SCB Economic Intelligence Center

Note by EIC

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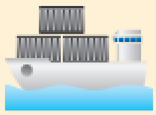
The future of Thai exports after the halt in European Union cooperation



Highlight

- The European Union declared that official visits to and from Thailand will be suspended and the EU will refuse to sign the Partnership and Cooperation Agreement with Thailand, making it unlikely that Thai-EU FTA negotiations will be concluded by 1 January 2015, when the cuts in GSP privileges will take effect.
- EIC views that various export products being severely impacted, especially frozen shrimp, octopus, and motorcycles. These products are particularly vulnerable because they heavily rely on the European market and greatly benefit from GSP tax privileges. However, the overall impact on Thai exports is estimated to be low, impacting only 0.5% of total Thai exports.

The European Union halted cooperation with Thailand. On June 23 2014, the European Union announced that it would rethink Thai-EU relationship until there are reliable and accelerated the plans to return constitutional authority and hold elections. Key fallout from the announcement is that official visits to and from Thailand will be suspended and the EU will refuse to sign the Partnership and Cooperation Agreement with Thailand.

The halt in Thai-EU cooperation delayed the countries' Free Trade Area (FTA) negotiations. Originally, there were seven planned rounds of FTA negotiations, with a completion target set for December 2014. However, the plan was interrupted due to political conflict in Thailand from late 2013 continuing into 2014. The 4th round of negotiations during 7-11 April therefore did not make much progress as Thai government did not have full authoritative power. With the EU canceling the signing of the Partnership and Cooperation Agreement with Thailand, the situation only became worse. Thus, it is unlikely that Thai-EU FTA negotiations will be concluded by January 1 2015, in which Thailand will be withdrawn from GSP tax privileges, based on country graduation criteria.

EIC see the GSP privilege cuts based on country graduation criteria impact Thai exporters at least USD 47 million through increased taxation. Countries eligible to receive GSP tax privileges are those not ranked as high-income or upper-middle income for three consecutive years. The World Bank has ranked Thailand as an upper-middle income country since 2011to 2013, making it ineligible to receive GSP privileges from early 2015 when GSP tax privileges will be discontinued for 723 products. As a result, exporters will have to bear higher costs, and products that will be at a disadvantage from this cuts include frozen shrimp, motorcycles, shoes, apparel, tires, and canned tuna. EIC estimates that the damage to the Thai economy will be at least USD 47 million.

Thailand's exposure to higher tax rates will inevitably lower the nation's price-competitiveness. Furthermore, rival countries with similar export market structures that still receiving GSP and FTA benefits, such as Indonesia, Vietnam, Malaysia, and Mexico, will make inroads into Thailand's existing markets.

Implication

- **Export products that will be heavily affected from the GSP tax cut are frozen shrimp, octopus, and motorcycles** since they rely on the European market and highly utilize GSP privilege. However, the GSP tax cut is estimated to have minor impact to the overall export market, around 0.5% of total exports.
- **Export products with high reliance on GSP tax benefits and the European market need to find ways to adapt.** Products that utilize GSP benefits exceeding 80% include frozen shrimp, refrigerator compressors, motorcycles, plastics, apparel, and octopus. Exporters of those products, especially those targeting the European market, should adjust their short-term strategies by finding new export markets, upgrading product value, and shifting their focus to emerging markets. Moreover, exporters can add value or upgrade existing products in order to differentiate and increase competitiveness.
- **In the medium to long-term, exporters can adjust by investing in countries still eligible for tax benefits** for instance, CLMV market members (Cambodia, Laos, Myanmar, and Vietnam). Vietnam is still eligible for GSP tax privileges, while Laos, Cambodia, and Myanmar receives tax exemptions on everything but arms (EBA). Moreover, investment in those countries will further benefit exporters through lower wages.
- **Unfortunately, Thai seafood exporters were further hampered by Thailand being downgraded in the US Trafficking in Persons (TIPs) report** Thailand downgraded to Tier 3, a country with the most severe human trafficking conditions. The downgrade ruined Thailand's product reputation, especially for fishery items such as frozen shrimp, canned tuna, and octopus. The human rights issue is likely to have an impact similar to the GSP tax cut, as the US will decide whether to sanction Thai products within 90 days after publication of the report. Hence, both government and exporters should be ready to answer questions to consumers from the US and other nations.

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Figure 1: Thai-EU FTA negotiation schedule

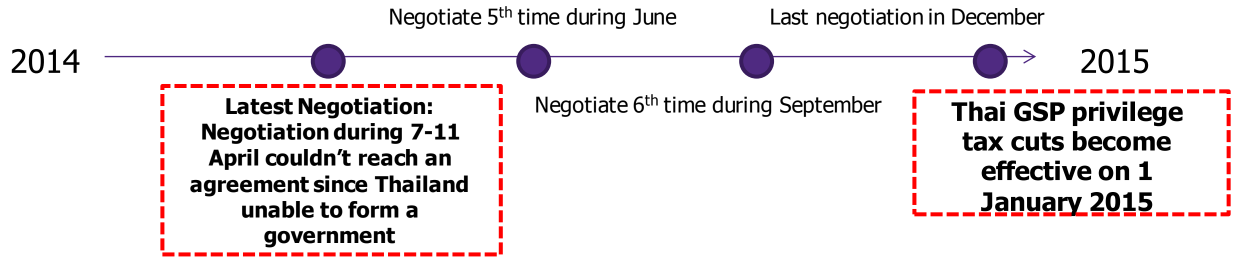
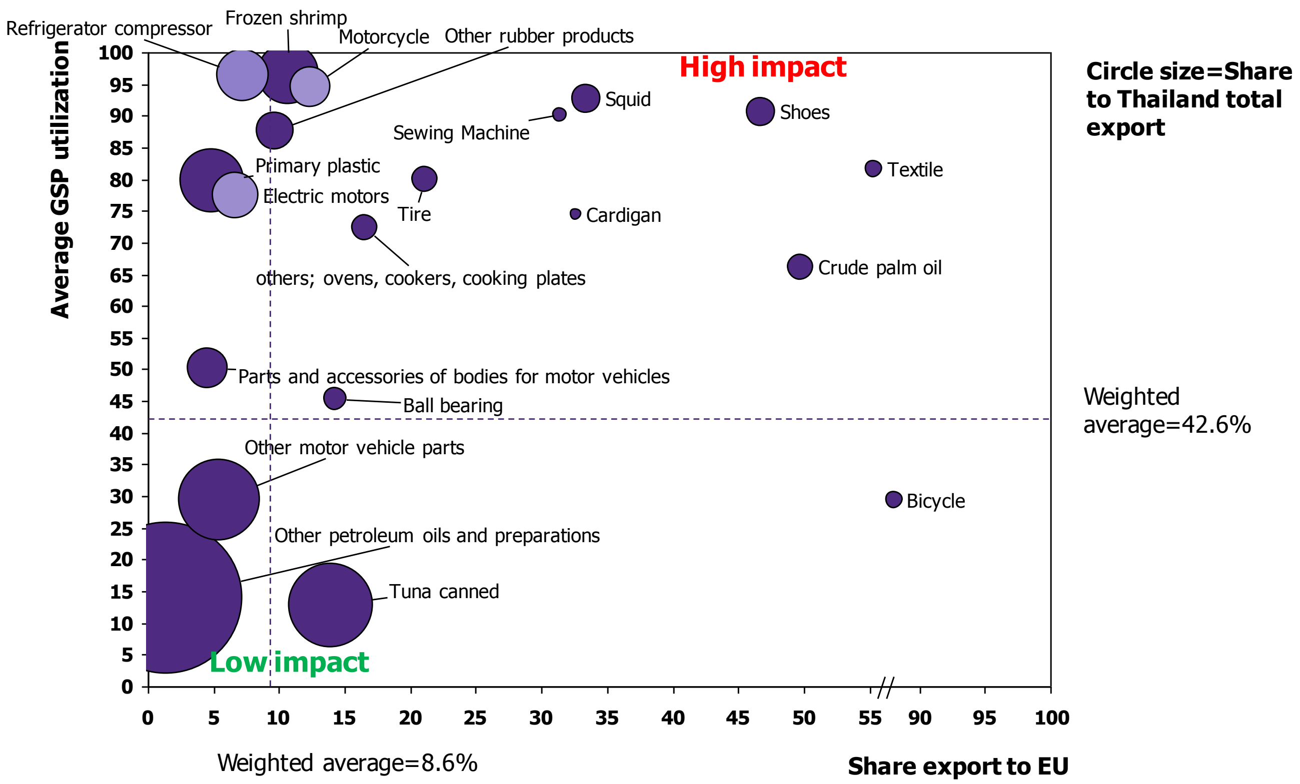


Figure 2: Thailand's impact after GSP privileges cut



Source: EIC analysis based on data from The Permanent Mission of Thailand to the World Trade Organization and Trademap