Foreign Direct Investment: Performance and Attraction
The Case of Thailand

The Brooker Group plc.[1]

Contents

1 This paper was prepared by Peter Brimble, with assistance from Hataichanok Techaratanawiroj of The Brooker Group plc. and Atchaka Sibunruang of the Thailand Board of Investment, to be presented at a Workshop on Foreign Direct Investment: Opportunities and Challenges for Cambodia, Laos and Vietnam in Hanoi from August 16-17, 2002. It draws heavily on three related pieces of work: Arnold, Erik, Martin Bell, John Bessant, and Peter Brimble. 2000. ***Enhancing Policy and Institutional Support for Industrial Technology Development in Thailand - The Overall Policy Framework and The Development of the Industrial Innovation System***; Brimble, Peter., Sherman, James., Sibunruang, Atchaka, and Rachatatanun, Witit. 1999. ***The Broader Impacts of Foreign Direct Investment on Economic Development in Thailand: Corporate Responses***; Brimble, Peter. 2002. ***Foreign Direct Investment, Technology and Competitiveness in Thailand***, Chapter in a World Bank Institute volume forthcoming in 2002.

Acronyms

ADB	Asian Development Bank
AFTA	ASEAN Free Trade Area
AIT	Asian Institute of Technology
ASC	Australian Submarine Company
ASEAN	Association of South-East Asian Nations
ASID	ASEAN Supporting Industry Database
ATTC	Ayutthaya Technical Training Center
BOI	Board of Investment
BOT	Bank of Thailand
BUILD	BOI Unit for Industrial Linkage Development
CCST	Certificate of Competence in Storage Technology
FCC	Foreign Chambers of Commerce
FCCCC	Foreign Chambers of Commerce Coordinating Committee
FDI	Foreign Direct Investment
FTI	Federation of Thai Industries
GDP	Gross Domestic Product
GNP	Gross National Product
GSP	Generalized System of Preferences
HDD	Hard Disk Drive
IDEMA	International Disk Drive Equipment and Materials Association
JPPSCC	Joint Public-Private Sector Consultative Committee
KMITNB	King Mongkut Institute of Technology North Bangkok
LDC	Less Developed Country
M&A	Mergers and Acquisitions
MNC	Multi-National Corporation
MOC	Ministry of Commerce
MOI	Ministry of Industry
MOSTE	Ministry of Science, Technology and Environment
NECTEC	National Electronics and Computer Technology Center
NESDB	National Economic and Social Development Board
NPL	Non-Performing Loan
NSTDA	National Science and Technology Development Agency
Plc	Public Limited Company
R&D	Research and Development
SME	Small and Medium Enterprise
STDB	Science and Technology Development Board
TBA	Thai Bankers' Association
TCC	Thai Chamber of Commerce
TGA	Thai-German Institute
TISTR	Thailand Institute of Scientific and Technological Research
TMT	Toyota Motor Thailand
UNCTAD	United Nations Conference on Trade and Development
USAID	United States Agency for International Development
VMC	Vendors Meet Customers
WTO	World Trade Organisation

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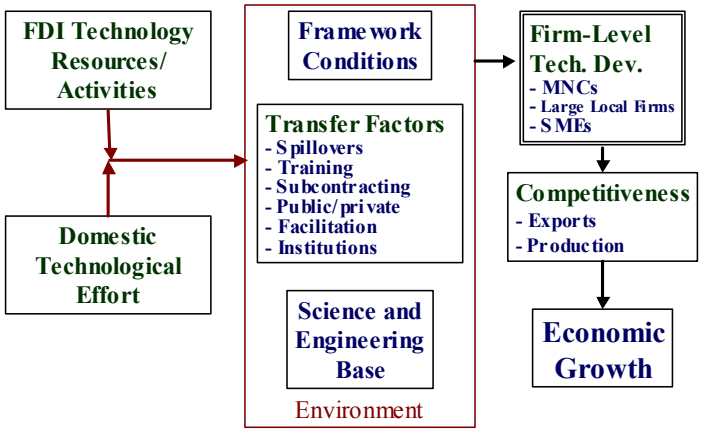
1. Introduction and Context

Foreign direct investment has been an important element of Thailand's economic development process. Given the growing importance of industrial competitiveness in an increasingly competitive global marketplace and the potential of the relationship between FDI and technological upgrading, this paper aims to explore two questions facing Thai policy makers: (i) what are the most effective ways in which technology transfer can take place through FDI; and (ii) how can such transfers be accelerated and enhanced through FDI promotion policies?

This paper examines the overall impacts of FDI and related policies at the macro-level as well as the promotion activities at the micro-level during the past twenty years in order to synthesize and provide key lessons from the Thai experience on utilizing FDI as a tool of economic development. Conclusions and recommendations will be supplied to support other countries in developing and utilizing the FDI strategies.

At a conceptual level[2], technological progress is achieved through a continuous upgrading of technology, information and skills. The process becomes more complex in an environment where both export competition and technical changes take place simultaneously and at very high levels. The two critical sources that determine the level of technological development - namely FDI and domestic technological effort – are shown in the framework as feeding through the environment to the firms in the economy.

Figure 1.1
FDI, Technology and Competitiveness
Framework for Analysis



The environment includes three elements: (a) the framework conditions – such as the state of the macro economy and overall policy environment; (b) the science and engineering base; and (c) the so-called transfer factors that condition the effectiveness with which the technological assets of the economy are transformed into firm-level capabilities. These include a range of

[2] The structure of the framework presented in Figure 1.1 was developed as an input into the Thailand paper for a research project of the World Bank Institute on FDI, Technology and Competitiveness in East Asia (see Brimble 2002).

elements including spillovers, training, subcontracting, public-private interaction, institutions, facilitators, etc.

The macro analysis is prepared based on desk research and secondary data complied from reference sources while the analysis of policy approach and implementation at the micro level are derived from interviewing certain key involved officials.

Following the introductory remarks, Section 2 presents a brief picture of the macroeconomic and industrial development scenes in Thailand since 1960. Section 3 analyses trends in FDI and its major impacts, the policy approaches to FDI and promotion activities carried out by the Thai BOI. Section 4 presents major conclusions, an agenda for FDI policies in Thailand, and indications as to major lessons learned.

2. Industrial Development Trends

2.1 The Macroeconomy

Before the economic crisis in 1997, Thailand's economic development was considered as a continuous success with an average economic growth rate of nearly 8% p.a. from 1960-1996. Despite the world recession of the mid-1980s, Thailand's economy grew at double-digit rates during 1988-1990 and by over 8 percent per year from 1991-1995.

This rapid growth, driven largely by growing FDI inflows and exports, was accompanied by a shift towards manufacturing, with the manufacturing share of total GDP reaching 29.9 percent by 1995, up from 11.6 percent in 1960. The key challenge to Thai-based producers, domestic and foreign, by the mid-1990s was to enhance production capabilities and move up the value-added ladder as competition from lower wage countries like China, India, Indonesia and Indochina intensified.

The enormous influx of foreign funds following the country's financial liberalization that started in 1990 further eroded the country's competitiveness as cheap and easy funds flowed to unproductive businesses or businesses with less competitiveness. This spurred the demand for local resources and hence the cost of production. The country faced a sharp decline in export earnings while the country's short-term debts and the non-performing loans of financial institutions were piling up, which resulted in a huge and increasing deficit in the current account balance. While the Bank of Thailand was seen as unlikely to devalue the Thai Baht, speculators attacked the currency. The central bank failed to defend and lost a tremendous amount of the country's international reserves.

Then came the financial crisis. On July 2, 1997, the Thai government floated the Baht, triggering a collapse of the financial sector and a devastating economic recession. GDP declined by 1.4 percent in 1997 and by a further 10.5 percent in 1998. This compares to expected 1998 growth rates of over 7 percent as recently as 1996. Inflation reached around 8 percent in 1998, after levels of around 5-6 percent for many years. The value of the Baht fell from 25 to the dollar to around 42-43 in early 2002 (though this was better than the rate of 55 seen in early 1998). Table 2.1 shows Thailand's key macroeconomic indicators.

Table 2.1
Thailand's Key Macroeconomic Indicators 1995-2001

	1995	1996	1997	1998	1999	2000p	2001p
GDP at Current Prices (US$ billion)	167.7	181.6	150.3	111.3	122.0	121.8	114.4
Real GDP Growth Rate (%)							
• Overall	9.2	5.9	-1.4	-10.5	4.4	4.6	1.8
• Agriculture	4.0	4.4	-0.7	-1.5	2.2	4.8	1.6
• Manufacturing	11.9	6.6	1.4	-10.9	11.9	6.0	1.2
• Construction	6.7	7.0	-25.6	-38.3	-6.8	-9.4	-3.0
• Services and Others	8.7	5.4	-0.4	-9.1	0.8	4.3	2.4
Sectoral Shares of GDP (%)							
• Agriculture	9.5	9.5	9.5	10.8	9.3	8.7	8.6
• Manufacturing	29.9	29.7	30.2	30.9	32.7	33.6	33.5
• Construction	7.2	7.4	5.7	3.8	3.6	3.1	2.9
• Services and Others	53.4	53.4	54.6	54.5	54.4	54.6	55.0
Inflation (% change)							
• Consumer Prices	6.1	5.5	5.6	8.1	0.3	1.6	1.6
• Producer Prices	N/A	1.8	5.1	-12.2	-4.7	3.9	2.5
Exports: Value (US$ billion)	56.7	56.0	58.4	54.5	58.5	69.8	65.4
Growth (%)	24.9	-1.3	4.4	-6.8	7.4	19.3	-6.3
Total Debt Service Ratio (%)	11.4	12.3	15.7	21.4	19.4	15.4	20.7
• Public (%)	2.8	2.5	2.7	3.3	4.0	4.0	8.0
• Private (%)	8.6	9.8	13.0	18.1	15.4	11.4	12.7
Fiscal Expenditures (FY)							
• Level (US$ billion)	25.7	32.3	29.6	20.3	21.9	21.2	20.4
• Fiscal Balance (% of GDP)	3.2	0.7	-1.8	-2.7	-2.6	-2.2	-2.6
Stock Exchange Index (end-period)	1,281	832	373	356	482	269	303

Sources: NESDB and Bank of Thailand, July 2002

While the financial collapse was primarily a short-to-medium term phenomenon caused by inadequate financial regulations and weak public and private sector governance, deteriorating industrial competitiveness exacerbated the situation. Export performance worsened dramatically in 1996, falling by 1.3 percent after many years of 10 to 20 percent growth rates[3]. The stock exchange went through a 'meltdown' in the same year. While GDP grew by 5.9 percent in 1996, the storm clouds were already looming[4].

The economy returned to 4.4 percent growth in 1999, albeit with continuing low capacity utilization and significant disruptions in the real sector, and continued to grow by 4.6 percent in 2000. In 2001 GDP growth slowed to 1.8 percent due to weak export demand caused by the global slowdown, especially for electronics products. This decline has placed pressures on the fiscal balance that was recovering from the negative levels caused by the economic crisis, and makes the economy more vulnerable to the weak performance in the US and Japan. Reducing the level of non-performing loans and restructuring the corporate sector become even more critical to continued economic improvement and investor confidence. Even if the global picture improves and the Government continues to reform the finance and real sectors, Thailand will still require significant increases in competitiveness in the major export sectors.

[3] A constellation of factors led to the rapid decline in exports in addition to declining competitiveness, including a slowdown in world trade, the emergence of China in global markets, EU restraints on certain Thai exports, and fluctuations in global electronic markets.

[4] See Siamwalla, 1997.

In this context of recession and relatively slow recovery (at least in light of previous very high growth rates), the role of FDI, important in the past, became even more critical. FDI was and is needed to help re-capitalize failing industries, bring in new technologies, generate or save jobs, assist with policy reforms and play a role in addressing the challenges in the areas of poverty and social unrest.

2.2 Structural Changes in Industry and Policy Responses, and Emerging Challenges

Since the early 1960s, when the first development plan was implemented, the government has supported private enterprise and limited government involvement in the economy to the key utility and infrastructure sectors and to maintaining an incentive structure to encourage the private sector.

Phase 1: In the 1960s, the government followed a traditional import-substitution strategy, imposing tariffs on imports, particularly on finished products. The role of state enterprises was greatly reduced from the 1950s and investment in infrastructure was raised. Attention was given to nurturing the institutional system necessary for industrial development.

Phase 2: By the late 1960s and early 1970s, the import substitution policy had led to balance of payments problems since most components, raw materials, and machinery to support finished product production had to be imported. A major policy shift towards export promotion took place.

Phase 3: The late 1970s and early 1980s saw continued interest in export industries, small-scale industries, resource-based and labor-intensive industries and the promotion of regional industries. In particular on the FDI front, in 1977 a new Investment Promotion Law was passed which provided the BOI with more power to provide incentives to priority areas and remove obstacles faced by private investors. Regional inequalities also became a key concern and the BOI steadily shifted its emphasis from promoting export activities to promoting regional areas.

Phase 4: By the early 1980s, policy makers had become aware of the inefficiencies fostered by high protection. In the late 1980s and early 1990s, therefore, they started to promote openness and competitiveness. However, the strategy of opening up was not well thought through; the selection of sectors was carried out in a rather *ad hoc* manner, based on short-term assessments of industrial weaknesses rather than on long-term strategy.

Phase 5: The financial crisis, in particular, forced the government to focus on the short-run financial restructuring and corporate restructuring of the large distressed companies. IN light of increasing awareness of the importance of competitiveness, and the declining position of Thailand in the international competitiveness sweepstakes, the post crisis period also saw a number of initiatives to develop the industrial base and exports, largely in the form of supporting institutes.

The 9th Economic and Social Development Plan to be implemented starting in 2002 identifies competitiveness as one of the main pillars and embodies the return to longer-term issues. More recently, the present administration of Prime Minister Thaksin has seen increasing attention to industrial development and competitiveness. In early 2002, a very high-level National Competitiveness Committee was established to spearhead government's policy efforts across a wide range of related areas, combined with the establishment of a special Office for SMEs Promotion, something akin to the Board of Investment focusing on supporting SMEs.

In terms of longer-term structural changes, Thailand has experienced GDP and export shifts that appear to be lagging those of the East Asian newly industrializing economies (see Table 2.2). In the other three countries, agriculture has fallen almost to negligible levels, industry has generally increased (with the exception of Taiwan), and services now account for around 50-60 percent. In Thailand, services are a little less important while agriculture remains at 10 percent.

Table 2.2
Changes in Thailand's Distribution of GDP (%) by Sector as Compared to the NIEs

	Korea					Singapore				
Sector	1960	1970	1980	1990	2000	1960	1970	1980	1990	1999
Agriculture	36.9	28.9	14.9	8.5	4.6	5.8	2.3	1.3	0.4	0.1
Industry	14.7	24.4	41.3	43.1	42.7	10.4	29.8	38.1	34.4	34.3
Services	48.4	46.7	43.7	48.4	52.7	83.8	67.9	60.6	65.3	65.6
	Taiwan					Thailand				
Agriculture	N/A.	17.7	7.7	4.2	2.1	37.1	30.2	23.2	12.5	9.1
Industry	N/A.	40.9	45.7	41.2	32.4	14.1	25.8	28.7	37.2	41.7
Services	N/A.	41.4	46.6	54.6	65.6	48.8	44.0	48.1	50.3	49.2

Source: ADB. (2000 and 2001) Key Indicators of Developing Asian and Pacific Countries 2000, Volume XXXI and Key Indicators 2001: Growth and Change in Asia And Pacific

On the export front, Thailand again appears to lag somewhat (see Table 2.3). While since 1980 resource-based and labor-intensive products have fallen in share by some 20 percentage points and science-based products have increased by around 25 percentage points, it is likely that much of this increase is in the lower-end, intensive-intensive sector of science-based exports. However, the trend is clearly towards electronics and related products.

Table 2.3
Distribution of Manufactured Exports by Technological Categories (%)

	Korea			Singapore			Taiwan			Thailand		
Sector	1980	1990	1999	1980	1990	1999	1980	1990	1999	1980	1990	1999
Resource-based	9.0	6.8	11.6	44.4	26.9	13.2	9.8	8.2	9.2	21.7	13.8	10.7
Intensive-intensive	49.2	40.8	23.2	10.6	10.3	7.6	54.3	41.2	31.0	47.0	45.5	35.8
Scale-intensive	23.6	19.3	21.0	9.3	5.9	5.5	9.1	10.3	10.6	7.8	6.3	7.7
Differentiated	11.3	15.6	18.7	20.5	22.3	21.2	12.4	20.6	20.4	22.2	14.1	19.5
Science-based	6.9	17.4	25.5	15.1	34.6	52.5	14.5	19.8	28.9	1.2	20.2	26.4

Source: Calculated from UN Comtrade data base

The issue of competitiveness became a critical area of policy focus throughout Southeast Asia following the economic crisis that struck in mid-1997. Countries such as Thailand re-examined their approach to growth and development and began searching for answers to what went wrong in the late 1990s. As mentioned earlier, Thailand's economic growth over the past few decades has been built on relatively low-tech industrial development dependent on a cheap and efficient workforce. Thailand was successful in shifting resources from traditional agriculture to labor-intensive manufacturing. Vast amounts of FDI helped fuel the Thailand economic miracle, and it appeared that the growth was limitless. However, with intense international competition, particularly from other Asian nations that offered lower cost labor and more abundant resources such as China, India, Indonesia, the Philippines, and Vietnam, Thailand gradually lost its competitive position in labor-intensive exports because of a strong Thai baht and rapid wage increases until the economic crisis struck in mid-1997.

Moreover, the country failed to undertake the necessary measures to continue moving up the value-added chain.

What accounts for this sharp drop in Thailand's competitiveness over the past few years? A recent analysis of the Thai response to the economic crisis (Flatters, 1999) concluded:

> "While overall productivity growth was moderate, most of it was in agriculture or arose from inter-industry shifts. There was little indication of growth of technological capabilities, or movements 'up the ladder of comparative advantage'. Among the widely recognized barriers to growth in competitiveness were very low levels and quality of education, serious deficiencies in infrastructure development, and a policy regime at the microeconomic level which was much too geared to creating and preserving rents than fostering market competition."

As the focus on developing competitiveness in Thailand shifts increasingly from macroeconomic to microeconomic factors, and as Thailand is forced to move up the value-added chain, the critical challenge will be one of developing the innovative capacity to develop and commercialize new technologies, products and processes. Innovation can be said to "drive the rate of long-term productivity growth and hence future competitiveness" (Global Competitiveness Report 1999), but Thailand has fallen far short in this critical determinant of competitiveness[5].

The crisis revealed Thailand's deficiencies in research and development, science and technology, and in its overall education system. The investments in human resources and R&D that are required to build the foundations for innovation involve a significant public good element, are relatively bulky (or indivisible), and require a long time for the results to become evident. This provides clear economic rationale for a strong government commitment to supporting programs to develop higher quality S&T manpower and increased attention to R&D both in the public and private sectors. If the Thai government waits any longer to make this critical commitment to research and development and high-level human resource development, one could expect a similar "competitiveness" crisis to reoccur after several years of mild recovery.

Thailand has thus reached a critical crossroads in its quest to build back the competitiveness of its industrial base. The Asian economic crisis dealt a heavy blow to the Thai development model. With an increased recognition that macroeconomic liberalization and an economy driven by manufactured exports would not ensure sustainable growth, Thai policy makers and firm managers are belatedly shifting their attention to technology matters and human resource development, and hopefully on ways in which FDI can be leveraged more strongly to support these objectives.

[5] See Brooker Group, 2001 and Arnold et al, 2000 for more information on these issues.

3. FDI Policies and Trends

3.1 Trends in FDI and Major Impacts

FDI inflows into Thailand increased substantially in the second half of the 1980s after the Plaza Accord, which resulted in currency appreciation in Japan and NIEs such as Taiwan, Hong Kong and Korea. From 1986 to 1989 Thailand attracted on average US$ 0.9 billion per annum of net FDI flows, accounting for around seven percent of private business investment.

From 1990 to 1996, FDI hovered around a plateau of over US$ 2 billion per year, with a slight drop to US$ 1.7 billion in 1993 and US$ 1.3 billion in 1994 as the effects of the political unrest in the early 1990s affected foreign investor confidence. During this period, there were substantial FDI flows into large-scale basic industries such as steel and petrochemical, as well as infrastructure projects.

Following the depreciation of the Baht in 1997, FDI inflows have shown a dramatic increase in both Baht and dollar terms, totaling US$ 3.6 billion in 1997, US$ 5.1 billion in 1998 and US$ 3.6 billion in 1999 before falling to US$ 2.8 billion in 2000 and increasing to US$ 3.7 billion in 2001(see Table 3.1). Initial indications from the first five months of 2002 are that FDI is headed for a dramatic fall in 2002, with an average monthly FDI inflow of US$ 45 million – compared with more than US$ 310 in 2002. This worrying development deserves careful evaluation, as it would represent a significant reduction in foreign exchange inflows as well as indicating a much smaller FDI base to leverage.

This growth of FDI in the post-crisis period was characterized by a dramatic increase in mergers and acquisitions (M&A) as foreign firms took over Thai companies that faced severe debt and liquidity problems. While hard statistics on this shift are not available, UNCTAD's *World Investment Report 2000* reported that cross-border M&A sales or M&A FDI in Thailand amounted to about US$ 0.6 billion in 1997 before rising to US$ 3.2 billion in 1998 and slightly dropping to US$ 2.0 billion in 1999 and US$ 2.6 billion in 2000. These orders of magnitude were confirmed by a firm-level survey on M&A (Brimble and Sherman, 1999). In terms of the contribution of M&A transactions to total net FDI flows[6], it is estimated to have increased from around 50-60 percent in 1998-1999 to 90% in 2000. Indications are that this massive shift to M&A activities fell almost as quickly as it rose, with much fewer deals and estimated values in 2001 and 2002.

[6] It should be noted that the Bank of Thailand did not include foreign capital inflows for banking capitalization in FDI statistics. The figure was about US$ 2 billion in 1998, which is when most of the capital injections into the banking sector occurred.

Table 3.1
Inward and Outward FDI Flows in Thailand

Year	(million baht)		(million US$)		
	Net FDI Inflows	Net Outward FDI	Net FDI Inflows	Net FDI Inflows Per Month	Net Outward FDI
1970	891	neg.	45	4	neg.
1971	808	neg.	40	3	neg.
1972	1,427	neg.	71	6	neg.
1973	1,605	neg.	80	7	neg.
1974	3,836	neg.	192	16	neg.
1975	1,745	neg.	87	7	neg.
1976	1,614	neg.	81	7	neg.
1977	2,164	neg.	108	9	neg.
1978	1,135	124	56	5	6
1979	1,128	80	55	5	4
1980	3,878	62	189	16	3
1981	6,414	51	289	24	2
1982	4,331	-7	188	16	0
1983	8,225	33	356	30	1
1984	9,638	14	412	34	1
1985	4,402	23	160	13	1
1986	6,908	28	262	22	1
1987	9,044	4,333	354	30	172
1988	27,964	615	1,106	92	24
1989	45,698	1,285	1,780	148	49
1990	64,695	3,576	2,542	212	140
1991	51,390	4,279	2,033	169	167
1992	53,691	3,461	2,151	179	136
1993	43,812	7,416	1,732	144	294
1994	33,241	10,582	1,326	111	422
1995	49,887	20,823	2,004	167	835
1996	57,472	20,649	2,271	189	816
1997	117,696	12,434	3,627	302	447
1998	209,888	4,671	5,143	429	124
1999	134,592	12,781	3,562	297	344
2000	115,286	2,098	2,813	234	52
2001p	167,664	7,634	3,759	313	171
2002pp	9,895	2,380	227	45	55

Source: Bank of Thailand; p - preliminary; pp - preliminary Jan-May.

Note: neg. - negligible; Thai net outward flows of equity only.

Net inward flows of both loans and equity, not including the banking sector

Table 3.2 shows FDI by sector since 1970. The manufacturing sector has consistently been a large recipient of FDI with an increasing share in net FDI flows. The sector share increased from an average of 37 percent during 1970-1995 to 57 percent in 2001. The trade sector has also gained share but at a lower magnitude from an average of 17 percent during 1970-1995 to between 20 and 30 percent of FDI over the past few years, dropping to only two percent in 2000 before recovering to 24 percent in 2001. FDI in financial institutions went up significantly in 1998 to over 16 percent as a result of the increase in limits of foreign participation in the banking sector; in the two previous years, the financial sector accounted for only three percent of FDI. Once the banking sector essentially reached its limits for foreign participation, FDI dropped to seven and five percent in 1999 and 2000, respectively, and saw a net outflow in 2001. A popular sector for FDI in the early to mid-1990s was real estate, which peaked at 33 percent of FDI in 1996, but once the property bubble burst in 1996 and 1997, the inflows almost completely dried up.

Within the manufacturing sector, the electronics industry relatively consistently attracts large volumes of FDI, amounting to 17.6 percent in 2001. For the period 1998-2000, however, electronics was overtaken by machinery and transport equipment, deriving mainly from the automotive industry, as many Japanese automotive parent companies injected capital to assist their subsidiaries and suppliers in Thailand following the crisis. The chemical industry surged in 2000 as a number of local producers were restructured, accounting for 13.6 percent of FDI, before completely dropping off in 2001.

Sources of FDI in Thailand have generally been quite diversified, including Japan, the United States, Europe, Taiwan, Hong Kong, and Singapore as shown in Table 3.3. Japan had been the largest national source of FDI since the late 1970s with the exception of being overtaken by the US in 1999 and by Singapore in 2001. Japanese FDI dropped sharply in 1999 as a result of the weak economic conditions in the home economy, but bounded back in 2000 and 2001 as Japanese firms increased equity shares in local subsidiaries. Since 1998, Singapore has ranked high as a number of high profile Singaporean investments took place in banking, telecommunications, and others, and certain foreign investors used their Singapore-based affiliates as vehicles for activities in Thailand. The importance of Singapore is potentially a worrying signal in light of the weaknesses in the global electronics sector and the potential for Singaporean investors to sustain such high levels of investment. European investment rose strongly in 1998 and 1999, led by the Netherlands, but fell off rapidly in 2000 to 2001, with a substantial net outflow of Dutch FDI in both years. This decline was mirrored by a dramatic fall-off in US FDI to only 1.5 percent in 2001.

Table 3.2
Net Flows of Foreign Direct Investment in Thailand by Sector

Million US$

Sector	1970-1995	1996	1997	1998	1999	2000	2001p
1. Industry	6,591	709	1,820	2,209	1,268	1,813	2,153
1.1 Food & sugar	499	45	226	74	93	94	108
1.2 Textiles	492	49	42	125	20	29	55
1.3 Metal & non metallic	774	113	216	342	263	93	355
1.4 Electrical appliances	2,311	241	604	264	425	298	662
1.5 Machinery & transport equipment	584	109	396	661	394	667	430
1.6 Chemicals	1,018	183	163	225	8	383	48
1.7 Petroleum products	-25	-250	10	329	8	30	277
1.8 Construction materials	57	3	-10	24	38	58	-3
1.9 Others	877	216	173	165	19	161	221
2. Financial institutions /1	1,215	72	110	842	247	134	-187
3. Trade	3,075	545	1,033	1,051	1,042	68	891
4. Construction	1,776	70	163	192	-151	-3	-3
5. Mining & quarrying	976	19	20	21	-42	-275	517
6. Agriculture	137	2	2	0	1	0	2
7. Services	726	125	292	275	485	449	164
8. Investment	59	-21	26	364	571	99	-49
9. Real estate	3,299	753	110	28	150	70	111
10.Others	-156	-3	51	161	-9	458	160
Total	17,698	2,271	3,627	5,143	3,562	2,813	3,759
	(% Share in Total)						
Sector	1970-1995	1996	1997	1998	1999	2000	2001
1. Industry	37.2	31.2	50.2	43.0	35.6	64.5	57.3
1.1 Food & sugar	2.8	2.0	6.2	1.4	2.6	3.3	2.9
1.2 Textiles	2.8	2.2	1.2	2.4	0.6	1.0	1.5
1.3 Metal & non metallic	4.4	5.0	6.0	6.6	7.4	3.3	9.4
1.4 Electrical appliances	13.1	10.6	16.7	5.1	11.9	10.6	17.6
1.5 Machinery & transport equipment	3.3	4.8	10.9	12.9	11.1	23.7	11.4
1.6 Chemicals	5.8	8.1	4.5	4.4	0.2	13.6	1.3
1.7 Petroleum products	-0.1	-11.0	0.3	6.4	0.2	1.1	7.4
1.8 Construction materials	0.3	0.1	-0.3	0.5	1.1	2.1	-0.1
1.9 Others	5.0	9.5	4.8	3.2	0.5	5.7	5.9
2. Financial institutions /1	6.9	3.2	3.0	16.4	6.9	4.8	-5.0
3. Trade	17.4	24.0	28.5	20.4	29.3	2.4	23.7
4. Construction	10.0	3.1	4.5	3.7	-4.2	-0.1	-0.1
5. Mining & quarrying	5.5	0.8	0.6	0.4	-1.2	-9.8	13.8
6. Agriculture	0.8	0.1	0.1	0.0	0.0	0.0	0.1
7. Services	4.1	5.5	8.1	5.3	13.6	16.0	4.4
8. Investment	0.3	-0.9	0.7	7.1	16.0	3.5	-1.3
9. Real estate	18.6	33.2	3.0	0.5	4.2	2.5	3.0
10.Others	-0.9	-0.1	1.4	3.1	-0.3	16.3	4.3
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0

1/ The figures cover investment in non-bank sector only. p - preliminary

2/ Direct Investment = Equity Investment plus loans from related companies.

Source : Bank of Thailand, by Economic Research Department

Table 3.3

Net Flows of Foreign Direct Investment in Thailand by Region/Country

Million US$

Region/Country	**1970-1995**	**1996**	**1997**	**1998**	**1999**	**2000**	**2001p**
Japan	**5,334**	**523**	**1,348**	**1,485**	**489**	**869**	**1,374**
USA	**3,000**	**429**	**780**	**1,284**	**641**	**617**	**57**
European Union (EU)	**1,884**	**170**	**360**	**912**	**1,369**	**507**	**178**
UK	**651**	**57**	**123**	**103**	**183**	**401**	**329**
Germany	**344**	**42**	**59**	**101**	**289**	**104**	**32**
France	**393**	**30**	**2**	**277**	**241**	**27**	**102**
Netherlands	**361**	**- 40**	**156**	**333**	**644**	**- 73**	**- 384**
Newly Industrialized Countries	**5,919**	**653**	**879**	**1,114**	**896**	**845**	**1,805**
South Korea	**107**	**25**	**31**	**72**	**4**	**- 5**	**23**
Taiwan	**1,070**	**138**	**133**	**106**	**122**	**159**	**57**
Hong Kong	**2,893**	**215**	**444**	**395**	**233**	**333**	**162**
Singapore	**1,849**	**275**	**271**	**541**	**537**	**358**	**1,563**
ASEAN (less Singapore)	**118**	**37**	**26**	**35**	**35**	**29**	**44**
Other Countries	**1,443**	**459**	**234**	**313**	**132**	**- 54**	**301**
Total	**17,698**	**2,271**	**3,627**	**5,143**	**3,562**	**2,813**	**3,759**
	(% shares in total)						
Region/Country	**1970-1995**	**1996**	**1997**	**1998**	**1999**	**2000**	**2001**
Japan	**30.1**	**23.0**	**37.2**	**28.9**	**13.7**	**30.9**	**36.6**
USA	**17.0**	**18.9**	**21.5**	**25.0**	**18.0**	**21.9**	**1.5**
European Union	**10.6**	**7.5**	**9.9**	**17.7**	**38.4**	**18.0**	**4.7**
UK	3.7	2.5	3.4	2.0	5.1	14.3	8.8
Germany	1.9	1.8	1.6	2.0	8.1	3.7	0.9
France	2.2	1.3	0.1	5.4	6.8	1.0	2.7
Netherlands	2.0	-1.8	4.3	6.5	18.1	-2.6	-10.2
Newly Industrialized Countries	**33.4**	**28.8**	**24.2**	**21.7**	**25.2**	**30.0**	**48.0**
South Korea	0.6	1.1	0.9	1.4	0.1	-0.2	0.6
Taiwan	6.0	6.1	3.7	2.1	3.4	5.7	1.5
Hong Kong	16.3	9.5	12.2	7.7	6.5	11.8	4.3
Singapore	10.4	12.1	7.5	10.5	15.1	12.7	41.6
ASEAN (less Singapore)	**0.7**	**1.6**	**0.7**	**0.7**	**1.0**	**1.0**	**1.2**
Other Countries	**8.2**	**20.2**	**6.4**	**6.1**	**3.7**	**-1.9**	**8.0**
Total	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

1/ The figures cover investment in non-bank sector only. p - preliminary

2/ Direct Investment = Equity Investment plus loans from related companies.

Source : Bank of Thailand, by Economic Research Department

Table 3.4 shows that there has been overall a decline in investment interest in Thailand. The total planned investment of foreign projects approved by the BOI dropped by 58 percent from 326 billion Baht in 1996 to 136 billion Baht in 1999. This trend resulted mainly from the shrinking of domestic demand following the crisis. In 2000 and 2001, the levels of BOI approvals increased to around 210 billion baht in both years, largely due to an increase in expansion investments of export oriented projects that performed very well after the Baht devaluation.

In addition to the clear effects of FDI on foreign exchange inflows and exports[7], it has been found that foreign firms on average utilized labor and capital 50 percent more efficiently than Thai firms, although a group of highly productive Thai firms also performed as well as their foreign counterparts[8]. This indicates strongly the critical role that FDI can play in contributing to overall productivity (Dollar et. al., 1998). It has also been found that foreign enterprises in Thailand are becoming more involved in innovative programs to train and to undertake technological activities[9]. While not yet constituting a statistically significant quantitative trend, there are a number of interesting stories of such activities.

The benefits of foreign firms go beyond training and technology development. One additional impact they have had in Thailand is to promote higher standards of employment practices such as safety and sexual discrimination. Foreign firms have also played an instrumental role in addressing issues such as AIDS in the workplace.[10]

It appears evident that FDI has made important contributions to the Thai economy beyond simply generating new employment. It saved many jobs during the crisis by helping to capitalize failing local industries. Other less evident benefits include bringing in new technology and industries to spur competitiveness, improving corporate governance and standards for working conditions, strengthening local capabilities through linkages, and assisting with policy reforms and industrial restructuring.

It is imperative that government and private industry better understand the potential spillover benefits from FDI, particularly in how it helps increase the country's and firms' competitiveness. The government will need to put forth a platform of policies designed to specifically enhance competitiveness, restructure the industrial base, strengthen the legal and regulatory frameworks that support business, and support closer interface among the government, foreign investors, and the domestic business community. Moreover, the government will need to explore selective interventions to encourage innovative programs with foreign investors—such as linkages with local firms, academic institutions, and communities. For its part, the local private sector will need to develop strategies to harness the technical and managerial capabilities of foreign firms, establish greater forward linkages with foreign firms, and discern ways of increasing their competitive position in global markets.

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7 See Brimble 2002 for a summary of previous studies in regard to exports and other impacts.

8 These results were calculated from firm-level data of more than 1,000 firms from which a simple production function was estimated. More details are provided in Dollar et. al, 1998.

9 See Brimble et al., 1999 for additional examples. More such case studies are presently being compiled by The Brooker Group for a number of research projects related to competitiveness.

10 An innovative position paper presented in Joint Foreign Chambers of Commerce in Thailand (JFCCT). 2001, contains additional examples of the beneficial impacts of MNCs and identifies, from the perspective of the MNCs themselves, ways and means to enhance these impacts.

Table 3.4
Foreign Investor Interest in Thailand: BOI Approvals

Million Baht

Country	1995		1996		1997		1998		1999		2000		2001	
	No.	Total Investment	No.	Total Investment	No.	Total Investment	No.	Total Investment	No.	Total Investment	No.	Total Investment	No.	Total Investment
Total Foreign Investment	**561**	**397,168**	**490**	**326,335**	**516**	**301,596**	**485**	**255,070**	**517**	**136,060**	**761**	**212,649**	**575**	**209,622**
100% Foreign Investment	136	36,856	142	75,109	188	36,846	204	79,977	264	77,226	380	123,231	315	106,679
Asia														
Japan	267	190,569	233	143,693	220	147,619	158	54,113	188	27,042	282	107,382	257	83,369
Asian NIEs														
- Taiwan	91	39,945	61	69,135	56	11,931	69	10,029	86	7,910	120	17,632	50	6,824
- Hong Kong	12	2,032	8	1,675	9	1,389	16	5,064	25	1,899	31	6,241	20	9,710
- Korea	14	42,247	19	22,189	20	3,965	13	1,836	19	981	17	1,394	21	1,437
- Singapore	36	32,033	41	41,798	43	59,028	49	10,647	52	7,003	84	19,910	51	8,985
P.R.C.	5	196	4	889	1	45	2	69	7	560	8	367	12	8,690
Malaysia	23	5,121	23	1,730	33	4,713	21	4,129	27	3,418	43	6,095	29	27,895
Indonesia	3	712	3	634	3	559	2	480	5	1,149	4	1,300	2	350
Philippines	2	220	0	0	0	0	0	0	1	72	0	0	0	0
India	9	8,658	11	8,307	5	180	10	10,157	6	1,374	11	10,166	12	1,954
North America														
U.S.A.	45	62,613	46	64,780	4	88,366	62	18,646	53	46,351	72	37,752	40	40,131
Canada	4	542	2	56	6	310	9	2,631	3	26,002	6	1,089	5	334
Australia														
Australia	7	14,775	6	1,026	16	4,733	13	2,756	10	1,177	21	2,705	21	6,030
All Europe	72	53,592	87	58,021	95	88,813	123	134,326	83	34,007	144	31,175	87	26,042
- UK	18	6,067	22	9,952	24	28,460	33	31,380	17	3,919	38	5,815	18	4,852
- Germany	12	4,352	19	7,775	19	9,425	22	8,606	12	1,868	39	6,394	24	13,719
- Switzerland	7	1,980	9	2,630	10	898	11	1,548	10	3,170	10	2,283	7	2,545
- France	5	558	8	4,389	9	1,698	12	181	11	2,829	13	1,097	11	1,293
- Belgium	5	927	7	3,498	3	1,720	8	948	7	858	2	316	7	384
- Italy	10	1,235	2	38	7	935	4	783	3	106	9	425	2	629
- Netherlands	9	1,749	15	17,476	12	4,258	22	88,066	18	22,481	21	6,329	10	3,698

Notes: Firms with investment from more than one country are double counted. Foreign projects are those with a foreign component of 10% or more.
Source: Board of Investment

3.2 The FDI Policy Approach

The Thai government has in general taken a very favorable approach towards FDI. Although there have been laws and regulations which limit foreign ownership in certain activities, they have been progressively liberalized over the past decade, with an acceleration of this trend in the period since the crisis.

Alien Business Law. The Alien Business Law, which was enacted in 1972 and restricted majority foreign ownership in certain activities, was amended in 1999. The new law relaxes limits on foreign participation in several professions such as law, accounting, advertising and most types of construction, which have been moved from a completely prohibited list to the less restrictive list of businesses in which Thais are not yet ready to compete. It also reduces previous limits on foreign ownership of firms and manufacturing certain products such as cement, pharmaceuticals, alcohol, textiles, garments and footwear. However, newspaper publishing, farming and antique trading have become more restricted. Previous restrictions on retail company and securities brokerage have been relaxed and no longer require special government approval of foreign ownership. However, the relaxation on retail business has caused public outcry about the impact of large foreign discount stores on local retail outlets, and the present government has been under pressure to review the Law[11].

[11] Indeed, a committee has been established to review the law, and preliminary indications are that a more restrictive definition of foreign ownership will be recommended as an amendment to the law. The time frame for the consideration and possible implementation of this are uncertain.

BOI's Ownership Limits/Conditions. The Board of Investment (BOI) used to restrict majority foreign ownership in promoted projects that are resource based, services, and manufacturing mainly for the domestic market. It has gradually relaxed this condition over the past decade. In 1993, it allowed 100 percent foreign ownership for manufacturing projects located in Zone 3 (the least developed provinces) or exporting at least 80 percent of total sales. The BOI also no longer considers the level of foreign ownership firms for projects that develop transportation systems and public utilities, improve the environment, and are directly involved in technological development.

Since the end of October 1997, the BOI provides approval on a case-by-case basis for foreign manufacturing firms in Zones 1 (Bangkok and the other developed provinces) and 2 (medium-range developed provinces) to change their equity ownership to become majority or 100 percent foreign-owned if local shareholders give their consent. From November 1997 to December 2000, 468 companies were granted permission to change their ownership structures. This represents a surge in a rather novel form of merger and acquisition (M&A) activities – the so-called BOI-type M&A which involved inflows of over US$ 1 billion by the end of 2000. The BOI also abolished foreign ownership restrictions for new manufacturing projects in Zones 1 and 2 since August 2000 under the new incentive package.

The BOI has been active in undertaking other policy and service measures to stimulate expansion projects from existing investors and new greenfield projects, and also to encourage foreign investment. Policy changes and incentives aimed at foreign investors include the following:

- The granting of investment promotion to existing non-BOI promoted companies seeking additional foreign equity participation. The following conditions shall apply in this case:
  - Companies must conduct activities eligible for promotion. However, location requirements shall not be imposed.
  - Applications must be submitted within 1999.
  - Only non-tax incentives will be granted, including permission to own land, and to bring in foreign experts and technicians.
- BOI-promoted companies are entitled to own land for residential and business purposes.
- Foreigners are now allowed to obtain permanent residence permits by investing certain sums in Thailand.
- Establishment of a one-stop shop in 1997 to provide foreign companies with expedited services related to bringing in expatriates to work in Thailand.
- The granting of non-tax incentives to trade and investment support offices, with a view to facilitating foreign companies' operations in Thailand.

The BOI has enhanced its role in matchmaking by introducing a Vendors Meet Customers Program (VMC), which involves regular arrangement of supplier tours to select automotive and electronics assemblers and aims to encourage subcontracting businesses in Thailand. The BOI has also launched the ASEAN Supporting Industry Database (ASID) in order to encourage sourcing of local parts and components.

Financial Sector Liberalization. Thailand's weak financial sector played a major role in triggering the economic crisis in 1997. The banking and financial sector has been practicing unsound lending activities, replete with inadequate or no collateral, low bank capital requirements, and misallocation of funds. Compounding the problems were an extremely lax regulatory framework, including inadequate supervision and a lack of transparency, a bankruptcy law without any teeth, and growing political interference in macroeconomic management. The result of these problems was the near collapse of the financial sector in

Thailand. Fifty-six finance firms closed by the end of 1997, and six banks were nationalized in 1998. The remaining banks were in frail condition, saddled by 2.73 trillion baht in non-performing loans (NPLs), equal to nearly half of all lending.

Faced with tremendous re-capitalization needs of the Thai financial sector, the authorities essentially removed foreign ownership controls for financial institutions. The government announced in October 1997 that it would allow foreign firms to hold a majority or 100 percent stake in operating financial institutions for up to 10 years, after which any further capital increases will have to be made available to local parties if foreign investors hold more than 49 percent. The government also embarked on a privatization program for state-owned banks, the sale of billions of baht worth of assets from the closed financial institutions, and more recently, drafted legislation to establish the Thailand Asset Management Corporation, which will consolidate the remaining NPLs in the banking sector.

*Legal Infrastructure***.** The legal framework for foreign involvement in industrial restructuring and M&A activities remains weak but has recently been considerably revamped. The Bankruptcy Law was significantly amended by Parliament in March 1999 to provide improved security for new lenders among other measures designed to facilitate corporate rehabilitation and debt restructuring. Parliament also approved the establishment of a specialized bankruptcy court. However, the Bankruptcy Courts and the application of the amended Bankruptcy Law have barely scratched the surface of the vast backlog of cases. Instead, more "informal" processes such as arbitration and payment rescheduling arrangements between the creditor and borrower have been more successful in reducing the number of NPLs.

Reforms were also made to the Foreclosure Proceedings Law to streamline the court processes for the settlement of claims and to the Foreclosure Law (in the Civil and Commercial Code) in order to increase the provision of secured credit. Overall, these reforms are expected by most observers to create an environment of certainty over ownership that will encourage much greater foreign involvement in the disposition of the assets from the defunct finance companies as well as working out the non-performing loan problems of the financial sector.

Although the general policy framework for foreign investment in the past few years has become more liberal, it must be admitted that relatively little attention has been placed on the technological features of FDI; it has been sought mainly to generate employment or exports, or to play a role in the massive restructuring process.

Recent BOI investment policies, especially the revision in 2000, still place emphasis on decentralization of investment into regional areas. The BOI also placed a cap on corporate income tax exemption, limiting such exemptions to not exceed the amount of investment capital (excluding costs of land and working capital). In addition, in order to strengthen competitiveness of Thai industries, the BOI has required investors with investment capital over 10 million baht to obtain ISO 9000 certificates within two years of operation.

The present government is now reviewing the BOI policy, with indications that the BOI will in the future begin to provide more customized incentives to attract investors in targeted industries, as compared to the relatively automatic approach in granting incentives that has been implemented by the BOI over the past decade. This trend will be in line with the deliberations of the newly formed National Competitiveness Committee.

3.3 FDI Promotion Activities

The Thai BOI has carried out activities under the three following broad headings, but with the emphasis varying from time to time.

1. Image building to demonstrate how the host country is an appropriate location for FDI. Promotion activities include:
   - Advertising in general and business media;
   - Participating in investment exhibitions;
   - Advertising in industry or sector specific media;
   - Conducting general investment missions; and
   - Conducting general information seminars on investment opportunities.

2. Investment generation by targeting investors through various activities:
   - Engaging in direct mail or telemarketing campaigns;
   - Conducting industry or sector specific investment missions;
   - Utilizing networks of overseas offices;
   - Meeting with existing foreign investors; and
   - Engaging in firm specific research followed by sales presentations.

3. Servicing investors by:
   - Providing investment counseling services;
   - Expediting the processing of applications and permits; and
   - Providing post-investment services.

Image Building

It was not until the mid-1980s that the BOI started to carry out systematic promotion campaigns Before that it had a very small annual budget and relied almost exclusively on overseas offices in New York, Frankfurt, Tokyo and Sydney and a few missions a year. In 1986, the BOI obtained an extra budget of 50 million baht to accelerate FDI from Europe and Japan. At that time, as the Yen appreciated significantly and Japanese firms needed to find cheaper production bases abroad, the BOI found the situation conducive to diversify FDI sources, especially from Europe. Activities that were carried out included advertising, arranging for investors and journalists to visit Thailand to explore investment opportunities, and organizing overseas missions.

In May 1992 Thailand experienced a political crisis that created a very negative image in the international investment community. Therefore, the BOI initiated a campaign under the slogan "Thailand: Open Society, Dynamic Economy" with cooperation from both the public and private sectors. The total budget was 80 million baht, with 50 million baht from the public sector and 30 million baht (both in cash and in kind) from the private sector. Activities under the program included: advertising in leading newspapers in targeted countries, organizing missions and presentations, inviting foreign business leaders and journalists to visit Thailand, organizing the Thailand Forum involving about 50 CEOs of leading foreign companies that had invested in Thailand to demonstrate their confidence in the Thai economy, and publishing newsletters to inform investors about economic and political developments in Thailand. The campaign appeared to be somewhat successful in restoring Thailand's image.

Another important campaign to demonstrate the capability of the Thai industry was the BOI Fair that was organized in 1995, also to celebrate the King's 50th anniversary on the throne. It was successful, with over a million visitors during 10-day period.

The economic crisis in 1997 again prompted the BOI to carry out an image building campaign. The 6-month campaign with a budget of US$ 3 million concentrated on demonstrating the Thai government's seriousness in solving the economic problems. It was a joint cooperation between the public and private sectors with the Time Warner group. The general consensus was that the campaign took place too early and that problems of validating claims compromised the image building efforts.

As the economy began to improve, another BOI Fair was organized in early 2000 to strengthen confidence among Thai as well as foreign investors. The exhibition-cum-trade fair was organized in conjunction with the CEO Forum that provided 200 foreign and Thai CEOs access to key government officials. In addition, 200 seminars were arranged during the fair. It was estimated that about 4 million visitors came to the fair.

Investment Generation

Since the early 1990s the BOI has placed more effort on strengthening the role of the overseas offices. Two more offices were added in Paris and Hong Kong (the latter was later closed and replaced by Osaka). Staff in overseas offices were required to make fixed numbers of new contacts with targeted companies. The BOI also carried out sector studies and seminars and sent mobile units to targeted countries. However, the target activities were not systematic and the tracking system was not well in place and varied from office to office. The BOI has just started to put in place a computerized tracking system for investors

A recent announcement by the BOI in June 2002 identified five industries to be targeted for proactive marketing: namely agro-processing; fashion industries especially garment, leather and jewelry; automotive; information and communication technology (ICT) including electronics; and high value added services such as long stay tourism and regional headquarters. However, the nature of the targeting and proactive marketing to be carried out is not yet clear.

Investment Services

The BOI has long provided comprehensive services to investors.

- Internet homepages that offer various types of information to investors.
- The BUILD Unit which helps develop linkage between MNCs and local suppliers by organizing various activities such as the Vendor meets Customer Program in which MNCS allow potential supplies to visit them to discuss possibility for more local sourcing, the Market Place for parts and components where buyers display parts that they want; and the BUILD Fair.
- One Stop Shop for Visas and Work Permits that issues visas and work permits within 3 hours
- The Investment Service Center that helps in match making and providing consulting services.

The BOI plans to put more emphasis on creating an enabling environment for investors, especially in providing adequate infrastructure and skilled workers, as well as helping investors to solve their problems. The Human Resource Development Unit has recently been

set up to work with the Department of Vocational Education and relevant institutes to supply technicians as required by the private sector.

4. Conclusions and Recommendations

4.1 The Main Conclusions: Opportunities Lost

The first and most pervasive conclusion is that the full potential of FDI has not been realized. Using the typology developed by Sanjaya Lall (2000), Thailand has essentially followed a strategy towards FDI that lies well to the passive end of the spectrum. Thailand receives billions of dollars worth of FDI, and the impact on the economy, growth, and employment is substantial. However, relatively little attention has been placed: (a) on exploring the potentially broader impacts of FDI in terms of linkages between foreign and domestic firms, technological capacity building, and knowledge and skills transfer; and (b) on the potential for undertaking more targeted investment promotion activities to fill technology gaps and meet technology needs.

In the area of technology development, and in other arenas as well, this partly derives from the need for key policy makers to recognize that firms are not only users of S&T services but also the major generators of S&T results; they are the center of the national innovation system. Attitudes toward the promotion of technological development activities in Thailand must recognize this, and be significantly changed to put in place incentive measures that will stimulate these firm-level efforts.

Second, Thai policy makers need to recognize that the challenge in the global economy of today is to build knowledge, not just buildings and machines. Most incentives, and in particular investment incentives, that are in place continue to primarily support capital investments of one kind or another. While there has been much discussion of the knowledge economy and the value of information, innovative FDI policies to support the domestic acquisition, utilization and development of such assets remain to be developed and implemented.

Third, the need to actively enhance the broader impacts of foreign investors. While prevailing perceptions are that MNC domestic strategies are completely determined by the head office and that little is to be gained by closer collaboration with domestic MNC affiliates, international evidence shows that MNCs are increasingly giving greater autonomy to their affiliates in developing countries to make decisions on allocating resources to a range of activities that support technological development, ranging from technical training to R&D activities (see Arnold et al, 2000). This trend is also becoming increasingly evident in Thailand and needs to be exploited.

Fourth, the need to carefully distinguish between the welfare and competitiveness objectives in considering policy measures to enhance industrial competitiveness. A common perception in Thailand is that large or foreign firms are capable of helping themselves and do not require assistance from the government. The weight of international evidence indicates that the use of public sector incentives to "encourage good firms to do good things better and with more spillovers" can be good investments if the true externalities are correctly evaluated and the programs are implemented fairly and efficiently. The critical lesson for Thai policy makers is to create an environment that stimulates the private sector to devote greater resources to technological development activities, especially those that lead to spillovers, and not to feel

threatened by the resulting "dynamism" generated by the business sector. Indeed, if channeled properly, this private sector dynamism will drive Thailand to higher levels of competitiveness.

Fifth, the need to strengthen the investment promotion activities and make them more proactive as tools of competitiveness policy, responding to the technological, managerial, marketing and financial needs of the industry. Efforts to date have been relatively extensive, but not well coordinated or monitored.

4.2 Towards An Agenda for FDI Policies in Thailand[12]

Selective Interventions. Efforts to enhance spillover benefits from FDI should become one important platform of policies to enhance competitiveness and restructure industry. Selective and active support from the government for innovative programs of foreign investors could be very effective at harnessing both the financial and technical resources of foreign investors. It is clear that the often-positive externalities associated with these activities provide a strong rationale for policies and programs that support such efforts.

Promoting linkages. Particular attention should be given to incentives and other programs that explicitly support linkages and interfaces between foreign investors and a wide range of local players. Virtually no real government support for these linkage programs exist at the present time.

- With government, in terms of inputs into formulating policies and providing regular feedback on the impacts and implementation of policies. The recent activities of the foreign business community to meet regularly with all key government agencies have been fruitful and should be intensified[13].
- With local firms, through vendor development programs and other activities such as cluster and supply chain development. The range of policies and programs available to countries that can be shown to have a demonstrable effect on backward linkage development is presented in World Investment Report, 2001, which finds that well-targeted government intervention can tilt the balance in favor of more linkages and thereby contribute to knowledge transfers from MNCs that can feed into the development of a vibrant domestic enterprise sector." An element of this type of policy could include matching grants for activities that can be demonstrated to create networks or linkages that support increasing efficiency of the value chain.
- With academic institutions, through university-industry linkages that involve two-way flows of information and technology. The types of activities undertaken by IDEMA (an international association of disk drive manufacturers with a Thai branch), jointly with AIT, demonstrates clearly the benefits of such linkages, with IDEMA actively been pressing for the introduction of better support programs for training activities in all firms, particularly SMEs and suppliers, but also for the major firms (as is the case in Singapore and Malaysia). Despite active efforts, and strong involvement of the hard disk drive industry, IDEMA to date has been able to identify very few programs that can be tapped to support these innovative activities.

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12 This section draws from Brimble, 2002.

13 See Joint Foreign Chambers of Commerce in Thailand (JFCCT) 2001, for more details on the content and nature of these meetings and related activities of the foreign business community.

Implementing strategic promotion activities. As competition increases and attention shifts to the "microeconomic foundations" of competitiveness, the importance of taking a more strategic approach to industrial development becomes more critical. In Thailand, there has been little in the way of strategic support programs for specific high-technology industry groups, and where such initiatives have been carried out, the approach is fragmented and characterized by lack of cooperation between the various government agencies. This contrasts with Singapore, which has implemented proactive strategic policies through various institutions, with a focus on cooperation between the public and private sectors to promote manpower development, technological upgrading, and the development of supporting industries, and with Malaysia that has an Industrial Master Plan which includes not only technology capability development but also research and development, product design and development of integrated supporting industries. Both Singapore and Malaysia have been very proactive with promotional strategies to attract new players to the their respective markets. Thailand needs to learn from these regional competitors. And the growing importance of so-called "created assets"[14] in the increasing competition for FDI also highlights the need for a more proactive role of the public sector in facilitating joint activities with foreign investors, as well as domestic investors, to stimulate the growth of competitiveness-enhancing networks and services.

Creating positive awareness. One element of the enabling environment that could be strengthened to facilitate FDI participation in Thailand is a more positive awareness of the potential contributions of foreign investors. This could involve better dissemination of information on the benefits of foreign involvement and the fact that most foreign investors make a long-term commitment to Thailand and are willing to go much further in supporting social and community development efforts.

4.3 Lessons Learned from the Thai Experience

A number of key lessons can be derived from the Thai experience:

- FDI policy making has tended to be determined in a reactive manner, rather than used as a tool to strengthen industrial competitiveness;
- The outputs of FDI have been judged more on the quantitative results (such as FDI inflows and exports generated by FDI) than on the qualitative impacts, which one could argue are becoming more important;
- In general, as the balance between investment promotion activities moves away from the provision of investment incentives, there is a strong need for better promotion activities;
- Investment promotion resources should increasingly focus on the strategic targeting of investment, and must address areas beyond the basic incentive package – such as technology and human resource development needs of industry;
- The critical need to work more closely with MNCs already in-country to maximize spillovers and enhance benefits to the domestic industry and community at large;
- The importance of building and maintaining networks with all key players – domestic and international;

[14] The growing importance of "created or strategic assets" in influencing foreign investment location decisions is documented extensively in World Investment Report, 1998. It is suggested here that one of the main results of greater so-called "broader" impacts of FDI could be to strengthen the level of "created assets" in the Thai business environment.

- The importance of a basic analytical capacity to relate FDI policies to broader policy issues, and the need for a firm-level tracking system to evaluate and improve promotion activities; and
- The availability of software and analytical tools means that even small BOIs can develop and implement Investor Targeting Strategies – something that can greatly enhance the investment promotion effort as well as utilize financial and staff resources more effectively.