Note by EIC

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Can Thailand's hotel industry meet the challenge of the services liberalization under the AEC?

Highlight

- Even though Thailand has increased the hotel sector equity ownership limit to 70% for ASEAN investors under the 8th package of specific commitment under the ASEAN Framework Agreement in Services (AFAS), the practical impact will be limited. This is because the shareholding structure will only apply to premium hotels with 6-stars or more. However, the impact may be more pronounced, especially on SMEs, if hotels with lower ratings are liberalized as well in order to match the degree of liberalization in other ASEAN countries.
- Thai companies should invest and expand to gain reputation as regional players since other ASEAN countries already enjoy a higher degree of hotel liberalization. This would help expand market coverage, especially to areas with tourism growth potential, and create brand awareness. Potential targets are capital cities and business towns with high business travel potential, especially in Indonesia and CLMV countries (Cambodia, Laos, Myanmar and Vietnam).

Under the 8th package of specific commitment, Thailand has increased the hotel industry equity ownership limit for ASEAN investors to 70%. This is the first increase, as the seven previously negotiated packages mandated by the ASEAN Framework Agreement on Services (AFAS) as part of the AEC limited equity ownership limit to 49%. Throughout the negotiated packages, Thai and ASEAN players have used the flexibility of the agreement to prohibit and limit equity ownership by ASEAN investors in their hotel industries. Since Thailand already limited the ASEAN investor equity ownership limit to 49% for all service industries there was no significant impact on those industries in Thailand. However, during the 8th negotiation package Thailand for the first time agreed to increase the ASEAN investor equity ownership limit in the hotel industry. The increase in the equity ownership limit will allow ASEAN investors to easily penetrate the Thai hotel segment, resulting in potentially fiercer competition, as the Foreign Business Act previously protected Thai hotel developers.

However, the 8th package of specific commitment should not have much impact on Thailand's hotel industry, as the equity limit increase this time will only apply to premium hotels with 6-star or above. The AEC agreement is somewhat flexible and places importance on the readiness of each member state, as each country has vastly different development levels. This flexibility allows Thailand to restrict the ASEAN investor equity ownership level of 70% to premium hotels with 6-stars or above. Therefore, the practical impact of the equity limit increase under the 8th package of specific commitment should be contained since 100% equity ownership of such a large-sized hotel investment is already allowed under investment incentives approved by BOI. A 6-star plus hotel investment normally require more than THB 500 million in investment which is qualified for investment incentives approval by BOI, in which BOI allows foreign investment of this size to be 100% controlled by foreigner. Besides, BOI approval of hotel investment should not be difficult since the large investment size usually requires foreign capital and foreign investors. Nevertheless, the establishment of restrictions on foreign investment in the negotiation packages is not unusual, as most ASEAN countries ask for similar restrictions as well, with the exception of Singapore and Vietnam. Examples of hotel restrictions set by other countries are Indonesia, which allows ASEAN investors to control 100% of hotel equity only in certain locations, Malaysia which allows ASEAN investors to control 70% of hotel equity only in 4 and 5-star hotels, and the Philippines, which lets ASEAN investors hold only minority shares in the hotel business (Figure 1).

Going forward, it is likely that Thailand will also be requested to increase liberalization in lower grade hotels, which will create concrete challenges as well as increase competition in the hotel industry. When comparing the level of hotel industry liberalization among ASEAN members, Thailand is only ahead of the Philippines. The negotiation packages are formatted in the style of request and offer, in which it is likely that other ASEAN countries will request that Thailand increase liberalization of its lower grade hotels, as currently Thailand has only offered to liberalize hotels with 6-stars or more. It is anticipated that other countries will request that Thailand open up its hotel industry because their hotel industries are more open, and because Thailand possesses a highest tourism market share and acts as a connecting hub for journeys to nearby countries. If Thailand were to increase the degree of liberalization in lower level hotels, the impact will be more pronounced, especially for SMEs. Currently, the hotel businesses in Thailand are already facing fierce competition. For example, in 2013 the hotel room rates could be raised by an average of only 2% amid strong tourist demand growth of 20%. Although, in the past large foreign companies were able to invest in the hotel business via complex channels and strategies, the AEC liberalization will further facilitate investments from other ASEAN countries, such as reducing costs from complex channeling, creating a fierce competitive atmosphere.

Though market liberalization will create investment opportunities in other ASEAN countries, Thai players still lack overseas investment experience compared to their Malaysian and Singaporean counterparts. When comparing top hotel players in Malaysia, Singapore, and Thailand, only a small number of Thai players currently pursue overseas expansion. On the other hand, top players in Malaysia and Singapore obtain revenue from overseas hotel investments or operations in more than one country (Figure 2). Hence, at the regional level, Thai players may be disadvantaged by limited overseas investment experience. However, Thai hotel companies should grasp the current opportunity to increase hotel coverage and add value to Thai brands during a period in which other ASEAN countries are opening up their hotel sectors. Thai players should especially consider investing in commercial locations, such as in capital or top tier cities, since tourist and business visits are trending upward. Furthermore, various ASEAN capitals are becoming more prominent final destinations, such as Jakarta, compared to traditional leisure destination. During the past five years tourist visits to Jakarta increased by an average of 12% per year, a rate higher than Bali's growth rate of 10% per year, supported by an increase in the number of flights and low cost airlines. Prior to this period tourist visits to Jakarta only increased by 1%, whereas visits to Bali increased by 5% per year.

Implication

- **Since other ASEAN countries already enjoy a more liberalized hotel market, Thai hotel investors should seize the opportunity to invest in commercial areas.** Higher hotel demand in ASEAN is anticipated due to solid economic growth, especially in Indonesia and CLMV countries. Economic growth will facilitate city expansion and increase the number of business trips, hence creating demand for hotels in commercial areas.

Players in the medium-low hotel segments should increase their competitive capabilities via such methods as reducing costs, consolidation, alliance building, and brand improvement because players need to adjust in order to cope with increased competition from anticipated liberalization. Small to medium hotels operated as family businesses dominate most of the Thai hotel market. Therefore the future will be more competitive, as ASEAN investors will take advantage of anticipated hotel liberalization to easily enter the market. Furthermore, small to medium hotel operators are being challenged by large domestic hotel players, since they have penetrated into the lower grade hotel segment by using their brand reputation to attract clients.

Figure 1: Thailand's hotel market liberalization is low when compared to other ASEAN countries.

Equity ownership limit for ASEAN investor in hotel business in ASEAN countries under the eighth package of specific commitment under ASEAN Framework Agreement on Services (AFAS)

Least liberalized → Most liberalized

Unit: %

ASEAN - 6

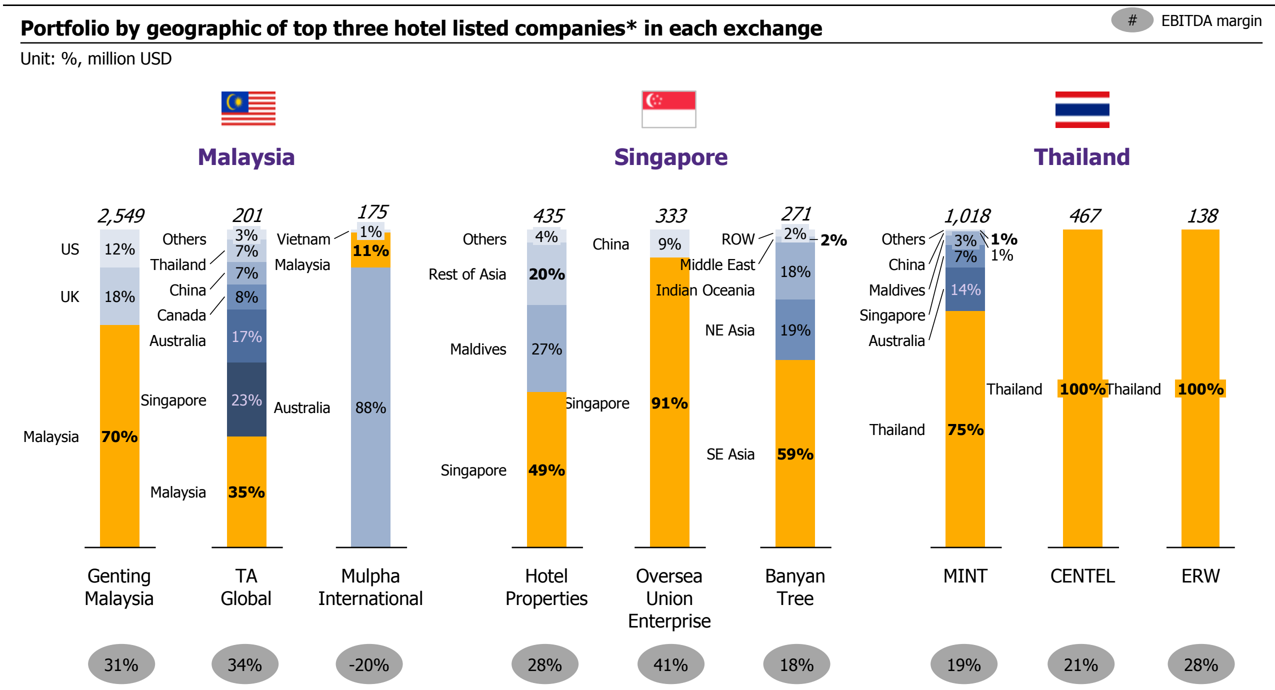
Country	Degree	Equity ownership	Remark
Brunei		70%	• Aggregate foreign shareholding in the JV not exceed 70%
Indonesia		70%	• For 3,4,5-star hotels, 100% is allowed in Kalimantan, Bengkulu, Jambi, Sulawesi and East Nusa Tenggara (NTT) • For 1 or 2-star, 70% is allowed in Sulawesi, Papua, Moluccas, Nusa Tenggara. For other areas, it is closed for foreign investment
Malaysia		70%	• Allowed for 4 and 5-star hotels only
Philippines		49%	
Singapore		100%	
Thailand		70%	• Allowed for Superior Deluxe or Six-star plus rated hotel only

CLMV

Country	Degree	Equity ownership	Remark
Cambodia		100%	• Allowed for 3-star or higher hotels only
Laos		100%	• Allowed for 3-star or higher hotels only
Myanmar		100%	• Hotel projects with 100 % foreign investment are allowed in BOT system under Foreign Investment Law
Vietnam		100%	

Source: EIC analysis based on data from ASEAN

Figure 2: Overall, Thailand's hotel industry still lack overseas hotel investment and experience.



* Include the companies which own and operate hotels and resorts and incorporated in Singapore, Malaysia, and Thailand, ranked by 2012 revenue

Source: EIC analysis based on data from ASEAN

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