

Economic Integration of Greater-Mekong Sub-Region and the Role of Small and Medium Enterprises

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1. Introduction

The Royal Thai government under the leadership of the Prime Minister, Dr. Thaksin Chinawat has set a clear direction of economic development of Thailand. On one hand, we would like to revitalize and strengthen the domestic social and economic structure by local wisdoms and domestic demand. We also would like to set target of progress of the nation by expanding our markets through several 'Free Trade Arrangements' or FTA.

Thai government has prepared linkages in consistent with the economic cooperation along the line of Greater Mekong Sub-Region (GMS). These are economic cooperation in the frame work of Ayrawadee—Chaopraya—Mekong Economic Cooperation (ACMEC) an extended version of Economic Cooperation Strategy (ECS) dialogue among countries like Thailand—Myanmar—Cambodia—Laos, Vietnam, and China (e.g., Yunnan Province), economic cooperation between Bangladesh—India—Myanmar—Sri Lanka—Thailand (BIMST EC), and economic cooperation between Indonesia—Malaysia—Thailand (IMT-GT). Here, the Thai government has laid down its strategy as follows; (1) Economic restructure, by gearing up its economic efficiency and cost cutting by procuring its intermediate material input from its neighboring countries through cooperation on agriculture development, (2) Promotion of SME through industrial development, (3) Thailand as hub for joint tourism in the region, for energy development, and transport and communication network, through giving Official Development Assistance (ODA) grant and loan for neighboring, (4) Human resource development through giving ODA grant for education promotion and training program. Here, the government has tried to set 'one stop service' of trade facilitations in most of important custom house connected to our neighbors.

The objective of this paper is as follows. First, we would like to depict briefly about Thai government policy and implementation towards the regional economic cooperation under GMS. Second, what is the role of small and medium enterprises (SME) in the regional economic development? And lastly, what is the role of Japan.

2. Thai Government Policy and Implementation on GMS Regional Economic Development

The 1997 crisis Thailand faced exposed inefficiency and internal flaws in our system. This painful experience has taught us the valuable lesson that we needed to comprehensively reform our industries, financial system, business sector and human resources to strengthen our immunity to such a crisis in the future. Here, Thailand seeks to reduce the risk exposure by expanding market horizon on the **demand side**. We realize that domestic market alone will not be sufficient to accommodate our production capacity. The government assigns the ambassadors to work on the top of diplomatic protocol, as ‘Chief Executive Officer or Ambassador—CEO’ in the country (market) of concern to promote Thai products. These are manufacturing products by SME, service like tourism, and local wisdom based product like ‘one village one product development’ that all of you perhaps are familiar with this idea.

The demand side management is matched by the assignment to 76 provincial governors to act as Governor—CEO to create a **supply response** to the external demand. The government aims to use this Ambassador—Ministry—Governor relation to manage the economic partnership with our neighboring countries, FTA economic partnerships. Clearly, on the provincial area, the governor would try to exert his effort to help develop his people. The main issue is to eradicate poverty and social problem in local area. Economic strategy on trade facilitation, industry and agriculture development, energy, tourism, HRD, transport and communication network mentioned earlier is key point.

The main objective of policy is to level up Thailand’s competitiveness away from ‘cheap wage’ and ‘low productivity’ to higher epoch of economic development. That is to say, we will proceed with economic restructuring for higher productivity of inputs, efficiency of production, creation of new value added, new product development. This is by concentrating in industrial development, especially, of the SME. The economic

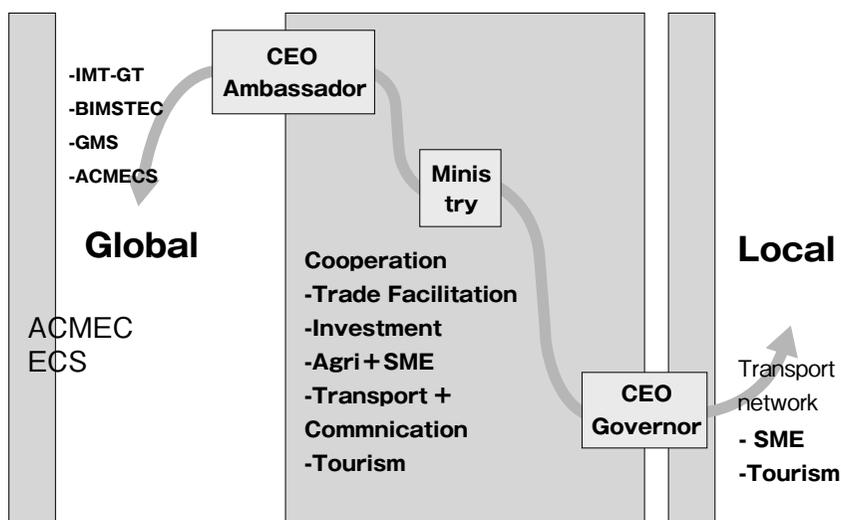


Chart 1: Thai Government Policy to Link Global - Local Development

restructure will head both for domestic and export market. The government also aims to nominate Thailand as 'Tourism Hub' to link routing of tourism such that all of us will gain from international tourism to multiple destinations. In practice, Thailand would cooperate with its neighbors such as Laos PDR, Myanmar and Cambodia to development joint 'ASEAN Energy—Grid' such that energy surplus can gain from selling electricity to energy deficit countries. More importantly, Thailand would like to provide its Official Development Assistance (ODA) to establish Transportation and Communication Net Work through out the sub—region. Currently, Thailand has given ODA grant and loan to its neighbors to link road system to Cambodia, Laos, and Myanmar. The cooperation with multilateral agency like Asian Development Bank (ADB) is clear in the case of land link between northern part of Thailand—Laos—and South China (*Yunan* Province). Also, Thailand— Australia, Thailand-Japan cooperation in helping construct two bridges between Thailand-PDR Laos are good example of how bilateral cooperation can be importantly applied.

3. Brief SME Development Plan of Thailand

Thailand has set its SME development plan for 2002—2006 aiming at strengthening role of SME to be main mechanism to support economic development. This is to level

up efficiency and competitiveness of SME both in manufacture and services. It also links SME to community development at grass root while trying to modernize SME to international level. One of the main ideas is to nurture new entrepreneur in Thailand to coincide with the world trend of 'new economies' where communication is main impetus.

Thailand recognizes the strength and weakness of SME development. The current world is facing a trend of regionalism, protectionism in various forms of Non—Tariff Barrier. Thus, in this new environment, scale may be necessary but surely not sufficient in competition. In stead, an economic of speed and network will replace the old competitive paradigm. Technology, creativity and innovation replace just physical asset and machine. More important, demand driven management rather than supply is mattered. Thus, firms with niche product will find niche market. The role of supply chain management and intellectual property will come in to play.

The SME in Thailand is in its preliminary stage. As economic development proceeds, new comer arrived from emerging economies has put threats on Thai SME. This situation of 'Nut-cracker Effect' facing Thai SME as low cost firms (in less develop economies) are chasing from below, while Thai SME could not compete with SME in advance economies in value creation. More over, most SME could not access to financial market as it has high exposure and sub—standard transparent balance sheet.

The five—year SME development plan aims to reach the following targets. First, it would like to see GDP contributed by SME to reach 50 percent share in the year 2006. The export by SME would be not less than 6 percent per year. Employment by SME should increase by 180,000 persons per year with industrial sector productivity improvement of 2.5 percent a year. More important, government would like SME to register its establishment not less than 72 percent by year 2006. In other word, government would like to see new entrepreneur created by 50,000 persons per year. The community business would reach 6,300 groups in 2006 as well.

According to the White Paper on Small and Medium Enterprises in Thailand by the Office of Small and Medium Enterprise Promotion (OSMEP), there are 1.639 million small and medium enterprises in Thailand, or 99 percent of the total 1.645 million enterprises of all sizes. The highest proportion, 31 percent of these SME are located in the Northeastern region of Thailand. Here, 21 percent are in the Greater Bangkok area,

and 17 percent are in the Northern region. SME accounts for 69 percent of employment in the business sector and 39 percent of the gross domestic product (GDP). Manufacturing exports by SME is 38 percent of Thailand's total manufacturing export.

In 2003, the GDP contributed by SME was 2.26 trillion baht. The export of SME in 2003 increased 25.4 percent to reach 1.51 trillion baht. Employment has reached 5.6 million persons.

In order to raise competitiveness of SME, the plan would like to concentrate on the following sectors. First, for existing high potential industries such as food processing, agro—industry such as rubber, wooden furniture, and fashion supporting industries like garment, leather products, jewelry. Second, those supporting industries like automobile spare parts, electrical appliances, and electronics needs further development on quality and management in logistic system to reduce import dependency. Third, high potential service sector like tourism, health services, education, designing and construction, engineer, architect, lawyer, accountant, entertainment, and meeting and seminar business need further level up competitiveness.

With the above mentioned SME development plan, the SME development bank has response by setting its strategic credit extension accordingly. The most important is government project including '**Tourism Capital of Asia**'. This is to promote Thailand as tourism hub of Asia. New forms form and services are offered such as long—stay resorts, world—class hotels, spas, and golf courses targeting high—potential travelers. '**Kitchen of the World**' project would like to promote food industries towards global market which Thailand has high competitive potential and rich agricultural land and biodiversity. '**Bangkok Fashion City**' aims to solidly push three business clusters together namely textile and garment, leatherwear and footwear and gems and jewelry to achieve global branding. '**Detroit of Asia**' aims to promote Thailand as Southeast Asia's automobile hub. '**IT City**' aims to create highly skilled workforce in information technology including software programmers and hardware parts and component developers respectively.

Despite solid development plan and SME bank activity on credit extension for the four clusters, we could not claim that Thailand did really achieve its target. Currently, Thailand is trying to introduce 'industry clinical system' some thing closed to 'Shin Dan' system of Japan. It is nonetheless, not sufficient in many respect. Thailand has to

create more ‘specialists’ on SME problem ranging from financial risk, inaccessible cost of technology, skill and number of human resource, energy use, marketing, and information etc.

4. GMS Economic Development and SME Integration, What is The Role of Japan?

Thailand’s economic cooperation strategy and SME development path mentioned above has clear direction on its own. Yet, the GMS development plan and role of SME has not been integrated before. SME development plan has been drawn in each particular country, but not as cooperation plan among countries in the GMS. We would like to discuss as follows:

- 1) Currently, GMS country is facing several challenges. First, the GMS region has *imbalance resource allocation* where one economy is abundant with land and labor but less of capital input. It lacks production technique, and machinery which is supported by long—term financial capital with reasonable cost of borrowing. Second, most of member countries are not oil producers. They may have natural gas but in total they are net energy importers. Thus, their trade accounts are very sensitive to energy prices fluctuation. As a matter of fact, price of fossil energy like crude oil will not be as low as in the last decades. Therefore, GMS countries are *constrained by energy cost* in their economic development.
- 2) The member countries need cooperation to write up joint development plan where SME is main impetus to raise economic activities and therefore GDP and income per capita of its people. GMS member countries can be clustered according to their resource and factor endowment and level of economic development i.e. ‘at what level SME in each economy has been developed’. There after, we need to construct an inter—industrial relationship matrix of GMS similar to the international Input—Output Table. This represents an existing industrial structure and linkages among GMS economy. In order to develop the density of inter-industrial relationship, the GMS member countries need to draw up SME development plan. In addition, the matrix will be basic in formulation of ‘**Vertical and Horizontal Integration**’ of industrial relationships. This is to achieve a better resource allocation over time and space across region.

- 3) Fundamentally, the plan comprises *prioritization of strategic sector* e.g., choosing among agriculture, agro—industry, food industry, etc., selected type of SME, choices of production technique and machinery. Most importantly, we need to match the compatibility of skills and choices of production technique. We also need to identify not only the gap of skill formation in each GMS member country but also a proposal on how to reduce skill differentiation in the long—run. In other words, **a special skill development plan** would be proposed as alternative solution to existing education development. The program is designed to suit a joint SME development on energy substitution and demand driven SME development program.
- 4) **Joint sustainable energy development** should be a key strategic industry by GMS member countries. Especially, the cooperation on substitution of non—fossil energy which is generated from residues of agriculture product such as cassava, sugar cane for ethanol, palm and other oil crop for bio—diesel as well as other bio—mass to current oil import. This is to call for regional cooperation where plantation of these energy substitution crops can be shared effort by GMS member countries. This joint program will on one hand reduce cost of energy consumption, as energy intensity of economic development of GMS countries is very high. Also, it can jointly generate employment and income to people. The simple SME development program in each stage of energy substitution can be designed to suit with factor inputs in each GMS member countries. Finally, reduction of fossil energy consumption intensity (fossil to non—fossil ratio) of the GMS would be a target. Most importantly, SME development should be designed such that energy saving type of production technique is sought.
- 5) **Joint SME Development Program** can be initiated by a cross—countries' vertical integration of industries. But it may not be sufficient for a full achievement if without economic partnership with Japan. The whole development program deduces from Thailand's strategy may be ambitious. The question is who will finance the economic cooperation program, given the current domestic saving capability of Thailand as compared with future investment program. Clearly, we can not rely only on 'Tax financing of development' alone. The tax collection is reaching its taxable frontier as economic growth rates will be quite moderate in

the coming years. Now, it may be reasonable to consider equity and bond financing of economic development and economic cooperation. Given the current level of public debt over GDP, although it decreases to a satisfactorily manageable level, yet it may not be able to increase public debt more than current level. Thus, we may have to rely on debt and equity financing of development projects.

- 6) Thailand has initiated idea of '**Asia Bond**' to co-finance infrastructure development in the region. In order to promote Asian Bond, we need to create a benchmark for pricing of long-term bond which investors can diversify risk. More importantly, bond guaranteed facility and issuance of baht-denominated bond would help strengthen the Asia bond market as well. In our views, loan to joint venture companies between Thai and Japanese manufacturers, loan to Japanese SME in Thailand in local currency may need a careful step such that it would not create a crowding out effect and raising interest rate pressure. The maturity matching between long-term 'sources of fund' (with reasonably low interest rate from saving abundance country like Japan) and 'uses of fund' by long term infrastructure projects is prime role of Japanese financial market. The currency matching between baht-Yen is costly. We do appreciate the idea of local currency matching to avoid currency risk. Japan may need to initiate either a wide 'Baht Economic Zone' in the GMS in the first step. Subsequently, an 'Asian Bond's Currency Basket' a mixing of RMB-Yen-USD-. is further developed.
- 7) The role of Japan in the creation of '**technology transfer**' channels is also important. Here, technology means every thing ranging from machines, machines center, software, designs, material know how, effective R&D. Here, '**technology market place**' needs to be developed in Thailand to match demand and supply of technology of technology through price mechanism with long-term financing. For example, the used machine market would be developed to support SME development in the GMS. Here we refer to 'market mechanism of technology transfer' in order to avoid the dumping of inefficient machinery and technology from one country to other. Market will determine appropriate used machine and technology with efficiency pricing and loan. The long-term ODA loan to this region can be done by either bilateral cooperation especially from Japan or multilateral agency like ADB. As we have mentioned earlier that most of GMS member

countries could not access to long-term capital market due to their exposure, thus we need certain guaranteed facility initiated under the cooperation between GMS member countries, Japan and multi-lateral agency like ADB and others.

Appendix Definition of SME

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Definition of SMEs

Type	Small		Medium	
	Labor (persons)	Fixed Asset (Million baht)	Labor (persons)	Fixed Asset (Million baht)
Manufacture	<50	<50	51-200	50-200
Service	<50	<50	51-200	50-200
Wholesale	<25	<50	26-50	50-100
Retail	<15	<30	16-30	30-60

Source: Ministry of Industry, Ministry's Regulation on Size of SME B.E. 2545