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Free Trade with Thailand - A New Threat for Michigan?

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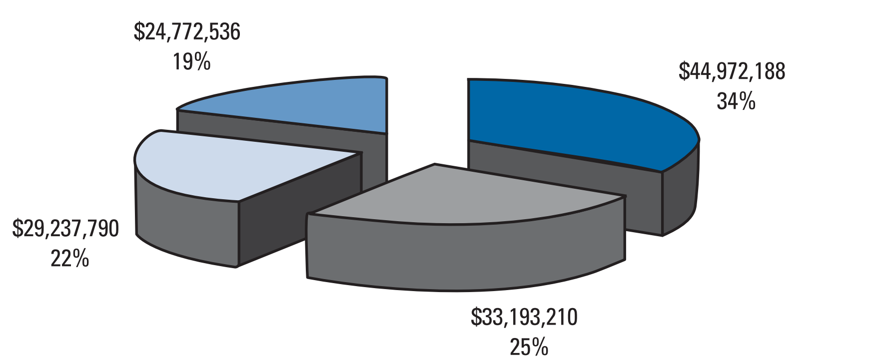
In 2003, President Bush announced that the U.S. would enter into trade negotiations with Thailand for a possible U.S.-Thailand Free Trade Agreement (UST-FTA). This is part of the President's desire to develop closer economic ties with the 10 ASEAN countries (Association of Southeast Asian Nations). The fifth round of negotiations for this FTA was completed in September 2005. The U.S. trade representatives hope to finalize the details of the agreement in early 2006, after which it would need to go to Congress to be ratified.

At first look, a trade agreement with Thailand would seem to be of little consequence for the U.S., as Thailand is only our 16th largest importer and 23rd largest export market. Thailand might seem similarly inconsequential for Michigan — Thailand accounts for only $132 million of state exports in 2004, making it our 25th largest export market (out of total Michigan exports of $36 *billion*). Of Michigan's exports to Thailand, 80% are chemical manufactures, transportation equipment, and machinery.

For Thailand, the benefits of an FTA with the U.S. seem more obvious. The U.S. is the top destination for Thai exports, its third largest importer, and its second largest foreign investor. The U.S. Embassy in Bangkok estimates that the total present value of U.S. investments in Thailand is over $21 billion, and U.S. Foreign Direct Investment in Thailand in 2004 totaled $112 million. U.S. investments in Thailand are concentrated in the petrochemical, finance, automobile, and electronics industries.

Michigan Exports to Thailand, 2004



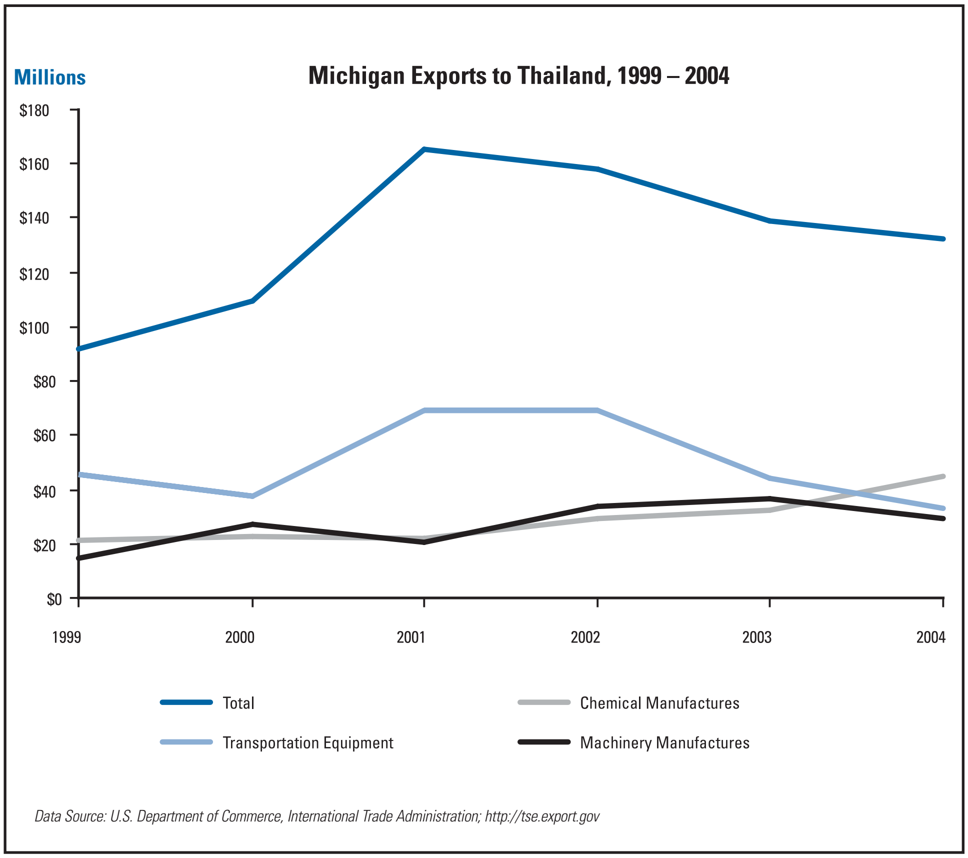
Data Source: U.S. Department of Commerce, International Trade Administration; http://tse.export.gov

The consequences of such an FTA for the U.S., and particularly Michigan, are much more striking when you hear the nickname that some give to Thailand — *The Detroit of Asia*. Over the last decade, Thailand has grown to become a large regional, and indeed global, automobile manufacturer. Thailand is the world's second largest producer of pick-up trucks. All of the light pick-ups manufactured in Asia by Toyota, Isuzu, and Mitsubishi, are made in Thailand. And although the dominant market share is from Japanese manufacturers (there are no purely Thai auto companies), Thailand's auto industry is not monopolized by Japan. U.S. auto manufacturers have invested heavily in Thailand. The first auto assembly company in Thailand was a joint venture between Ford and Britain's Inchcape Group back in 1961. Ford and Mazda have developed a $1 billion joint venture in Thailand during the last decade, and General Motor's Thai subsidiary (GM-Thailand) was the first manufacturer to export Thai-made vehicles to Japan.

To date, the automotive trade between Thailand and the U.S. has been relatively small — U.S. exports of motor vehicles and parts to Thailand amounted to less than $102 million in 2004, while U.S. imports of auto parts from Thailand in 2004 were just over $318 million. (The volume of U.S. imports of motor vehicles from Thailand is so low — less than $20,000 in 2004 — that it's not shown in the accompanying chart.)

The looming problem for Detroit is that the U.S. has a 25% tariff on imported pick-up trucks. Because the FTA has not been finalized, we don't yet know the specifics for auto trade with Thailand (although agreements like NAFTA and CAFTA have "free trade" in their title, there are usually some products for which trade barriers remain). However, this import tariff was eliminated/phased out under NAFTA, CAFTA, and the U.S.-Australia Free Trade Agreement, so it is likely that the tariff will be reduced, if not eliminated, if a UST-FTA goes through.

There is some good news though, because Thailand is also the world's second largest consumer of pick-up trucks. About 60% of new vehicle sales in Thailand are pick-up trucks, with more than 72% of these sales coming from Isuzu and Toyota. Additionally, Thailand's current tariff on imported passenger vehicles is 80% (40–60% for commercial vehicles). Reduction/removal of these tariffs under the FTA would be beneficial for U.S. automakers and parts manufacturers.



The impact of a UST-FTA on Delphi and other auto parts manufacturers is a double-edged sword. The opening up of Thailand's large auto market is a potential boon for sales to manufacturers and consumers there, but there will also be increased competition in the U.S. from Thai parts suppliers.

With the continued concern about Michigan's economy in general, and the auto industry in particular, it might be tempting to oppose the passage of a UST-FTA, but we should tread that path carefully. In the last few years, Thailand has entered into trade agreements of varying scopes with China, India, and Australia. An FTA between Thailand and Japan that will reduce trade barriers in their auto industries over the next few years is being finalized. This will be bad news for the U.S. auto companies with operations in Thailand, as it will put them at a competitive disadvantage with their already dominant Japanese rivals. The UST-FTA could help redress this imbalance.

If the U.S. and Thai auto markets are liberalized by the UST-FTA, the impact on the U.S. auto industry could be extensive. This doesn't necessarily mean that the auto manufacturing companies themselves will suffer—we could experience a substantial volume of imports of Thai-made trucks coming from the Thailand subsidiaries of Ford, GM, and the Japanese companies that also have operations here in the U.S. This switching of production from the Midwest to Thailand would be an additional blow to American workers in these companies.

It's also likely that the above impact would not instantaneously follow the passing of a UST-FTA into law. The U.S. and Thai auto tariffs would probably not be removed immediately—tariffs on U.S. autos and auto parts are being phased out over five years under CAFTA, and a similar (or even longer) phase-out period is to be expected with Thailand. This would give manufacturers time to make adaptations to their current models to reflect different tastes as well as different safety and emissions standards.