UTILIZATION OF TARIFF ADVANTAGE FROM ASEAN-CHINA FREE TRADE AGREEMENT: THAI-LAO BORDER TRADE

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Abstract - China has distributed many apparel products to various ASEAN countries. Especially the Thai-Laos border market focused in this study is the destination forproduct distribution. China has used the tariff benefits from ACFTA as well, resulting in lower prices of apparel products in Thailand and Laos which affecting domestic entrepreneurs. Thai and Laotian entrepreneurs are also covered by the tax benefits of ACFTA in the import and export of apparel products, but not yet fully understand.This research aims to study the benefits of the ACFTA policy that affects the profitability of the apparel product seller of the Thai-Lao border market by collecting data from in-depth interviews from apparel products dealers at Tha Sadet Market, Nong Khai Province, Thailand and Khlua Din Market, Vientiane city, Laos PDR. Thisstudy uses a linear probability model (LPM) to analyze the utilization of tax benefits of ACFTA on the profitability of entrepreneurs. The study found that factors affecting the profitability of Thai dealerare shipping service and logistic cost of goods from China. In the part of Lao entrepreneurs,the study found that the tax benefits of ACFTA increase the profit opportunity of Lao entrepreneurs.

Index terms - Border trade, Thailand, Laos, ACFTA, Garment.

I. INTRODUCTION

The Thai-Laos cross-border trade has increased every year. And most products sold between the two sides of the border consist of products which manufactured domestically and imported from abroad. It is particularly interesting that imported goods from China come through major wholesale agents in Thailand and distribute to retailers around the country and neighboring countries.In 2018, the impact of the trade war between the United States and China Causing more clothing products from China to spill into Thailand and neighboring countries, especially Laos PDR.The United States has raised tariffs on textiles from China, but garments or clothing have not been hit yet. But it is likely that the United States to raise taxes on products from China whichaccounted for 267 billion US dollars. Usually, clothing products from China come through the border continuously.Unfortunately, these products do not have clear identification numbers and mostly came through by illegal way.

Only part of the goodshas entered the customary process.However, most importer do not declare or specify the tariff classification or accurately identify the actual quantity.The domestic operators are affected by imported products from Chinawhichsold at lower prices. And China also utilized tariff benefits from the ASEAN-China Free Trade Agreement (ACFTA), which result in the lower total operational cost of product sold in ASEAN countries than in other countries of the region.In addition to China's export of apparel products to Thailand and Laos, Thailand has also exported clothing and apparel to China as well. In 2018, value of Thailand exported clothing and apparel to China is 2,934 million THB. Most of the Thai garment products exported to China are top tier products with special functions including sports clothing andwomen's underwear.The Chinese prefer underwear from Thailand Because there are a variety of designs, styles and functions, good quality and inexpensive. But in the past year, it was found that in 2013, Thai entrepreneurs who export and import apparel products had a very low utilization of tariff advantage accounted for only 43.1%("OIE Pointing out the benefits of the FTA of the Thai industry," 2013). TDRI also surveyed the use of FTA rights of Thai entrepreneurs and found that the utilization is low, causing a loss of up to 1.9 billion THB("Not fully exercising FTA, losing 1.9 billion baht benefit," 2016).Resulting in a very high chance of wasting tax benefits which otherwisecould increase the advantage of exporting and importing products.

The researcher tries to answer the question that whether the operators who sell apparel products do not give priority oftaking advantage of tariffrelated measureor the government's trade policy does not affect the profitability of the entrepreneurs. The researcher therefore analyzed and comparedthe effect of tariff benefitsfrom the ACFTA that affects the profitability of traders of Thai garment manufacturers at Tha Sadet market, Nong Khai province and Khlua Din market, Vientiane province, Laos PDR.

Thispaper begins withintroduction follow by literature review which related to China-ASEAN trade relationship and the situation of Thai-Lao border trade. In the next sectionmaterial and method were discussed. The result was present and discussed.

Finally, the main finding of this research and suggestion were provided.

II. LITERATURE REVIEW

A. Background on Thailand border trade

Thailand's shift from import-substitution to export-orientation policies took place in the early 1970s(Sally, 2007)Trade-and-FDI liberalization has a dramatic effect on the landscape of the Thai economy, with manufacturing industries becoming the part of global markets. Merchandise trade accounts for about 100 percent of overall GDP(Sally, 2007). To keep pace with the globalization, not only export but also cross-border trades hasbecomesignificant instrument to drive economics of Thailand.

The border trade of Thailand combine four countries includes Cambodia, Lao PDR, Myanmar, and Malaysia. The Thailand's export includes not only commodities such as machine, electronic, fuel, and chemical but also labor.Evident of continuously rise of import and export value is shown in Figure 1.

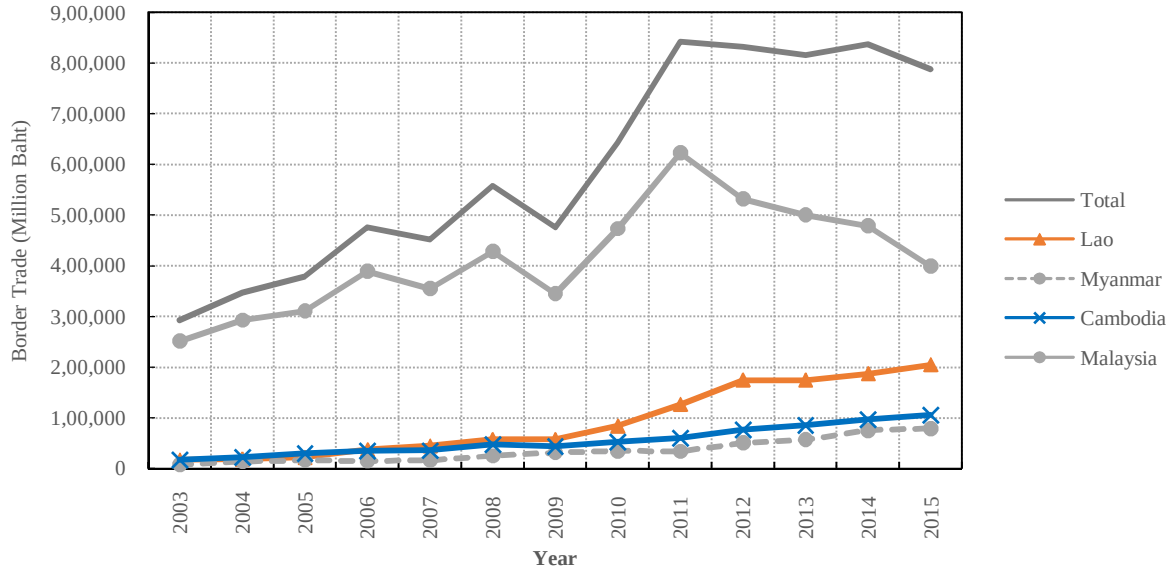

Figure 1 The trend of Thailand's border trade value, 2003 – 2015
Source: Bank of Thailand

The border trade along Thailand and Lao border was conduct through custom office in Nong Khai, Mukdahan, Ubon Ratchathani, Nakon Phanom, and Bueng Kan located in the north-eastern part of Thailand.In the border trade with Myanmar, the customs office in Kanchanaburi also operate the imports of natural gas. Other offices are situated in Tak in the west, Ranong in the south and Chiang Rai in the north. Border trade with Cambodia is conducted through the customs office in Sa Kaeo and Trat in the eastern part of Thailand.Finally, Border trade with Malaysia is conductedthrough the customs offices in the south such as Songkhla, Yala, Narathiwat and Satun.

It can be seen that the border trade value is continuously increasing. Until 2011 that trade across Malaysian border is decreasing. Interestingly, Takao (2008) pointed out that the border trade between Thailand and these four countries has been increasedat an even higher rate than the rate of increase of total trade between these countries.

B. Influence of China on Southeast Asia

The other aspect of Thailand's border trade is the influence of China in Southeast Asia.There is little doubt that China is rising to a prominent status in the Asia-Pacific region. The ways to cope with the ever increasing influence of China are, as suggest by Roy (2005), balancing or bandwagoning. The bandwagoning may be equate with economic operation suggest by the forming of organization such as ASEAN+3 (China, Japan and South Korea). This also explain China's successful campaign to establish economic presence in the region.

China outward economic expansion not only comes in the form of product export but also investment in host country's natural resources. As of 2009, there are at least 45 Chinese government and private sector funded hydro-electric power dams built in Southeast Asia (McDonald, Bosshard, & Brewer, 2009). Within this figure, 13 dams alone were built in Lao PDR with approximate gross power of 4900 MW.

C. Benefit of FTA on China and Southeast Asian Country

Initially, Thailand promotes trade with neighbor countries through policy such as Cross Border Transportation Agreement (CBTA)(Takao, 2008) which, to name a few, include single stop/single

window custom inspection; visas for person in transport operation; and agriculture and veterinary inspection, etc.

As from the comment in previous section, China and ASEAN are more competitive than complementary (Wong & Chan, 2003)because of their similarity in economics structure. However, if they take further step their trade collaboration would be more effective in the long term. Wong and Chan (2003) further suggested that FTA with ASEAN is one of the incenses to embrace strong relationship between China and the Southeast Asian countries.

III. MATERIAL AND METHOD

A. Qualitative Regression Model

Qualitative regression model is one of the regression modelswhich defines the value of the variable according to two values only that represents the probability of events that occur or does not occur in various cases(Gujarati & Porter, 2009). In this study, linear probability model (LPM) was chosen. The probability model is widely used because the results are easy to interpret, and the model is easy to use. Although this model is convenient for analysis, the main problem of this model is the problem of unstable variance of independent variables (Heteroskedasticity) and the problem of forecasting values that are greater than 1 and below 0 (Outside 0-1 range). The mentioned problems can be solved with the utilization of statistical package and careful attention ofthe user (Gujarati & Porter, 2009; Heckman & Snyder Jr, 1996). Despite the problems, in practice, the linear probability model is still widely used to describe various events in various disciplines, such as estimation of preferences for legislators (Heckman & Snyder Jr, 1996), estimation of alternative travelling choice(Stopher, 1969) and medical applications(Stopher, 1969).The linear probability model based on the parameter estimation with the ordinary least squares method (OLS) is shown in equation,

$$Y_i = \beta_0 + \beta_1 X_i + u_i \quad \ldots (1)$$

As with the general regression analysis model, the suitability of the model in practice is determined by the F-test, the measurement of non-constant variance of independent variablesand the ratio of the predictedprobability value. R-squared cannot be used for consideration because the characteristics of the estimation obtained is quite parallelto the x-axis, so the R-squared values do not reflect the reality.

B. Data used in this study

In this study, the performance data of apparel business owners was collected in 2 areasfrom both Thai and Lao border: Tha Sadet Market, Nong Khai Province, and Khlua Din Market, Vientiane respectively.The data were collected using purposive sampling and in-depth interviews with questionnaire. Data collection was conducted from October 2017 to March 2018.It was found that the sample group at Tha Sadet market was mostly female, with an average age of 46 years of primary school education. The operation period is between 1 - 7 years, type of business classified as a retailer.While the sample group at Khlua Din market is mostly female, with an average age of 35 years and diploma level education. The operation period is also 1 - 7 years and has a business classified as retailer and wholesaler as shown in Table 2.

Table 2 Characteristics of the sample

	Nong-Khai				Laos			
	Frequency	Percentile	Mean	S.D.	Frequency	Percentile	Mean	S.D.
Gender								
Male	6	25			14	46.7		
Female	18	75			16	53.3		
Age			46.21	11.31			34.50	6.55
Education								
Primary Education	9	37.5			1	3.3		
Secondary Education	8	33.3			6	20		
High Vocational	3	12.5			15	50		
Undergraduate	3	12.5			8	26.7		
Graduate	1	4.2			-	-		
Opening Period [Year]								
1 - 7	10	47.7			27	90		
8 - 13	7	29.2			3	10		
14 - 18	3	12.5			-	-		
19 - 24	3	12.5			-	-		
25 - 30	1	4.2			-	-		
Business Types								
Retail	14	58.3			7	20.7		
Whole Sale	1	4.2			1	3.4		
Mixed	9	37.5			22	75.9		

Note: Calculated by author

C. Methodology

To study the impact of importing products from China under the influece of the tariff benefits from the ASEAN-China Free Trade Agreement (ACFTA) on the profitability of Thai-Lao border trade enterprises. In this study, the researcher selected the linear probability model. The variables used in the forecasting consist of the following variables: the profitability of the traderin 2018 (Profit).The independent variable is the rate of change in sales (Sale),the use of tariff benefits from the ASEAN-China Free Trade Agreement (ACFTA), suppliers of apparel products (Material Source), product cost (Production Cost), logistics cost (Logistic Cost),the variety of products (Various Goods), and wheter or not the suppliers have providing free shipping services (Shipping Service). The variables used in the forecasting were summarized in Table 3.

Table 3 Variables Description

Variable	Description
Profit	Profit change "increase = 1"
Sale	Sale change "increase = 1"
ACFTA	The effect of free trade area.
Material Source	Source "China = 1"
Product Cost	Cost of producing
Logistic Cost	Cost of transportation
Various Goods	China material seller options "many kinds of goods = 1"
Shipping Service	China material seller options "free shipping = 1"

The researcher has set the model for two case studies as follows:

1) The tariff utilization model from ACFTA that affects the profitability of border trade operators that import apparel products from China, case studies of Tha Sadet Market:

$$\delta_i = f[\phi_i', \lambda_i] + \nu_i \quad \ldots (2)$$

When δ_i is the change of the result of the operation (Profit), $\phi_i'$is the set of members of the independent variable in the model, λ_i is the parameter value obtained from the estimation, and ν_i is the error value in the model.

2) The tariff utilization model from ACFTA that affects the profitability of border trade operators that import apparel products from China, a case study of Khlua Din market:

$$\omega_i = f[\theta_i', \beta_i] + \varepsilon_i \quad \ldots (3)$$

When ω_i is the change of the result of the operation (Profit), $\theta_i'$is the set of members of the independent variable in the model, β_i is the parameter value obtained from the estimation, and ε_i is the error value in the model.

Both models need to be verified for the variance of unstable variables (Heteroskedasticity) by the White's method under the hypothesis as follows:

H_o:Homoskedasticity … (4)

H_a:Heteroskedasticity … (5)

Table 4 Regression Output

	Nong-Khai			Laos		
	Coefficient		Std. Err.	Coefficient		Std. Err.
Constant	0.4127		0.3206	0.5668		0.6275
Sale	0.3801	***	0.0903	0.2415	***	0.1206
ACFTA	0.0540		0.0736	0.2768	**	0.1206
Material Source	0.2345		0.1759	-0.1052		0.2505
Product Cost	0.0407		0.0924	-0.2661		0.1732
Logistic Cost	-0.2028	**	0.0876	-0.0950		0.1161
Various Goods	-0.0489		0.1687	-0.4087		0.3482
Shipping Service	0.6006	**	0.2948	-0.3243		0.4840
F-test	4.76	***		4.76	***	
R-Squared	0.6623			0.6023		
Adj R-Squared	0.5232			0.4758		
Root MSE	0.3287			0.4078		
White's TestChi-sq [df]	25 [23]			30 [20]		
Outline Prediction	5			6		
Observations	25			30		

Note:*, **, * denote to statistically significant at 0.1, 0.05, 0.01**

IV. RESULTS

Result obtained from regression model is shown in Table 4.

From the regression model, it is found that all variables used to describe the changes in the profit are appropriate considered the F-test which has statistically significant results. That is, every independent variable in the model can describe meaningful changes in performance. The square root of the error is low. The testfor unstable variance of independent variables yieldnonsignificant results,

thereforethe evaluated model can be considered appropriate.

Model 1,case study of Tha Sadet market, showed that when sales increased by 1 unit, resulted in 38.01 percent opportunity to increase the profit. Contrary, the increase in 1 unit of transportation cost resulted in the 20.28 percent opportunity to decrease the profit. In case of suppliers of goods from China that deliver the products with no additional charge will resulted in an opportunity for entrepreneurs to increase profit by 60.06 percent compared with the low-price strategywith statistical significance at the level of 0.05.But the ability to explain the changes in profitability of entrepreneurs towards the use of tariff advantage from the ACFTA is not statistically significant.

Model 2,case study of Khlua Din market found that when sales increased by 1 unit, resulted in24.15 percent opportunity to increase the profit. and an impact from ACFTAresulted in a 27.68 percent opportunity for entrepreneurs to increase profit with a statistically significant level of 0.05.

CONCLUSIONS

The sales of a border trade market between Thai and Lao apparel productsentrepreneurs in Tha Sadet market, Nong Khai province and Khlua Din market, Vientiane City is worth up to 15 - 20 million baht per year and has an average sales value of 500,000-1,000,000 baht per year.This market in particular,is the target of China in the development of trade system and wholesale destination of many types of apparel products.The sale strategy includes selling cheap products and the transportation of goods straight to the hands of the operators.The Chinese operator is responsible for all transportation cost which is a strategy to increase purchase orders for Chinese apparel products from Thai-Lao border trade entrepreneurs.In Thai trader's point of view, China provisionof free transportation services for Thai entrepreneurs is considered to beanopportunity to make more profit. Which is different from Lao entrepreneurs who view the use of the tax benefits of ACFTA as a main channeltoincrease profit. The research results are consistent with the results of the survey on the use of the FTA tax benefits of Thai entrepreneurs.

Less than 50% of operatorin both import and export sector take advantage of tariff benefit ("OIE Pointing out the benefits of the FTA of the Thai industry," 2013).But in 2018, various industries of Thailand have increasedthe utilization of tariff benefits under the FTA which worth up to 69,602.11 million USD, increased by 14.76 percent from 2017("Thai FTA and GSP rights in 2018 surpassed the target of nearly 8 billion US dollars.," 2018).But mostly is a large industry who want to use tax benefits to increase their ability to compete in cost and product prices. Which can be said that Thai border trade operators are still small entrepreneurs and have a low level of education, which were not fully understand the process of applying for such benefit. Including not giving priority to the use of such benefits in order to increase the opportunity to increase the return of the business.Consider the competitive situation and the ability of Thai entrepreneurs to easily access the product source due to the variety of supplier contact channels and many types of apparel products produced domesticallyas well as the Chinese trade strategy, it clearly points out that the entrepreneurs feel that the need to use privileges from the FTA is not necessary. In contrast to the Lao entrepreneurs who have small production of apparel in the country and most of them must be imported from abroad especially China.Transportation of goods must be carried across the border from Thailand or from Vietnam causing a large amount of customs duties to be paid. Therefore, the border trade operators of Laos are paying more attention to the benefits of customs tax benefits. Which is consistent with the research results in increasing the profit opportunity of entrepreneurs if the tax benefits of ACFTA are increased.

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