machinery	Exemption of import duty on raw material imported for use in production for export	Non-tax
A1	8 years (No Cap)+Merit	Yes	Yes	Yes
A2	8 years + Merit	Yes	Yes	Yes
A3	5 years + Merit	Yes	Yes	Yes
A4	3 years + Merit	Yes	Yes	Yes
B1	0 year + Merit (for some activities)	Yes	Yes	Yes
B2	-	-	-	Yes

For Vietnam, it has everything today because of Doi Moi policy. This economic reform policy has made Vietnam's economic and social development thrive since 1986 which similar to those policies launched in China under Deng Xiaoping in the late 1970s.

Over the past decade, Vietnam has succeeded in attracting foreign direct investment. The government of Vietnam has amended the trade regulations the increase the flow of investment complies with international standards. Promote investment in privileges such as land ownership, tax measures, facilities, plant registration procedures and accelerate one-price policy in order to reduce investment costs for foreign investors in the field of telecommunications, electricity and transport. Vietnam has given importance to investment in various projects, especially, investment in energy and industrial district which conducive to producing products that can compete in the global market. Including to create jobs and Technology Transfer.

Over the years, investors invest more in infrastructure projects and communications. As a result, monopoly power of the government has reduced and the increase in trade and investment in the private sector has made the Vietnamese economy grow rapidly at an average of 9.6% per year during 1985-1995 and continues to grow at an average of 6-7% per year until present. Foreign investment is encouraged, industry has switching from traditional technology to advanced technology and changing foreign investment policies.

For this reason, after Vietnam began funding from Foreign investment has increased rapidly and continuously. Foreign investment in Vietnam has grown significantly. After the implementation of economic reform policy. The economy of Vietnam has a remarkable growth rate. Gradual and tend to grow continuously. It can be seen from the past few years.

The economy of Vietnam has developed and grown significantly and the economy of Vietnam is one of the most stable countries in the Greater Mekong Sub region area comprises with the economic potential of Vietnam itself make Vietnam become Countries that have high investors attraction which can said that it is the target countries of most foreign investors in the region. Moreover, the Government of Vietnam has created the most favorable investment climate for investors, whether it be amendment of the law Privilege in various fields of investment.

Currently, foreign investment law and the latest edition of the Unified Enterprise Law and Common Investment Law have been introduced in July 2005. The law of investment in Vietnam is quite clear and beneficial to investors by the government to promote foreign investment and insist not to seize the state. Also allowed to send funds and profits back to the home country. The government will not levy taxes on machinery, equipment and construction materials which imported to produce export products.

Government support and control in the wide range of businesses, while also being updated the approval of foreign investment projects by using "one-stop service" to resolve the delays of obtaining investment licenses to promote and control many investments in Vietnam. (DTN, 2015)

- ***Tax Incentives***

Vietnam's Law on Investment has incentives that are available for companies operating within the country. The exemption or reduction of import tax on goods imported as fixed assets on raw materials, supplies, and parts used for the project;

Tax incentives	Tax holidays
10% for the lifetime of the entire project	Tax exemption for 4 years, 50% reduction of payable tax amounts for 9 subsequent years
10% for 15 years from the first year of income generation	Tax exemption for 4 years, 50% reduction of payable tax amounts for 5 subsequent years
17% for the lifetime of the entire project	Tax exemption for 2 years, 50% reduction of payable tax amounts for 4 subsequent years
17% for 10 years from the first year of income generation	

- ***Legislation***

One of the factors people choose to invest or built production base is legislation in that country on how it benefits investor. Each country has different law. Thailand and Vietnam give benefit to foreign investor in various ways.

First of all, both countries promote special economic zones. For Thailand, there is 10 provinces that are special economic zone, investor would get several things which are 8-year Corporate Income Tax (CIT) exemption and additional 5-year 50% reduction of CIT, double deductions from the costs of transportation, electricity and water supply for 10 years, additional 25% deduction of the cost of installation or construction of facilities, exemption of import duty on machinery, exemption of import duty on raw materials used for export production, other non-tax incentives, permission to use foreign unskilled workers. Where in Vietnam, economic zone investment incentives are 2 to 4 years of tax exemption and 4 to 9 years of 50% reduction on payable CIT. Furthermore, both countries promote investment in poor income per capita or disadvantage area. For Thailand, according to 7-year investment promotion strategy (2015-2021), there is section using merit on decentralization which will receive additional incentives. In Vietnam, economic zones in disadvantage areas get 17% CIT for 10 years, 2 years of CIT exemption and 4 years of 50% reduction on payable CIT where in extremely disadvantaged areas get 10% CIT for the lifetime of the project, 4 years of tax exemption and 9 years of 50% reduction on payable CIT. Foreign investors in these zones also benefit from tax incentives extended by the Vietnamese government. Most economic zones will qualify an investor for tax holiday incentives. In limited cases, where the zone is located in a disadvantaged area, a preferential rate of corporate income tax will also apply. 10% for the lifetime of the entire project, 10% for 15 years from the first year of income generation, 17% for the lifetime of the entire project, 17% for 10 years from the first year of income generation. (BOI, 2016) (Dezan, 2018)

Mainly, incentives that investor will get from countries is tax incentives. Thai Board of Investment (BOI) give investment incentives to investor depending on type of industrial project which divided into two groups of investment incentives which are activity-based and merit-based incentives. On activity-based incentives, there are A1, A2, A3, A4, B1 and B2 as industrial type and tax incentive that investor will get already be mention previously.(BOI, 2016)

Another one is measure for improvement of production efficiency containing three sub measures of machinery upgrade to promote energy conservation, alternative energy utilization or reduction of environmental impact, machinery upgrade to improve production efficiency e.g. utilizing machinery automation in existing production lines, investment in R&D and advanced engineering design for efficiency improvement (investment must not be less than 1% of the total revenue for the first 3 years or 0.5% for SMEs). Incentives of these are exemption of import duty for machinery, 3-year corporate income tax exemption on the revenue of an existing project, accounting for 50% of the investment under this measure (excluding cost of land and working capital), and corporate income tax exemption period shal start from the date of revenue derivation after promotion certificate is issued. (BOI, 2016)

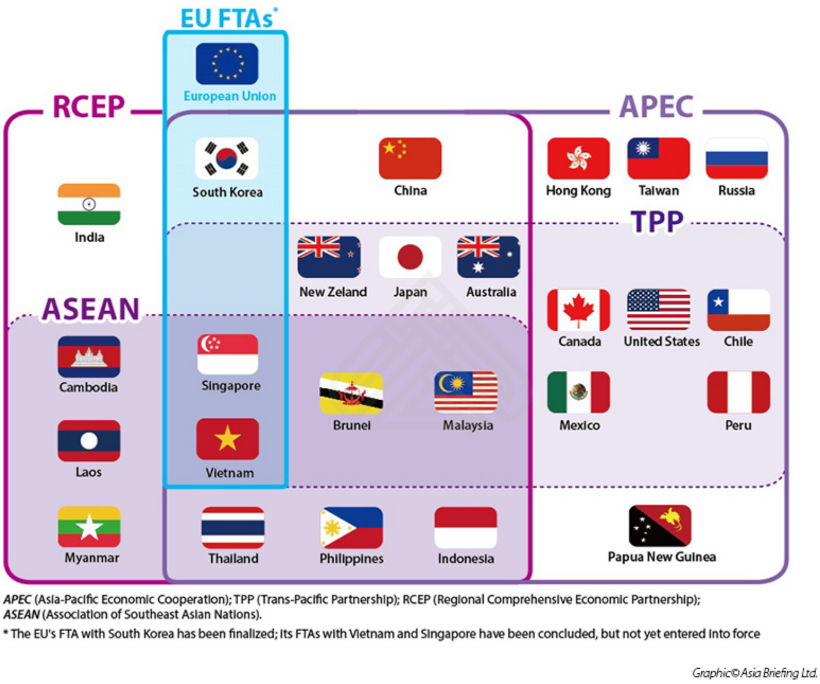
Moreover, Thailand has investment promotion policy on super cluster which includes automotive and parts cluster, electrical appliances, electronic and telecommunication cluster, digital cluster, eco-friendly chemical and plastics cluster, food innopolis, aviation & aerospace cluster, automations and robotics cluster, and medical hub. Incentives for super clusters are 8-year corporate income tax exemption and an additional 5-year reduction of 50%, for future-driven industries with significant importance, the ministry of finance will consider granting 10-15 years corporate income tax exemption, import duty exemption on machinery, personal income tax exemption for renowned specialists who work in the specified areas, both Thais and foreigners, consideration of granting permanent residence to leading specialists, permission for foreigners to own land to implement promoted businesses. (BOI, 2016)

Vietnam's tax incentives are standout feature of tax regime and said to be one of the most competitive tax regimes throughout Southeast Asia. By going through new laws that going to be in effect in 2018, there are some interesting law. Law on foreign trade management regulates external trade management measures and deals with trade disputes aiming to increase transparency and domestic production. An interesting one is FDI strategy for 2018-2023. It will focus on priority sectors and quality of investments rather than quantity aiming to increase foreign investment in high-tech industries, rather than labor-intensive sectors. Manufacturing, services, agriculture, and travel are the four major sectors in focus in the draft. Foreign firms in Vietnam are offered huge tax and other incentives such as exemptions or reductions in corporate income tax, import duties, and VAT. For some industry even gets reduction of land rents and land levy. And recent years, Vietnam policy has promoted projects in high tech industries, large capital and social importance, which get benefits from CIT exemption.

High tech	Large scale	Social importance
10% CIT for 15 years	10% CIT for 15 years	10% for entire life of project
4 years of CIT exemption	4 years of CIT exemption	4 years of CIT exemption
9 years of 50% reduction on payable CIT	9 years of 50% reduction on payable CIT	5 years of 50% reduction on payable CIT

- *Trade agreement*

Figure 6



In this topic, we will focus on trade agreements that Thailand and Vietnam familiar with. Since Thailand and Vietnam are in the ASEAN community, they almost have the same of trade agreement. But because Vietnam is still a little behind. Vietnam has more trade benefits than Thailand. From the picture that we attached (Figure 6), you will see that Vietnam have more trade agreements than Thailand which are GSP: General System of Preferences and TPP: Trans-Pacific Partnership and EU-FTAs or EU-Vietnam Free Trade Agreement (EVFTA). Those agreements have played a significant role in term of competitiveness between two countries. So, we will only focus on the trade agreement that Vietnam has more than Thailand.

Most countries which having a free trade area will usually have a similar advantage over other non-member countries, such as import and export quota, lower tariff rates. So, in this topic, we will say the idea in Thai perspective instead. What Thailand going to face, when they did not enjoy these benefits of those agreement.

First, GSP or generalized system preference. It is a tax privilege that Developed countries give to some developing countries. The benefits which developing countries would get is free import-export tax in some product to the member countries. They doing like this in order to make developing countries to be able to export goods and to compete with goods from developed countries. Or compete with countries that have the ability to produce cheap and effective products such as China. When developing countries can sell their products, this will create production, employment, the economy of the developing countries will grow and people will have high living standard.

In addition, GSP also helps the entrepreneur of the developed countries to reduce the cost of production when they have to imports of raw materials from GSP-eligible countries which are not subject to import duties.

The bad thing of not getting benefit from this agreement is Thailand have to pay import-export tax in the normal rate which very high when comparing to our main competitors. (DFT, 2015)

The next trade agreement is the Trans-Pacific Partnership (TPP) or the Pacific Economic Partnership Agreement is a free trade agreement in the Pacific Rim countries which set up to increase trade volume, services and investment in member countries. They also set common standards for trade and regulation on intellectual property protection, labor standards, environmental law and mechanisms for resolving disputes between government and foreign investors. Currently, TPP members are comprised of 12 countries: The United States, Japan, Canada, Chile, Mexico, Peru, Australia, New Zealand, Singapore, Malaysia, Brunei and Vietnam. It's about 40% of world GDP and that makes TPP became the largest free trade agreement in the world.

The impact on the Thai economy from not being a member of the TPP?

The fact that Thailand does not become a TPP member may lead to Thailand losing its competitiveness. In terms of exports and attracting foreign investors to TPP members which effect the export sector since about 40% of all Thailand export products are export to TPP member countries.

The industry that is losing its benefits most is an industry that relies heavily on exports to the US market. for examples, Electronics, electrical appliances, apparel, processed seafood and processed fruit etc. Thai cars and components are another commodity that relies on exports to countries in the TPP. The impact in term of foreign investment. Thailand will lose to its competitors in TPP like Vietnam and Malaysia in which to attract foreign investors since Thailand does not get any of tax privileges between TPP member.

In addition, the TPP deals with the protection of foreign investors through dispute resolution mechanisms between investors and the public sector. At present, foreign investment in Thailand is relatively stable. Unlike Vietnam, where foreign investment continues to grow. (SCBEIC, 2015)

And the last one, the EU-Vietnam Free Trade Agreement (EVFTA). It is a trade agreement which covering a wide area of sectors and also has an equal elimination of tariffs from both sides, is anticipated to bring about benefits and opportunities for both economies in multiple ways throughout the years.

According to the agreement, the EU and Vietnam has committed to further market access and to reduce the tax over 99 percent on industrial and agricultural products, in addition to duty free rate quotas on a number of goods including clothing, footwear, seafood, tropical agricultural products, furniture, automobiles, machinery, equipment, beverages, medicine, and temperate agricultural products and others which will come from the EU and Vietnam.

These two sides' commitments on services sectors go largely beyond both WTO commitments and any other FTA that Vietnam has concluded. Therefore, EU companies will have more benefits when investing and doing business in the Vietnamese market, particularly in the sectors of their strength which include finance, banking, insurance and maritime transport. Vietnam's commitments to ensure an open and transparent investment and business environment will help to boost high quality investment from the EU into Vietnam.

The disadvantage not having this agreement with European union is same as TPP case, which we have to pay a normal tax rate and having less quota for export our Thai product to Europe countries. So, in the Thailand cannot compete with Vietnam. (WTOcenter, 2017)

Interview from Toyota Motor Corporation

We have got opportunity to interview Miss Supawan Pornwuttikorn, staff at Toyota about the expanding production base of Toyota. Even though Toyota does not shift the production base but expanding give the similar behind reasons. Furthermore, it shows us how different industry have different decision in shifting production base. It was being emphasized that the factors to choose a place to be production base are several. The most important one is government, policy and regulations. It needs to be clear, stable and continued where regulations need to be flexible and international standard. Other factors are labor, market size, market volume, privilege and logistic cost.

Specially, the important reason is if cost of having production base on the country is less than exporting cost like logistic cost, it is worth to have production base. Furthermore, it there is growth in the industry where in production are fixed cost and variable cost. Fixed cost will be push to domestic. The higher domestic sale, the lower fixed cost. variable cost is push to export as exporting have no tariff because of some agreement, the lower cost. with lower cost and high-quality product, it increases competitiveness.

So, the next questions that has been asked was what factors that Toyota chose Thailand to be production base? The answer is related to the previous talk about factors choosing place to be production base. First of all, the government and policy are clear, stable and continued. There is industrial investment promotion, Board of Investment (BOI), and model scheme of industrial that show clear policy. Moreover, even there was military coup for several times occurring in the country, main policy about investment do not change which reflect the stability. Also, she emphasized about the correlation between public, private and institute. The public is the government where private are those CEO and MNCs. The correlation helps the policy to work well with every sector. Furthermore, when there is a topic needed to be discussed, all ministries will attend. For example, if hybrid plugin car policy is going to be launched, not just the Ministry of Finance but also Ministry of Energy to have the best result from many aspects.

Next factors being mentioned was labor. Every firm wants low wage and skilled labor but they usually do not come together. In the past, to assemble a car does not require skilled much because there was no electric vehicle, no hybrid and the method being used was completely knock down (CKD). To give an easy understanding, it is like a Lego which have many small parts to build together to get a car. From that day until now, labor in Thailand has become more skilled labor due to there are institute to help training until the point we reached now as a Pick-up car production base of Toyota.

Market size and volume are another factor being concerned. Because before becoming production base, looking at the market size and volume is what investor need to do first. The boost up the market. First, may import products from foreign countries because lack of ability to produce by ourselves and it can be freely import due to government support. Then, when there is enough production incentive, government would start to promote the production to attract FDI into country. Next step is to establish BOI in order to promote investment to the country. Promoting is actually giving privilege to investor by saying that if you invest in our country, these are benefits you would get. After these procedures, it will eventually reach the economy of scale. At the point, the localization will start. Other factors that are being considered as well are well infrastructure. She also mentioned that during tom yum kung crisis, Toyota came to Thailand and the industry grow because of government and skilled labor which make us be able to export to 108 countries at a very standard-produced car.

There was a rumor saying that Toyota have expand production base to Myanmar but Ms. Supawan told us that, by looking at factors that has been mention, do we still that the expanding is true? Even though there is large amount of labor force and young generation, other factors are not quite good to be the base. The market volume is not big enough, the policy has no stability and infrastructure is not so good. Another question that we have asked is why Thailand, not other countries? She gave an example of Laos regulations that you cannot exchange currency over 20,000 baht per day, which is very difficult for selling a car. Also, the banking system is not so well, the business would stop.

The reason why Toyota does not shift production base to Vietnam are that Vietnam welcome Korea Car and government is socialist which they can change anything at any time showing no stable policy. She also mentioned about the reason LG and Samsung shift production base to Vietnam, Korea may have some privilege and political benefit from Vietnam. Moreover, the agreement like TPP may give benefits in exporting from Vietnam more than produce and export from Korea.

Here is timeline showing supported policy about automobile industry in Thailand from the past until now which shape action of Toyota.

Initial stage: Import substitution policy (1960-1968)

- 1961: Industrial Investment Promotion Act provided incentives for the local assembly for automobile.
- 1962: Revised Industrial Investment Promotion Act announced 50% reduction in tariff on Completely Knocked Down (CKD): Completely Built up (CBU) new rates, passenger cars 30%, pickups 20% and trucks 10%

  [Completely Knocked Down refers to cars that produced and assembled domestically.]

  [Completely Built up refers to cars that produced, assembled internationally and shipping to foreign nations.]

Second stage: Localization and acceleration of LCR (1969-1990)

- 1969: Ministry of Industry (MOI) set up Automotive Development Committee. 20% increase in tariffs on Completely Built up (CBU).
- 1971: MOI restricted the number of locally assembled vehicles. Announced local content requirement (LCR) measures to become effective: domestically assembled vehicles had to use locally produced parts to at least 25%.
- 1990: Abolished restrictions on domestic production of series and models.

Third stage: Partial liberalization and export promotion (1991-1996)

- 1991: The Cabinet reduced all types of tariffs on Completely Built up (CBU) and Completely Knocked Down (CKD) kits.

- MOC announced an abolishment of passenger car import restriction, while an import of used car was prohibited.
- 1994: MOI allowed new restriction of car-assembly plant to increase investment and competitiveness on productivity. BOI ranted rights and privileges concerning the Promoted Area Policy for automotive industry.
- 1995: Thai become a member of WTO.

Forth stage: The Asian Crisis and recovery (1997-1999)

- 1997: The financial crisis hit Thai economy. Government allowed a majority equity holding by foreign firms.
- 1999: MOI announced the abolishment of “local content requirement policies”. MOF announced the new automotive tariff structure to supplement the abolishment of “local content requirement policies”.

Creating International Competitiveness and Product Champions (2000-2010)

- 2000: Employ various fiscal policies tactically to foster the industry: increasing CKD tariff rate, reducing excise tax on double cab.
- 2001: BOI announced a new incentive program to promote large automotive cluster investment. A cluster should comprise both car assembly and auto parts manufacturing.
- 2003: BOI launched new incentive for industries that generated the development in skill, technology & innovation (STI).
- 2004: The Cabinet revised the automotive excise tax.

- 2005: Thai automotive industry became one of top fifteen largest automotive producers in the world.
- Free Trade Agreement: Thailand-Australia: Australia eliminated tariff on some type of vehicles.

International car and next generation automotive (2011- present)

- 2013: MOI launched International Car Policy
- 2016: BOI launched “Super Cluster Scheme”. The government promote hybrid cars by lower excise tax rate.

RESULTS

Due to push pull theory that had been mentioned in the previous section, the push factors on Korean side consists of Outward FDI(OFDI) policy by Korean government and natural disaster.

Outward FDI(OFDI) policy consists of Loan programs, Information provisions and Reduction of non-commercial risks.

Firstly, loan program will enable investors to raise a loan up to 80% of the total OFDI amount. In addition, loan program is applicable in developing countries which the return periods will be extended. Secondly, Korea trade and investment promotion agency will support investors regarding the essential information in doing international investment. Lastly, reduction of non-commercial risks, Korean export insurance corporation provide insurance for investors including losses from war, nationalization, etc. (UNescap, 2007)

Natural disaster is another push factor that influenced Korean investors. Since Korea has unavoidable natural disaster such as earthquake so Korean investors decided to avoid risk by invest abroad and find another location for production base rather than Korea itself.

Pull theory is examined regarding Thailand and Vietnam side. By considering Thailand, Thai government always support FDI by publishing policies for international investors also becomes a member of an agreement such as FTA, WTO which has no restrictions in the manufacturing sector, no local requirements nor export conditions. Thai labor is skilled labor with advanced technology. Furthermore, Thailand located in the middle of Southeast Asia and Thailand also connected with Mae-Kong region where it is easy to transit. (Santander Trade, 2018)

Vietnam has rich natural resources which it is ready to be use. Even though Vietnam had been governed by single-party socialist republic but political sector is considerably stable. Vietnam has high economic growth which it is still growing in the future. Moreover, Vietnam has a huge amount of labor force with low wage.

From the observed indicators, the important indicators are listed below which consisted of GDP per capita growth, export and import of goods and services, average monthly wage, human resource and government policies.

In the figure 7, GDP per capita growth in 2017 of Vietnam showed how Vietnam grew in each year also it was more than Thailand. Investor can use GDP per capita growth in deciding whether they should shift their production base or not.

In the figure 8 and 9, export and import of goods and services in 2017 of Vietnam had higher growth percentage than Thailand by six-fold which it showed that Vietnam had more transactions with the rest of the world.

In the figure 10, average monthly wage in 2017 of Vietnam is less than Thailand. This figure is important for labor intensive firm who seeking for labor with low wage rate.

In the figure 11, human resource in 2017 of Vietnam is more than Thailand. Since Thailand is now facing the aging society problem and Thailand are lacking of human resource. So, Thailand are lacking behind Vietnam in terms of human resources.

Both countries have good incentives to attract investor and the regulations are quite clear and mainly incentives are about tax. To say that which countries are better to invest in varies on your firm on what industry you are in and where your location. As it could be seen through regulations that the differences of tax exemption or reduction vary by factors. Suggestion is firm should look through details carefully in order to seek for the best benefits one could get.

Figure 7: *GDP per capita growth(%) in 2017*

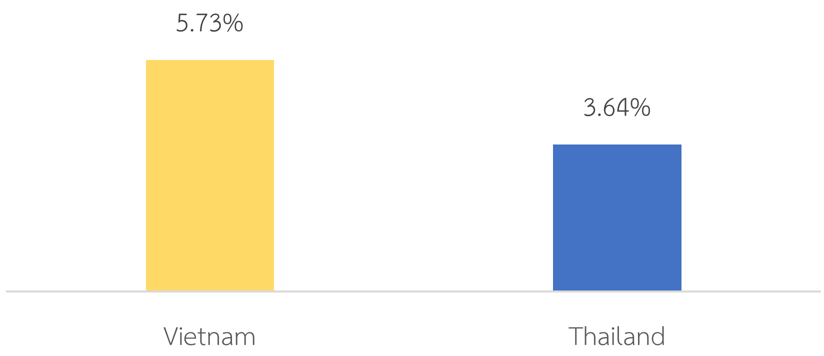


Figure 8: *Export of goods and services (annual % growth) in 2017*

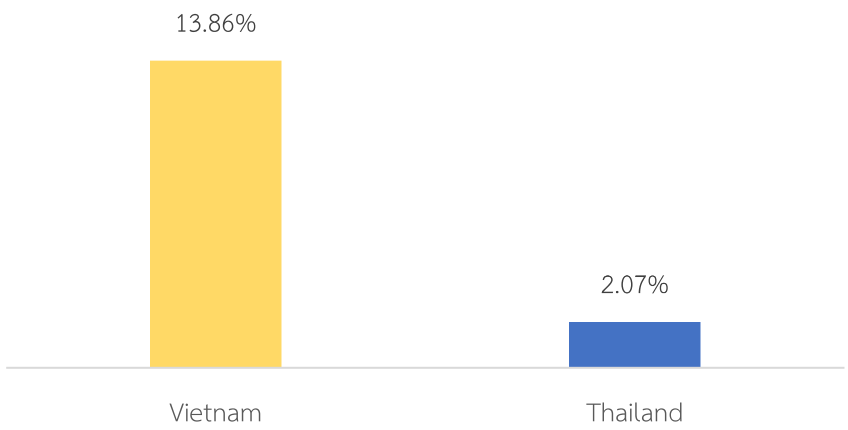


Figure 9: *Import of goods and services in 2017 (%)*

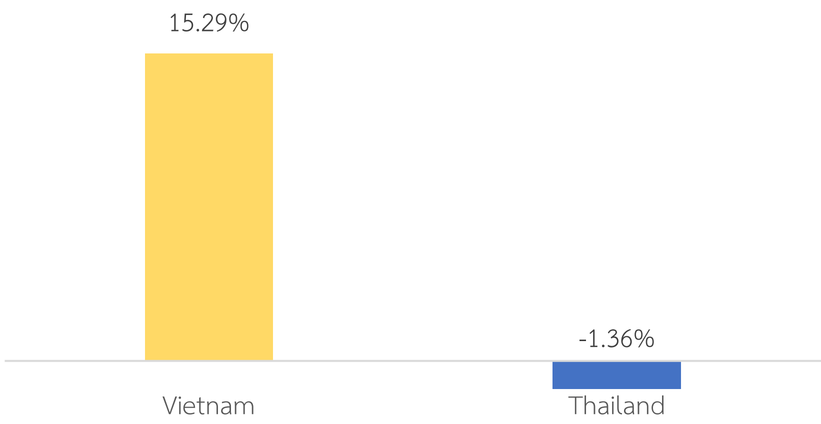


Figure 10: *Average monthly wage rates in 2017 (Baht/month)*

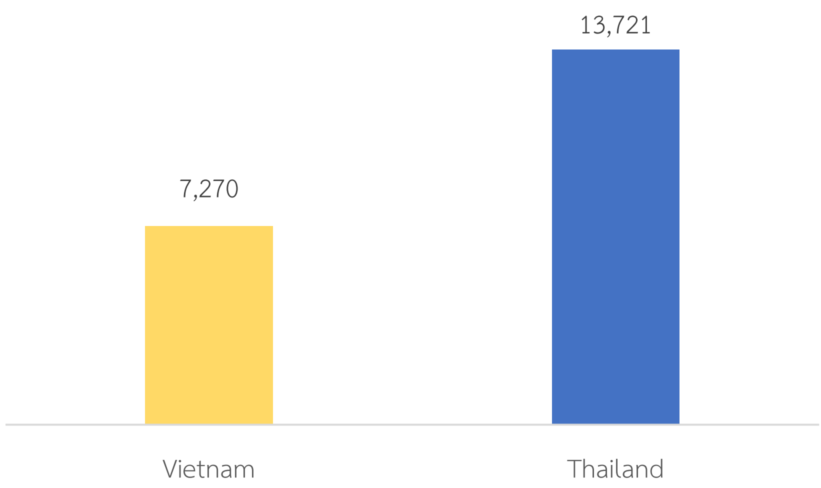
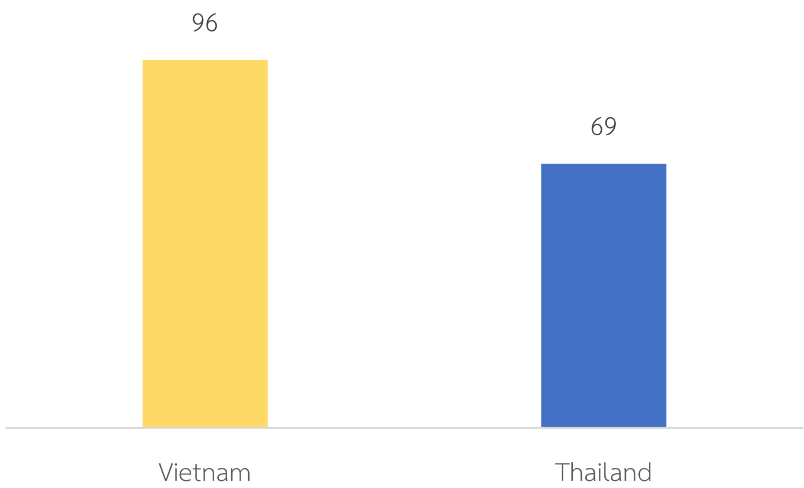


Figure 11*: Human resource in 2017 (Million)*



To answer the research question: Why do investors shift production base from Thailand to Vietnam, it showed that GDP per capita growth, export and import of goods and services, average monthly wage and human resource of Vietnam are better than Thailand. Even though Thailand and Vietnam policies are quite similar but Vietnam just had an economic reform in 1986 which is called “Doi Moi” so Vietnam still have more natural resource than Thailand. So those mentioned indicators are the factors that influenced investors to shift production base from Thailand to Vietnam.

CONCLUSION

Throughout the analysis, shifting production base is a big decision that needs to concern a lot of factors. From clearly seen cost like labor cost to overlook aspect like government policy. As there are many considerations, there are conflict between them for instance, wage may be low in Vietnam but stability of policy in Thailand is better. There are many trades off which investors need to think thoroughly. With these contrast between factors, decision of investors from different industry is not the same. From the news that LF and Samsung which are electronics industry choose to shift production base to Vietnam but by interviewing Toyota, which is automobile industry, choose not to shift. Toyota seems to give priority to policy and regulations which Thailand is better. Different industry may focus on different point.

Suggestions for Thailand to improve FDI to flow into country are first, increase productivity of labor. When investors demand for labor, they want skilled labor and low wage. Vietnam has low wage comparative advantage where Thailand has skilled labor. So, Thailand should improve skilled labor by supporting the training for higher skilled like education policy and finding strength and weakness of labor and help them improve. Secondly, increase quality of product by using new technology in purpose of minimize the number of errors. Moreover, to ensure the quality and gain trust from international Thailand could use measures such as ISO and Thai industrial standard. Lastly, Thailand should join more trade agreement to gain more benefits. For example, bilateral trade agreement with China because now there are only free trade agreement between countries.

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APPENDIX

Photos from interviewing Toyota motor corporation at CRC Tower, 25 July 2018.

With Miss Supawan Pornwuttikorn, Principle of Mekong Actioner 1 project