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Which country in the region will benefit if foreign investment is diverted from Myanmar?

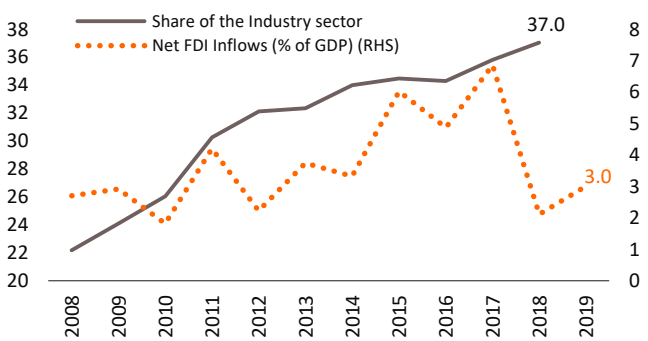
Political disruptions leading to a worsening business and investment climate could divert foreign direct investment from Myanmar. The diversion is expected to happen primarily in the manufacturing sector which is dominated by the export-oriented and labor-intensive garment and footwear industries which currently account for over a third of Myanmar's total exports. While Myanmar's economy will be adversely affected, other garment manufacturing hubs in Asia will benefit from the diversion. We construct a composite index comprising key factors that influence investors and buyers in choosing a stable and favorable sourcing country. **The index identifies Cambodia, Vietnam, Bangladesh, and Sri Lanka as potential beneficiaries. This is not only because of the potential in their garment and footwear industries – one of the sunrise industries – supporting their competitiveness, but also because of other advantages including low labor cost, trade privilege, export structure and market, and proximity to China, the largest supplier of raw materials for garment production.**

Political disruptions in Myanmar will divert Foreign Direct Investment (FDI) elsewhere

Prospects for foreign investment in Myanmar have been worsening since 1 February when the military (locally known as Tatmadaw) seized power from the civilian government. That had immediately triggered negative sentiment and created uncertainties, domestically and externally. In response to the coup, there have been nationwide protests and public criticism, including a civil disobedience campaign. The opposition against military rule is likely to persist and escalate. This paints an unfavorable picture that could make it challenging to conduct business and investment in Myanmar.

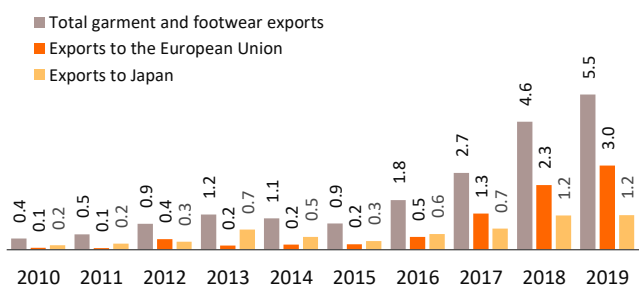
Several large MNCs and foreign businesses have announced they would postpone or suspend investment in the country. Major economies and economic partners have introduced economic and political sanctions and other retaliatory measures, worsening prospects for foreign investment. Since 2011, FDI inflows have been a driver of the rising role of Myanmar's industry sector, especially the labor-intensive manufacturing sector. In 2018, the industry sector accounted for 37% of nominal GDP, transforming the country from an agrarian economy toward an industrial economy (Figure 1). Exports of manufactured goods, especially garment and footwear products, have risen to reach more than 30% or USD5.5bn of total exports in 2019 (USD18bn; Figure 2). However, the political intervention by the Myanmar military is likely to deter FDI inflows significantly, at least in the medium term. Growth of labor-intensive activities, primarily garment and footwear production, would be severely derailed and investment could shift to other countries in the region. We explore which countries in this region, especially key garment exporters, will benefit from the diversion of foreign investment away from Myanmar through the lens of international trade data, including the implications of such diversion.

Figure 1: Industry share of Nominal GDP (%) and Net FDI Inflows



Source: CEIC, Krungsri Research

Figure 2: Myanmar's garment and footwear* exports (USD bn)



Note: *garment and footwear products refer to all products in HS61-HS64 HS code
Source: CEIC, Krungsri Research

FDI has played a crucial role in driving economic growth and the export-oriented manufacturing sector in the past decade, particularly the garment industry

"It takes 20 years to build a reputation and five minutes to ruin it. If you think about that, you'll do things differently".

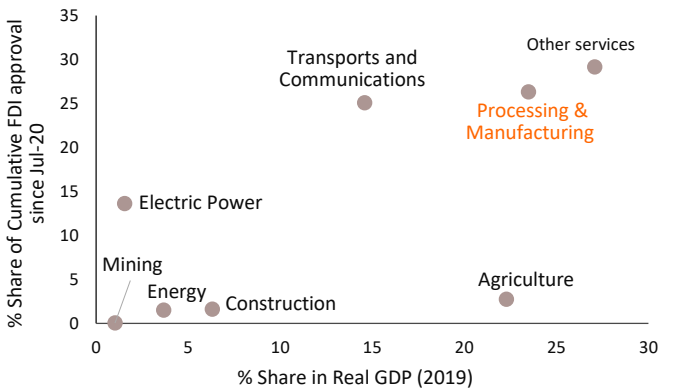
— Warren Buffett

With supportive fundamentals, Myanmar could become one of the next manufacturing hubs in the region. They include its strategic location between the two largest and growing economic powerhouses, China and India. With abundant natural resources and a 55-million population, most of them young, the country offers untapped opportunities and a sizeable domestic market. In addition, since its re-engagement with the global economy in 2011, Myanmar has benefited from the relocation of labor-intensive manufacturing activities especially from China, which has supported its industrialization efforts. And following sustained inflows of foreign investment, the manufacturing sector has surged to account for about 25% of GDP in 2019 compared to 18% in 2010 and contributed to national economic growth substantially (Figure 3).

By adopting the export-led growth strategy, labor-intensive manufacturing production, particularly the garment & textile industry, has flourished to become a main driver of Myanmar's exports. Despite taking-off not long ago, exports of garment and footwear products have surged to account for over a third of the country's total exports in 2019 from 4.5% in 2010. In addition, the sector has paved the way for Myanmar to integrate into regional and global supply chains following over half a century of economic isolation.

Figure 3: Role of Foreign Indirect Investment (FDI) in Myanmar's economy and industrial sector

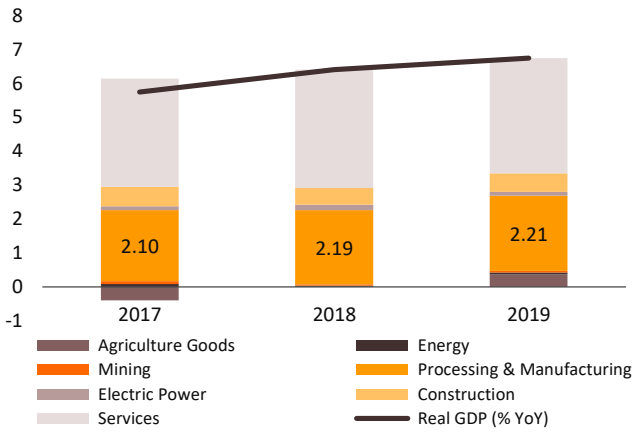
Figure 3a: Significance of FDI and key industrial sectors



Note: Other services include financial services, wholesale and retail trade, social and admin. services, rental and other services

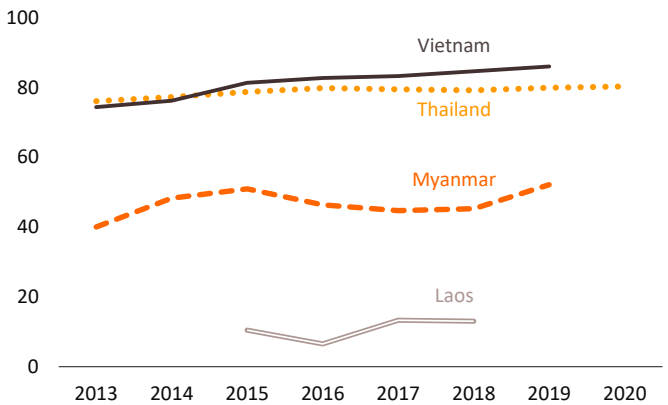
Source: CEIC, Krungsri Research

Figure 3b: Sources of real GDP growth on the Supply Side (ppt)



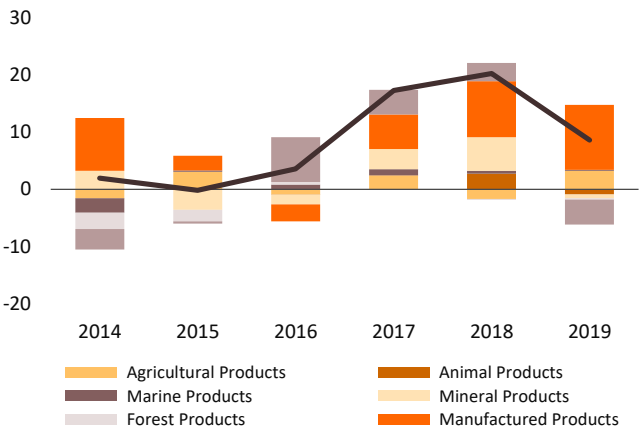
Source: CEIC, Krungsri Research

Figure 3c: Exports - Manufactured Products (% of Total Exports)



Source: CEIC, Krungsri Research

Figure 3d: Sources of Myanmar's export growth by major product (ppt)



Source: CEIC, Krungsri Research

Figure 4: Myanmar's exports by major product group

Major Export Group	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Live animals/products	3.6	6.4	7.9	5.8	3.8	4.0	4.7	4.9	6.8	5.7
Vegetable products	12.5	22.6	25.5	23.1	21.4	24.1	23.0	20.8	16.0	17.4
Animal or vegetable fats	0.0	0.0	0.1	0.1	0.0	0.0	0.0	0.0	0.0	0.0
Prepared foodstuffs	0.2	0.3	0.3	0.6	0.3	2.4	9.8	6.5	5.2	1.1
Mineral products	33.2	36.1	24.7	34.0	40.7	42.5	28.4	26.9	21.7	24.6
Products of the chemical	0.0	0.1	0.0	0.1	0.0	0.0	0.1	0.2	0.1	0.1
Plastics and articles	1.5	3.9	2.1	2.3	1.2	1.2	1.5	2.0	1.7	1.8
Raw hides and skins	0.1	0.1	0.1	0.1	0.1	0.1	0.2	0.7	0.9	2.1
Wood and articles	6.7	7.3	21.5	6.0	3.6	1.6	2.0	1.6	1.2	0.9
Pulp of Wood	0.1	0.2	0.0	0.0	0.0	0.6	0.0	0.1	0.4	0.1
Fabrics	0.1	0.0	0.1	0.2	0.2	0.4	0.3	0.2	0.4	0.3
Garments	3.9	6.1	9.4	10.3	9.1	7.5	13.9	17.8	25.0	28.0
Footwear	0.6	0.7	0.7	0.7	0.7	0.7	1.3	1.9	2.5	2.9
Articles of stone	0.0	0.0	0.0	0.1	0.0	0.0	0.0	0.0	0.0	0.0
Precious metals	19.5	15.0	4.4	7.2	9.5	5.5	3.6	2.8	5.7	4.6
Base metals	0.6	0.6	1.0	0.9	2.8	3.6	3.7	6.8	7.1	6.2
Machinery and mechanical appliances	0.0	0.0	0.2	0.3	0.2	0.3	5.3	1.6	1.8	2.0
Vehicles	0.0	0.1	0.2	0.1	0.0	0.0	0.4	3.7	2.3	1.1
Optical	0.1	0.2	0.2	0.0	0.3	0.2	0.9	0.5	0.8	0.6
Arms and ammunition	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Miscellenous manufactures	0.0	0.1	1.2	0.2	0.0	0.2	0.2	0.2	0.1	0.2
Antiques	0.0	0.0	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.1
Others	17.2	0.3	0.2	7.8	6.0	5.1	0.8	0.7	0.2	0.0
Total Exports (USD bn)	**8.9**	**8.1**	**9.1**	**11.4**	**11.5**	**11.4**	**11.7**	**13.9**	**16.7**	**18.0**

Note: *garments include HS61-HS63 and footwear includes HS64 in the HS code

Source: Author's calculation based on data from ITC Trade Map

As the economy moves toward industrialization led by labor-intensive garment production, the roles of traditional sectors such as agriculture and extractive industries have correspondingly declined. For example, exports of vegetable products have dropped from 25.5% of 2012 national GDP to 17.4% in 2019, and exports of mineral products have dropped from its peak of 42.5% in 2015 to 24.6% in 2019 (Figure 4).

The European Union (EU) has become the largest export market for Myanmar in 2020, accounting for 37.4% of Myanmar's total export value in 2020 based on mirror data reported by Eurostat. **It has surpassed China, the long-standing largest export market** (Figure 5)**.** The EU has emerged as the largest export destination because of rising garment and footwear shipments primarily driven by preferential trade arrangements. These have been granted by major markets including the EU, the US, and Japan. For the EU, Myanmar has been granted tariff-free access to its single market under the Everything But Arms (EBA) scheme since 2011. This also explains why Myanmar was the 10th largest non-EU source of garment and footwear imports in 2020, with 2.3% share.

Figure 5: Myanmar's top export destinations (% share of total exports)

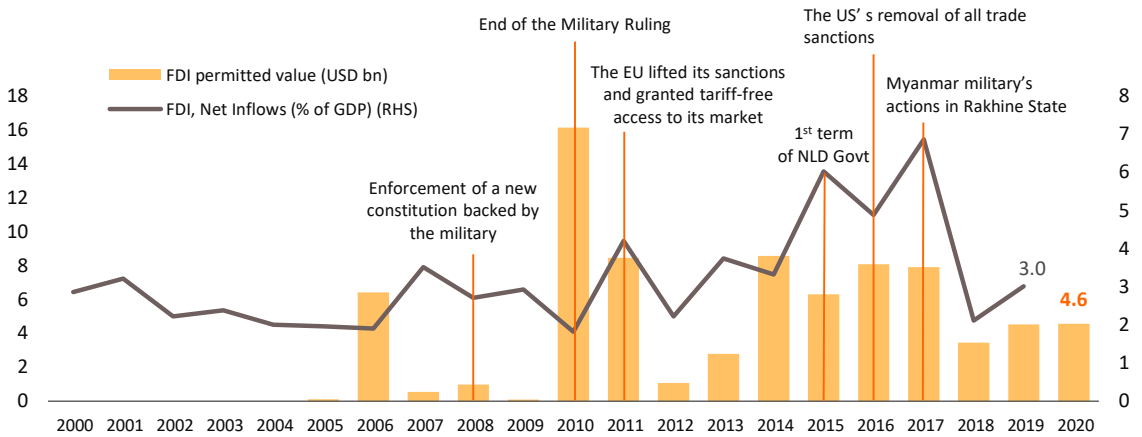
Major Export Markets	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
China	10.6	14.7	19.8	15.0	26.0	64.4	39.9	35.5	33.7	29.7	32.3
The EU-28	3.9	3.5	3.0	2.6	2.9	2.3	6.2	11.1	16.6	22.2	22.7
Thailand	45.8	42.7	38.6	42.5	36.7	16.2	26.7	20.3	18.5	19.1	16.6
Japan	5.6	5.9	7.0	7.8	6.9	3.6	6.5	8.0	7.9	8.1	7.2
The US	0.0	0.0	0.0	0.0	0.3	0.4	1.1	2.2	2.8	3.2	4.3
South Korea	1.3	2.4	3.5	4.1	4.4	2.4	3.8	3.9	3.4	3.4	3.0
India	19.5	17.0	14.9	15.6	12.4	5.8	7.6	9.3	5.5	2.9	2.6
United Kingdom	0.9	0.8	0.8	0.7	0.8	0.5	1.2	1.8	2.2	2.4	2.5
Malaysia	2.4	3.5	2.8	2.1	1.8	0.7	1.3	1.7	1.7	1.9	1.3
Netherlands	0.2	0.1	0.1	0.2	0.1	0.1	0.3	0.6	0.9	1.1	1.2
Viet Nam	1.1	1.6	1.0	1.3	1.1	0.6	0.4	0.8	0.9	1.0	1.2
Singapore	1.9	1.3	1.0	0.9	1.6	0.7	0.9	0.9	0.8	1.2	1.0
Indonesia	0.5	0.5	0.8	0.7	0.7	0.5	1.2	1.0	1.1	1.0	0.9
Philippines	0.1	0.2	0.2	0.3	0.2	0.1	0.2	0.2	0.1	0.2	0.7
Canada	0.0	0.0	0.0	0.0	0.1	0.1	0.2	0.5	0.7	0.6	0.7
Russia	0.1	0.2	0.3	0.5	0.3	0.1	0.1	0.2	0.4	0.4	0.6
Switzerland	0.0	0.0	0.0	0.1	0.1	0.1	0.4	0.3	0.5	0.7	0.6
Hong Kong	0.7	0.6	0.6	0.5	0.4	0.3	0.5	0.7	0.7	0.6	0.5
UAE	0.0	0.0	0.0	0.6	0.4	0.3	0.7	0.7	0.6	0.5	0.4
Saudi Arabia	0.2	0.2	0.3	0.5	0.4	0.2	0.4	0.4	0.4	0.2	0.4

Source: Author's calculation based on data from ITC Trade Map, Krungsri Research

Expect FDI inflows to drop significantly over the medium-term and rein in the manufacturing sector, and be diverted to other destinations in the region

FDI inflows, particularly from the West, have dropped substantially since 2017 following the Rohingya crisis (Figure 6). FDI has been rising since 2011 with net inflows averaging 4% of GDP, but the trend has reversed since 2017 when the refugee crisis in Rakhine State erupted and allegations of human rights violation by the Myanmar military drew global attention. Foreign investment from the West started to drop. By country of origin, FDI inflows into Myanmar has been dominated by funds from Asia Pacific countries such as Singapore (the region's financial center), China, Hong Kong, Vietnam, Japan and Thailand. By sector, manufacturing has been the largest beneficiary of foreign investment and has fueled the country's industrial development led by labor-intensive production such as garment, footwear and electronics. Other major recipients of foreign investment are transportation & communication, power sectors which are crucial to improve Myanmar's competitiveness and address infrastructure development gaps such as shortage of electricity (Figure 7).

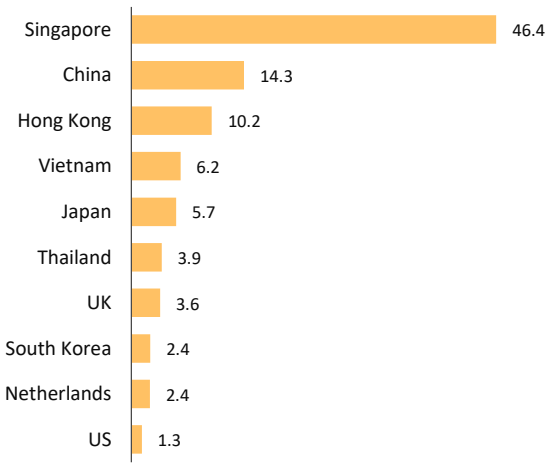
Figure 6: FDI inflows into Myanmar (2000-2020)



Source: CEIC, Krungsri Research

Figure 7: Structure of Foreign Investment in Myanmar

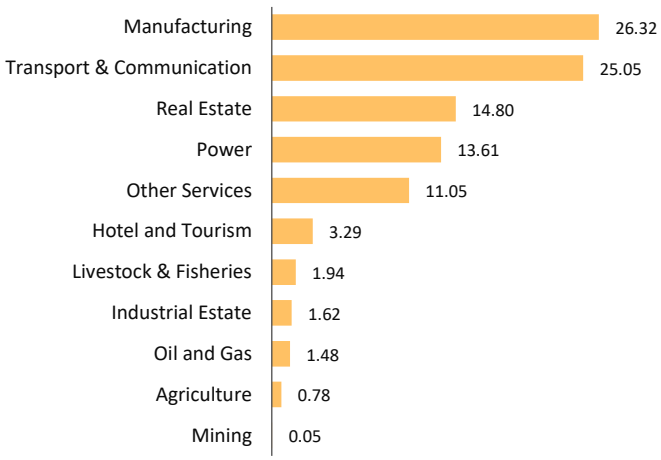
Figure 7a: Share of FDI inflows by country (% share of approved amount)



Note: The data is presented in terms of shares of cumulative approved amount of FDI projects between July 2020 to January 2021.

Source: CEIC, Krungsri Research

Figure 7b: Share of FDI inflows by sector (% share of approved amount)



Note: The data is presented in terms of shares of cumulative approved amount of FDI projects between July 2020 to January 2021.

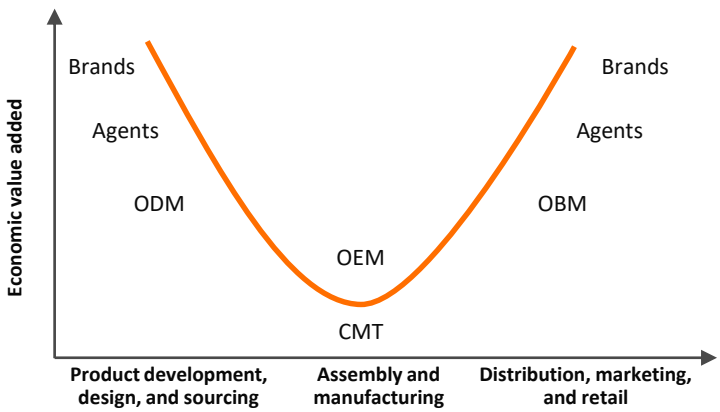
Source: CEIC, Krungsri Research

Falling FDI inflows into Myanmar could be further exacerbated by the military's intervention in politics, against a backdrop of an economy already severely hurt by the COVID-19 pandemic. Political risks and policy uncertainties could cause a significant delays in new inflows and divert foreign investment to neighboring destinations. We expect the diversion to happen first in the labor-intensive manufacturing sector, particularly garment and footwear production where new investment or purchase orders can be moved relatively fast across source countries with a similar production structure in the region. We identified at least five key reasons that would motivate foreign firms to shift their investment away from Myanmar to more stable countries:

1. **To reduce political risks and policy uncertainties**
   Firms may need to reduce risks and contain possible loss as the investment and business climate becomes worsening.
2. **To minimize reputation risk**
   MNCs may need to protect their reputation and branding by not conducting business in a country which government is non-democratically elected
3. **To avoid adverse effects of targeted sanctions by the US, the EU, and other countries**
   Sanctions, despite being targeted, could complicate cross-border financial transactions for international businesses
4. **To reduce political pressure**
   Businesses may need to reduce pressure from all stakeholders, particularly consumers.
5. **To minimize losses arising from the civil disobedience movement**
   The entire economy including the garment industry has been paralyzed by the civil disobedience movement supported by workers in most industries, both private and public.

Myanmar's garment and footwear production will be severely hit by the diversion of foreign investment. FDI inflows have fueled the growth of Myanmar's garment industry over the past decade, but the sector itself is prone to diversion of foreign investment or relocation of foreign factories because of its current structure. Myanmar's export-oriented garment sector is primarily driven by low value-added cut-make-trim (CMT) production. This type of production is prone to relocation. Box 1 presents a simplified supply chain of the garment industry.

Figure 8: Relative positions of actors in the garment sector 'smiling curve'



Note: ODM = Original Design Manufacturers, OEM = Original Equipment Manufacturers, OBM = Original Brand Manufacturing
Source: Adapted from ILO (2017)[1/] , Krungsri Research

Under the CMT production process, factories only supply labor to cut, make and trim designs into completed products. They are provided with product specifications, tech packs, fabrics, patterns, stitching requirements and other details demanded by tier-1 suppliers or international agents in the industry, without direct contact with brands or retailers. Factories are paid a processing fee rather than prices for final products. The CMT process simply comprises assembly and manufacturing activities that require low skills and the factories depend mainly on low wages to stay competitive. As a result, that derives the smallest economic value-add in the entire production chain. In addition, CMT production is sensitive to labor costs and can be shifted to any sourcing country that offers competitive wages. Based on the ILO report[1/], in Asia, only garment exporters in Cambodia and Myanmar operate at the CMT stage. Exporters in other countries such as Bangladesh, Indonesia, Pakistan, and Vietnam have OEM capacities, while China, India, and Sri Lanka have OEM and ODM capacities.

1/ ILO (2017), From Obligation to opportunity: A market system analysis of working conditions in Asia's garment export industry

Box 1: Structure of the Garment Industry's Supply Chains and Simplified Production Process

To understand how the garment industry is operated, we provide the overview of key players in the industry in Figure 9 and a simplified garment production process in Figure 10.

Figure 9: Supplier tiers in the garment industry

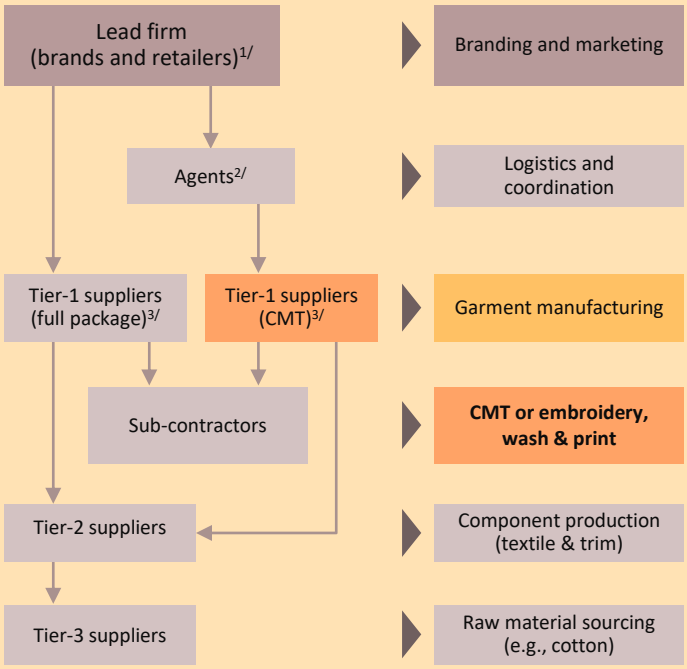
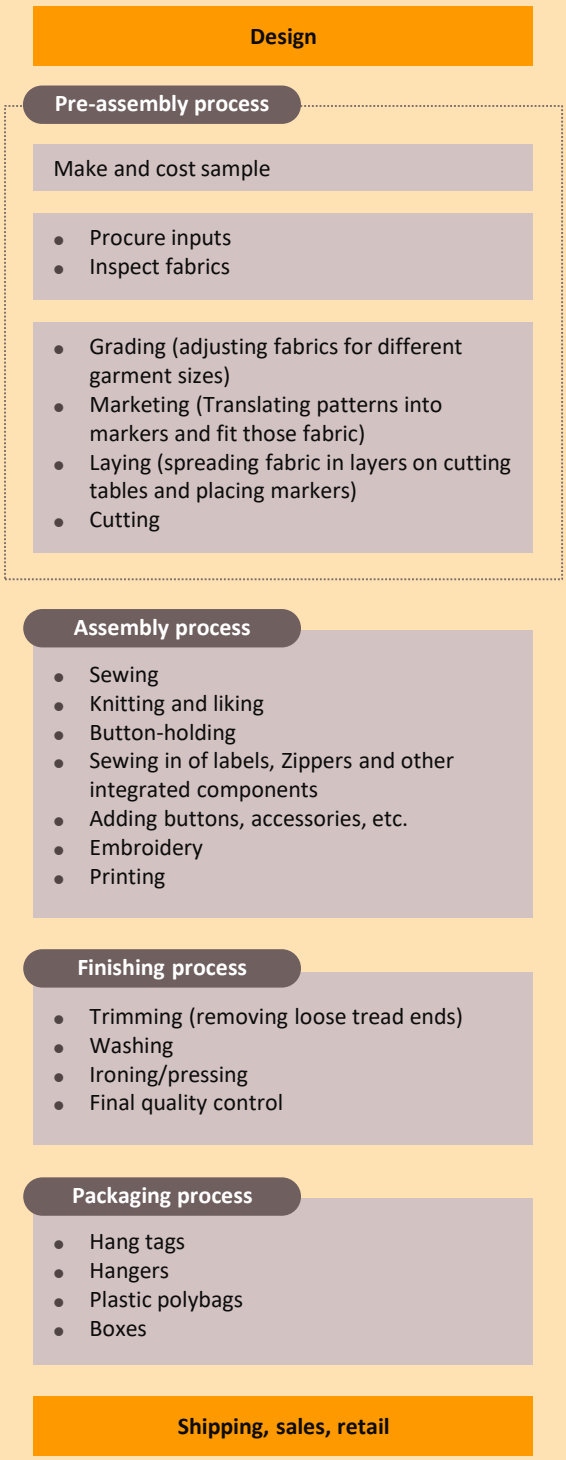


Figure 10: Simplified Garment Production Process



Note: 1/ There are two types of brands and retailers. **First,** brand marketers or manufacturers without factories including fast fashion brands such as H&M, Zara, Uniqlo, Nike, Adidas, Polo Ralph Lauren and Calvin Klein and other global luxury brands as well as designer brands, normally let overseas contractors manage the whole production process. **Second,** Brand manufacturers running an integrated supply chain with larger operations. Currently, the number of brand marketers outnumber brand manufacturers.

2/ Agents or buying houses, vendors or trading companies, act as intermediaries on behalf of retailers to coordinate a network of garment suppliers. In addition, agents locate, qualify, and inspect overseas garment producers, negotiate orders with them, and sometimes conduct quality control and monitoring against the retailer's standards and codes of conduct.

3/ Full production package is a clothing production where a manufacturer provides all stages of garment building to a brand including pattern making, fabric and trims sourcing, sample making, and final garment production.

CMT manufacturing is a clothing production service provided by factories to cut, make and trim designs provided into fully produced products. Factories are also provided product specifications, tech packs, fabrics, patterns and stitching requirements and other details demanded by brands or agents.

3/ Garments refer to wearable clothing produced by the readymade garment industry. Textiles refer to the design and production of cloth and woven fabrics using natural or artificial fibers.

Source: ILO (2017), From Obligation to opportunity: A market system analysis of working conditions in Asia's garment export industry

The garment industry has been influenced by international fashion brands and multi-national fast fashion retailers. We expect them to seek alternative low-cost sourcing destinations in the region to avoid disruption to business and to minimize reputation risk as well as risks associated with targeted sanctions. For brands and buyers to remain competitive in the red ocean fast-fashion markets, they need to consider several factors when choosing a sourcing country. They include low labor costs, proximity to main consumer markets or source of materials, short lead times, and flexibility to meet fast-changing consumer demands, and environmental, social, and governance (ESG) issues as there is rising awareness among consumers of the industry's social and environmental footprint. The recent examples are ongoing issues surrounding sourcing cotton from China's Xinjiang region and fast fashion retailers such as H&M[2/]. Therefore, manufacturers in sourcing destinations are expected to be able to respond to emerging global trends as well as changing end-consumer behaviors. By taking buyers' views into consideration, there is likely to be a diversion of foreign investment from Myanmar to other countries in the region.

Figure 11: Major global exporters and importers of garment and footwear products

Figure 11a: World's Largest Exporters
(% Share of world garment exports in 2019)

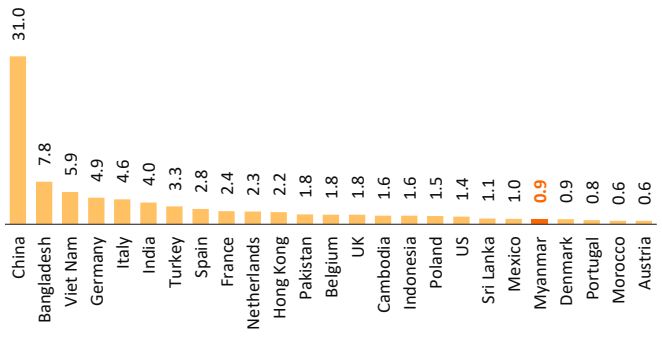
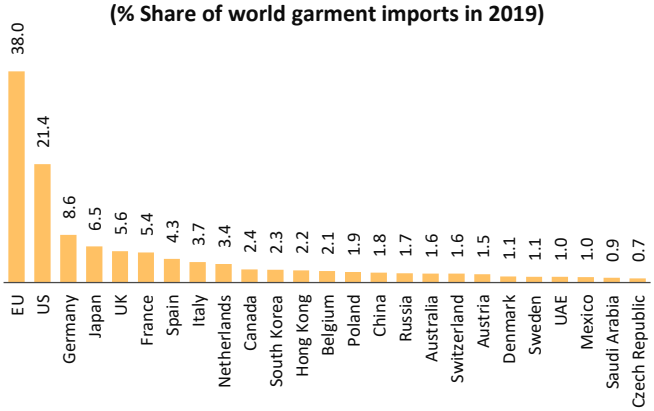


Figure 11b: World's Largest Importers
(% Share of world garment imports in 2019)



Note: garment and footwear includes HS61-HS64
Source: CEIC, Krungsri Research

Other garment production hubs in the region could become an alternative production destination for Myanmar. Myanmar accounted for about 0.9% of global export value of garment products in 2019, which is relatively small compared to regional peers such as Vietnam with 5.9% share and Cambodia with 1.6%. Given the simple and low value-added process, the CMT production in Myanmar can be easily shifted to other production hubs in the region as Asia is the world's largest garment producer. They include Bangladesh, Cambodia, China, India, Indonesia, Pakistan, Sri Lanka, Thailand and Vietnam. Based on 2019 data, China is the largest exporter of garment and footwear products with 31% share. According the ILO, the ecosystem and supply chains for garment production in China is fully-developed. However, rising wages and the expansion of higher value-added sectors, mostly labor-intensive manufacturing, have prompted producers to relocate to Southeast and South Asia. Consequently, there is a flourishing garment industry in Bangladesh, Cambodia, Indonesia, Myanmar, Sri Lanka and Vietnam where there is a large pool of cheaper labor and tariff-free access to major markets, particularly the EU and the US.

Cambodia, Vietnam, Bangladesh, and Sri Lanka could receive a windfall from FDI diversion from Myanmar

Cambodia, Vietnam, Bangladesh, and Sri Lanka, respectively, could be key beneficiaries if there is substantial diversion of foreign direct investment triggered by political disruptions in Myanmar. Given the unfavorable investment climate, there is high probability that CMT production activities in Myanmar would be relocated to other Asian countries with similar or higher-value add production, and that are equally attractive foreign investment destinations, especially for garment manufacturing. Cambodia, Vietnam, Bangladesh, and Sri Lanka are potential alternative investment destinations because they have several comparative advantages: (1) efficiency – low labor cost, (2) eligibility for tariff-free access to major markets, and (3) similar export structure and destinations, as well as proximity to China, a main source of raw materials,. These four destinations are among the key garment production hubs in Asia based on ILO data, along with China, India, Indonesia, Pakistan, and Thailand.

2/ For information please refer to, for example, *What Is Going On With China, Cotton and All of These Clothing Brands?,* the New York Times.

We identified the potential beneficiaries of FDI diversion based on a composite index comprising 10 sub-indices: (1) labor cost, (2) free trade agreements or trade privileges in major markets –the EU and the US, (3) export structure, (4) export markets, (5) proximity to China, (6) production specialization, (7) ease of doing business, (8) business start-up costs, (9) trade openness, and (10) political stability (Figure 12).

Figure 12: Criteria for assessing major garment exporters potentially emerging as beneficiary from the FDI diversion

Components of the Index	Bangladesh	Cambodia	China	India	Indonesia	Pakistan	Sri Lanka	Thailand	Vietnam
Labor cost									
Trade priviledges/EU-EBA									
Export structure									
Export destination									
Proxity to China									
Production specialization									
Ease of doing business									
Cost of business start-up procedures									
Trade openness									
Political stability									
Overall Composite Index									

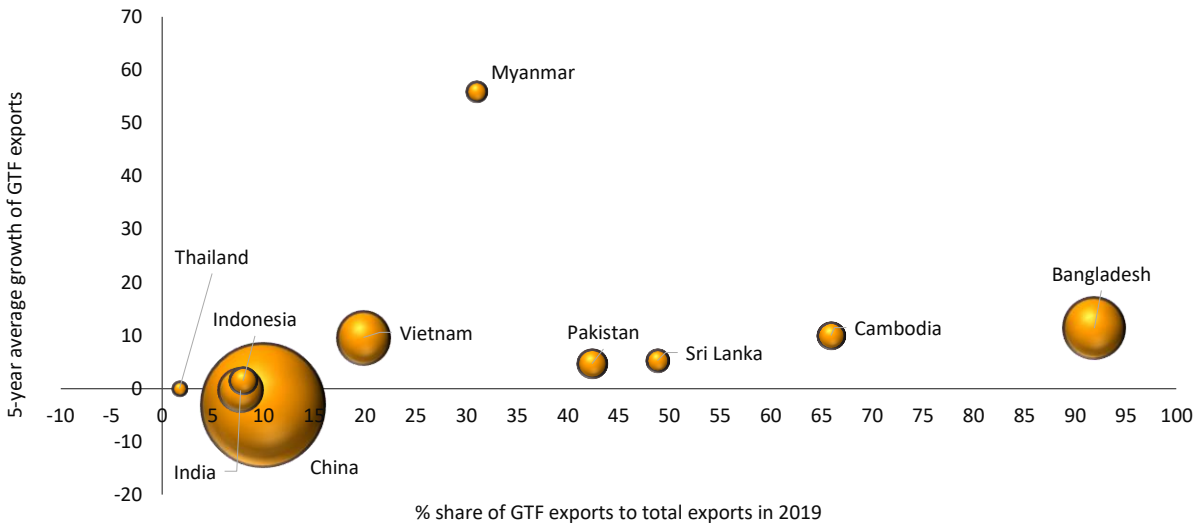
Denotes the most competitive score compared to that of Myanmar and likely to be alternative location for foreign investors

Denotes the least competitive score compared to that of Myanmar and unlikely to be chosen by foreign investors as a production choice

Source: Author's own calculation based on data from CEIC, World Bank Data Bank, ILO, JETRO

The export-oriented garment and footwear production sectors in Cambodia, Vietnam, Bangladesh, and Sri Lanka remain a sunrise industry. They account for a substantial share of the respective country's total export value and register strong export growth. This means that it would be easy to divert sourcing orders to these countries, while buyers would receive at least the same level of competitiveness or attractiveness offered by Myanmar. In Cambodia, exports of garment products accounted for 66% of national exports (by value) in 2019 and the 5-year average growth rate was 10% (CAGR). In Vietnam, GTF exports accounted for about 20% of total exports and growth averaged 9.6% CAGR (Figure 13).

Figure 13: Growth Potential of the GTF Sector in some of Asia's Largest Exporters of GTF Products



Note: The size of the bubble represents % share in the global exports of the GTF products in 2019.
Shares of China, India, and Indonesia are 31.0%, 4.0%, 1.6%, respectively.

Source: ITC Trade Map, Krungsri Research

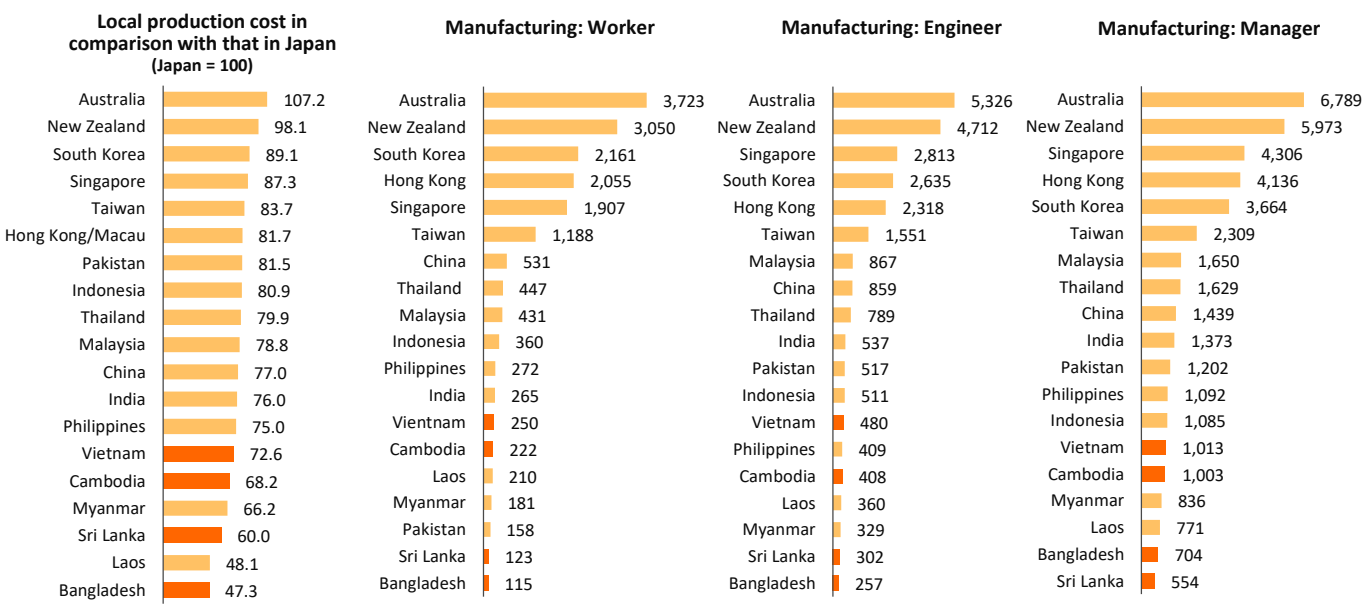
Figure 14: Exports to the European Union (EU) from selected Asian countries

Structure of Exports to the EU in 2019 (% share of total export value)										
	Bangladesh	Cambodia	China	India	Indonesia	Myanmar	Pakistan	Sri Lanka	Thailand	Vietnam
Live animals/products	1.2	0.0	0.7	1.6	1.3	0.2	0.3	2.9	1.6	2.0
Vegetable products	0.0	3.6	0.6	3.4	2.7	5.2	5.3	6.0	1.9	5.9
Animal or vegetable fats	0.0	0.0	0.1	0.7	16.2	0.0	0.0	0.6	0.1	0.0
Prepared foodstuffs	0.3	0.3	0.7	1.5	6.6	0.0	1.9	4.0	6.5	1.8
Mineral products	0.0	0.0	0.7	14.4	2.4	0.0	0.5	0.1	0.1	0.1
Products of the chemical	0.0	0.4	5.2	15.1	11.6	0.0	0.4	0.9	2.1	0.6
Plastics and articles	0.1	0.2	3.6	3.9	8.6	0.0	1.2	9.4	9.6	3.0
Raw hides and skins	0.5	3.5	1.8	2.7	1.0	2.3	6.2	0.4	0.5	2.5
Wood and articles	0.1	0.0	0.7	0.2	3.0	0.9	0.0	0.2	0.1	0.6
Pulp of Wood	0.0	0.0	0.7	0.4	1.8	0.1	0.0	0.2	0.3	0.1
Fabrics	0.2	0.0	2.1	3.1	2.6	0.2	12.9	1.3	1.3	0.6
Garments	93.7	70.4	8.6	11.5	8.4	84.2	64.5	62.9	2.8	10.4
Footwear	2.8	12.7	3.2	2.5	8.8	5.9	1.3	0.7	0.8	13.0
Articles of stone	0.1	0.0	2.0	1.4	0.4	0.0	0.0	0.3	0.9	0.4
Precious metals	0.0	0.1	0.3	6.0	0.2	0.0	0.1	1.6	7.4	0.4
Base metals	0.1	0.2	6.4	10.1	4.8	0.1	0.6	0.2	3.5	3.2
Machinery and mechanical appliances	0.0	0.9	45.1	13.0	11.5	0.6	0.7	4.5	44.8	48.6
Vehicles	0.3	7.6	4.2	5.3	2.4	0.1	0.6	1.2	10.0	2.0
Optical	0.1	0.0	3.8	1.6	1.7	0.0	1.7	0.7	4.4	1.3
Arms and ammunition	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Miscellenous manufactures	0.3	0.2	9.2	1.6	3.8	0.2	1.8	1.8	1.4	3.4
Antiques	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Others	0.0	0.0	0.4	0.0	0.1	0.0	0.0	0.1	0.0	0.0

Source: ITC Trade Map, Krungsri Research

The export structure of and destinations for Cambodia, Vietnam, Bangladesh, and Sri Lanka are similar to Myanmar's. This would be another pull factor for them to be alternative production destinations. In 2019, Myanmar's exports to the EU was dominated by garment and footwear products, at more than 90% share. That is second only to Bangladesh with 97%. Cambodia has two major categories of exports to the EU: (1) garment and footwear at 83% share, and (2) bicycles at 8% share. Among the four candidate countries, Vietnam has a relatively wide range of exports to the EU. Exports of electronics and machinery products dominate total exports with 48.6% share, while exports of garment and footwear products hold 23.5% share. China is at the stage of exiting low-end garment production as labor costs are rising and there are other challenges, including the extended trade dispute with the US and the COVID-19 pandemic shock. India and Indonesia have relatively small share of garment and footwear exports and weak export growth, which suggests their garment industry remains small and is still developing. In Thailand, it is a sunset industry (Figure 14).

Figure 15: Production cost and wages in the manufacturing sector in Asia and Oceania



Source: Data based on JETRO Survey Report: Survey on Business Conditions of Japanese-Affiliated Companies: Asia and Oceania, December 2020

In term of efficiency, the four candidate sourcing destinations offer favorable wages for manufacturing activities, including for the CMT production, compared to Myanmar. While there a number of factors that influence international brands and buyers in choosing their suppliers and sourcing destinations, wage is one of the key factors, particularly for the CMT production which is labor-intensive. To measure and compare production costs and wages across the region, we refer to the survey conducted by JETRO in December 2020[3/]. Although production costs and wages are slightly higher in Cambodia and Vietnam, they remain lower than those in China, India, and Indonesia. In Bangladesh and Sri Lanka, production costs and wage rates are even more attractive (Figure 15).

Figure 16: Garment buyers' perspective on competitiveness among major garment exporters in Asia

Key Issues	Bangladesh	Cambodia	China	India	Indonesia	Myanmar	Pakistan	Sri Lanka	Vietnam
Cost									
Speed									
Compliance									
Quality									
Trade priviledge	EU-EBA	EU-EBA		EU-Standard GSP	EU-Standard GSP	EU-EBA	EU-GSP+	EU-GSP+	EU-FTA/ Standard GSP
		US-GSP			US-GSP	US-GSP	US-GSP	US-GSP	

The greener the more competitive of garment exporters

Source: ILO, From obligation to opportunity (September 2017), European Commission, USTR, compiled by Author

Lastly, Cambodia, Bangladesh, Sri Lanka, and Vietnam are developing countries that are eligible for trade privileges or tariff-free access to major markets, particularly the EU and the US, similar to Myanmar (Figure 16). Tariff-free access to these major importers is another key deciding factor for buyers in selecting their sourcing destinations to reman competitive in the red ocean fast fashion industry. Myanmar has been unilaterally granted preferential access to the EU market under the Everything But Arms (EBA) scheme since 2011 after the bloc lifted all its sanctions and signed a bilateral investment protection agreement. Over the past decade, this has led to a surge in garment exports to the EU, from only USD0.06bn to around USD3bn in 2019. This reflects the importance of preferential trade arrangements in driving garment exports. And, based on the buyers' perspectives on the strength of each major garment exporter, Cambodia and Vietnam, have a network of unilateral and reciprocal trade privileges. For example, Cambodia signed an FTA with China in October 2020 which would help the Cambodian garment manufacturers to access cheaper raw materials from China.

Implications for Thai businesses and investors

There is high probability of foreign investment being diverted away from Myanmar to other countries in the region. The following are key implications for Thailand:

1. **The diversion could put additional downward pressure on Myanmar's vulnerable macroeconomic conditions, financial sector, and external sector stability, on top of the domestic political chaos.** Amid the persistent current account deficits and suspension of foreign partners' assistance, the diversion of FDI inflows would severely hurt a country that is dependent on foreign investment, like Myanmar. Over the past decade, FDI inflows have sufficiently financed current account deficits and supported the exchange rate stability. But going forward, if foreign investment drops drastically, the exchange rate could fall substantially. This could cause trouble for Myanmar's external stability. In addition, the weak currency would put additional upward pressure on inflation through higher import prices as the country also depends substantially on imports. In a country where financial markets are in its infancy with limited tools for currency risk management, businesses are recommended to have risk management strategies in place.

2. **Higher risk of severe disruption to bilateral trade and investment between Myanmar and Thailand.** The political disruptions and subsequent unrest are likely to lead to an extended period of economic recession in Myanmar, especially against a backdrop of the economy that is already reeling from the COVID-19 impact. This could lead to a substantial drop in Thailand's exports to Myanmar as we expect domestic demand to be weak.

3/ JETRO Survey Report: Survey on Business Conditions of Japanese-Affiliated Companies: Asia and Oceania, December 2020

Although Thailand's exports to Myanmar is dominated by necessity products (Figure 17), unrest and civil disobedience would disrupt trade flows and transportation. In addition, Thai investors should have measures and strategies to contain risks and costs arising from targeted sanctions imposed by the US and the EU, particularly costs involving cross-border financial transactions.

Figure 17: Thailand's exports to Myanmar by major product group

Major Product Group of Thailand Exports (% of total)	2016	2017	2018	2019	2020
Prepared foodstuffs, beverages, spirits, and vinegar	25.8	23.8	23.1	19.5	21.4
Machinery and mechanical appliances	17.0	15.3	14.7	13.8	13.6
Products of the chemical	9.6	10.3	11.0	11.4	11.6
Mineral products	11.3	11.5	12.5	13.8	11.4
Vehicles	6.2	6.9	6.1	6.3	7.2
Plastics and articles	6.2	6.4	6.9	6.5	6.8
Base metals	5.7	7.3	6.7	6.4	6.0
Fabrics	5.2	5.0	5.1	5.6	4.5
Articles of stone	2.2	2.3	2.5	2.9	3.1
Vegetable products	2.0	2.1	2.6	3.0	2.9
Live animals/products	0.8	1.1	1.4	1.7	2.6
Miscellenous manufactures	1.7	1.9	1.8	1.9	1.8
Animal or vegetable fats	1.1	1.1	1.1	1.2	1.7
Precious metals	0.5	0.4	0.3	1.4	1.5
Footwear	1.2	1.1	1.0	1.1	1.1
Pulp of Wood	1.0	1.2	1.1	1.3	1.1
Garments	1.5	1.2	1.2	1.4	1.0
Optical	0.6	0.8	0.5	0.6	0.4
Wood and articles	0.3	0.3	0.2	0.2	0.2
Raw hides and skins	0.1	0.1	0.2	0.2	0.1
Antiques	0.0	0.0	0.0	0.0	0.0
Arms and ammunition	0.0	0.0	0.0	0.0	0.0
Others	0.0	0.0	0.0	0.0	0.0
Total export value (USD bn)	**4.1**	**4.3**	**4.6**	**4.4**	**3.8**

Source: Author's calculation based on data from ITC Trade Map

3. **Thai businesses in Cambodia and Vietnam, particularly in garment and electronics production, could suffer from management problems such as shortage of workers, higher wages, and higher costs for other manufacturing elements.** On the one hand, the diversion of FDI would be favorable as this could help to boost the post-COVID economic recovery and stimulate domestic demand in Cambodia and Vietnam . On the other hand, greater FDI inflows could also increase competition for local workers, which would push up wages, and possibly lead to shortage of labor, particularly for the labor-intensive garment and footwear industries.

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