NOTE

SCB Economic Intelligence Center

Cross-Border Logistics to Vietnam…A Golden Opportunity should not be missed!!

18 July 2019

- **Cross-border trade between Thailand and Vietnam tends to grow by approximately 30%CAGR over the next 3 years. Key drivers of this growing trend are an expansion of manufacturing sector and a growth of domestic consumption in Vietnam, which will generate positive impacts of Thai cross-border logistics business. However, problems concerning road conditions, differences between transportation laws in each country, and complexities in customs procedures remain important obstacles to cross-border trade to Vietnam.**
- **In June 2018, member countries of the Greater Mekong Subregion (GMS) has implemented cross-border transport operations according to the GMS-CBTA (Cross-Border Transport Facilitation Agreement), with the aim of reducing obstacles from customs procedures and traffic systems. EIC estimates that the agreement will help to reduce transport leadtime by 45% and save logistics costs over 20% compared to traditional cross-border logistics model.**
- **Based on a past performance analysis of the cross-border logistics business landscape, EIC found that the number of registered vehicles do not reflect the competitiveness of this business. This is shown in the operating results of logistics service providers with**

over 100 registered vehicles, which performed below the average market - an average revenue growth of around 10% and an average gross profit margins of around 20%.

- **Nevertheless, cross-border logistics business must confront with numerous challenges, including infrastructure limitations, intense competition from both Thai and international competitors under the GMS-CBTA agreement, and the expansion of the railway network as an alternative mode of transportation to Vietnam.**

Cross-border trade has become increasingly important for Thai economy, especially given that Vietnam, as a main cross-border trade partner, contributes over 60% of Thailand's total cross-border trade. It is well-known that Thailand has long-standing trade relations with neighboring countries and the government has worked continuously to promote trade in the regional area. Over the past 5 years (2014-2018), border trade to Myanmar, Laos, Cambodia, and Malaysia expanded by 3%CAGR, while cross-border trade with southern China, Singapore, and Vietnam grew by more than 12%CAGR. In 2018, Thailand's cross-border trade was valued at over 300 billion baht, or over 2 million tons in trade volume. Despite the fact that cross-border trade with southern China fetched the highest value amounting to 100 billion baht, there was a relatively low share of trade volume because the majority of cross-border exports consisted of high-value products such as computer components and electronic equipment. Meanwhile, the volume of Thailand's cross-border trade with Vietnam amounted to 1.3 million tons, contributing over 60% of Thailand's total cross-border trade volume and 95% being exports. Given this, the Vietnam market could present an opportunity for logistics service business.Key Thai export products to Vietnam include fresh, chilled or frozen fruits, non-alcoholic beverage, and electronic equipment.

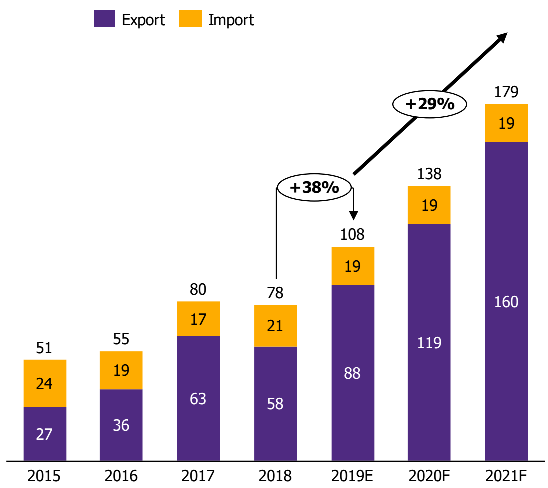
For the medium term (2019-2021), Thailand's cross-border trade with Vietnam is expected to improve by around 30%CAGR relied on Vietnam's economic growth, from an expansion of manufacturing sector and domestic consumption. Vietnam is one of the world's fastest-growing economies, attracting foreign investors who are interested in establishing production base in the country for exports. Chinese investors, in particular, are also increasingly relocating their manufacturing base to Vietnam to avoid trade wars. However, Vietnam's manufacturing sector relies much on imports of raw materials and intermediate goods which is positively impacting Thailand's export supplying to these factories.

In terms of domestic consumption, over 90 million of Vietnam's population with middle class accounting for over 15% has boosted demand for high-quality and luxury goods. Coupled with a rapid expansion of Thai modern trade retail in Vietnam (e.g. Big C Vietnam under Central Group and Metro under TCC group) who are key players in the market will help to increase the popularity of Thai products, ultermately improve imports.

Figure 1: Value of Thailand-Vietnam Cross-Border Trade

Cross-Border Trade between Thailand-Vietnam

Unit: Billion Baht



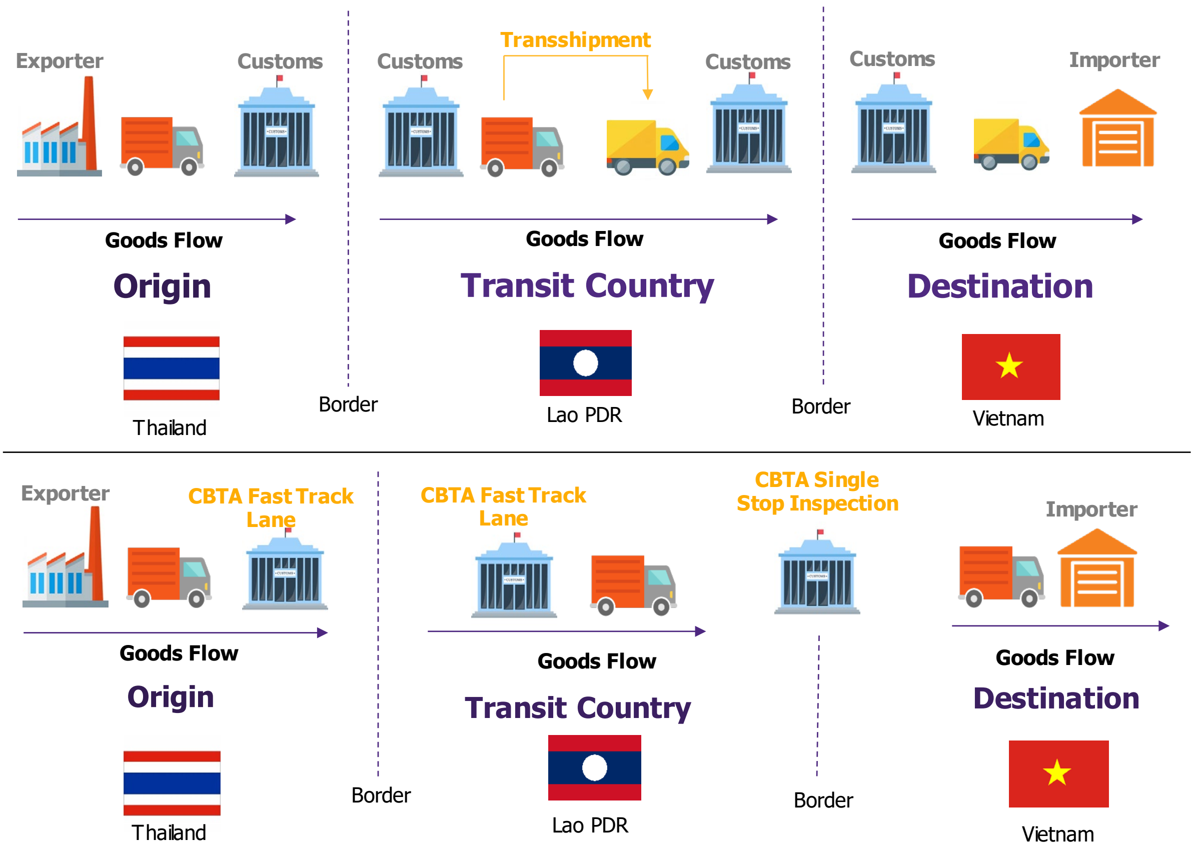
Source: EIC analysis based on data from MOC

Over the years, roads conditions, differences in transportation laws, and complexities in customs procedures continue to pose important obstacles to cross-border logistics to Vietnam, with having a direct impact on logistics costs. In general, the main route for cross-border transport from Thailand to Vietnam is Route R12 (Bangkok-Nakhon Phanom/Thakhek-Na Phao/Cha Lo-Vinh-Hanoi), as it is the shortest distance compared to other routes and connects to the city of Nanning and Guangdong Province in southern China. This route is a two-lanes road running alongside a landscape of valley slope interspersed with farmland and road maintenance for repairing potholes have been often found. In practical term, Vietnam's transportation laws do not allow Thai trucks to enter its territory, meaning that cross-border logistics to Vietnam requires to transship goods at the Lao border onto Lao trucks then continue onwards to Vietnam. In addition, the traffic laws of Laos and Vietnam differ from Thailand's, for instance in maximum weight limit and speed limit, while the customs procedures and international trade regulations of each country are complex and often subject to change, resulting in a congestion at the border checkpoint. These factors directly lead to unpredictable delays and cost overrun for cross-border logistics business.

Since June 2018, member countries of the Greater Mekong Subregion officially launched cross-border transport operations under the GMS-CBTA agreement to facilitate cross-border transportation in the early harvest stage. EIC estimates that this will help to reduce leadtime by around 45% and save logistics costs by more than 20%. Member countries of the Greater Mekong Subregion (GMS), comprised of Cambodia, China, Laos, Myanmar, Thailand, and Vietnam, initially started implementing cross-border transport operations under the GMS-Cross Border Transport Facilitation Agreement (GMS-CBTA) to reduce the limitations and obstacles of traditional cross-border logistics model. The agreement extend the facilitation of cross-border trade in both customs procedures and traffic control systems such as Single-Window Inspection (SWI) and Single Stop Inspection (SSI). The East West Economic Corridor (EWEC) also known as Route R9 is designated as a pilot route, border crossing at the Mukdahan border gate to Savannakhet-Dansavanh (Lao PDR), Lao Bao-Da Nang (Vietnam). In the early harvest stage, the agreement established a quota of 500 GMS Road Transport Permits per country, which allows Thai trucks transporting goods entering to Vietnam territory without transshipment. At the moment, there are 12 logistics service providers with a total of 400 vehicles have received permits, and from March to April 2019, the Department of Land Transport announced an expansion of the quota to an additional 200 vehicles.

Upon evaluating the logistics costs and leadtime required to transport goods from Bangkok through the Lao border into Hanoi, Vietnam, EIC found that logistics service providers operating under the GMS-CBTA quota will be able to shorten their leadtimes by around 45% from customs procedures and transshipment process. This will reduce logistics costs by over 20% compared to the traditional cross-border logistics model.

Figure 2: Comparison between Cross-Border Transport with transshipment and GMS-CBTA



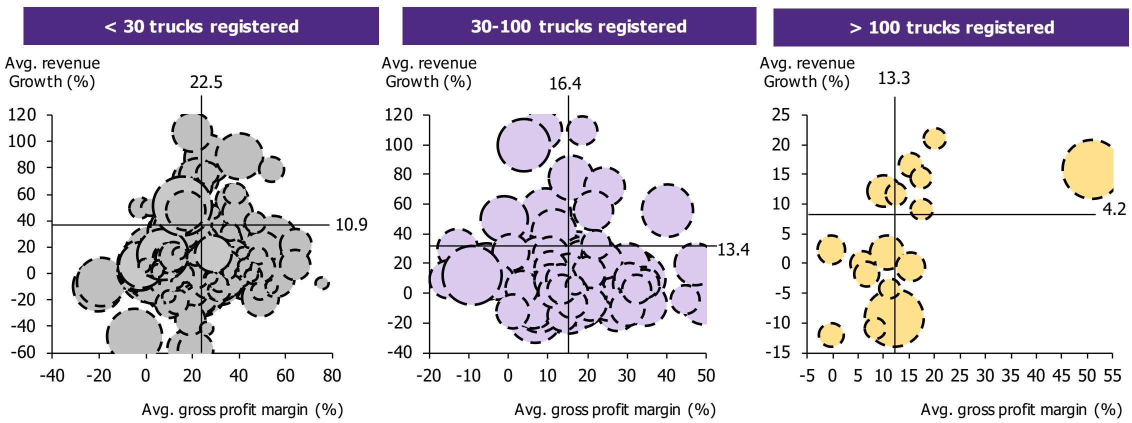
Source: EIC analysis based on data from GMS

A strong uptrend in cross-border trade generated increase revenues to logistics service providers with an average revenue growth of 10% and an average gross profit margin of 20%. EIC expects that the gross profit margin of business under the GMS-CBTA quota tends to increase due to lower logistics costs. In examining the overall picture of the cross-border logistics landscape, EIC found that over 80% of the market is serviced by large- and medium-sized businesses with at least 30 vehicles registered with the Department of Land Transport. EIC's analysis revealed that over the past 5 years (2013-2017), the number of registered vehicles does not reflect the competitiveness of logistics business. Logistics service providers with less than 30 registered vehicles had an average gross profit margin of 23%, and an average revenue growth for logistics service providers with 30 to 100 registered vehicles was at 13%. Meanwhile, the operating results of logistics service providers with over 100 registered vehicles performed below the average of the overall cross-border logistics market. This is partly because large businesses mostly utilize tractors and trailers for transporting goods in container, making their costs higher than those of smaller businesses, which transport goods by 6-wheel and 10-wheel trucks.

After the launch of cross-border transport operations under the GMS-CBTA agreement, EIC found that businesses holding quotas is likely to better control overall logistics costs, reduce leadtimes, and increase competitiveness as they would rely less on local businesses. As a result, businesses tend to improve average gross profit margin. In addition, cross-border logistics will become another option for those wanting to transport goods to Vietnam with a shorten leadtime, the ability to offer door-to-door delivery services and only a slightly higher cost compared to shipping. This will raise demand for cross-border logistics which will provide an opportunity to generate revenue for logistics service provider in the future.

Figure 3: Five-Year Financial Performance of Cross-Border Transport Businesses (2013-2017)

Unit: %



Remark: The size of the circle refers to the number of registerred trucks
Source: EIC analysis based on data from ENLITE and Annual Report 56-1

EIC's analysis reveals that there are 3 important strategies toward the success of cross-border logistics business: geographical proficiency, strategic partnerships and integrated logistics services. There is no doubt that cross-border logistics business relies upon the expertise in route, custom regulation from the country of origin to destination, and knowledge of local languages – as all of these factors lead to reduced work processes and operational costs. Likewise, building strategic partnership with local operator, manufacturers and retailers for distribution network expansion will allow business enhance their logistics service and reduce the risk of backhauling. Furthermore, business that provide integrated logistics services which connect shipping, rail, and air transport will be able to fulfil a wide range of service requests.

Nevertheless, cross-border logistics businesses must prepare to confront 3 challenges: infrastructure limitations, contense competition, and the expansion of railway networks. In the future, cross-border logistics business will have the potential for substantial growth and a collaboration of governments at regional level will continue to support the development of trade and logistics networks. Therefore, cross-border logistics has become an attractive opportunity for business expansion. However, there are 3 key challenges including: 1) Infrastructure limitations, for instance road condition that still need to be developed and other facilities including rest area, gas stations and vehicle maintenance station are insufficient for an expansion of logistics sector, 2) intense competition will stem from the rise in number of registered international logistics businesses as well as international logistics service providers under the GMS-CBTA quota and 3) The expansion of railway networks within the ASEAN region, such as Thailand's double track railway project connecting the Trans-Asian Railway, could serve as another option for those needing to transport goods to Vietnam due to a lower logistics costs.

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