PITO

PRIVATE INVESTMENT AND TRADE OPPORTUNITIES

ECONOMIC BRIEF
NO. 3

ASEAN COUNTRY PROFILE
THAILAND: THE SIXTH DYNAMIC ASIAN ECONOMY

East-West Center

The *PITO Economic Brief* Series

The Private Investment and Trade Opportunities (PITO) project seeks to expand and enhance business ties between the U.S. and ASEAN private sectors. PITO is funded by a grant from the United States Agency for International Development (AID) with contributions from the U.S. and ASEAN public and private sectors.

The *PITO Economic Brief* series, which is published under this project, is designed to address and analyze timely and important policy issues in the ASEAN region that are of interest to the private sectors in the United States and ASEAN. It is also intended to familiarize the U.S. private sector with the ASEAN region, identify growth sectors, and anticipate economic trends. The *PITO Economic Brief* series is edited and published by the Institute for Economic Development and Policy of the East-West Center, which coordinates the Trade Policy and Problem Resolution component of PITO.

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Thailand is one of the fastest growing and most dynamic countries in the world; nowhere does the private sector seem more alive and vibrant than in Bangkok. The country's outward-looking, market-based policies combined with a stable macroeconomic environment have attracted investors and pushed Thailand into the ranks of the "middle-income" countries. The country is included among the group of six countries called the dynamic Asian economies (DAEs) and is considered by some to be on the verge of becoming one of Asia's "tigers." Nonetheless, its per capita income is still about US$1,200, or one-third that of Korea.

Covering 542,000 square kilometers, Thailand has a population of 55.5 million and total output of US$70 billion (Table 1), making it a middle-sized country as compared to its neighbors. The Thai populace is generally characterized by ethnic and cultural homogeneity. There is a small Muslim population and about a 7 percent Chinese population which is concentrated in Bangkok and which has assimilated well with the general population.

In terms of natural resources, deposits of tin, natural gas, and some petroleum in the Gulf of Thailand are important assets of the country, though its principal natural resource is agricultural land. Rice is the main agricultural product, with maize and cassava assuming importance in the Northeast and rubber in the South. Higher agricultural yields and strong exports of agricultural products have played an important role in Thailand's economic success.

Table 1 Size of ASEAN Countries in 1989

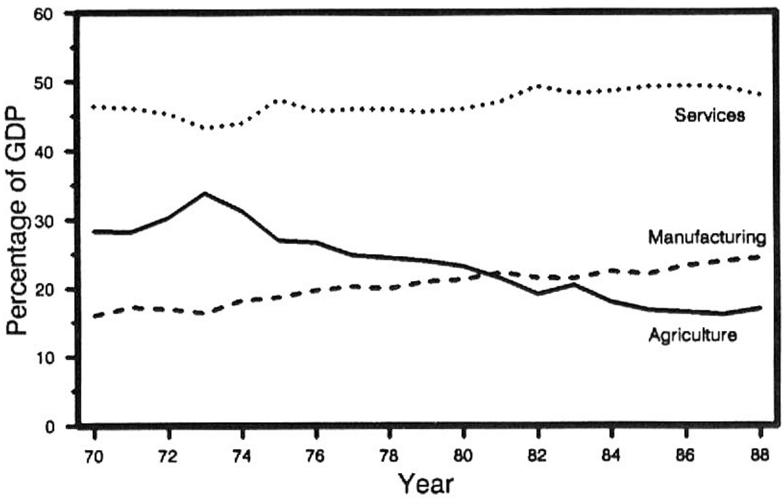
Country	Population (millions)	Area (1,000 km^2)	GDP[a] (US$m)	GDP[a] Per capita (US$)
Indonesia	179.1	1,919	82,726	471
Malaysia	17.4	330	37,453	2,152
Philippines	60.1	300	44,349	738
Singapore	2.7	1	28,360	10,582
Thailand	55.5	542	69,676	1,225

NOTE:
a. 1988 for Indonesia.

The industrial sector, however, has been the main source of Thailand's remarkable growth. Since 1981, the contribution of the manufacturing sector to the country's gross domestic product (GDP) exceeded the contribution of agriculture (Figure 1). Manufacturing now accounts for about 25 percent of GDP, up from about 15 percent in 1970. The services sector is also becoming increasingly important in Thailand, with tourism being a major element in its growth.

Thailand is governed by a constitutional monarchy. Unlike its ASEAN neighbors, Thailand was never colonized by the

Figure 1 Major Sectors of Thailand's GDP



Sources: Asian Development Bank, Key Indicators of Developing Member Countries of ADB, various issues.

Western powers. After 1932 when a coup ended the absolute power of the Thai monarchy, Thailand was governed by military regimes (except for three years of civilian rule in the early 1970s). Nevertheless, the Thai monarchy remains highly respected and continues to play an important role in the government. In 1988, Prime Minister Prem Tinsulanond was forced to step down after eight years of rule due to popular pressure for an elected leader. Chatichai Choonhavan, a close supporter of Prem, was elected. This turned Thai politics into a completely new ball game with some fears of instability due to interparty rivalry and conflicting partisan interests. These fears proved to be warranted; in 1991 there was a military coup which removed the Chatichai administration. The new government consists of a group of technocrats appointed by the military.

In many respects, the overthrow of the Chatichai government was greeted with ambivalence. On the one hand, the coup was welcomed by the Thai populace because corruption and mismanagement had gotten out of hand. Yet, on the other hand, there was a general disappointment in that the military move seemed to be a retrograde step in the evolution of Thai politics.

In terms of social development, Thailand has been highly successful. Since 1960, life expectancy has improved by more than 10 years to 65 years of age (Table 2). Infant mortality rates have dropped by more than 70 percent to 30 per 1,000 births. The country has basically achieved a universal primary educational system. However, the share of young people enrolled in secondary education in Thailand is lower than the average for lower middle-income countries. This has created a bottleneck in Thai industrial development. Although attainment of higher education appears to be high in Thailand, the World Bank reports that only 3 percent of the population have a university degree, and two-thirds of these graduates obtained their degrees from low-quality open universities.

Table 2 Indicators of Social Development in Thailand

	1960	1988
Life expectancy	52	65
Infant mortality rate (per 1,000 live births)	103	30
Literacy rate	62	91[a]

NOTE:
a. 1985.

ECONOMIC TRENDS: PAST, PRESENT, AND FUTURE

Economic growth in Thailand has been consistently higher than the average for developing countries, and in the late 1980s, its growth was the highest in the Asia-Pacific region. After two years of double-digit growth in 1988 and 1989, growth in 1990 was expected to slacken somewhat, due to increasing bottlenecks associated with explosive economic growth, external shocks such as the Middle East crisis, and a looming global recession. However, Thailand maintained double-digit growth in 1990, and although growth rates are expected to drop to about 7 percent in 1991 and 1992, Thailand will continue to be one of the fastest growing countries in the world.

Table 3 Basic Statistics of Thailand

	1960–1969	1970–1979	1980–1989	1988	1989	1990[a]	1991[a]	1992[a]
Growth of real GDP	8.3	7.4	6.9	13.3	12.4	10.3	7.0–7.3	6.8
Export growth	7.4	23.8	15.2	35.9	26.7	16.0	13.0	13.0
Import growth	11.5	20.2	15.4	56.9	23.7	25.0	17.0	16.0
Inflation rate	2.2	8.0	5.8	3.9	5.4	5.5–6.0	6.1–6.3	5.1
Debt service ratio (period average)	na	12.5	18.5	19.3	10.0	na	na	na
DFI inflow (US$m) (period total)	154[c]	738	3,324	1,118	na	na	na	na

NOTES:
na = Not available.
a. Estimate/projection.

A large factor for this growth is the sound macroeconomic policies of the government. Overall, the fiscal and monetary policies of the government have been conservative, even by Asian standards. Inflation has been increasing since 1987 when it was about 2 percent, but remains moderate at about 6 percent in 1990. This increase is partly due to rising import prices and the overheating of the domestic economy. Inflation is expected to remain between 5 and 6 percent over the next two years. The Thai baht has remained extremely stable at about 25 baht/dollar throughout the 1980s when it was devalued from the 20 baht/dollar that had been maintained for the previous three decades. There is every indication that the new government will remain committed to macroeconomic stability.

Another important element for Thailand's surging growth is its emphasis on market initiatives. The private sector is given relative freedom to pursue its goals. Further liberalization of the domestic economy occurred in the 1980s with the enactment of an export promotion policy. Export procedures were streamlined and investment for export activities was promoted. Investors were granted tax benefits and special services to facilitate exporting.

In response, exports boomed in the late 1980s. Export growth rates exceeded the rate of growth of GDP throughout the past two decades, resulting in a growing share of exports to GDP from about 15 percent in 1970 to 25 percent presently. Export growth slowed in the 1990s but is likely to remain higher than GDP growth. Import growth has exceeded export growth, accounting for 36 percent of GDP. Imports will continue to grow rapidly due to imports of oil and capital and intermediate goods which are needed to support Thailand's industrial expansion.

The United States has assumed increasing importance as an export market for Thailand over time, and presently purchases 20 percent of the country's exports. The share of Thai exports destined for Japan rose until the mid-1970s after which it fell to about 16 percent of the total, which is slightly higher than Thailand's exports to other ASEAN countries. In terms of imports, Japan still provides more than 30 percent of the total import bill, though this represents a declining trend. The United States has been able to maintain its share in the Thai market, accounting for about 14 percent of total imports and is second only to Japan. Thai imports from other ASEAN countries have increased markedly from about 3 percent of total imports in 1970 to more than 11 percent today.

Corresponding to the changes in the direction of trade and the higher level of industrialization, the commodity composition of Thai exports and imports have changed substantially. Shares of primary products exports declined continuously from 96.5 percent in 1963 to about 50 percent presently. The sharpest declines were in rice, tin, and rubber, while vegetables and fish became more important. In turn, the share of manufactured products increased from 2.5 percent in 1963 to about 50 percent today. Manufactured exports are dominated by textiles, apparel, leather products, jewelry, and integrated circuits. More recently, electrical machinery has also become important. Imports continue to be largely made up of industrial goods—including chemicals, machinery and transport equipment—which support the country's rapid growth and industrialization.

A consequence and further stimulus to the country's domestic growth in recent years is the surge in direct foreign investment (especially since the last quarter of 1986). Japan has been the largest investor, accounting for 41 percent of total direct investment in 1989; Taiwan, the United States, and Hong Kong each account for about 10 percent. Investment approvals and applications for promotion privileges have increased and many large investment projects that had been approved in previous years are now on-line.

PROSPECTS FOR THE THAI ECONOMY

Thailand has had to decide how to sustain the present high growth without overheating the economy and without undermining stability. On the fiscal front, the government has moved to reduce income taxes and has raised the interest rate ceiling to discourage inflation. To encourage trade and investment activities, Thailand has accepted Article 8 of the IMF and moved to eliminate restrictions on international payments and transfers. It has also recently announced reductions in tariffs for machinery and computer imports to facilitate investment and modernization of its industries. The tariff on automobiles (parts and completely assembled) has also been slashed drastically to force the Thai industry to become competitive. Bans on new factories in some restricted industries have also been lifted.

Thailand is also faced with the issue of how to distribute the benefits of high growth more evenly. To this end, the government has raised the minimum wage, and the Ministry of Finance has moved to increase use of direct rather than indirect taxes. Major new overhead investments, especially outside of Bangkok, have also been planned to improve income distribution. The development of the Eastern Seaboard, in particular, has attracted much interest due to the success of the first project in this development, a petrochemical plant.

In recent years, some bottlenecks to the rapid industrialization have appeared. First, the demand for skilled labor has increased. While Thailand has experienced significant improvements in social development, shortages of skilled labor are beginning to push up costs. It is now widely accepted that major structural reforms will be required in education and research and development if Thailand is to maintain its competitiveness into the 1990s. There is a long lag before changes in education policies affect the labor force, however, and continued shortages are expected to be a major bottleneck in the medium term.

Second, the lack of adequate transportation and communications infrastructure and water shortages have been cited as a problem by prospective investors. Bangkok traffic jams are legendary and international phone calls are relatively expensive to make. Although the Thai government has plans to alleviate some of these concerns, progress is viewed as being too slow. Its plan for privatizing the Electricity Generating Authority of Thailand (EGAT) may begin to move forward as the new government's effective ban on unions has eliminated a major source of opposition to the plan. Delays in other infrastructural projects are of great concern, however. The continued strong economic performance will ensure that profitable trade and investment opportunities still exist but the government must take action to keep these bottlenecks from choking growth. Some industries and issues of interest are discussed below.

<u>Automobiles</u>. A great deal of change and restructuring will occur in this industry as companies adjust to the massive tariff reduction which occurred in July 1991. The Thai automobile industry has been a sacred cow; the high rate of protection has made automobiles in Thailand among the most expensive in the world. In a dramatic move, the government ended this protection

to force the fledgling industry to grow up. Tariffs on knock-down units dropped to 20 percent from more than 100 percent, while tariffs on finished automobiles were reduced to 60 percent from 180 percent for compacts and to 100 percent from 300 percent on mid-size models. Despite the decrease in protection, foreign automotive companies in Thailand are increasing production citing the differential between knock-down units and finished autos as being sufficient. This attests to the increasing competitiveness of the Thai automotive industry and may lead to further expansion in the industry.

Financial Services. The financial sector in Thailand has also become more liberalized and modernized, though banking remains one of the most restricted sectors in Thailand. The number of banks is controlled by the government; there are 15 commercial domestic banks and about the same number of foreign banks. The deregulation on foreign exchange, however, allows Thailand easy access to foreign markets. The government has cautiously begun to institute reform to broaden the scope of activities in this sector, but is likely to continue to restrict entry. Other financial sectors have also been modernizing in recent years. The volatile stockmarket has been growing rapidly.

Intellectual property rights. One of the key trade and investment issues involving Thailand is the lack of protection of intellectual property rights. This issue is especially sensitive in pharmaceuticals which is excluded in Thailand's current patent law (among other products) but the issue is also important in other industries due to the lack of enforcement of the patent law.

Negotiations are presently continuing between the United States and Thailand. There is evidence that changes are in store as Thai firms begin their own research and development activities and feel the need for stronger intellectual property rights protection. The Thai government has already begun to take steps to increase enforcement which may encourage foreign companies that have been reluctant to invest in Thailand in the past.

In conclusion, Thailand is a truly dynamic economy. Inflationary pressures and infrastructural and labor bottlenecks related to rapid development will moderate this country's growth, but Thailand will remain one of the fastest growing economies in the world.

Table Sources

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