



OECD Investment Policy Reviews

**THAILAND**

**HIGHLIGHTS**





# Preface

Thailand has had a remarkable economic development trajectory over the past 60 years and foreign direct investment (FDI) has been pivotal in this success. A pioneer in building its development strategy around FDI and integration in global value chains, Thailand is now a net outward investor, with rapidly growing presence in neighbouring countries. Its success in investment attraction was enabled by a combination of its early liberalisation of inward FDI for the manufacturing sector, on the one hand, and proactive investment promotion and facilitation policies under a strong Board of Investment, on the other.

Along with economic growth and integration into the global economy, Thailand has also made considerable strides in the area of inclusive and sustainable development. Poverty rates have dropped to less than 10% of the population. Efforts to improve the quality of education and to equip the workforce with skills that meet the emerging needs of the services economy are starting to bear fruit. While challenges remain in some areas of responsible business conduct (RBC), there is strong political will to address them. A regional leader in RBC; Thailand became the first country in Asia to adopt a standalone National Action Plan on Business and Human Rights in 2019.

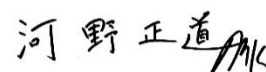
Thailand aspires to transition from upper middle-income to high-income economy by 2037, as outlined in its 20-year national strategy. The government aims to achieve this objective by upgrading to a value-based green economy, as made evident by the recently introduced Thailand 4.0 vision and Bio-Circular-Green (BCG) economy model. This ambitious plan relies heavily on inward FDI and will therefore require a continued and concerted effort to reform and improve the investment climate. New challenges related to the ongoing COVID-19 pandemic could delay progress toward this objective, as the crisis interrupts Thailand's long period of growth. The economy is predicted to contract by approximately 7% in 2020, and exports and FDI are likely to decline even more.

This first *OECD Investment Policy Review of Thailand* identifies potential priority areas for investment climate reform in support of a green, inclusive and sustainable recovery from the COVID-19 crisis, and the fulfilment of Thailand's development ambitions. It covers recommendations for improving the domestic and international legal framework for investment, suggestions for institutional reforms as well as directions for implementing policy frameworks in the area of RBC and green growth. The Government of Thailand and the OECD are very pleased to have joined forces in producing this *OECD Investment Policy Review of Thailand*, as part of the OECD-Thailand Country Programme. This report is one of the deliverables of this Country Programme.

We thank all government agencies in Thailand and the OECD Secretariat who have contributed to this Review. We hope it will help improve the investment climate in Thailand, and the achievement of its sustainable development goals.



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# Foreword

This *OECD Investment Policy Review of Thailand* uses the OECD Policy Framework for Investment to present an assessment of the investment climate in Thailand and to discuss reform opportunities that support Thailand's development ambitions and contribute to the Sustainable Development Goals (SDGs). After describing Thailand's development path and future development strategies, the Review provides a snapshot on Thailand's competitive edge to identify where challenges may lie and policy efforts are needed. It further studies trends and qualities of FDI and discusses how investment contributes to Thailand's inclusive and sustainable development. The Review examines a broad range of policy areas including investment promotion and facilitation, the domestic and international legal framework for investment, policies to promote and enable responsible business conduct and green growth, and efforts to promote outward foreign direct investment. While the global COVID-19 crisis could slow the speed of progress towards Thailand's ambitions, policy recommendations provided in this Review should be considered as possible investment climate reform priorities for an inclusive and sustainable recovery.

The Review was prepared in close collaboration with the Ministry of Foreign Affairs of the Kingdom of Thailand (MFA), in consultation with an inter-ministerial taskforce created for the Review. The Review has also benefited from consultations with OECD Investment Committee Delegates, representatives from OECD country embassies in Thailand as well as stakeholders from international organisations, the private sector, civil society and academia. The Review is implemented as part of the OECD-Thailand Country Programme.

The Review was prepared by Martin Wermelinger, Fares Al Hussami, Alessandra Celani, Fernando Mistura, Letizia Montinari, and Baxter Roberts from the Investment Division, and Naeeda Crishna Morgado, external consultant, under the overall guidance of Stephen Thomsen, Head of Investment Policy Reviews. The RBC chapter was authored by Tihana Bule from the OECD Centre for Responsible Business Conduct as part of the broader project on Responsible Supply Chains in Asia funded by the European Union. Silvia Appelt from the Directorate for Science, Technology and Innovation provided substantive inputs. Edward Smiley helped prepare the report for publication. Angèle N'Zinga provided administrative assistance. Secretariat comments were received from Ana Novik, Head of Investment Division, David Gaukrodger, Senior Legal Advisor, and Alexander Böhmer, Malory Greene, and Tiyyarat Niamkohphet-Cader of OECD Global Relations.

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# Executive Summary

Thailand has had an impressive economic development trajectory over the past decades. Foreign direct investment (FDI) and integration in global value chains (GVCs) have been important enablers of this success. Inward FDI's share in GDP has increased to above 50% today. The emerging global economic crisis related to the COVID-19 pandemic is expected to bring this long period of growth to a sudden halt. According to the OECD, the economy is predicted to contract by approximately 7% in 2020, where exports and FDI are likely to slow even more. Thailand's past experience of severe floods in 2011, which also resulted in a sudden – but only temporary – interruption of GVC networks, provides some hope that Thailand's GVC integration is quite resilient.

Progress in the area of inclusive and sustainable development is ongoing, with poverty rates dropping to less than 10%, but challenges remain. Although access to basic education at primary and secondary levels is universal, there is a need to address the quality of education being provided. In particular, higher and vocational education needs to equip the workforce with skills required by the industry and the emerging needs of the services economy. Pressures remain in some areas of responsible business conduct (RBC), but are now being addressed with determination. Rapid economic growth in Thailand has also led to significant use of natural resources, resulting in rising environmental challenges.

Thailand aspires to graduate from an upper middle-income to a high-income country by 2037, along with inclusive and sustainable development, as outlined in the 20-year national strategy. With its recently introduced Thailand 4.0 vision and the Bio-Circular-Green (BCG) economy model, the government would like to achieve its objectives through economic upgrading toward a value-based and green economy.

Investment promotion and facilitation policy under the Board of Investment (BOI) has an impressive record in stimulating foreign and domestic investments. The 2015-21 investment promotion strategy includes novelties, such as a shift toward more targeted and merit-based incentives for R&D and skills development and a reduction of activities eligible for promotion. The incentive scheme could however be further streamlined, simplified and made increasingly merit-based so that all firms, including SMEs, can compete on a more equal basis. Besides investment promotion, the BOI engages in non-tax concessions such as providing eased restrictions on foreign shareholdings and expatriate workers. This could affect its efficacy and credibility as the BOI has to represent investors' interests in policymaking while regulating them at the same time. Streamlining the wider institutional framework for the entry of foreign investors and workers could be a longer term reform priority, potentially liberating the BOI from regulatory mandates.

With the creation of the Foreign Business Act (FBA) in 1999, Thailand was early in opening up to foreign investment in manufacturing, but has not liberalised further since then. Thailand's primary and services sectors remain particularly restrictive to foreign investment, according to the OECD FDI Regulatory Restrictiveness Index. The development of competitive services has great potential to promote inclusive growth and productivity including in manufacturing; liberalising services should therefore be envisaged. Meanwhile, some foreign investors have found ways into restricted activities by exploiting legal loopholes, such as preferential shares and indirect ownership. The resulting policy inconsistency and uncertainty are likely to come at a cost for investors, and resolving them should be prioritised in future reforms.

Thailand has made important reform strides in terms of its domestic legal framework to facilitate investments into knowledge assets; namely with respect to IP protection and cyber security. The implementation of these efforts should be prioritised in the short-to-medium-term, while broader reforms to align investment protection into a single law and removing restrictions to land ownership for foreigners could be longer term priorities.

Reviewing Thailand's investment treaties indicates that Thailand, like many other countries, has a significant number of older-style investment treaties with vague investment protections that may create unintended consequences. Where treaties set forth vague provisions, arbitrators deciding investment disputes have had wide discretion to interpret the scope of protection which has generated inconsistencies and uncertainty. The Thai government is well aware of these challenges. It plans to start the process of seeking to update existing older-style BITs with treaty partners once its new model BIT is finalised later in 2020. Experiences with the COVID-19 pandemic may further shape how the government views key treaty provisions or interpretations and how they assess the appropriate balance in investment treaties.

Promoting and enabling responsible business conduct (RBC) is of central interest to policy-makers wishing to attract and keep investment and ensure that business activity contributes to broader value creation and sustainable development. Thailand is a regional leader on RBC; it became the first country in Asia to adopt a standalone National Action Plan (NAP) on Business and Human Rights (2019-2022). While the efforts by the Thai government to set RBC policy direction are commendable, the real test will be in implementation. Building on the support for the NAP and the swell of support for RBC, Thailand is in a unique position to promote bold and consistent implementation of RBC principles and standards across the economy.

Thailand's vision of transitioning into a resilient, innovation and technology driven economy will not be achievable without significant progress towards green growth, especially in a post- COVID context. Recognising these challenges, Thailand has made strides in developing a comprehensive and consistent policy framework for green growth and environment and in promoting green investment. The BCG economy model puts green growth related concepts at the heart of continued development. Priority should be on implementing and strengthening the policies on green growth that are in place and ensuring that environmental objectives are systematically integrated across Thailand's broader policy framework for investment.

Outward foreign direct investment (OFDI) has become an important pillar of Thailand's economy; outward flows have surpassed inward flows in recent years. OFDI can increase Thailand's competitiveness and is central for long-term growth, GVC integration and sustainable development. OFDI is a strategic priority in Thailand's National Economic and Social Development Plan (2017-21). While Thailand's current institutional and policy setup is likely to enable further OFDI growth, policy considerations could focus on better inter-agency coordination and targeted policy packages to promote relocation of labour-intensive activities that are no longer competitive in Thailand, on the one hand, and acquiring brands, knowledge as well as new technologies and innovation capacity, on the other hand.

While the COVID-19 crisis could slow the speed of progress towards Thailand's ambitions, policy recommendations provided in this Review provide potential priority areas for investment climate reform in support of an inclusive and sustainable recovery.



# Assessment and recommendations

## Thailand's strategy for the future and focus of this Review

Thailand has had an impressive economic development trajectory over the past decades, with annual growth rates at around 8% before the Asian Financial Crisis, and more moderate growth since then. Incomes have been increasing rapidly throughout the past half century due to rapid demographic transition, moving agricultural workers into manufacturing. Thailand joined the group of upper middle-income countries in the early 2010s. Foreign direct investment (FDI) and integration in global value chains have been key in Thailand's development process. Inward FDI's share in GDP increased to 50% by 2017. More recently, outward investments have become an important pillar in Thailand's upgrading in global and regional value chains. The emerging global economic crisis related to the COVID-19 pandemic is expected to bring this long period of growth to a sudden halt. The economy is predicted to contract by approximately 7% in 2020, where exports and FDI are expected to slow even more.

Progress in the area of inclusive and sustainable development is ongoing but challenges remain. Poverty rates have dropped to less than 10%. Although access to basic education at primary and secondary levels is universal, there is a need to address the quality of education being provided. In particular, higher and vocational education needs to equip the workforce with skills required by the industry and the emerging needs of the services economy. Pressures remain in some areas of responsible business conduct (RBC), including with respect to human trafficking and forced labour, but are now being addressed with determination. Rapid economic growth in Thailand has also led to significant use of natural resources, resulting in rising environmental challenges.

### ***Thailand's ambition for inclusive and sustainable development***

Thailand aspires to graduate from an upper middle-income to a high-income country by 2037, along with improved security and inclusive and sustainable development, as outlined in the 20-year national strategy (2018-37). With its recently introduced Thailand 4.0 vision, the government would like to achieve its 20-year strategy through economic upgrading toward a value-based, innovation-driven economy away from the production of commodities and low value added manufacturing.

Thailand's vision will not be achievable without progress towards environmental sustainability and socially inclusive growth benefiting all parts of society and all regions. This is consistent with Thailand's long-standing 'Sufficiency Economy Philosophy' prioritising economic self-reliance for all. Thailand therefore introduced the Bio-Circular-Green (BCG) economy model in 2019, involving a strategy and reform agenda on how to achieve the Thailand 4.0 vision and long-term objectives related to the Sustainable Development Goals (SDGs). While the COVID-19 crisis is likely to slow the speed of progress towards Thailand's ambitions, the focus on an inclusive and sustainable development pathway needs to be upheld during the crisis as well as its recovery. The role of the private sector is critical in this regard. Evidence has already shown that responsible companies have been more resilient during the crisis. As governments are

designing recovery policies, they are well-positioned to promote responsible business conduct standards and tools. RBC can help governments and companies make decisions that balance environmental, social and governance issues in the crisis, while ensuring that such responses do not create further risks to people, planet and society – or contribute to further destabilising supply chains down the line.

### ***Focus of this Investment Policy Review***

Guidance on how to embed these efforts in the broader policy and institutional landscape is of key interest in this Investment Policy Review. It reviews investment climate reform opportunities that support Thailand's development and contribute to the SDGs, relying on the Policy Framework for Investment (Box 1) which is a tool developed at the OECD to help governments address investment climate challenges. The Review has been conducted by the OECD in close co-ordination with the Ministry of Foreign Affairs of Thailand and implemented as part of the OECD-Thailand Country Programme. It was supported by an inter-agency taskforce including various Thai government agencies. While the bulk of the Review was prepared before the COVID-19 outbreak, possible economic and sustainability implications of the emerging crisis are reflected across chapters. Policy recommendations provided in the Review should be considered as possible reform priorities for the investment climate to enable an inclusive and sustainable recovery in Thailand. Thailand could also consider making an official request to adhere to the OECD *Declaration on International Investment and Multinational Enterprises*, which would involve an OECD-assisted process building on the work already undertaken in this Review.

After further elaborating on Thailand's development path and future development strategies (Chapter 2), the Review provides a snapshot on the current competitive edge with a particular focus on competitiveness in manufacturing activities and services, targeted under Thailand 4.0 and the Board of Investment's (BOI's) investment promotion policy, as well as on innovation capacity and skills (Chapter 3). This assessment helps identify where challenges may lie and policy efforts are needed. Chapter 4 studies trends and qualities of FDI and discusses how investment contributes to Thailand's inclusive and sustainable development, aligned with Thailand 4.0 and the SDGs.

Chapter 5 focuses on investment promotion and facilitation. It describes the institutional framework and strategy for promotion and highlights related outcomes. Based on the experience of OECD and other countries, the chapter looks at how to attract FDI in high-technology and R&D sectors, including attraction of foreign talent that may currently be insufficient in Thailand. Chapter 6 focuses on the foreign investment regime, particularly restrictions to FDI in services and possible reform opportunities of the Foreign Business Act (FBA) that would enable a greater contribution of investment to Thailand 4.0 ambitions. Chapter 7 discusses the broader legal framework for investment. Intellectual property rights protection and contract enforcement are at the centre of discussion, given their key role for developing higher value added activities. Relatedly, Chapter 8 describes Thailand's investment treaty practice and presents opportunities for alignment with modern practices.

The subsequent chapters focus on RBC (Chapter 9) and the role of investment for green growth (Chapter 10). The chapter on RBC reflects Thailand's achievements towards promoting more responsible business practices, including state actions and frameworks that have been put in place for that purpose. It provides recommendations on how promoting RBC is a strategic choice for upgrading in global supply chains while also enabling policy coherence and encouraging the private sector's contribution to the SDGs. This will become even more critical in a post-COVID world. Chapter 10 describes the policy framework for green growth and climate change in Thailand and points to significant challenges with respect to policy coherence and implementation.

With economic development, Thailand has become an important investor abroad. This can improve efficiency by moving activities in which Thailand no longer has a comparative advantage to neighbouring countries and help knowledge acquisition by investing in foreign technologies. Chapter 11 presents outward investment trends, points to opportunities and risks and suggests directions for policy.

This assessment chapter provides a synthesis of main findings and recommendations of this Investment Policy Review. For each policy reform area, a prioritisation of possible policy options is proposed. Short- and medium term policy priorities could typically be addressed unilaterally by concerned government agencies, while long-term priorities may involve coordination and action of several agencies, and could imply changes in the legal framework itself. Long-term policy considerations may be initiated immediately but could be delivered over a time horizon of several years.

### Box 0.1. The Policy Framework for Investment

The Policy Framework for Investment (PFI) helps governments to mobilise private investment in support of sustainable development, thus contributing to the prosperity of countries and their citizens and to the fight against poverty. It offers a list of key questions to be examined by any government seeking to create a favourable investment climate. The PFI was first developed in 2006 by representatives of 60 OECD and non-OECD governments in association with business, labour, civil society and other international organisations and endorsed by OECD ministers. Designed by governments to support international investment policy dialogue, co-operation, and reform, it has been extensively used by over 30 countries as well as regional bodies to assess and reform the investment climate. The PFI was updated in 2015 to take this experience and changes in the global economic landscape into account.

The PFI is a flexible instrument that allows countries to evaluate their progress and to identify priorities for action in 12 policy areas: investment policy; investment promotion and facilitation; trade; competition; tax; corporate governance; promoting responsible business conduct; human resource development; infrastructure; financing investment; public governance; and investment in support of green growth. Three principles apply throughout the PFI: policy coherence, transparency in policy formulation and implementation, and regular evaluation of the impact of existing and proposed policies.

The value added of the PFI is in bringing together the different policy strands and stressing the overarching issue of governance. The aim is not to break new ground in individual policy areas but to tie them together to ensure policy coherence. It does not provide ready-made reform agendas but rather helps to improve the effectiveness of any reforms that are ultimately undertaken. By encouraging a structured process for formulating and implementing policies at all levels of government, the PFI can be used in various ways and for various purposes by different constituencies, including for self-evaluation and reform design by governments and for peer reviews in regional or multilateral discussions.

The PFI looks at the investment climate from a broad perspective. It is not just about increasing investment but about maximising the economic and social returns. Quality matters as much as the quantity as far as investment is concerned. It also recognises that a good investment climate should be good for all firms – foreign and domestic, large and small. The objective of a good investment climate is also to improve the flexibility of the economy to respond to new opportunities as they arise – allowing productive firms to expand and uncompetitive ones (including state-owned enterprises) to close. The government needs to be nimble: responsive to the needs of firms and other stakeholders through systematic public consultation and able to change course quickly when a given policy fails to meet its objectives. It should also create a champion for reform within the government itself. Most importantly, it needs to ensure that the investment climate supports sustainable and inclusive development.

The PFI was created in response to this complexity, fostering a flexible, whole-of-government approach which recognises that investment climate improvements require not just policy reform but also changes in the way governments go about their business.

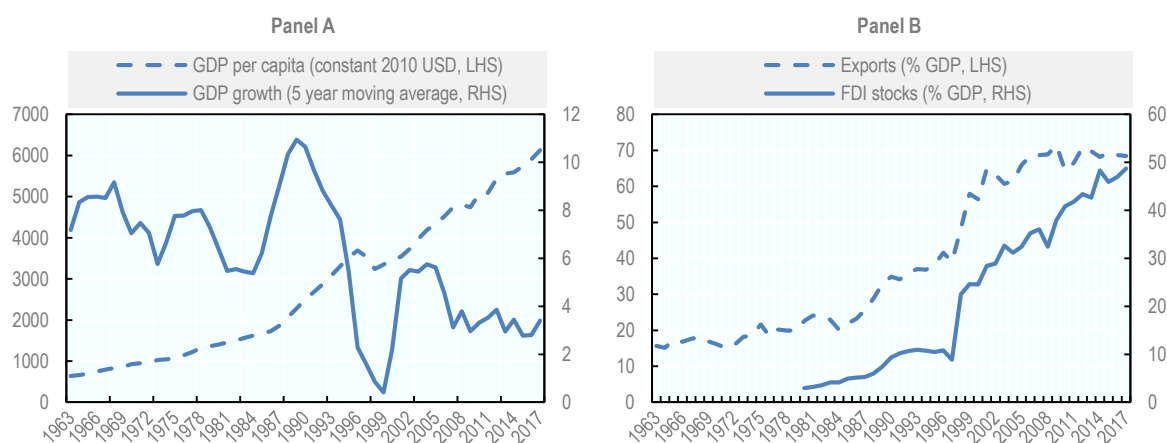
For more information on the Policy Framework for Investment, see:

<http://www.oecd.org/investment/pfi.htm>.

## Thailand's development trajectory

Thailand experienced rapid growth, at an annual rate of around 8%, before the Asian Financial Crisis in 1997. It recovered quickly from the 1997 crisis but economic expansion has remained more modest ever since. Despite slower growth in recent decades, per capita incomes have continued increasing due to rapid demographic transition, moving agricultural workers into manufacturing (Figure 1.1, Panel A). Thailand joined the group of upper middle-income countries in the early 2010s. Nonetheless, one-third of the population is still involved in agriculture and it remains important to ensure that an agrarian population, already the lowest income sector in the country, does not get left further behind. Their function remains important for the Thai economy, not least for food security. The emerging global economic crisis related to the COVID-19 pandemic is expected to bring Thailand's long period of growth to a sudden halt. The economy is predicted to contract by approximately 7% in 2020, where exports and FDI are expected to slow even more.

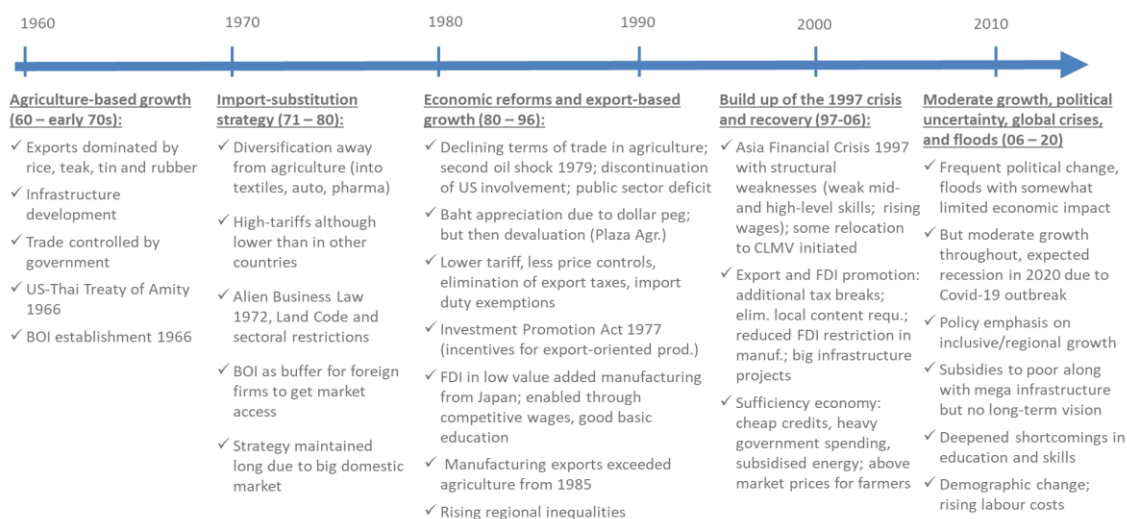
**Figure 0.1. Thailand's strong economic growth has been enabled by exports and FDI**



Source: OECD based on World Development Indicators.

Embedded in 5-year development plans since the early 1960s, Thailand's macroeconomic policy has been relatively stable over the past decades despite frequent changes in government (Figure 1.2). Thailand followed a development model like many in Asia and elsewhere, involving a long-term structural shift from agriculture to industry. The shift from an import substitution policy to greater emphasis on export promotion was essential for the rapid growth of manufacturing production and exports. Nonetheless, the export boom came slightly later with more favourable exchange rate policies and an investor-friendly industrial policy. More recent development policies have emphasised inclusive and sustainable growth, but challenges remain particularly in light of the emerging global crisis due to the COVID-19 outbreak. Responding to the crisis, the government has introduced strong measures to address economic challenges for individuals, businesses and the economy more broadly, which total approximately 15% of GDP – among the highest in Asia.

Figure 0.2. Thailand's development trajectory: 1960-today



Source: Based on OECD research (see Chapter 2).

### ***Foreign investment has been key in Thailand's development and integration in global value chains***

FDI has played a key role in Thailand's industrialisation process and integration in GVCs. FDI in Thailand was dominated in the early period by US investors, but over the 1980s, Japanese foreign investment exceeded threefold that from the United States. Foreign investment in the automobile, electronics and textile sectors enabled rising exports, while some of these investments involved assembly of imported components for domestic sale. Inward FDI's share in GDP increased to 50% by 2017 (Figure 1, Panel B). Investment is still dominated by Japanese manufacturing investors, but with rising shares of other investors from both within the ASEAN region, mostly Singapore, as well as outside, for example China and Europe.

As a share of ASEAN, however, both FDI stocks and flows have fallen steadily over the past two decades (Chapter 4). This is partly explained by growing investments in neighbouring Cambodia, Lao PDR, Myanmar and Viet Nam (CLMV). The CLMV region has become an attractive destination for some investors, due to their low-cost labour and improving investment and trade regimes, including related to preferential import tariffs in the European Union and the United States.

Investments abroad have increased rapidly over the past decade, including in CLMV (Chapter 11). Thailand is the second largest investor in terms of outward FDI (OFDI) stock in ASEAN, surpassing Malaysia in 2018. Outward investments have become an important pillar in the economy, with OFDI stocks as a share of GDP reaching 25% in 2018. Annual growth of OFDI has surpassed that of inward FDI in recent years. Thai enterprises are venturing into neighbouring ASEAN markets and increasingly beyond regional markets, driven by slower domestic market growth, rising labour costs and export market access.

Trade and investment in global value chains (GVCs) have come to a sudden halt in many sectors as a result of the COVID-19 outbreak. Thai exports may fall by as much as USD 22 billion in 2020, with the biggest impacts on exports of manufacturing goods and (travel) services. Likewise, FDI is set to fall in 2020 by more than 30% globally and is likely to affect developing countries, including Thailand, relatively more given their exposure to crisis-affected manufacturing sectors. Cross-border M&A deals and announced greenfield FDI in Thailand have dropped considerably in the first months of 2020 compared to the previous years (Chapter 4). With almost the whole world having entered full or partial lockdown in March, the downward trend is likely to have magnified since then. Thailand's past experience of severe floods in 2011,

which also resulted in a sudden supply shock and interruption of GVC networks, may provide some hope that Thailand's GVC integration is quite resilient. GVCs remained in place and operations of many foreign firms expanded soon after the floods in 2011. Going forward, it will be important to promote and enable responsible business conduct by companies participating in GVCs considering the increased attention being given to environmental and social impacts in GVCs.

### ***Progress toward inclusive and sustainable development continues but challenges remain***

Economic development has also brought some social progress to Thailand. Poverty rates, measured against the national poverty line, have decreased considerably from around 60% in 1990 to 7% today. Although access to basic education at primary and secondary levels is universal, there is a need to address the quality of education being provided. In particular, higher and vocational education needs to equip the workforce with skills required by the industry and the emerging needs of the services economy. The government has reinforced its efforts to address the skills and innovation capacity challenge over recent years (Chapter 3).

Social pressures remain significant, particularly in poorer regions, where precarious employment conditions are prevalent, despite some improvements over the past decades. As the labour market tightened in the early 1990s, the borders were implicitly opened to admit labour migrants from neighbouring countries, mostly Myanmar. Today, almost 10% of the labour force or 3.5 million are low-skilled migrant workers employed predominately in agriculture, fishing, construction, domestic services, manufacturing and retail. Many of those migrant workers, but also many low-skilled Thai workers, have informal work arrangements and are sometimes paid below the minimum wage without unemployment protection. More recently, basic social protection has improved in some areas: the 2002 universal health coverage scheme and the 2009 universal allowance for the elderly provide access to services for all, including those in the informal sector.

Significant informality among migrant workers also results in persistent issues in other areas of responsible business conduct, although government efforts have been strengthened with enhanced inspection frameworks, improved laws and increased penalties in case of abuse. Thailand is the first Asian country with a National Action Plan on Business and Human Rights (Chapter 9).

The COVID-19 outbreak is putting new pressure on income and wealth inequalities in Thailand. Both the 1997 and 2008 crises led to increased unemployment and income inequalities and these are likely to spike once more. Significant job losses are already being reported by the Department of Employment. People with informal and precarious employment conditions, including those with small family businesses, are most affected. The government has introduced important measures to address economic challenges facing households (Chapter 2).

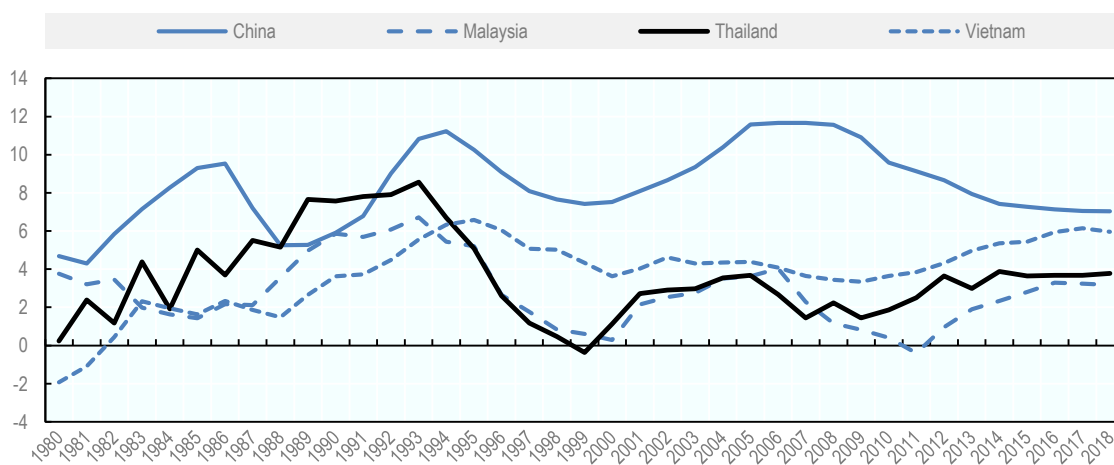
Rapid economic growth in Thailand has also led to significant use of natural resources, resulting in rising environmental challenges (Chapter 10). Thailand suffers from frequent and severe floods and droughts, causing loss of life and significant economic disruption, and is particularly vulnerable to climate change. Air pollution is an increasing challenge, particularly in urban areas, exacerbated by increasing vehicles, construction activities and agricultural burning. Waste management and water pollution are also a severe problem, and illegal dumping of plastics into water bodies in Thailand has global ramifications for oceans' health. Carbon dioxide (CO<sub>2</sub>) emissions from the use of fossil fuels have increased rapidly but remain below the OECD country average. Recognising these challenges, Thailand has made strides in developing a comprehensive and consistent policy framework for green growth and the environment and in promoting green investment and sustainable finance. The COVID-19 outbreak further hampers the green transition. The planned transition from fossil fuels to renewable energy is now being challenged by the unprecedented health emergency and economic crisis, and the collapse in oil and gas prices and decline in coal prices may reduce support for renewable energy.

## Thailand's competitive stance

Thailand's competitiveness moved from the production of agricultural to industrial goods between 1980 and the mid-1990s. This transition was accompanied by rapid growth in labour productivity, at yearly rates often above 8% (Figure 1.3). Productivity has slowed in the past few decades, as Thailand no longer benefits from shifts of labour from agriculture to more productive manufacturing activities. Competitiveness in labour intensive manufacturing is constrained by rising labour costs related to an ageing workforce and higher worker expectations. Rising labour costs have not been matched with improvements in worker skills and the capability of firms to engage in higher value added activities in manufacturing and services.

**Figure 0.3. Relatively low productivity growth since mid-1990s**

Labour productivity growth (5-year moving average, in %)



Source: OECD based on Conference Board's Total Economy Database.

The Thai government has confronted the challenge to competitiveness and the ambition of Thailand 4.0, the 20-year strategy and the BCG economic model with highly ambitious plans and programmes to enhance productivity of five existing and five new target sectors (including some services), boost innovation capacity, accelerate human resource development and promote area-based economic development to reduce income and territorial inequalities (Chapter 2). Investment promotion and facilitation policy, led by the Board of Investment (BOI), plays an essential role in achieving the Thailand 4.0 vision and is discussed in details in the next section and Chapter 5. Investment promotion activities are complemented and to some extent coordinated with those of other ministries and state agencies (e.g. Ministry of Finance, Ministry of Commerce; Ministry of Higher Education, Science, Research and Innovation, MHESI); Eastern Special Development Zone Policy Office; Industrial Estate Authority; Ministry of Industry; and Office of Small and Medium Enterprises Promotion). This section summarises key findings on Thailand's competitiveness, the contribution of FDI and related policy initiatives.

Thailand's productivity challenge might become yet more important as the world has moved into a global economic crisis related to the COVID-19 pandemic. There are a number of factors which might further impair global and Thai productivity growth, including higher transactions costs, lower mobility, and a reduced scope of resource reallocation across firms, sectors, and countries. SMEs are likely to be the most affected, potentially increasing already severe productivity inequalities. On the other hand, innovations prompted by the need for new ways of working could generate a positive productivity impulse. While crisis implications should be taken into account for short and longer term policy priorities, it is important to take stock of Thailand's competitiveness even if it based on pre-crisis data at the moment. Understanding

Thailand's competitiveness will help identify strengths and weaknesses of the economy and inform policy directions during the recovery.

### ***Productivity in targeted activities is improving***

Although Thailand's labour productivity in targeted manufacturing and service activities has been improving recently, productivity levels in these activities still lag considerably behind levels in more advanced economies, particularly in services. This is associated with a persisting dominance of lower value added activities within targeted sectors. An alternative measure of competitiveness is the extent to which Thailand has a revealed comparative advantage to manufacture specific products and sell services on global export markets. The analysis shows that activities of strategic priority (such as the manufacture of modern batteries, aircraft and spacecraft, bio fertilisers, or advanced business and IT services) are currently far from having a comparative advantage on exporting markets.

The BOI provides tax exemptions to enhance investments into specific productivity-enhancing activities within the ten target industries and services. More generous tax exemptions are provided for higher levels of technology and value creation within the supply chain, as Thailand 4.0 focuses on developing advanced services and services also play an important role in enabling higher value chain activities in manufacturing (Chapter 6). Nevertheless, foreign investments in a number of services require prior permission under the FBA. Government efforts to attract FDI into targeted sectors under Thailand 4.0 have started to pay off, although at a relatively slow pace which could continue due to the COVID-19 crisis. For example, automobiles, electronics and logistics have received comparatively high shares of total FDI, but FDI growth over the past five years has remained modest in most of these sectors. Based on the analysis in Chapter 4, it is unclear to what extent prioritised, high-value activities within these sectors are expanding investment or whether the mass of new investments involve activities in which Thailand has had a comparative advantage over a long period.

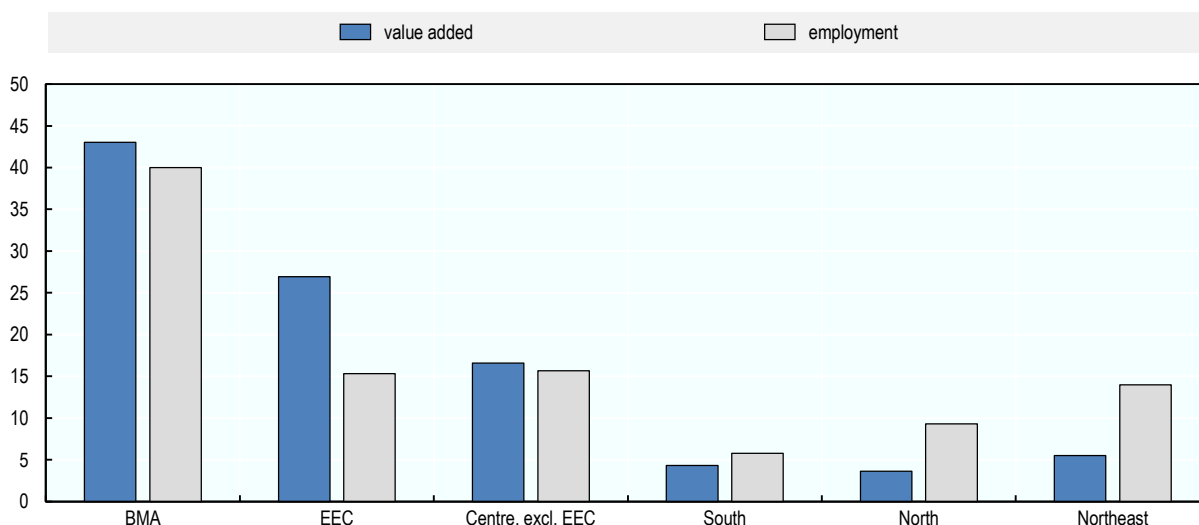
Beyond attracting FDI into targeted sectors, the role of foreign investment in Thailand's efforts to enhance productivity and sustainable development is also revealed by foreign firms' performance premium over average domestic firms. In most manufacturing and services sectors, foreign firms tend to be more productive, invest more in research and development (R&D), pay higher wages, and hire larger shares of skilled workers and women. While these performance premia of foreign firms confirm the importance of the direct contribution of foreign firms to the Thai economy, it may also point to persistent gaps in adequate capabilities of domestic firms, which in turn are an important prerequisite of positive FDI spillovers.

### ***Recent policy efforts address regional and firm-level productivity disparities***

Competitiveness remains highly unequal across regions and provinces, with wider Bangkok and the Eastern Economic Corridor (EEC) leading the way and reporting growing labour productivity in priority activities. Foreign firms are also concentrated primarily in the Bangkok Metropolitan Area (BMA), the EEC provinces, and the rest of the Centre (see Figure 1.4 for manufacturing).



Figure 0.4. Foreign activity is concentrated in BMA, EEC and the Centre



Note: BMA = Bangkok Metropolitan Area; EEC = Eastern Economic Corridor provinces. Services include trade, hospitality and professional services.

Source: OECD based on Thailand's Industrial Census.

In recent years, various area-based schemes have been introduced to advance Thailand's economic development towards higher value added activities and expand socio-economic development to regional and local levels. The BOI used a cluster-based policy in 2015-17 to promote business clusters that operate within concentrated geographic areas and function through interconnected businesses and related institutions. Investment uptake was relatively low under this policy, however. With the introduction of Thailand 4.0, area-based policies moved away from wide ranging cluster development across Thailand towards a geographically much more concentrated strategy, namely the EEC whose Act came into force in 2018. The EEC strategy is supplemented by numerous ministerial projects, such as the EECi Innovation Hub that fosters international innovation collaboration in target sectors and is governed by the MHESI. Thailand continues to promote inclusive growth through additional area-based policies, including the Border Special Economic Zone (SEZ) Development Policy, as well as promotional efforts in border provinces in Southern Thailand and in the 20 poorest provinces in the East and North of Thailand. Broad-based economic and sustainable development across all regions is also being reinforced with the newly introduced BCG economic model. These efforts need to further ensure that protecting local communities rights (e.g. over land acquisitions) is guaranteed and industrial practices are environmentally sustainable.

Significant productivity disparities are also observed across foreign and large domestic firms as well as SMEs. Foreign firms are the most productive in all sub-national regions, closely followed by large domestic firms. SMEs are only half as productive as larger and foreign firms in wider Bangkok and EEC provinces and fall even further behind in less developed regions. Some of these disparities are partly alleviated through business linkages between foreign and domestic firms, as Thai firms that develop linkages with foreign firms are more productive relative to Thai firms that do not (Chapter 4).

Recognising firm-level disparities between foreign and large domestic firms on the one side and domestic SMEs on the other side is highly important when it comes to the design of policies and programmes related to Thailand's upgrading in GVC positions in support of progress toward Thailand 4.0. While SMEs are often less productive than larger firms, SMEs in Thailand are revealed to face particular difficulties to compete and upgrade due to the dominance of large domestic conglomerates, including state-owned companies, as well large affiliates of foreign firms.<sup>1</sup> It is further shown that it is mostly large firms, both domestic and foreign, that benefit from BOI promotion, which puts larger firms at an additional competitive advantage

vis-à-vis domestic SMEs (Chapter 5). As mentioned above, BOI promotion involves tax incentives such as tax holidays to attract investment into targeted, high-value activities in which domestic SMEs do often not compete.

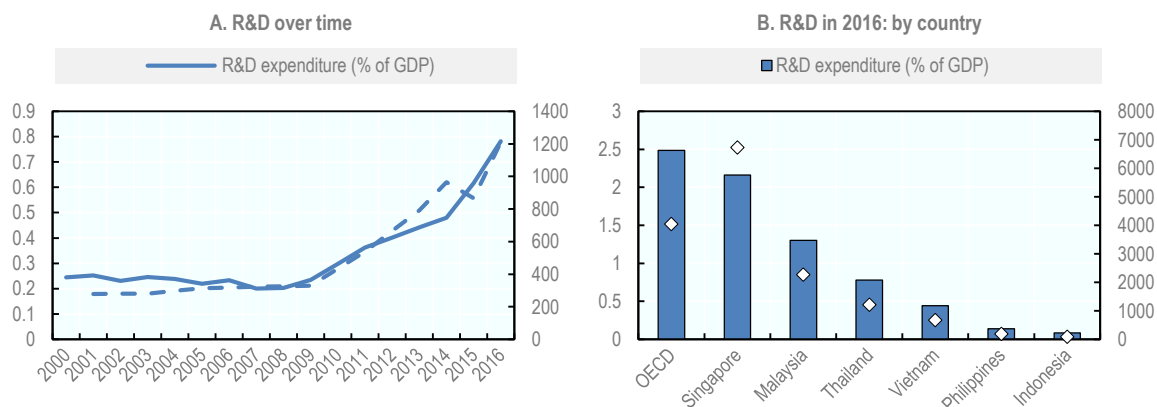
Thailand 4.0 ambitions can only be attained if public policies help to level the playing field for all types of firms. For example, all firms – independent of whether or not they are promoted – should benefit from import duty reductions and may benefit from merit- or performance-based support but this is currently not the case (see policy directions provided below and in Chapter 5). It is of utmost importance to put the emphasis on SME upgrading, even if upgrading does not involve technology frontier-type of activities. BOI promoted firms may receive performance-based tax exemptions if they engage in developing and training local suppliers. SMEs themselves may receive specific information and technical support from the BOI, as well as from a number of other state agencies involved in the promotion and support of local firms and SMEs (e.g. the Ministry of Industry, or the Office of Small and Medium Enterprise Promotion).

**Innovation capacity and human capital are increasing**

In terms of innovation capacity, important progress is being made. Research and development (R&D) has increased in recent years (Figure 1.5), resulting in a patenting surge of Thailand-based inventions. Nonetheless, total innovation output need to be accelerated to catch up with comparator countries, such as Malaysia or Singapore.

Thailand’s investment promotion policy aims to attract investment into research and development (R&D) projects in the 10 target sectors and particularly in the area of four core technologies in which Thailand is considered to have potential to enhance the country’s overall competitiveness, namely biotechnology, nanotechnology, advanced material technology and digital technology (Chapter 5). Projects must involve a component on technology transfer by cooperating with educational and research institutions, for example via programmes of the National Science and Technology Development Agency (NSTDA) or the Thailand Institute of Scientific and Technological Research, under MHESI. Technology-based projects can receive a corporate income tax exemption of up to 13 years from the BOI. If considered as high-impact investments under the newly enforced Competitiveness Enhancement Act 2017, tax exemptions may be granted for up to 15 years. Beyond programmes of the BOI and MHESI, other government agencies – such as the Revenue Department – are also providing support and incentives to improve innovation capacity.

**Figure 0.5. R&D activities are picking up in Thailand**



Note: R&D expenditures and researchers includes activities by public and private institutions (include business sector).  
 Source: OECD based on World Bank Development Indicators

The lack of adequate human resources has long been a challenge for Thailand's competitiveness and requires a systematic overhaul in education starting from primary level upwards. Thailand's plan to become a value-based, innovation-driven economy, and to attract investment accordingly, is only possible if the remaining skills gap and mismatch is addressed. This holds not only for the most advanced skills of researchers, engineers and managers, but also and essentially for skills of technicians and vocational workers. Thailand has a systematic undersupply of secondary and lower vocational skills. In 2013, the labour market demand of secondary and lower vocational skills exceeded 50% of total demand, while the supply of those skills was only around 10% of total supply. The Office of the Vocational Education Commission, along with programmes of the BOI and MHESI, have recently boosted efforts and programmes to increase both the quantity and quality of vocational skills and make technical training more attractive to Thai students. These programmes are increasingly developed and coordinated with the private sector and educational institutions. They often require students to combine practical training in companies with classroom education; an example is the Work-integrated Learning (STI-WiL) programme, introduced in 2012 by the former National Science Technology and Innovation Policy Office (STI).<sup>2</sup>

Turning to advanced skills of researchers, engineers and managers, the system has not been producing the types and quality of graduates required by the labour market. For example, in 2010, approximately 15 000 engineers graduated from Thai universities but the predicted demand was more than six times as high. STEM qualifications are required by 40% of total demand for workers with a university degree in Thailand, while only 20% of total supply of higher education graduates have a background in STEM. More recently, the challenge may no longer lie in the quantity but rather the quality of STEM skills. The creation of the MHESI in 2019 and its determined reform agenda – including related to enhanced coordination and joint initiatives of government agencies, educational and research institutions, industry and the local community – is an essential step to address the skills and innovation challenge.<sup>3</sup> The Thai government is also inclined to attract foreign talent to develop the ten target industries. For that purpose, the SMART visa programme has been designed to attract foreign science and technology experts, senior executives, investors and start-ups (see further discussion below and in Chapter 5). While this programme is useful to address an immediate challenge, broader alignment and reforms are required to facilitate entry of foreign workers and to produce required skills within Thailand.

Government efforts and adaptation of firms to labour and skill shortages seem to be fruitful in Thailand's manufacturing sector. In Thailand's two manufacturing centres (wider Bangkok or BMA; and EEC), labour shortages have been decreasing in recent years. While in 2011 around 30% of foreign and large domestic firms reported labour shortages to be a major problem for their operations, only around 20% said the same in 2016. The provision and expansion of in-house training among foreign and large domestic firms is particularly common: over 40% of firms provide training, with increasing numbers in recent years. Rising and relatively high shares of in-house training among larger firms (foreign firms are also often large) is due to the requirement for firms with more than 100 employees to do so under the Skills Development Act 2002. While firms have been adapting with worker training to address the skills gap, more than a fifth of foreign and large domestic firms still expected the government to increase efforts to provide adequate training and skills to workers in Thailand in 2016.

## Investment promotion policies to build a knowledge-based economy

Investment promotion and facilitation policy in Thailand has an impressive record in stimulating foreign and domestic investments, which has profoundly transformed the economic landscape, contributing to the emergence of new industries such as the automotive sector. Overall, promoted companies' weight in the Thai economy is colossal and they are pivotal for the enhancement of strategic areas such as the EEC. Despite forming less than 3% of registered companies, they generate one-third of national value-added, employ one in ten skilled workers and constitute almost a quarter of all business expenditures on R&D and training (Table 1.1).

**Table 0.1. The weight of promoted industrial establishments in the Thai economy**

Promoted firms in % of all establishments (unless otherwise specified)

	2011	2016
Promotion certificate status	2.5%	2.4%
Promoted foreign-owned (% of all foreign-owned firms)*	68%	68%
Promoted exporter (% of all exporters)	32%	35.5%
Value-added	34.4%	29.7%
Employment, among which:	20.3%	20.9%
<i>Skilled</i>	10.4%	10.9%
<i>Unskilled</i>	7.5%	7.4%
<i>Other</i>	2.4%	2.5%
Spending on R&D	52%	23%
Spending on training of employees	32%	20%

Note: \* foreign-owned: 51% or more foreign shareholding.

Source: OECD based on the Industrial Census of Thailand 2012 and 2017.

The net positive impact of investment promotion in Thailand is, however, not a given as the government's forgone revenues due to tax incentives can be considerable. In addition, the effectiveness of investment promotion policies in contributing to the development of a knowledge-based economy, supporting technological progress, closing the skills gap and reducing income and territorial inequalities has become a growing challenge for the government. For instance, the percentage of promoted manufacturers that engaged in R&D and skills expenditures, and the budget they devoted to these activities were lower in 2016 than in 2011 (Table 1.1). The COVID-19 outbreak may further exacerbate these structural challenges.

### ***Modernising the institutional framework for investment promotion and facilitation may help the BOI focus on core investment promotion activities***

The BOI is a key pillar of Thailand's institutional ecosystem. The initial duty of the agency five decades ago continues to be its core mandate today, which is to issue promotion certificates (for both domestic and foreign investors) and amend the list of activities that are eligible for tax incentives and non-tax concessions such as eased restrictions on foreign shareholdings and expatriate workers. Foreign investors subject to Foreign Business Act (FBA) restrictions are in fact more likely to enter Thailand under the Investment Promotion Act than under the FBA or provisions under international treaties (Chapter 6).

Because of its recognised efficiency among state agencies, the BOI has inherited new responsibilities over the years, such as attracting foreign talent, including entrepreneurs, and facilitating their entry. Thailand's over reliance on the BOI could end up weighing on the capacity of the agency to perform its various mandates effectively. Attracting investors and talented foreign workers on the one hand and ensuring that they comply with legal requirements on the other are two different functions with different objectives. Mixing the mandates could affect the efficacy of the agency and also its credibility as it is supposed to represent investors' interests in policymaking while regulating them at the same time.

### ***Investment promotion strategy supports wider goals such as Thailand 4.0...***

The current investment promotion scheme of the BOI runs from 2015 to 2021 and aims to enhance Thailand's competitiveness, overcome the middle-income trap and achieve sustainable growth, all in line with greater ambitions related to Thailand 4.0, as described above. Since 2015, the scheme has been augmented and more specifically tailored to higher level plans and strategies and the promotion of the ten target sectors.

The strategy introduced a few novelties with regard to the pre-2015 incentives scheme but did not bring fundamental changes (Chapter 5). The BOI's proclaimed shift from broad-based to more targeted incentives was a positive development. Around 50 activities were no longer promoted when the strategy entered into force in 2015, although it is not clear whether the eligible list has been further reduced since then. The government amended the Investment Promotion Act in 2017 to introduce technology-based incentives, which are more horizontal and less sector-specific, thereby reducing their distortive impacts on the economy.

***...but the incentive scheme is complex and could make it harder to level the playing field for all firms***

The wider tax incentive scheme continues to be complex and its generosity can weigh on the ability of non-promoted firms, particularly SMEs, to compete on equal basis with promoted businesses. Activity-based incentives such as exemptions of corporate income tax (CIT) and import duties still dominate the basic incentives scheme. The main innovation was the introduction of merit-based incentives that provide an add-on to the basic scheme with additional CIT exemptions and tax deductions if a project undertakes R&D or skills development activities or locates in specific regions or in an industrial area (cost-based incentives). The merit-based scheme is a positive development as it is preferable to activity-based incentives, which can generate important forgone revenues. The design of the merit-based scheme could be further improved to attract investment with higher development impacts. This involves streamlining the application process, clarifying the decision criteria and reduce overlaps with incentives schemes granted by other government bodies.

***Recent investment facilitation initiatives should help improve the business climate...***

The Thai business climate is one of Southeast Asia's most favourable for investment. Thailand has registered notable improvements in World Bank's Doing Business ranking since 2016. Over the past 12-months, it has surpassed six other countries and now ranks 21<sup>st</sup> out of 190 countries worldwide. This progress was driven by improvements in the indicators dealing with construction permits, starting a business, getting electricity and resolving insolvency. Further improvements can be made to cope with fiercer competition and generalised improvements in neighbouring countries' business environments. Policy areas that are crucial for attracting higher value-added investments in R&D and advanced technologies could be further improved, such as enforcing intellectual property (IP) rights (Chapter 7).

The 2015-21 investment promotion strategy did not include major changes with respect to investment facilitation. Nonetheless, the BOI undertook other important initiatives to improve the wider framework for investment facilitation and retention. These new initiatives include, but are not limited to, the creation of the Strategic Talent Centre and the SMART visa programme to attract foreign talent and start-ups, easing restrictions on the entry of unskilled foreign workers and improvements in the administration of the One Start One Stop Investment Centre (OSOS) and the services it provides. Monitoring regularly the impact of these different initiatives, and ensuring that they are well-coordinated, would increase their success rate.

***...but whole-of-government reforms to attract foreign talent are necessary***

Notwithstanding the relevance of recent initiatives to attract foreign talent, streamlining the wider legal and institutional framework for the entry of foreign workers continues to be necessary. The benefits and costs of stringent migration policies such as TM30 (landlords must register non-Thai nationals living in their properties) must be assessed against the wider objective of attracting foreign talent. If there are any identified benefits, other tools must be considered to remedy the situation, such as through reforms envisaged by the Guillotine Unit (Simple and Smart Licence project). In the medium to long term, structural reforms easing foreign talent entry would make obsolete those initiatives such as the Strategic Talent

Centre or the SMART Visa programme, which affect the capacity of the BOI to focus on its core investment promotion and facilitation mission.

### ***The COVID-19 pandemic triggered immediate policy responses to support existing investors and pave the way for a sustained recovery***

The COVID-19 outbreak, and the risk of reduced FDI flows as a consequence, makes it even more relevant for the BOI to accelerate its transition toward promoting activities with a high developmental impact, supporting a sustainable recovery. During the first quarter of 2020, the number of applications submitted to the BOI increased slightly compared to the same period last year but the total invested capital declined by 44%, as projects were smaller. To respond to the crisis, the BOI rapidly adapted its activities and adopted new measures. It has taken measures on the investment facilitation front, followed by other measures to mitigate the impact of the crisis on investment, including tax incentives to accelerate investment in the medical sector.

### ***Policy options to make investment promotion and facilitation more effective***

It is premature to draw definite conclusions on the outcomes of the 2015-21 strategy and its wider effects on R&D and skills, particularly with the COVID-19 outbreak, but interim analysis raises a few observations. First, the incentive scheme did not radically change the distribution of investment by sector, at least until the end of 2019. Second, the most generous incentives are not granted to investment projects with higher foreign ownership shares or higher shares of foreign workers which is somewhat unexpected given that the most generous incentives are granted to activities with no or very few existing investments in Thailand, which would therefore potentially depend on foreign investment and knowledge brought in by foreign workers. Third, incentives to spend on R&D and skills have had a modest impact although this may improve with time. Last but not least, promoted firms are more geographically concentrated than their non-promoted peers. Activity is confined to the EEC, and border SEZs may not be able to reverse this pattern.

#### *Short- and medium-term policy priorities:*

The following policy considerations to strengthen promotional efforts could be implemented without adjustments to BOI's broader mandate and legal obligations and would not require coordination with other government agencies involved in attracting investment into R&D and skills development, for example:

- Streamline the tax incentive framework and rethink the design of some schemes to limit forgone revenues and attract investment with higher development impacts:
  - In the short-term, and to pave the way for a post-COVID-19 recovery, maintain the level of granularity in the general list of activities eligible for investment promotion but continue lowering the number of promoted activities and progressively reduce the incentives of those in sectors with lower comparative advantage. The next strategy could focus, instead, on more horizontal activities that can continue building the foundations for a knowledge-based economy, such as promoting investment in advanced technology, R&D, skills development, and the medical sector.
  - In the medium-term, improve the design of the merit-based scheme to attract investment with higher development impacts and eventually expand the scheme to all firms to level the playing-field with non-promoted companies, particularly SMEs. The application process could be further streamlined and the decision criteria could be eased. Furthermore, gradually move from exemption of corporate income tax and import duties to a scheme with tax credits and deductions as the main type of tax incentives. In parallel, explore reducing import duties.
- Conduct a thorough and informed cost-benefit analysis of the overall effectiveness of the 2015-21 tax incentives scheme. The results should be made publicly available. Disclosing information on

overall forgone revenue through tax incentives would greatly support the government in its efforts to move away from a profit-based investment promotion to a merit-based strategy to attract and retain more sustainable investments.

- Sharpen the quality of the investment generation activities to better target top foreign multinational firms, particularly foreign R&D performers, and continue the efforts to facilitate investment entry and retention and improve the broader business climate for R&D performers. After-care services could focus on enhancing reinvestments, particularly in R&D activities.
- Further involve the private sector and other relevant stakeholders in the decision-making process of the BOI to ensure that the views and interests of all businesses are taken on board in BOI's broad strategic directions. The Board of the BOI could also include public and private representatives from the innovation and education policy communities and wider civil society as well as being more gender balanced.

#### *Long-term policy priorities:*

The following policy considerations require coordination and alignment across multiple government agencies and broader policy and institutional reforms, beyond the scope of the BOI mandate. They could be initiated in the short-term but are likely to involve a medium-term planning horizon.

- Ensure that investment promotion and facilitation responsibilities are balanced across government agencies, sufficiently funded, explicit, and mutually understood and clear for all. To safeguard the BOI's efficiency over the longer-term, consider the option of liberating it from some of its functions (e.g. separating policymaking and regulatory mandates and promotion and facilitation tasks) if, and only if, the same quality of services can be provided. The success of such an option is conditional on undertaking other reforms:
  - Re-evaluating and reforming the FBA may be an opportunity to adjust the Investment Promotion Act and eventually liberate the BOI from its mandate to provide non-tax incentives to foreign investors (Chapter 6).
  - Clarifying the wider institutional framework for attracting and facilitating foreign workers' entry and assessing how best to perform the mandate of foreign talent attraction across government agencies. The know-how of the BOI as an effective agency could be replicated for such reform.
  - Continue streamlining the wider legal framework for the entry of foreign workers, with the ultimate, long-term objective to make BOI's SMART visa and related programmes obsolete as they are not part of the agency's core competencies. Available and transparent data on the stringency of migration policies could raise awareness and help concerned agencies advocate for policy change.
- Provide better statistics to support evidence-based investment promotion policy making. The BOI could develop a nomenclature for promoted activities that can be matched with product-level trade statistics. In addition, the agency, in co-operation with the National Statistical Office, could match the project-level data collected by the BOI with the establishment-level data of the Industrial Census of Thailand to assess more accurately the outcomes of the merit-based incentives on productivity, exports, R&D, skills development, and other outcomes.

## **Improving Thailand's foreign investment regime**

It has long been recognised that globalisation offers substantial opportunities for participating countries, but that it also requires an ability for rapid adjustment for them to benefit from these opportunities. Possibly no other region has grasped such opportunities as well as Southeast Asia. Thailand was among the first in the region to recognise the powerful role that foreign investors could play in fuelling export-led growth,





'servicification' of manufacturing activities is reflected in the increasingly significant share of services value added embedded in manufacturing value added. To achieve Thailand 4.0, the service sector will need to be further developed to match the profile of countries which have already achieved such a status. Services account for about 30% of the value added embedded in its manufacturing exports, which is only slightly below the OECD average, but only about half of it is domestically generated (the rest being imported), against about 90% in the case of OECD economies.

It is, therefore, timely for Thailand to reflect on its strategy towards developing such a high-end services and high-tech manufacturing economy. As with its export-oriented manufacturing strategy back in the 1990s, there are likely positive ways in which services FDI liberalisation could be helpful in this context. Although services tradability has increased over time with the rise of digital and communication technologies, they remain naturally more complex to trade than goods. Unlike trade in goods in which factors of production are built into the traded goods themselves, services typically require the actual relocation of capital and labour across borders, often through FDI.

Thailand's current FDI policy concerning services still shares similarities with its policy back in the early 1970s, with the exception of investment incentives (see previous section). Back then, faced with a backlash against growing foreign investment in Thailand, the government promulgated the Announcement of the Revolutionary Council No. 281 of 1972 (ARC 281), which was the first law explicitly governing FDI. The act introduced strict barriers to entry and operation of majority-foreign investors across all sectors, including manufacturing and services. The objective was overtly to protect indigenous Thai businesses given that Thai technology was not yet competitive, together with national security considerations in a few sectors.

In 1999, the law's incompatibility with attempts to promote foreign investment and international trade and the more open approach adopted in other countries gave rise to the Foreign Business Act of 1999 (FBA), still in force today. The FBA liberalised FDI in many sectors, mostly in manufacturing, but still kept most of the restrictions pertaining to services, notably foreign equity limitations in certain activities (such as media and transport) and the need for government approval for holding majority shareholding stakes in all but a few services activities. Apart from the FBA, the government exercises similar controls through sector-specific and other legislation, which prevail over the Act. Looking back, the liberalisation embodied in the FBA was circumscribed even in manufacturing where, unusually given the experience worldwide, it kept some restrictions as well. Compared to other economies in the region at the time, Thailand still maintained a relatively more open environment to FDI, but with almost no additional FDI liberalisation in Thailand since then. As a result, many other ASEAN Member States have now surpassed Thailand in openness.

The government is, nonetheless, currently considering pursuing further services FDI liberalisation. In 2019, the Foreign Business Commission reviewed the list of restrictive business categories under the FBA and identified four additional activities to be removed from the list, namely: i) Telecommunications business (type 1 licence) in accordance with the Telecommunications Business Act; ii) Treasury center in accordance with the Exchange Control Act; iii) Certain aircraft maintenance; iv) High value-added software development activities. Foreign investments in these activities would be dispensed from obtaining a foreign business licence under the FBA. The proposed changes are justified *inter alia* on the basis of the importance of such business categories for supporting the development of Thailand's 'New S-curve' digital industries (see Chapter 3 and 5), as well as on the need to reduce duplication of government oversight as these businesses are governed by specific laws. Another 18 business categories are proposed to remain restricted until further study is undertaken by the Foreign Business Commission. Proposed changes are not yet in force, awaiting needed ministerial regulations for becoming effective, but denote a welcoming step towards modernising Thailand's foreign investment regime.

### ***Exemption channels and legal loopholes enable foreign investment into restricted activities***

Although the law includes screening mechanisms and restrictions, some flexibility is offered to foreign investors through different exemption channels. Preferential treatment is accorded to foreign investors under bilateral treaties. Promoted investors under the Investment Promotion Act and the Industrial Estate Authority of Thailand Act can benefit from an exemption of certain restrictions enshrined in the FBA. Unofficially, some investors have also exploited legal loopholes, such as preferential shares and indirect ownership, to by-pass some of the restrictions in place

Hence, in practice, Thailand has been more open than a simple reading of the legislation would suggest. But remaining legal loopholes and inconsistencies are likely to impose an additional cost for investors and Thailand. In 2007, the Ministry of Commerce prepared a bill to amend the FBA to limit if not end existing legal loopholes, which would render the regime *de facto* more restrictive, but the proposed reform did not go forward in the face of opposition from investors.

### ***Objectives of the foreign investment regime should be re-assessed to prioritise reforms and reduce legal uncertainty for investors***

Considering all these issues, it seems timely and appropriate for Thailand to undertake an assessment of the impact of the FBA and remaining sectoral restrictions to FDI on the economy. For almost 50 years, various domestic services industries have to a great extent been insulated from foreign competition. Such an assessment would identify to what extent this policy has served its intended public purpose of enabling the development of vibrant local firms and capabilities, as well as activities or sectors that should be accessible for foreign competition. It is also suggested to assess the effect of this policy on other parts of the economy.

Thailand's inaction in correcting the FBA's legal loopholes, in spite of the above-mentioned attempts, may suggest a more lenient attitude from the authorities towards foreign investment over time. If this is the case, a reform bringing the regulatory regime in line with current practice would serve to reduce uncertainty and provide a signal to the business community that Thailand welcomes foreign investors. If, instead, there are strong arguments for maintaining restrictions in place, such as national security, then the government could reconsider addressing some of the legal loopholes that currently erode the FBA's original intent.

Moreover, FDI in Thailand is subject to a dual-track system of foreign entry into Thailand. Generally, investment in Thailand without incentive and promotion is governed by the FBA which applies screening and restrictions to FDI. On the other hand, the legal framework for attracting FDI in Thailand is based on the Investment Promotion Act (IPA) which encourages FDI in some restricted activities under the FBA. Under the Investment Promotion Act, the BOI is mandated to fulfil a *de facto* regulatory function involving eased restrictions on foreign shareholding, on top of its core investment promotion mandate (e.g. provision of tax incentives for promoted firms). Re-evaluating and reforming the FBA may also involve an opportunity to adjust the Investment Promotion Act and eventually liberate the BOI from its mandate to provide non-tax incentives to foreign investors and focus instead on core investment promotion activities (Chapter 5).

### ***Main policy options for consideration by the authorities***

The right of governments to favour some investors over others in order to achieve social, economic or environmental goals is widely accepted, but any policy that discriminates against one group of investors involves a cost. Discriminatory measures can thus only serve the broader public interest to the extent that their potential costs in terms of forgone investment and potential efficiency gains are compensated by broader social and economic benefits. For this reason, they need to be constantly re-evaluated to determine whether their original motivation remains valid, supported by an evaluation of the costs and

benefits, including an assessment of the proportionality of the measure to ensure they are not more restrictive than needed to address specific concerns.

*Short- and medium-term policy priorities:*

- Undertake a comprehensive regulatory impact assessment of existing restrictions on FDI and publish the results. Include an assessment of potential non-discriminatory measures that could achieve the same objectives as the FBA.
- Reform the institutional setting of the Foreign Business Commission in charge *inter alia* of annually reviewing and proposing amendments to the list of restricted activities for appreciation by the Minister, notably to include representatives of the Office of the Trade Competition Commission, civil society and academia, as well as from the Joint Foreign Chambers of Commerce of Thailand, and to make meeting records public available, as well as any documentation supporting deliberations relating to the regular review of the list of restricted activities in the FBA.
- Align the general minimum capital requirement for foreign investors to start a business in Thailand with capital requirements for domestic investors. The currently discriminatory minimum capital policy is particularly stringent for investors in less-capital intensive activities, including many high-value added services that could contribute to Thailand's 4.0 strategy. Worldwide, where minimum capital requirements still exist, they are rarely discriminatory – in 2012 only eight countries out of 98 assessed in the World Bank's Investing Across Borders imposed a discriminatory minimum capital requirement – and typically much lower than what is required from foreign investors in Thailand. This is the case even across economies with a level of income per capita much greater than that of Thailand.

*Long-term policy priorities:*

- Align the statutory regime with current practice where feasible in order to avoid unnecessary regulatory uncertainty, and clarify the scope of application of listed activities by indicating their standard industrial classification code under Thailand's Standard Industrial Classification, which conforms to the International Standard Industrial Classification (ISIC Rev 4).
  - The existence of exemption schemes and legal loopholes allowing foreign investors to by-pass some of the regulatory restrictions on FDI serves to attenuate Thailand's FDI restrictiveness *de facto*, but does not fully eliminate regulatory uncertainty for foreign investors.
  - The dual-track system implies that there two channels that foreign investors can choose: the approval process under the IPA or under the FBA. Foreign investors who have obtained a BOI Certificate under the IPA will be exempted from a Foreign Business Licence under the FBA, but they have to obtain a Foreign Business Certificate from the Department of Business Development, at the Ministry of Commerce, in order to operate their business in Thailand. In either case, it would be advisable to improve policy coherence to avoid unnecessary regulatory uncertainty. This is the case, for instance, with activities which are promoted under the IPA and at the same time restricted in the FBA, and with activities and sectors where the use of preferential shares and legal loopholes to circumvent restrictions has been largely tolerated.
- Further liberalise FDI restrictions particularly in services sectors to match levels of openness in other emerging economies and to foster greater convergence towards Thailand 4.0.
  - Many primary and services sectors remain partly off limits to foreign investors, potentially limiting economy-wide productivity gains.
  - Most restrictions date from the 1970s. They were introduced to shield Thai businesses from foreign competition until they were ready to compete on their own. There have been few changes to the regulatory environment since then.

- In the past, these policies may have served to discriminate against FDI, but in the current context of GVCs and the intensified 'servicification' of manufacturing activities, these measures also possibly discriminate against Thai manufacturing producers and consumers, who may have to pay relatively higher prices for needed quality-adjusted services inputs.

## Enhancing domestic investment protection and dispute settlement mechanisms

Rules that create restrictions on establishing and operating a business, principally under the Foreign Business Act 1999, are only one aspect of the broader legal framework that affects investment. Protections for property rights, contractual rights and other legal guarantees, combined with efficient enforcement and dispute resolution mechanisms, are equally important elements of this legal framework for all investors.

Thai law provides guarantees regarding protection from expropriation without compensation and non-discrimination for some, but not all, investors. A range of other treatment guarantees are provided for BOI promoted investors under the Investment Promotion Act 1977 (No. 4) (2017 revision), but these are only available to investors who hold a BOI promotion certificate. There is room for improvement in the levels of protection that investors can expect under Thai law when compared with international good practices. There may also be scope to consolidate the key protections, incentives and obligations for investors (including non-promoted investors) into a single law to improve accessibility. Unlike many of its ASEAN partners, Thailand does not have a single investment law, which means that these aspects of the legal regime affecting investors are scattered across a range of different laws.

Thailand has a well-established system for land rights that is generally upheld in practice, but the legislation governing land tenure still significantly restricts foreigners' rights to acquire land. The current land titling and registration system has undergone a substantial overhaul since the mid-1980s, with a number of important efficiency and technological advances. Some concerns persist regarding coordination between the various land administration authorities, deficient levels of smallholder rights and the level of electronically-available land records. For the most part, these challenges remain to be addressed. Ongoing efforts to computerise land titling information, especially in regional land offices, are encouraging in terms of their ability to improve the land record management system and reinforce the security of land titles.

### ***Recent reforms related to the protection of intellectual property rights and cybersecurity are key to enable investments into knowledge assets***

The government is stepping up its efforts to tackle two important areas for the government's vision of moving towards a value-based and innovation-driven economy – the protection of intellectual property (IP) rights and cybersecurity. Strong IP rights provide investors with an incentive to invest in R&D for innovative products and processes. The legal and institutional framework for protecting investors' IP rights has been strengthened in a number of respects in recent years as the government seeks to bring Thailand's IP regulations closer to international good practices and standards. The government is pursuing a range of different initiatives to address persistent concerns from investors regarding the effectiveness of IP enforcement measures.

Likewise, cybersecurity and data protection are of increasing concern for all investors in Thailand, not only digital and new technology firms that Thailand's 4.0 vision have placed at the forefront of the government's policy agenda. The government has recently gazetted two important new pieces of legislation in this area – the Cybersecurity Maintenance Act 2019 and the Personal Data Protection Act 2019. The implementation of these new regimes will be challenging in many respects and will no doubt be closely followed by investors.

## ***Dispute settlement mechanisms are improving in Thailand***

In terms of dispute resolution, the Thai courts have a reasonable record for rule of law and contract enforcement when compared to similar economies. The main concerns for investors interacting with the Thai court system relate to the speed and efficiency of case management and the availability of electronic court services, among others. The government has in recent years prioritised efforts to improve the legal framework and institutions for public integrity as part of a broader focus on public sector reforms aimed at improving the business environment. Alternative dispute resolution, primarily arbitration, is widely recognised and well-practiced in Thailand, which is generally considered to be an arbitration-friendly jurisdiction. The new Arbitration Act B.E. 2562 (2019), which amended the previous Arbitration Act to allow foreign arbitrators and lawyers to perform their duties in arbitral proceedings conducted in Thailand without having to obtain work permits, will contribute to the development of Bangkok as a regional hub for international arbitration in the near future.

## ***Policy considerations***

Thailand has made important reform strides in terms of its domestic legal framework to facilitate investments into knowledge assets; namely with respect IP protection and cyber security. The implementation of these efforts should be prioritised in the short-to-medium-term, while broader reforms to align investment protection into a single law and removing restrictions to land ownership for foreigners could be longer term priorities.

### *Short- medium-term policy priorities:*

- Continue to prioritise efforts to improve the effectiveness of intellectual property (IP) enforcement measures. Despite a relatively well-developed legal framework for IP rights protection in Thailand, investors continue to report relatively high levels of IP rights infringement, including through the widespread availability of counterfeited goods and unlicensed computer software. The government is already pursuing a range of different initiatives that seek to address these problems but further progress in the implementation of these initiatives may improve overall investor confidence.
- Maintain cybersecurity as a national policy priority. Investors will no doubt follow closely the government's implementation of the Cybersecurity Maintenance Act 2019, which came into force in May 2019, and the Personal Data Protection Act 2019, which is set to come into force in May 2020. All efforts should be made to ensure that these Acts are implemented in a manner that achieves a measurable impact on reducing cyber threats in Thailand and establishes an effective framework for data protection in line with international good practices.

### *Long-term policy priorities:*

- Evaluate possibilities for improving key investment protections under Thai law. Consolidating the key protections, incentives and obligations for investors (including non-promoted investors) into a single law may improve transparency and predictability of the legal framework by helping investors to navigate easily the rules that apply to investments in Thailand. This process might also provide an opportunity to bring the levels of protection from expropriation in line with international standards, codify a non-discrimination principle and consider the appropriate level of obligations placed on investors.
- Evaluate the costs and benefits of maintaining the current restrictions on land ownership for foreigners. While there are some ways for foreigners to acquire land under Thai law, including for the purposes of carrying out a promoted business under the BOI investment promotion regime, the overall effect of the Land Code 1954 is to place significant restrictions on the ability of foreign nationals to own land. Access to electronic information in English regarding land administration system and land tenure rights for foreigners could also be improved.

## Investment treaty policy in Thailand

Like many countries around the world, Thailand has taken on international obligations to grant foreign investors specific treatment in international investment agreements (referred to as investment treaties or IIAs). These international obligations in bilateral investment treaties (BITs) or investment chapters of trade and investment agreements have become part of Thailand's legal framework for investment protection. Investment treaties grant protections to treaty-covered investors in addition to and independently from protections afforded by domestic law to all investors. Domestic investors are generally not covered by treaties.

Investment treaties typically contain substantive protections for covered investments against expropriation or discrimination. Provisions requiring “fair and equitable treatment” (FET) are also common and have given rise to widely varying interpretations. While there are some significant recent exceptions, investment treaties also generally give covered investors access to investor-state dispute settlement (ISDS) mechanisms that allow them access to international arbitration to seek monetary compensation in cases where they claim that the host country has infringed these provisions. While domestic law does not typically provide compensation beyond narrowly-defined situations, such as cases of expropriation, compensation has been a common remedy for investors in ISDS cases.

Investment protection provided under investment treaties can play an important role in fostering a healthy regulatory climate for investment. Expropriation or discrimination by governments does occur. Government acceptance of legitimate constraints on policies can provide investors with greater certainty and predictability, lowering unwarranted risk and the cost of capital. Domestic judicial and administrative systems provide investors with one option for protecting themselves. Access to international arbitration under investment treaties gives substantial additional leverage to covered foreign investors in their dealings with host governments.

Investment treaties are frequently promoted as a method of attracting FDI and this is a goal for many governments. Despite many studies, however, it remains difficult to establish strong evidence of impact in this regard. Some studies suggest that treaties or instruments that reduce barriers and restrictions to foreign investments have more impact on FDI flows than BITs focused only on post-establishment protection. These assumptions continue to be investigated by a growing strand of empirical literature on the objectives of investment treaties and how well they are being achieved.

### ***Thailand's investment treaty policy deserves continued attention***

The current review of Thailand's investment treaties indicates that Thailand, like many other countries, has a significant number of older-style investment treaties with vague investment protections that may create unintended consequences. Where treaties set forth vague provisions, arbitrators deciding investment disputes have had wide discretion to interpret the scope of protection which has generated inconsistencies and uncertainty. Notably following early reactions in the context of ISDS cases under the North American Free Trade Agreement (NAFTA) in the early 2000s, many governments have substantially revised their investment treaty policies in recent years in response to increased public questioning about the appropriate balance between investment protection and sovereign rights to regulate in the public interest, the uncertain scope of many investment treaties and the costs and outcomes of ISDS. Experiences with the COVID-19 pandemic may shape how governments view key treaty provisions or interpretations and how they assess the appropriate balance in investment treaties.

The Thai government is well aware of these challenges. It plans to start the process of seeking to update existing older-style BITs with treaty partners once its new model BIT is released later in 2020. In the meantime, it is taking a leading role in multilateral discussions on ISDS reform that are developing in UNCITRAL's Working Group III. It has also established in 2019 the Committee on the Protection of International Investment to steer government policy on investment treaties and enhance policy coherence.

The government may wish to recall that regional and plurilateral trade and investment agreements involving ASEAN members offer an opportunity to create an integrated investment region in ASEAN and establish common approaches to investment protection, dispute settlement and liberalisation. At the same time, in the absence of active management of the replacement of treaties, this approach can lead to multiple investment-related agreements being concluded with the same treaty partners. This situation may jeopardise the consistent implementation of Thailand's investment treaty policies: claimants may be able to circumvent newer treaties or domestic legislation by invoking protections and ISDS provisions in older-style treaties that remain in force concurrently.

### ***Considerations for reform of investment treaty policies***

The discussion and recommendations below are intended to assist the government in reconsidering its investment treaty policies in light of the above challenges and recent developments in investment treaty policies around the world.

#### *Short- and medium-term policy priorities:*

- Conduct a gap analysis between Thailand's domestic laws and its obligations under investment treaties with respect to investment protections. There are differences between Thai law and Thailand's investment treaties in these areas. Overlapping legal regimes for investment protection may raise a number of policy concerns. Identifying and reviewing the impact of these differences may allow policymakers to ensure that these overlapping legal regimes are coherent and do not detract from the government's objectives with respect to investment protection. The newly-established Committee on the Protection of International Investment would appear to be the most obvious body to lead such a process given its steering role for investment treaty policy.
- Manage potential exposure under existing investment treaties proactively. The government should continue to develop ISDS dispute prevention and case management tools. The impact of the newly-established Committee on the Protection of International Investment – which has a centralising role in dispute prevention – should be monitored and measured so that it can be improved over time. The government should continue to participate actively in the work of UNCITRAL's Working Group III and other multilateral fora on these topics. Ongoing awareness-raising efforts for line agencies and treaty negotiators regarding Thailand's investment treaties and the significance of the obligations they contain for the day-to-day functions of government officials are commendable and should be continued on a regular basis. Developing written guidance manuals or handbooks for line agencies on these topics could encourage continuity of institutional knowledge as personnel changes occur over time.
- Continue to actively participate in and follow closely government and other action on investment treaty reforms including at the OECD's FOI Roundtable and at UNCITRAL. Many governments, including major capital exporters, have substantially revised their policies in recent years to protect policy space or to ensure that their investment treaties create desirable incentives. For example, the US and Canada recently agreed to terminate the NAFTA and will now provide only for state-state dispute settlement (SSDS) between them in the United States-Canada-Mexico Agreement (USMCA), which came into force on 1 July 2020, replacing NAFTA, rather than permitting direct investor claims for damages in ISDS. The EU has rejected investment arbitration in favour of a court-like model with government appointed adjudicators for ISDS. Consideration of reforms and policy discussions on frequently-invoked provisions such as FET are of particular importance in current investment treaty policy. Emerging issues such as the possible role for trade and investment treaties in fostering RBC as well as ongoing discussions about treaties and sustainable development also merit close attention and participation.

### *Longer-term policy priorities:*

- The government should continue to implement its plans to assess and where appropriate update its investment treaties to bring them in line with the government's current priorities. The government's experiences with the COVID-19 pandemic may shape how it views key treaty provisions or interpretations as well as the appropriate balance between investor protections and the right to regulate. Depending on the context and treaty language, it may be possible to achieve these goals through joint interpretations agreed with treaty partners. In other cases, treaty amendments may be required. Replacement of older investment treaties by consent may also be appropriate in some cases.

## **Promoting and enabling responsible business conduct**

Promoting and enabling RBC is of central interest to policy-makers wishing to attract and keep investment and ensure that business activity contributes to broader value creation and sustainable development. RBC expectations are prevalent throughout GVCs and refer to the expectation that all businesses – regardless of their legal status, size, ownership structure or sector – avoid and address negative consequences of their operations, while contributing to sustainable development where they operate. RBC is an entry point for any company that wishes to contribute to the SDGs or to achieve specific economic and sustainability outcomes.

The COVID-19 crisis has exposed significant vulnerabilities in company operations in global value chains, including as related to disaster preparedness and supply chain continuity and resilience. Evidence has already shown that companies that are responsible are better able to respond to COVID-19. An RBC lens can help them make more balanced decisions, while ensuring that they do not create further risks to people, planet and society – or contribute to further destabilising supply chains down the line. Promoting and enabling RBC as part of overall COVID-19 policy responses will be essential for ensuring coherence between their government recovery policies and their expectations of how businesses should contribute in this regard.

### ***Thailand is a regional leader on RBC***

Several initiatives have been implemented over the course of the last few years. Notably, in 2019, Thailand became the first country in Asia to adopt a standalone *National Action Plan on Business and Human Rights (2019-2022)* (NAP). The Thai NAP outlines four key priority areas, namely actions to address 1) labour; 2) community, land, natural resources and environment; 3) human rights defenders; and 4) cross-border investment and multinational enterprises. It also envisions an implementation plan and indicators for monitoring and evaluation. This is a significant achievement to promote RBC in Thailand and among Thai enterprises operating domestically and abroad (Chapter 9).

Thailand has also promoted RBC in other ways. For example, several stakeholders in Thailand promote sustainability and corporate social responsibility (CSR) awards. Additionally, the National Human Rights Commission of Thailand (NHRCT) has played a critical role by raising the visibility of the complaints received in the business and human rights field and by organising awareness raising events and workshops. The government has also taken steps to promote RBC among Thai state-owned enterprises (SOEs), with SOEs being directed to follow RBC standards and practices. There have also been sector or thematic policy commitments, such as in fishing where Thailand was the first country in Asia to ratify the ILO Work in Fishing Convention. The Securities and Exchange Commission (SEC) was an early champion of sustainability, notably connecting the topics of corporate governance, ESG, sustainability, and anti-corruption, in the Sustainability Development Roadmap which was adopted as part of the SEC Strategic



Plan 2013-2015. The SEC Strategic Plan 2020-2022 addresses the importance of sustainability as one of its five priorities.

RBC-related activities in Thailand have also been undertaken by the private sector and civil society. Businesses spearheaded the creation of the Thailand chapter of the UN Global Compact Network in 2016, which in 2019 counted 46 members. Businesses and business associations, including the Joint Steering Committee on Commerce, Industry, and Banking, Federation of Thai Industry, Thai Bankers' Association and Stock Exchange of Thailand organised awareness raising events and workshops to familiarise businesses with international standards on RBC and to engage in the process of developing the Thai NAP.

### ***Policy direction***

While the efforts by the Thai government to set RBC policy direction are commendable, the real test will be in implementation. It will be crucial that the gains are not lost in light of the COVID-19 crisis. Building on the support for the NAP and the swell of support for RBC, Thailand is in a unique position to promote bold and consistent implementation of RBC principles and standards across the economy.

#### *Short- and medium-term policy priorities*

- Support, enable and promote RBC due diligence among businesses throughout the economy. Explicitly promote broad dissemination and implementation of due diligence in accordance with the OECD *Due Diligence Guidance for RBC*, including efforts at the provincial level. The *Guidance* is a practical tool to implement the due diligence expectations as set out in the ILO, OECD and UN instruments, including the UN *Guiding Principles on Business and Human Rights*.
- Provide and communicate clear expectations to businesses on RBC standards for outward Thai investments in the services provided for investors, in collaboration with BOI, the Federation of Thai Industries and the Board of Trade, EXIM Thailand and the SEC. These services include organising overseas business visits, business seminars and dialogue with business associations of other countries. The information and expectations should also be integrated in BOI's Thailand Overseas Investment Centre and the Thai Overseas Investment Promotion Department (Chapter 11). Assess whether further alignment in risk management policies is necessary and whether specific due diligence requirements should be considered.
- Make RBC due diligence a standard operating procedure in the context of special economic zones and the EEC, including promoting transparency around selection of projects and the establishment and operations of zones, as well as meaningful stakeholder engagement with affected communities.
- Encourage and support implementation of RBC in the financial sector, including by promoting RBC due diligence in the operations of large institutional investors (such as the Social Security Fund), following the lead of the Thailand Government Pension Fund.

#### *Long-term policy priorities*

- Promote due diligence in the activities where the state is an economic actor. This includes procurement and activities of state-owned enterprises. Notably, due consideration should be given to how RBC expectations can be reflected in the implementation of the *Public Procurement and Supplies Management Act of 2017* and whether amendment is necessary. Additionally, the policy guidance for SOEs should be aligned with the 2015 OECD *Guidelines on Corporate Governance of State-Owned Enterprises*, and the specific expectation that SOEs establish and implement due diligence according to international standards should be made clear.
- Consider expanding the labour laws, regulations, and initiatives applied in the context of fisheries to other industrial sectors that have a large migrant worker population. Ensure that recent

protections for human rights defenders are implemented and consider whether further policy action is necessary. The role of non-judicial grievance mechanisms and alternatives means of dispute resolution should be considered.

## Prioritising the promotion of green investment to achieve broader ambitions

Green growth and green investment will be key to meeting the vision for Thailand 4.0, especially in the context of COVID-19 recovery. A green growth pathway allows Thailand to grow and develop while ensuring that natural assets continue to provide resources and environmental services for future generations, and that growth pathways remain resilient to global shocks such as climate change or future pandemics. A key step in pursuing green growth is to catalyse investment and innovation in environmentally sound technologies and infrastructure which helps to sustain growth gives rise to new economic opportunities and creates jobs. In addition, with the increasing need for global action to address climate change, investment for green growth must promote a rapid transition to a low-emissions and climate resilient development pathway. Investment for green growth includes, among other things, investment in infrastructure – such as renewable energy, energy efficiency, water purification and distribution systems, transport and housing – as well as in conservation and efficient usage of natural resources, and waste management.

A green investment framework has much in common with a general policy framework for investment, but an investment-friendly policy framework does not necessarily result in green investment unless certain elements are also in place. These include: a strong governmental commitment at both the national and international levels to support green growth and to mobilise private investment for green growth; policies and regulations to provide a level playing field for more environment friendly investments, including through pricing instruments; policies to encourage more responsible business conduct, including promoting environmental due diligence; an institutional capacity to design, implement and monitor policies to foster green growth objectives; and financial mechanisms for green investment.

### ***Thailand has a good policy framework for green growth***

Thailand's vision of transitioning into an innovation and technology driven economy, especially through its BCG economy model, will not be achievable without significant progress towards green growth. This is especially relevant in the context of post-COVID recovery, where Thailand must restart its economy and create local employment, while ensuring underlying growth drivers remain resilient to future shocks. The major gains made in growth and development in the last few decades were accompanied by the unsustainable and unchecked use of resources, which in turn has hampered the country's efforts to promote environmental sustainability. Rapid urbanisation, industrialisation and infrastructure development have exacerbated air and water pollution, with Bangkok recording hazardous levels of air pollution in the last two years. Thailand generates significant waste, and a lack of adequate waste management continues to result in plastics dumping and pollution in water bodies. Climate change exacerbates existing environmental issues, with Thailand highly vulnerable to changing temperature and rainfall patterns. Increasing greenhouse gas emissions from the use of fossil fuels will need to be checked.

Recognising these challenges, Thailand has made strides in developing a comprehensive and consistent policy framework for green growth and environment and in promoting green investment (Chapter 10). The BCG economic model puts green growth-related concepts at the heart of continued development. Green growth is reflected in Thailand's development strategies, and consistent climate mitigation targets are in place. Thailand's policy framework for environmental protection has a long history of implementation, and investment incentives have been put in place to promote investment in green sectors and activities. In the energy sector, Thailand is a regional success story in promoting private investment for renewable energy, and has used public finance strategically to mobilise commercial financing for green investments.

## ***Implementing and strengthening the policies on green growth is already a priority***

Key to this will be ensuring that environmental objectives are systematically integrated across Thailand's broader policy framework for investment, and misalignments in Thailand's policies need to be addressed. Some of the proposed action can be addressed unilaterally by relevant agencies (short- and medium-term priorities), while others require longer term and inter-ministerial coordination.

### *Short- and medium-term policy priorities:*

- Consider scaling down or phasing out investment incentives for 'non-green' activities such as the manufacturing of non-biodegradable plastics or generation of electricity using fossil fuels. Providing incentives to both green and non-green activities reduces the ultimate effectiveness of efforts to promote green investment. For example, gains made by promoting investment in green sectors, such as the manufacturing of biodegradable plastics or generation of renewable energy, are offset by promoting investment in non-biodegradable plastic packaging or coal-fired power. A possible first step could include a mapping of green and 'non-green' activities building on emerging taxonomies for green finance.
- Assess the applicability of creating targeted financing vehicles to mobilise financing for green investment beyond the energy sector, building on lessons learned from the Energy Efficiency Revolving Fund. Thailand has had success with using budget funds in specialised structures to encourage local banks to engage in green lending for energy, and such experience could be built on to promote green lending for waste, water, and transport projects.

### *Long-term policy priorities*

- Establish a legal system and framework for the application of Strategic Environmental Assessments and stakeholder consultations, so that environmental considerations can be systematically integrated along with social and economic issues in policy planning and decision making related to sectoral or geographical issues. This can also help avoid downstream conflict with local communities and other actors during the project impact assessment stage. When it comes to private sector involvement, require risk-based responsible business conduct due diligence according to international standards such as the *OECD Due Diligence Guidance for Responsible Business Conduct*.
- Consider introducing pricing instruments, such as an environmental or 'green' tax, to put a price on pollution and incentivise efforts to increase the efficiency of resource use. Such instruments are considered key to green growth policies globally, and help to shift producer and consumer behaviour towards more environmentally beneficial activities. These taxes are prevalent across most OECD countries, with environmental tax revenues estimated to represent, on average, 2% of GDP across OECD member countries. Thailand should also continue its efforts to develop other pricing instruments by scaling up recent pilots to establish an emissions trading system.
- Develop a roadmap to support greening of the national financial system, including the tracking and disclosure of ESG risks. Building on the new roadmap on sustainable capital markets, Thailand should continue to invest in building a cohesive framework, through its sustainable finance taskforce and working group, bringing together the financial sector, the insurance sector and listed companies, to encourage a more targeted performance on green finance and the SDGs. While efforts to establish a system for green bonds are beginning to pay off, a national standard or taxonomy, based on the ASEAN Green Bond Framework and national guidelines, could add further transparency for issuers and investors. Lessons can be learned from the EU Action Plan on Sustainable Finance which lays out a roadmap for greening EU's financial system, including a taxonomy, labelling for financial products and measures to increase the transparency of reporting. Another example is China's guidelines for establishing a national green finance system, which

includes a classification of eligible activities and promotes clear reporting of green credits, among other measures. OECD tools for responsible business conduct in the financial sector can be useful for these efforts.

## Developing and implementing a policy framework for outward investment

Outward investment has become an important pillar of Thailand's economy, as outward flows have surpassed inward flows in recent years. OFDI can increase Thailand's competitiveness and is central for long-term growth, GVC integration and sustainable development. Outward investments allow firms to grow by tapping into new and potentially larger markets abroad. Outward investors can improve competitiveness by shifting operations that are no longer competitive at home to neighbouring countries, for example due to rising labour costs, or remaining preferential import duty regimes for exporters from neighbouring CLMV countries which are no longer available for Thai exporters. Investors can also access technology and knowledge that may not be available in home markets and thereby contribute to the development of activities and industries targeted under Thailand 4.0. These positive effects benefit OFDI firms themselves, but benefits can also spill over onto the home economy more broadly. The positive impacts of OFDI on the home economy can positively contribute to the economic recovery in Thailand. The global economic crisis related to the COVID-19 pandemic is expected to cause Thai OFDI to fall in the short-run. As economic recovery is expected to begin at different paces in various economies, delayed OFDI projects may resume.

### ***Considerations to develop an OFDI policy framework for Thailand***

Public policies can play an important role in influencing firms' decisions to invest abroad. Governments can support FDI outflows both through dedicated OFDI support measures (e.g. loans and grants for outward investors, investment insurance as well as technical and information services) and, more implicitly, through wider policies that support economy's internationalisation (such as capital flow liberalisation and trade policy). Dedicated OFDI policies can reduce the costs and risks associated with investment projects, making venturing overseas more attractive. Dedicated OFDI policies that should be prioritised depend on the intended policy objective, as is the case for inward FDI.

In Thailand, several public institutions<sup>4</sup> are involved in OFDI related policies and OFDI is a strategic priority in Thailand's National Economic and Social Development Plan 2017-22 (Chapter 11). While Thailand's current institutional and policy setup is likely to enable further OFDI growth, a number of short-, medium- and longer term policy considerations can be made that would enable a strong and targeted OFDI policy framework better supporting Thailand's development ambitions.

#### *Short- and medium-term policy priorities:*

- Strengthen the OFDI policy framework through inter-agency coordination. Thailand has a comprehensive policy package on OFDI which ranges from (1) continued capital account liberalisation, (2) good coverage of investment treaties and double taxation agreements, (3) the availability of financial and insurance instruments to protect and incentivise investments, to (4) the provision of informational services and technical assistance for smaller firms intending to venture into foreign markets. OFDI's concrete contribution to strategic policy objectives under the 2017-22 plan and Thailand 4.0 is still not well defined and, in some cases, agencies have overlapping roles. An inter-agency committee, chaired by one or several state agencies, could be mandated to formulate strategic OFDI objectives, clarify roles and align reform priorities across government bodies. A clear and coordinated policy message is increasingly important in light of COVID-19 uncertainties.

- Conduct a comparative review of OFDI policy frameworks and governance in other relevant outward investing countries (such as Japan and Korea). Such a review would help define and prioritise OFDI policies in Thailand.
- Clarify policy approaches for two distinct sets of OFDI priorities in support of Thailand 4.0 ambitions. Thailand 4.0 aims to (1) enhance productivity and competitiveness of selected high-tech industries and (2) boost technological and innovation capacity, including in new industries. On the one hand, OFDI can support the relocation of labour-intensive, lower skill production stages to lower cost neighbouring countries (particularly CLMV). This liberates resources for higher value activities at home and enhances overall competitiveness of the investing firm. This type of OFDI has increased importantly in recent years. On the other hand, OFDI has a potential role in acquiring brands, knowledge as well as new technologies and innovation capacity. Acquisitions of high-value assets abroad are not yet picking up in Thailand. It is important to distinguish the two sets of OFDI priorities and then engage in the discussion and formulation on respective – and potentially varying – investment promotion activities.

#### *Long-term policy priorities:*

- Increase resources dedicated for OFDI information services and technical advice and align efforts across government and private actors. The assessment in Chapter 11 shows that Thai firms are sometimes not aware of public and private services providing assistance on OFDI projects. The BOI reports that their efforts remain limited due to resource constraints, including with respect to staff, and their role vis-à-vis other agencies such as the Department of Trade Promotion is not fully clear. OFDI information services and technical advice are revealed to be essential in Thailand's efforts to enhance OFDI and competitiveness. Providing up-to-date OFDI information will be particularly important as COVID-19 recovery policies are put in place to stimulate new investments. The government could consider expanding resource allocation with respect to these services while aligning efforts across government and private actors.
- Augment OFDI technical advice with services related to RBC supply chain due diligence. Under the OECD *Due Diligence Guidance for Responsible Business Conduct*, enterprises are subject to the same expectations with respect to RBC when operating in their home country or overseas. Capacity building and training on RBC supply chain due diligence could be introduced as part of information and technical advice services (Chapter 9).
- Design and implement a policy package dedicated to promoting OFDI in high-value assets in advanced economies, potentially including financial instruments. Thai firms are currently not investing much in foreign assets that could support their transition towards higher value added activities and facilitate the development of their domestic capabilities. Few firms are acquiring assets in technology, R&D or high value brands. Thailand's 2017-22 plan recognises the need to boost OFDI in such assets but does not clarify what policy instruments are dedicated to it. Various state institutions provide financial incentives (such as loans) and investment risk insurance. These incentives (and potentially even OFDI tax incentives which are currently not available in Thailand) could play an important role in promoting investments into high-value and high-risk assets. The government could use available policy instruments to develop a package of targeted support mechanisms and incentives dedicated specifically to OFDI in high-value assets. A pre-requisite for the success of such a policy package would be an assessment of the experience of peer and more developed OFDI investors, including in the OECD.

## Notes

<sup>1</sup> While this Review focuses on an enabling environment for investment, it does not specially discuss competition policy even if this policy area requires attention for reform and improving the business climate in Thailand. Recent OECD research examines competition policy in Thailand, with a particular focus on the logistics sector.

<sup>2</sup> With the creation of MHESI, STI has been replaced with Office of National Higher Education, Science, Research and Innovation Policy Council (NXPO).

<sup>3</sup> The MHESI combines higher education policy, previously under the Ministry of Education, with science and technology policy under the former Ministry of Science and Technology.

<sup>4</sup> The Bank of Thailand regulates capital outflows. The Ministry of Commerce is in charge of negotiating free trade agreements, the Ministry of Foreign Affairs is in charge of negotiating investment promotion and protection agreements (Chapter 7 and 8), and the Board of Investment (BOI) carries out OFDI promotion and facilitation policy. The BOI focuses on outward investment in ASEAN and other targeted countries, while the Department of International Trade Promotion (DITP) offers indirect support i.e. providing information through the Office of Commercial Affairs abroad. The Ministry of Finance (Revenue Department) has the authority to grant tax exemptions on dividends from offshore investments, while the Export-Import (EXIM) Bank of Thailand provides loans and foreign investment risk insurance.



## OECD Investment Policy Reviews

# THAILAND

Thailand has had a remarkable economic development trajectory over the past 60 years and foreign direct investment (FDI) has been pivotal in this success. Thailand was one of the first movers in opening up to manufacturing FDI and in establishing proactive investment promotion and facilitation policies. While challenges remain in some areas of responsible business conduct, there is strong political will to address them. Thailand aspires to become a high income economy by 2037 by upgrading to a value based green economy. Inward FDI will play a prominent role in achieving this goal but this requires a concerted effort to reform the investment climate to remain an attractive host to foreign investment and to benefit to the full extent from that investment. While the COVID-19 crisis might temporarily delay progress, the policy recommendations in this review draw attention to potential reform priorities to help Thailand fulfil its development ambitions aligned with the Sustainable Development Goals and to contribute to a more inclusive and sustainable recovery from the pandemic.

