Chapter 14

State intervention, linkage formation and supplier development in Thailand

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It is generally believed that shifts in global corporate strategies - concentration on core competencies and a process of vertical disintegration - have created new opportunities for independent domestic suppliers in developing countries. Managers of foreign owned plant in developing countries show an increasing willingness to expand 'local sourcing' of inputs and enter into tighter relationships with domestic SMEs in a range of low-tech processes where labour costs are crucial or in mid-tech items where transport costs are important. Conversely, the same processes have also produced new challenges for local suppliers (cf. Chapter 4).

TNCs are in the process of modernising their supplier base and of reducing the number of suppliers on which they depend. They now buy from the most competitive suppliers on a world-wide basis and often induce their established home-based or global suppliers to follow them to new locations. As a consequence, local suppliers[109] in developing countries compete against both overseas suppliers and global suppliers that have invested in the country in question. The previous lower domestic market supplier standards are being replaced by international standards, putting a strong pressure on domestic suppliers of parts and components to approach the new standards of price, quality and timely delivery. If the local SMEs does not move fast in the upgrading direction or if the barriers of entry are insurmountable such suppliers will be replaced by imports or by the global in-place suppliers mentioned above.[110]

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[109] Here and in the following the terms local enterprises and domestic suppliers refer to enterprises that are owned or controlled by host-country nationals (Thais).

[110] In the latter case, backward linkages may of course be formed between transnational first-tier suppliers and domestic suppliers at the second- and third-tier levels.

Under pressure from these challenges, host governments in developing countries were forced to reconsider and to adjust their policy portfolio to this new reality. In principle, policy interventions may be able influence technology and other spillovers from TNCs through backward linkages in three ways. They may do that by attracting more foreign investment, by ensuring an appropriate selection of TNC investments, and by assisting development of local capabilities and absorptive capacities so that the local firms can take advantage of the links with foreign investors (cf. chapter 4).

By mid-1990s, Thailand was presented as the Fifth Tiger in Asia. The country had recorded rapid and sustained growth rates, it had diversified both its agriculture and industrial sector, and it had the fastest growing export of manufactures among Asian economies during 1985-96. At the same time, there was increasing concerns about whether it was a sustainable pattern of industrialisation and in particular whether the new fairly import-dependent TNC-driven export industries actually contributed to the long-term competitiveness of Thailand. This led in turn to the formulation of TNC linkage policies as well as a set of broader SME- and supplier development policies to supplement the unfolding liberalisation of trade- and investment policies. The present chapter is concerned with the extent to which the Thai government were able to formulate and in particular implement a credible and adequate set of linkage- and supplier development policies during the 1991-2001 period.

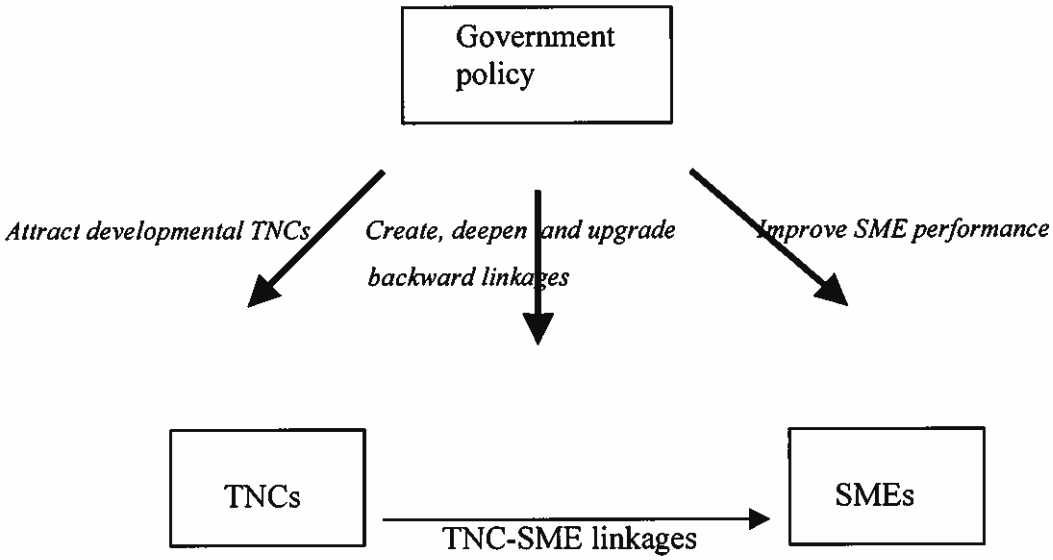
The following section discusses the role of as well as the types of linkage- and supplier development policies. The third section deals with design and implementation of various linkage development policies in Thailand. The following section studies supplier development through SME policies during the same period. The fifth section looks at supplier development through industrial restructuring programmes and new sectoral institutes. The concluding section addresses state capacity and policy orientation.

It is generally argued that the Thai governments failed to implement a credible and adequate set of linkage- and supplier development policies, and that it thereby missed an early opportunity of supporting upgrading among Thai owned parts producers. The reason for that had to due with policy design, meagre high-level political support, inter-ministerial rivalry, bureaucratic fragmentation and weak institutionalised public-private sector links.

Linkage and supplier development policies

Linkage and supplier policies are policies that aim at promoting the creation of new backwards linkages as well as deepening and upgrading existing linkages with the ultimate aim of upgrading the capabilities of local suppliers (UNCTAD 2001). They consist in fostering and supporting dense networks of suppliers who can reliably deliver high-quality, low-cost parts and components. By doing this they can 'deepen' formerly import-intensive ISI-assembly industries as well 'deepen' import-intensive EOI-assembly industries. Such policies must also address information- and co-ordination problems, because it is not obvious that individual assembly companies (often TNC subsidiaries or joint ventures) necessarily are concerned with establishing and developing a local supporting industry.

Figure 1 Linkage and supplier development policy - the linkage triangle.



Source: Adapted from Altenburg 2000, 33

Linkage and supplier development policies combine and expand to related policy fields – FDI promotion policies and SME development policies – and can be presented as a 'linkage triangle' consisting of willing TNCs, capable SMEs and government policies directed at TNCs, SMEs and the linkages between them (Altenburg 2000). First, a country needs to attract foreign investors and in particular investors that have a large linkage potential - and/or it needs to upgrade existing TNC

activities so that they are more conducive to developmental linkage formation. Second, policies should aim at expanding the local supplier base by preparing them for partnerships and by supporting potential domestic supplier firms in such areas as technology upgrading, training and financing so that they can exploit such partnerships to their own advantage. Third, policies can enhance linkages and support technology transfer from affiliates to local suppliers.

When policy makers do not just leave the creation of linkages to private initiatives and the market forces, they can develop specific linkage policies by re-lying on 'harder' command and control measures or by utilising 'softer' policy instruments giving particular incentives or promoting co-operation efforts. The traditional linkage policies were mostly of the former kind. Many developing countries used high tariffs on imports on parts and components and imposed local content requirements on foreign affiliates with the aim of expanding local procurement and strengthening domestic supplier industries. However, these measures did not necessarily promote local procurement because foreign affiliates may also choose to produce them in-house or source them from foreign suppliers located in the host country. More important, due to trade liberalisation, more liberal investment rules and the restrictions on the trade-related investment measures (TRIMs) such measures have lost importance (Battat et al 1996, 13-15; UNCTAD 2001, 167-71).

As backward linkages no longer can be forced upon TNCs and because they increasingly show an interest in expanding their local sourcing, softer policy instruments have taken over. Promotion of co-operation is an often-used policy instrument. Many countries have introduced information provision and match-making services, in which the former consist of various kinds of data banks, listing potential partners for subcontracting, while the latter goes a step further organising seminars, factory visits and follow-up initiatives. Such matchmaking services are conducted either by public officials or consultants from private firms/private associations (for details see the overview in UNCTAD 2001, 174-175). Moreover, there is a range of policy measures that rest on economic incentives for foreign affiliates.[111]

[111] For at listning of the various policy measures (with country examples), see Meyanathan and Munter 1994, 7-9 and UNCTAD 2001, 207-208.

The specific linkage policies can be divided into types (UNCTAD 2001, Battat et al 1996). One is general policies that help domestic firms to link up with foreign affiliates and which support local (would-be) suppliers in improving their technological and managerial capabilities. Another type of policy is linkage promotion programmes that may be organised at the national level or at the sub-national level (sometimes as cluster programmes). These policies are more pro-active. They typically focus on a limited range of industries and firms - making selective use of scarce public resources. They work closely with the selected foreign enterprises to identify supplier requirement and diagnose supplier capabilities just as they may invite foreign affiliate to participate actively in tailor-made provision of technical and managerial support. Both types of specific linkage policies draw upon information and matchmaking measures to create linkages and strengthen existing linkages in the areas of technology upgrading, training and financial support.[112]

From the deliberations above, it should be clear that design and implementation of coherent linkage- and supplier development policies is not an easy matter. First, such policies have to take into account the broader development strategies, the economic environment and the institutional setting in the country. Second, in order to be effective they must be built upon a vision of supplier development through backward linkages and this vision must be based on a strong political commitment and be shared among all stakeholders in 'the linkage triangle'. Third, it is important that programming is done in a co-ordinated manner and that the needs of the domestic suppliers are carefully thought out. When more ministries and agencies are involved contradictory initiatives arise, just as functional duplication and conflicting lines of authority often result in 'blocking', inconsistency in implementation or 'side-tracking' during the process of implementation. For that reason and because a range of intermediate supporting institutions are involved there will thus be a strong call for co-ordination both at the level of programming ('a joint promotion strategy') and at the level of actual service delivery. Furthermore, policy failure tends to prevail if weak, low-status agencies staffed with a few, poorly paid and inexperienced officials are responsible for the actual implementation. Finally, in relation to policy impact, it should be noted that even a well-designed

[112] Furthermore, linkage policies cannot be confined to the extent or density of supplier relation policies but must also to take into account the issue of asymmetry, stratification and power.

and well-implemented policy and institutional framework might not have the expected impact. A global downturn, new modes of organisation of the TNC or better investment opportunities and cheaper suppliers elsewhere may work against linkage formation.

In the following, we are concerned with linkage and supplier development policies in Thailand. During the 1990s, the Thai authorities have launched several such policy schemes.

Linkage development policy during the 1990s

During the pre-1987 period, import protection and investment promotion were the main industrial policy instruments utilised in order to stimulate local investments as well as to attract foreign investments. Both policies favoured large enterprises that also became attractive partners to incoming foreign investors. In contrast, the Thai government did not manage to develop an effective policy of supporting small-scale producers in the industrial sector through subsidised credits and appropriate advisory services. Consequently, the industrial structure became relatively biased towards final product industries, and Thailand ended up with under-representation of medium-sized part producers and equipment producers in the industrial structure. This pattern was somehow modified by in particular local content requirements (LCRs). They were imposed by the Board of Investment (BoI) as part of investment promotion packages by the Ministry of Industry (MoI) in selected industries. The most prominent being the automobile industry where they were instrumental in supporting a local auto parts industry linked to foreign assemblers (cf. chapter 13).

From 1987 and onwards, Thailand experienced an economic growth boom that to a considerable extent was linked to exceptionally high growth rates in manufacturing export. These did to a considerable extent reflect a boom in incoming foreign investments to Southeast Asia during the post-Plaza Accord years. The 1987-95-export boom concealed the missing linkages to local Thai enterprises and import-dependent nature of this mode of industrialisation. According to the calculations of Karel Jansen, the increase in Thailand's import/GDP ratio was mainly due to a rapid rise in the import-dependency. In turn, this was probably a result of the growing role of FDI, partly because it led to expansion in more import intensive sectors and partly because more imported inputs were utilised in production to export markets compared to production for the domestic market (Jansen 1997, 179-181). Comparing 1998 with 1985, Tambunlertchai found that local

content ratio had increased in the automobile industry, while he observed that the electronics goods industry relied on imported components and was characterised by 'very low backward linkages' (Tambunlertchai 2002, 99-100).

Around 1990, foreign donors and local bureaucrats became increasingly concerned about the hollow nature of Thailand's industry. This led to formulation of a set of linkage- and supplier development policies that came into being during a period in which processes of financial, investment and trade liberalisation were also initiated.

The Board of Investment (BoI) drove linkage policy. BoI had generally relied on a relatively passive and liberal approach to investment promotion. Thailand had a welcoming FDI regime and when targeting was on the agenda, the focus had been on either exporting or decentralised geographical location, while linkages, skill upgrading and technological development played a marginal, if any, role in actual implementation of BoI incentives. When industrial linkages were taken up the focus was therefore less on attracting 'developmental enterprises' that could crowd-in local firms, and more on expanding backward linkages from existing TNCs and through this facilitate technology transfer and skill development in supplier industries.

In 1991, BoI launched a specific industrial linkage development programme – *the BoI Unit for Industrial Linkage Development (BUILD).* The main objectives of the BUILD programme were: to encourage the development of supporting industries and promote the deepening of Thailand's industrial structure; to strengthen linkages between final product producers and companies producing components and parts or supplying technical services; to assist small and medium supplier companies in improving efficiency, productivity, and quality; to foster co-operation between foreign investors, Thai supplier manufacturers, and related government agencies; and to remove impediments to subcontracting and improve backwards linkages (BoI July 1994).

In the actual implementation, the scope of the programme was almost limited to match-making and information provision. The work was subcontracted to local research institutes and consulting firms. During the first phase the activities focused on electronics, automotive parts and metal-working and machinery industries. The main activities were development of an information base to support matchmaking in the form of ten investments opportunity studies inside the three

industries and a database of suppliers as well as principals; dissemination of information, arrangement of regional seminars with potential suppliers and principals and upgrading of suppliers through seven training courses (in production management, ISO 9000, inventory management etc.). Then followed a pro-active phase (starting September 1993) with matchmaking undertaken by a consulting firm, "SEAMICO". The consultants selected 15 major assemblers for pro-active match-making activities. BUILD teams visited these assemblers, provided them with information on potential local - mostly Thai-owned - suppliers, listed parts and components being sought by these assemblers and worked with them to develop these relationships However, during the following phase (starting June 1994) - that was run by two new consulting firms - match-making and related activities was de-selected, while database development and computerised information on subcontracting opportunities in Thailand were developed further. Additionally, BoI organised missions abroad, in particularly to Europe and Japan which allowed local suppliers to participate in international trade fairs and exhibitions. During the fourth phase (May 1996 to May 1997) the project was subcontracted to leading trade industrial trade association "The Federation of Thai industries" (FTI) and missions, trade fairs and general seminar activities became the primary focus (BoI Investment Review vol 3, No.1, 1994, p.9, Brimble and Pattanun May 1994; Information provided by the BUILD Unit, Nov. 1996).

It thus appears that already by 1994-95, the BUILD programme had lost steam, and that site visits to TNC assemblers had been abandoned. It turned out that the new more export oriented TNCs were less interested in forming backward linkages to the local suppliers than the older TNCs and large domestic enterprises (Felkner 2001, 172). Though publicly advocated by the Secretary General of BoI, there was not similar strong organisational support.

In principle, the BUILD team was made up of BUILD officers and staff from the BOI Planning and Development Division plus staff from sector and regional divisions. In reality, there were difficulties in obtaining a strong involvement of the BOI staff to bring in the available sectoral knowledge into the backward linkages support activities. During the whole period, the BUILD unit was staffed with 2-3 officers from the Planning and Development Division but rather than building-up (and utilising) in-house expertise. BUILD activities were from the very early beginning contracted-out to shifting consortiums of consulting firms. Apart from the problems of being able to consistently

follow matchmaking through, the BUILD was also handicapped by not having the authority and capacity to be able to enhance the capabilities and competence of domestic suppliers.

To mitigate that problem BoI in 1994 proposed a comprehensive supplier development programme - the National Supplier Development programme (NSDP) - to develop an internationally competitive base of supplier SMEs in Thailand. It was planned as a multi-agency effort in which the Board of Investment and the Ministry of Industry should divide the overall responsibilities but it did also encompass a range of other ministries, agencies and associations (Brimble and Sripaipan1994). Though a steering committee was set up, the initiative failed to materialise, in part because the MoI did not in reality commit itself to the programme

Linkage formation and supplier development was also compromised by BoI's general policies. First, the overall promotion policy through its duty- and tax-deduction mechanism actually tended to favour import of machinery rather than local parts production. Second, the primary mission of BoI was to attract foreign investors rather than to establish backward linkages to local Thai-owned suppliers. BoI did in 1993-94 decide to give special investment incentives to 14 supporting industries (including e.g. mould & die, jig & fixture, cutting tools, electronic components made from metal or plastic and engineering plastic products and parts).[113] Following the controversial 1991 decision to allow 100 per cent foreign-owned firms to sell up to 20 per cent of their output on the domestic market, it was decided that in supporting industries such investors could sell all output at the domestic market. Therefore, rather than supporting domestic suppliers, BOI from 1995 gave priority to getting in particular Japanese SMEs to follow their principals to Thailand (BOI Investment Review, Vol. 5, No.3, September 30, 1996, 2; EIU 1996:2, 21). This met little if any organised protest from the local business community. 'The Federation of Thai Industries voiced no specific objection to the promotion of FDI by foreign suppliers firms. Indeed, final goods assemblers, for whom the entry of foreign component suppliers posed no competitive threat, dominated the representative associations." (Felkner 2001, 173).

The financial crisis and later the abolishment of local content requirements made the situation extremely difficult for domestic SME

[113] In 1997 expanded to 19 supporting industries.

suppliers. The BoI revitalised BUILD programme and expanded it in 1997 to include 'the ASEAN Supporting Industry Database' (ASID) and 'the Vendors Meets Customers (VMC) Programme' (VMC). The ASID provided information on more than 12,000 manufacturers in the ASEAN area, including about 7,000 firms in Thailand. The VMC Programme was established to introduce local automotive and electronics parts suppliers to potential buyers. In this programme, BoI acts as a broker to match assemblers (buyers) and suppliers (vendors). By September 1999, a total of 17 and two years later 50 assemblers had been visited by potential part suppliers. BOI was also undertaking so-called "local-to-local meetings" introducing Thai SMEs to counterparts in Japan, hoping for technology transfer and other possible alliances. Finally, BUILD started expanding its activities from local assemblers to overseas buyers (BUILD homepage on http://www.boi.go.th/english/build; Bangkok Post 19 June and 5 November 1999. UNCTAD 2001, 202-203).

Altogether, though now staffed with eight full-time staff and a five million baht annual budget, BoI/BUILD remained constrained by the scope of its mission, mandate and expertise. The activities were in the field of information and increasingly again in matchmaking, while the agency were not able to provide direct technical, financial managerial support to Thai suppliers. Furthermore, BoI by inviting foreign suppliers to invest in Thailand tended to give priority to upgrading of the TNC sector rather than to linkage formation and upgrading of domestic (Thai) suppliers.

Supplier development through comprehensive SME policy

While the BoI was in charge of linkage policy, it was the Ministry of Industry - and in particular its Department of Industrial Promotion (DIP) - that became the core agency in relation to supplier development and SME policies. The first initiative was *the Master plan for the Development of Supporting Industries in Thailand* (1995). During the early 1990s, Japan became increasingly interested in protecting their investments in the ASEAN and in developing local supporting industries to promote the competitiveness of Japanese affiliates in the region and Japanese products more broadly. Through MITI and the Japan International Cooperation Agency (JICA) it advanced 'the supporting industry' strategy. In the Thai context, the Japanese were particularly interested in two supporting industries: auto parts and electrical/electronics parts. DIP agreed with JICA on a so-called

comprehensive "Study on Industrial Sector Development - Supporting Industries in the Kingdom of Thailand." The overall objective of the Study was to formulate a master plan for supporting industries covering the two supporting industries. (JICA-DIP 1995 Annex A, A 10-2).

The conclusions and recommendations in the study report were organised around six elements which together added up to a very comprehensive programme: Policy and legislation, market development, technology upgrading, financial support, upgrading of management and investment promotion. Under the heading of "policy and legislation", the report suggested a basic law of SME development as well as a law of subcontracting promotion. Market development support referred to promotion of subcontracting business.

At the organisational level, the study advocated a reorganisation of MOI in order to make DIP into a "pilot agency" for SME development. In relation to backward linkages, it included on the one hand an expansion of BUILD's intermediary activities and the units transfer to a new reorganised DIP in MoI, and on the other hand a full-scale subcontracting assistance programme for those pairs of buyers and suppliers who wanted to enter into linkage arrangements to be promoted in the future by a new DIP unit (JICA-DIP 1995: 11-1-14 ff, 11-3-1ff and 11-4-3).

The Master Plan for Supporting Industries was approved by the Cabinet in May 1996. There was an implementation period of seven years (1995 - 2001). However, the master plan met resistance inside the MoI where the industrial planning unit (OIE) pushed for inclusion of also 'non-metallic industries'. Similarly, the BoI tended to favour its own broader definition of supporting industries. By the end of 1996, no particular budget had been established for the Master plan, so DIP would have to apply the Budget Bureau on an early basis. The implementation process started inside the DIP with the formation of a Bureau of Supporting Industries Development (BSID), but any signs of implementation outside DIP jurisdiction were not visible.

The financial crisis let to further political marginalisation of SME- and supplier development issues. The Chuan II government gave priority to macroeconomic policies and financial sector reforms. In late 1998, when it became clear that the large conglomerates were in deep trouble and when local entrepreneurs and social activists voiced their dissatisfaction with the government's IMF-oriented policy, there was a sudden shift among the political elite. Leading Thai politicians suddenly presented themselves as strong devotees of SME programs.

The Thai Rak Thai Party, headed by Thaksin Shinawatra, suggested assistance to particular export-oriented SMEs using local technology. Chart Pattana Party, and its de facto leader Industry Minister Suwat Liptapallop, suggested a more broad-based support to SMEs, including those in rural areas. Finally, the Democrat Party, headed by Prime Minister Chuan Leekpai, supported the idea of channelling low interest loans to SMEs through state agencies. At the bureaucratic level the director-general of the Department of Industrial Promotion, Manu Leopairote was pushing for a comprehensive SME support package, encompassing a SME basic law. The BoI were in favour of support to local Thai suppliers to large enterprises. The Japanese aid agencies (JETRO and JICA) used their financial leverage to push for their supporting industry model and they were still eager to see a new assistance agency (with technical support from Japanese) heading these efforts. Finally, the World Bank were also in favour of SME support but not of cheap (non-market based) loans to SMEs (Bangkok Post 6 November 1998; 9 November 1998, 11 December 1998).

In contrast to the pre-crisis period, there seemed to be a coalition of agents that had expressed their strong interest in assisting SMEs in exporting industries and in supplier industries to these industries. Financial assistance through the Miyazawa plan brought the Japanese strongly back in SME policy. From March to August 1999, JICA conducted a Follow-up Study on Supporting Industries Development that presented a framework of a detailed Master Plan for SME Promotion based on the Japanese experience (JICA-DIP 1999).

In December 1998, the Cabinet endorsed the draft of a *SME Promotion Act* proposed by the Ministry of Industry. After a lengthy parliamentary process it was finally adopted in January 2000. In order to insure coherence and co-ordinated efforts, the new legislation put a SME Promotion Committee and an Executive Committee. Further, it was decided to establish a semi-autonomous SME Promotion Office (SMEPO) and a SME Promotion Fund. Finally, it was decided to create an Institute of SME Development (ISMED) focussing on entrepreneurial development and to draw up a SME Promotion Action Plan covering 18 areas, of which promotion of linkages between SMEs and LEs was one (http://www.dip.go.th/policy/epolicy2.htm, 14 December 2000).

In the meantime a comprehensive *SME Master Plan* (1999-2004) was drawn up by MoI/DIP with financial and personnel support from Japan. The plan was approved by the Cabinet in April 2000 and

encompassed seven strategies: Upgrade technological & management capabilities of SMEs; development of entrepreneurs and human resources of SMEs; enhance SME's access to markets; strengthen financial support system for SMEs; provide conducive business environment; develop micro-enterprises and community enterprises; and develop networking of SMEs and clusters. The third strategy encompassed a strategy of promoting subcontracting and linkage formation with large enterprises plus development of buyer-supplier database and information network. Apart from the strategy six and seven that stemmed mainly from ILO or UNIDO (Japan), the plan simply repeated the programme elements already presented in the above mentioned Master plan for SME Promotion (http://www.dip.go.th/policy/epolicy6.htm, 14 December 2000).

In April 2000, Thailand had finally a comprehensive SME policy in place. However, the policy process was top-down and had been driven by a mixture of local 'political entrepreneurship' and strong donor involvement. In contrast, though having three members in the SME Promotion Committee, SMEs and business associations with many SME members played a limited role. The Federation of Thai industries - which represented mostly large enterprises and assemblers - were involved but were not particularly interested in SME policy (Interviews with public officials).

The implementation process was not always well co-ordinated. Thanks to the Miyazawa funds and after the model of the Japanese Institute for Small Business Management and Technology (JSBC), ISMED was set up in April 1999. ISMED became an autonomous agency under the MoI and it was planned as a centre point for assisting new and existing SMEs through training, counselling and information services (ISMED Brochure 2001). ISMED was located at the Thammasat University Rangsit campus and consisted of a network of ten universities which may not be the optimal agent for approaching the target group - SME owners and middle management of SMEs (Sevilla & Kusol 2000, 41). Furthermore, the division of labour between and co-operation with the sectoral institutes (see below) was not clear (Régnier 2000, 85). Problems of targeting and co-ordination were also observed in relation to the SME Financing Advisory Centre (SFAC) set up in October 1999. SFAC had its main office in Bangkok but the 24 nation wide centres were located at accounting & management departments at the provincial universities (ibid., 82; Bangkok Post 11 August 2000). Finally, by January 2001, DIP still served as an interim SME promotion

office and was in the process of formulating detailed projects under the seven strategies. (Interview with DIP official January 2001).

In sum, a fairly coherent SME policy was designed during 1998-1999. This was less a result of collective organised SME entrepreneurs and more due to an alliance between donor agencies distributing Japanese aid and the Ministry of Industry. The latter was headed by a Minister that managed to use the SME issue as a policy platform, and he had by then a leadership team in its Department of Industrial Promotion that had tried to advance SME- and supporting industry policies for long. However, implementation of a credible and well co-ordinated SME policy with a supplier development potential hat not taken off by early 2001.

Supplier development through industrial restructuring and new technical institutes

The SME promotion policies were actually preceded by a set of sectoral industrial promotion policies that also received Japanese financial report - *the Industrial Restructuring Plan (IRP)* 1998-2002 and the establishment of industry specific institutes.

The IRP was a comprehensive plan to upgrade mid- and long-term competitiveness in Thailand's industrial sector (13 targeted industries). The Ministry of Industry presented a set of 'Guidelines for Industrial Restructuring' for the cabinet in September 1997, and a National Industrial Development Committee (NIDC) was established to be in charge of the planning process. The final 'Industrial Restructuring Master Plan' was approved in January 1998 and an 'Action Plan for Industrial Development' approved by the NIDC in June the same year. This plan consisted of eight programmes encompassing 34 different projects. The plan had a total budget of 1.2 million US$ to be financed by foreign long-term loans from the World Bank, the Asian Development Bank and the Japanese Government. The funds were to be spent partly (84 per cent) as soft loans to industrial sectors channelled through industrial financing institutions, and partly as funds to government agencies and industrial institutes to be used to cover (half of) the costs of hiring (expatriate) experts. Further, they should cover institutional upgrading of these organisations themselves. The fourth programme on 'incubation and strengthening of small and medium supporting industries' encompassed seven projects. Besides a project to develop industrial linkages through BUILD, the remainder was supplier

development projects run by various sections of DIP (NIDC 1998; JICA, 1999: 2-1-14 – 2-1-21).[114]

While the content and process of the policy making process around IRP in many ways was impressive, the implementation was slow and fragmented. During the first phase 1998-99, 24 projects (out of 440 projects ideas) to a total value of US$ 123 million were chosen and approved by the Cabinet. Of these 21 were actually implemented and IPR-sponsored loans worth 100 million US$ were approved to be distributed through two industrial finance corporations. The first basket of implemented projects consisted of a fairly arbitrary collection of diverse project proposals from various public agencies. The NIDC acknowledged that only 'slight progress' had been achieved with its restructuring programme. NIDC referred both to the low commitment to change in industry and to the lack of leadership on behalf of the government. This was in turn linked to political rivalry between the smaller Chart Pattana party (Industry Minister Suwat) and the leading Democrat party (EIU Country Report, 2000 -1, 29 and interviews with public officials January 2001).

The second IRP phase consisting of 59 projects (chosen out of 140 project proposals) at a total cost of US$ 80 million was approved in March 2000. During the IRP-Phase II, a 220 million US$ credit facility was also set aside. The project formulation phase was more in-depth going, and during the evaluation and planning process there was a stronger involvement of trade associations but implementation of many projects was slow. Hence, in late February 2001, the new Industry Minister ordered a revision of the IRP because the implementation was too slow. The first phase was reported to have achieved only 70 per cent of its goals, and implementation of the second phase had not started yet (Bangkok Post, February 28, 2001).

Despite the systematic, comprehensive and high-profile approach chosen at first, the IRP ended up as a collection of fairly isolated projects that did not add to a coherent programme, had little private sector input, and was not co-ordinated with similar projects outside IRP - carried out by the same agencies or other agencies (JICA-DIP 1999, 2-17; Tambuntlertchai 2002, 9).

The formation of *industry specific institutes* had started prior to IRP but the establishment of Thailand Automotive Institute (TAI) and the Electrical and Electronics Institute (EEI) became part of the IRP

[114] One project was to formulate a Master Plan for SME development

process (July 1998). The general idea behind these institutes was that of transferring some of MOI's activities to semi-public institutes that were expected to work tightly with the private sector. Both the TAI and the EEI was established as part of the IRP process with strong Japanese involvement. They were set up as independent institutes under a newly formed Industrial Development Foundation and aimed at developing the two industries to become competitive at the international level. TAI and EEI were given a five years budget support (1999-2003) and were expected to become financially independent after these five years. At the same time, there was an expectation that they concentrated on improving the competitiveness of the local suppliers and in particular the local SME suppliers, mostly found in the second tier. Both institutes organised their strategy so as to ensure institutional survival beyond year 2003. Thus, TAI chose to focus on both global and local suppliers at the first tier because they have the best potential for upgrading, and EEI targeted 'the big fish' that could ensure higher revenue to the institute. Further, neither TAI nor EEI were particularly concerned whether they supported Thai-owned or foreign-owned enterprises, and their main customers tended to be joint-ventures (Interview with TAI and EEI representatives January 2001).

In sum, the potential advantage of the new institutes to advance the local supplier industry in automobile and electronics industries in a non-bureaucratic manner had not materialised by early 2001.

State capacity, policy orientation and concluding remarks

During the 1990s, promotion of backward linkages as well supplier development- and SME policies came on the policy agenda in Thailand. For a long time, local content regulations and other import substitutions policies had created space for a layer of locally owned parts producers. By the mid-1990s, it became increasing clear that LCR's would be lifted within few years and that changing assembler strategies would force domestic suppliers to deliver parts of world market grade (cf. Chapter 13).

It was against this background that linkage- and supplier development policy initiatives evolved in Thailand. Foreign donors and selected Thai officials became increasingly aware of the need for structural change in the manufacturing industry. They were especially preoccupied with how to develop low-level assembly processing towards the production of higher-value added items involving a greater

use of locally made inputs. At the overall level, the introduction of a value added tax in 1992 changed the incentive structure in favour of vertical disintegration of production. Further, linkage- and supplier development policies were integrated into the overall national planning and adopted by the leading industrial policy agencies – BoI and MoI.

The BoI developed three comprehensive linkage and supplier-development programmes – the BUILD programme, the VMC programme and the NSDP. The latter was a multi-agency effort that failed to obtain support outside the NESDP and did not reach the final stage of cabinet decision making. The BUILD programme started in 1992 but when implemented the scope of the activity was narrowed down. From being originally interested in linking local Thai parts producers to foreign assembly companies, the main BoI strategy ended up being that of encouraging foreign (Japanese) suppliers to follow their principals to Thailand.

The MoI never agreed internally on the content of a supplier development strategy. One strong department (DIP) took advantage of its 'Japanese connection' and advanced a Master Plan for the Development of Supporting Industries. The cabinet approved the plan in 1996 but budgets were not allocated to it. In the wake of the financial and economic crisis 1997 and with the arrival of the Miyazawa funds, the plan was reinvigorated in the form of a Master Plan for SME development - along the lines suggested by a Japanese consultancy firm. In parallel, the Industrial Restructuring Program came into being. The IRP had a separate programme for SME supporting industries. Finally, the MoI was also in charge of setting up industry specific institutes to assist local manufacturers in general and local parts producers in particular.

We generally found that many policy initiatives were taken and that there was a stronger policy attention to SMEs and supplier development issues. Nonetheless, the policy orientation was ambiguous, policy formulation was not co-ordinated across (and in some cases even within) agencies, and the policy implementation process remained slow. The reason was threefold.

First, 'real sector' problems were given only secondary priority by the political elite. Prior to the crisis, there was a strong focus on how to attract FDI, portfolio capital and commercial bank loans to cover the deficit on the current account, while the role of FDI in the linkage triangle was not reflected in the FDI policies. During and after the crisis, the neo-liberal oriented Chuan-government (in alliance with IMF

and the World Bank) gave priority to structural and macro-economic reforms to improve short-term economic efficiency. When 'real sector problems' - including distressed SME parts producers - came on the policy agenda, the policy tended to be driven by a mixture of compliance with donor demands (including short-term disbursement requirements) and political manoeuvring, rather than by strong political support for an effective and realistic linkage-, supplier- and SME policy.

Second, these policies were the responsibility of a range of ministries. Both unstable coalitions governments and 'party ownership' to particular ministries worked to the detriment of comprehensive policies. Old plans tended to be scrapped before implemented when incoming governments brought new ones forward. Further, in the coalition governments, individual parties had a preference for particular ministries, and cabinet members and their respective parties focused exclusively on their own ministries, showing little interest in general economic policies and strategies. A final reason for the lack of co-ordination was the long tradition of departmental parochialism, leading to fragmentation, functional duplication and overlap inside ministries.

Third, there was the lack of dense and effective institutionalised public-private sector links, partly because FTI did not represent the interests of SMEs, partly because of the particularistic links between politicians and business remained the dominant form of public-private sector interaction, and partly because priority (in the policy design phase) was given extraverted policy networks.

In sum, the analysis demonstrated that by 2001 Thailand was not institutionally prepared - i.e. did not have sufficient state capacity - to implement an effective set of linkage-, supplier- and SME development policies. As a consequence, the 1990s turned out to be a period of lost opportunities for introducing an effective set of institutional and policy support for actual and potential SME suppliers in Thailand.

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