Note by EIC

SCB Economic Intelligence Center

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TPP: Minimum Impact on Thai Auto Industry

Highlight

- Thailand will remain a key global production hub for Japanese car makers. Rather than obstruct, TPP will complement Thailand's positioning with other existing and overlapping trade agreements.
- Japan's key interests in automotive negotiations are on tariff privileges for parts exports from Japan to North American facilities. These parts are not expected to compete directly with ones exported from Thailand.

Although Thailand did not participate in the agreement, the twelve participating countries accounted for 42% of Thailand's total exports of automotive products in the first seven months of 2015. Not to mention that Japan and the US, the two car superpowers, are in the trade pact, and Australia alone accounted for almost a fifth of Thai auto exports. This raises the question of whether TPP, if implemented, would have any negative impacts on the future development of the Thai automotive industry in retaining its position as a major production hub for Japanese car makers. In other words, would the new trade pact hinder the key growth engine and expanding exports of Thai made cars and parts, especially at a time of a sluggish domestic market? Would Thailand be less attractive to Japanese automakers? In short, EIC expects minimum impacts, if any, on the Thai auto industry for the following two key reasons. First, Thailand's position in the Japanese automotive production network will not be altered by the trade pact. Rather, it would complement existing FTAs. And second, TPP is more about the interaction between the two automotive superpowers, Japan and the US.

Japanese car makers have continued to favor Thailand in their global value chain, with Thailand long being the key investment destination for Japanese car makers. The high level of capital accumulation over the years could be seen in increasing localization of R&D activities, the highest value added process within the production value chain. In fact, on the same day TPP reached its final agreement, Toyota held a press conference for its Thai R&D unit, emphasizing its recent performance and capability. It is reported that as much as 40% of the design and development of the newly launched Revo pickup was conducted by the Thai unit. Trucks produced here are exported to destinations around the world. And it's not just Toyota, other Japanese car makers are planning to increase their R&D capacity in Thailand to strengthen the nation's position as the key production hub for their global markets. The rise of Indonesia would possibly pose more of a threat than the TPP.

In addition, Thailand already has trade agreements with key markets for Japanese cars. Of the twelve participating TPP countries, Thailand has agreements with all but the US, Mexico, and Canada. But those three total only 5% of Thai auto exports. Car makers, not limited to the Japanese, have long enjoyed tariff privileges through these agreements, producing and exporting cars from Thailand. Actually, four ASEAN countries currently joining the TPP have had a link with Thailand through AFTA since the 1990's, and linkages with Japan, Australia and New Zealand through both bilateral and regional agreements started almost a decade ago. Agreements with Chile and Peru are also expected to see improvement before the APEC forum later this year. In addition, Thailand has concluded/negotiated trade agreements with other key markets not participating in the TPP, such as China, India, Indonesia, the Middle East, and the EU. In fact, this is the very key geopolitical reason that the US is exerting its presence in Asia through the TPP, in contrast to the China-dominant and ASEAN-centric RCEP, in which it is not included.

Direct competition between Thailand and Mexico on CBU exports is not expected. Although it is true that stagnant sales in developed markets and more stringent environmental regulations in emerging markets are now pressuring car makers to shift more toward global car models than ever, and increasing trade liberalization has enabled car makers to consolidate production of one car model in a few locations and export them to the world, EIC sees that this would actually smoothen the ongoing international division of labor between the two countries, especially on a perspective of risk mitigation. For players with facilities in both countries, this would merely be another round of re-adjustment of their annual production plans. The Nissan March, Mazda2, or Ford Fiesta, for example, will continue to be produced in both Mexico and Thailand.

There is currently limited linkage between the regional value chain in South East Asia and North America. From another angle, the 5% share of the NA in Thai auto exports also sheds light on the next reason why TPP should have minimum impacts on Thai auto industry. This goes back to the development of the Japanese auto industry itself. Long before Thailand or other Asian markets would grow to a significant size, the US was the key market for Japanese car makers. Together with other industrial products, demand for cars in the US has been the key driver for Japan's industrialization. And the Japanese have invested heavily there for more localization of production. Compare this: in 2014 1.7 million cars were exported to NA from Japan while 4.8 million Japanese cars were produced locally. In other words, Japanese car makers have separately established their production networks in the NA region long before those in SEA or Thailand. The build-up of Japanese production networks in Mexico and the US through Maquiladora and NAFTA is well-known. Thus, Japan's interest would more likely be on the abolishing of tariffs on 87% of all automotive parts exported from Japan to production facilities in NA. It is unlikely that key auto parts and components from Thailand to NA, currently around 10%, would be directly competing here. Even if they did, EIC believes that Japanese suppliers would not jeopardize their Thai facilities. Once again, this will be just a regular re-allocation of their production plans.

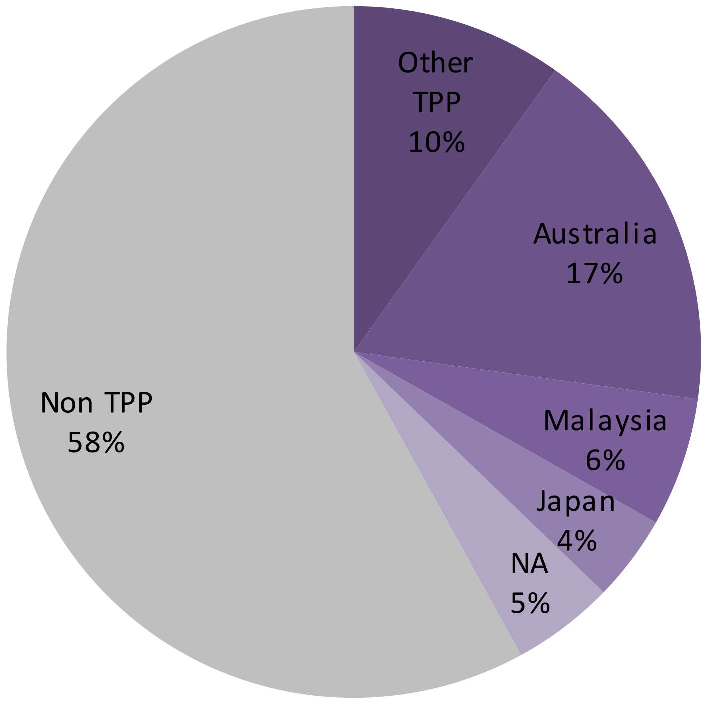
Non-tariff measures in Japan were top priorities for the US. On the other end, while Japanese cars have around 40% share in the NA car market, American cars have had a hard time penetrating Japan, currently having a market share at less than 5%. Forty% of the market is for Kei cars, a mini vehicle type specific only to the market, and Japan has been criticized by the US for measures thought to be protectionist, such as vehicle standards. These are the subject of key negotiations between the two countries, along with highly protected agricultural products in Japan. Of the 18 topics Japan has negotiated with other TPP countries, four were related to automotive non-tariff measures with the US.

Non-tariff measures were also key interests in overall negotiations, because not only are tariffs already low in participating countries, key trade agreements between Japanese/American overseas production facilities and destination markets have already been made. As mentioned above, production facilities in Thailand have long enjoyed market access to ASEAN, Australia, and New Zealand. Mexico has also negotiated/concluded trade agreements with South American countries and the EU. In fact, another key message emphasized by the Japanese government in automotive negotiations is on better, although just slightly, preferences in automotive products than the one Korea, a key rival in the car making industry, enjoys in a bilateral agreement with the US. In sum, EIC anticipates that rather than threatening the future development of Thai auto industry, TPP would complement the currently overlapping trade agreements/negotiations Thailand has engaged in. TPP would contribute to the improvement of Japanese automotive global value chains, where Thailand's positioning would remain important. For Japan, the interest is mainly on the abolition of tariffs on auto parts, which are currently exported from Japan to production facilities in NA. These products are not expected to be the same ones, at least currently, exported to NA from Thailand.

Implication

- **Plan for exposure to other global production hubs:** Although the automotive value chain has been understood to be limited within a region due to the cost of transportation and the Just-In-Time production nature as has been the case between NA and South East Asia, improvement in transportation, the proliferation of trade agreements between regions and pressures on commonization of parts and components can be expected in the long term. Therefore, parts suppliers must be well-prepared not only for technological changes but also for potential competition with players in other global production centers, as similar mega regional trade agreements are also expected in the future. In the medium term, both India and China are expected to have closer relations with the ASEAN automotive industry. Suppliers offering similar products that could be procured elsewhere could be affected by the changing environment and the adjustment of customer global procurement plans.

Figure 1: TPP countries have a high share of Thailand's Automotive Exports* (January – July 2015)



*Including CBUs and Parts

Source: EIC analysis based on data from UN Comtrade

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