

Chapter 1

Introduction

Thailand's economic development has gone through a number of phases. While the war in Vietnam was still continuing with American military personnel stationed here, until the mid-1970's, Thailand approached international banks for recommendations on the strategy it should employ in planning its growth. Both social and economic policies were initiated focusing on lowering birth rates, raising standards of living, education and medical care in the rural areas, and putting Thailand's resources to their most effective use. Promoting tourism was one of the first economic initiatives. Increasing foreign investment, with a focus on exports and not hiding domestic industries behind a high tariff wall were also approaches recommended and implemented. By the early 1980s Thailand was experiencing its first industrial revolution based on liberalisation of capital markets and the establishment of manufacturing.

In the four years, 1987-91, more and more large industrial plants diversified their production ensuring that a wider variety of Thai products were shipped to markets in North America, Europe and Asia. But a number of external developments in the early 1990s affected the world economy and the Thai economic cooled down. The Gulf War in 1991 and the U.N. sanctions against Iraq affected Thailand's markets in the Middle East.

In 1995 and 1996 the Mexican peso crisis, which shook investor confidence in the emerging markets, made financing of these deficits increasingly difficult. The appreciation of the US dollar further weakened Thailand's export competitiveness, as its currency, the baht, had been effectively fixed to the US dollar. This weakness in the Thai economy induced a strong attack on the baht in February and again in May 1997.

The performance of Malaysia remained strong in 1995, with growth in real gross domestic product (GDP). The strong growth in 1995 reflected higher domestic

demand and sustained export growth. In 1996, the moderation in economic activity was due primarily to a slowdown in aggregate domestic demand. In 1997 Malaysia was also caught in the severe and prolonged regional currency crisis that has swept across East Asia. At the early stage of the crisis, foreign analysts and international fund managers had placed Malaysia in the same category with the other countries in the region.

Economic indicators were selected for this study, which involves a comparison between Thailand and Malaysia. This study investigates the trend and pattern of economic indicators in both countries. Economic indicators indicate the economic system in many countries, and which countries have better economic systems than others.

Thailand and Malaysia were selected in this study because they are located in Southeast Asia and both have a democratic governments system. The period of this study is from 1983 to 1996, before the economic crisis occurred in the region.

The following components define the economic indicators and related information in Thailand and Malaysia.

Economic Indicators

The economic indicators of this study are composed of six leading indicators, namely economic growth, international reserves, the money supply, the value of exports, the value of imports, and the trade balance. The unit of economic indicators from this study used US\$ in both countries.

1. Economic Growth

Defined quite generally, economic growth is the expansion of an economy's capacity to produce goods and services that takes place over prolonged periods of times, year in and year out, from decade to decade, from one generation to the next, or even over the course of centuries (Waud, 1986: 406).

The sources of economic growth are determined by disentangling the observed interrelationships between such variables as (a) population growth, (b) investment, (c) labor supply, (d) the stock of capital, (e) technological advances, and (f) other factors such as social and political policy (Thomas and McDougall, 1980: 263).

2. International Reserves

A country's international reserves may be defined as the resources at the disposal of the monetary authorities for purposes of intervention in the foreign exchange market. To give empirical meaning to this concept, it is necessary to define somewhat more precisely the qualities that assets must possess to qualify as international reserves. Two criteria are most commonly used: the assets have to be liquid, and they must be unconditionally available to the monetary authorities. The types of assets that qualify under this operational definition vary from time to time. At present there is wide agreement that the four following assets should properly be regarded as constituting a country's international reserves (Heller, 1974: 176-185)

2.1 Gold

Gold is the most traditional component of international reserves. It has been used as a monetary metal and reserve asset for centuries and continues to play an important role on the international monetary scene.

2.2 Foreign Exchange

Convertible foreign currencies are another component of international reserves. We stated previously that international reserves are held by the monetary authorities for intervention purposes in the foreign currencies with which they can directly intervene in the foreign exchange market. The currencies that are widely held by other countries as part of their international monetary reserves are generally referred to as key currencies or reserve currencies. Traditionally the pound sterling has played an important reserve currency role, but since World War II, the US dollar has assumed the dominant role.

2.3 IMF Reserves Position

The International Monetary Fund (IMF) was established in 1944 and one of its main functions is to provide a source of international reserves for its member countries. Upon becoming a member, a country is assigned a quota that establishes the basis for the country's rights and voting privileges with the IMF. Once the quota is established, the country has to make a subscription payment to the IMF that is equal to its quota. Twenty-five percent of the subscription is payable in gold, and the remaining 75 percent in the country's own currency. By this device the IMF acquires an initial stock of member countries' currency, which it can lend to countries that find themselves in balance-of-payments difficulties.

2.4 Special Drawing Rights

In 1968 the Articles of Agreement of the IMF were amended to allow for the provision of Special Drawing Rights (SDR) in addition to the facilities of the general account. These SDRs are allocated to countries in proportion to their quotas. Any new SDR allocations must first be proposed by the managing director of the IMF, concurred to by a majority of IMF's executive directors, and then approved by an 85 percent majority of all votes of the IMF's Board of Governors.

The main difference between the IMF general account and the Special Drawing Rights lies in the fact that in the general account the IMF does not engage in new asset creation, while it does so in the case of SDRs. In the general account the IMF makes currencies previously paid in one member country available to other member countries. In the case of the SDR account, the IMF creates an entirely new reserves asset that constitutes a net addition to world reserves.

The effect of financing a balance-of-payments disequilibrium on a country's international reserves is rather direct. Whenever there is a balance-of-payments surplus, the country's reserves holdings will increase, and when there is a balance-of-payments deficit its reserves will decrease.

In most circumstances, an increase in a country's monetary reserves will be accompanied by an increase in its own money supply. The reason for this linkage is obvious: a country that runs a balance-of-payments surplus finds that there is an

excess demand for its own currency. If the monetary authorities want to prevent the currency from appreciating in international markets, they sell their own currency against gold or foreign exchange that is added to their international reserves. But the sale of the country's own currency increases the money supply in the hands of the public (Heller, 1974: 206).

3. Money Supply

A country's money supply is the total quantity of money existing at a point in time. Definitions of money supply are as follows (Case and Fair, 1992: 717-719).

3.1 The narrowly defined money supply (M1) is the value of all currency (including coins and notes) held outside of bank vaults, in addition to the value of all demand deposits, travelers cheques, and other checkable deposits.

$$M1 = \text{Currency Held Outside Banks} + \text{Demand Deposits} + \text{Travelers Cheques} \\ + \text{Other Checkable Deposits}$$

3.2 The broadly defined money supply (M2) includes all items in M1 savings accounts and money market accounts. This study used M2 to analyse the data.

$$M2 = M1 + \text{Savings Accounts} + \text{Money Market Accounts}$$

The money supply depends on various factors, such as open market operations, the rediscount rate or bank rate, the legal minimum reserve requirement, and the interest rate.

4. Exports and Imports

Exports comprise the goods and services produced by one country which are sold to another in exchange for the second country's own goods and services, for gold and foreign exchange or in settlement of debt. Countries tend to specialise in the production of those goods and services in which they can be relatively most efficient, because of their indigenous factor endowment (Black, 1997: 167).

Imports comprise the flow of goods and services that enter for sale into one country and which are the products of another country (Black, 1997: 220).

The value of exports is calculated from free on board and imports is calculated from cost, insurance and freight, which the following components.

4.1 Free on board is commonly abbreviated as 'fob', is a term of trade that must be accompanied by a named port of shipment. For example, a price quoted as 'fob Rotterdam' includes the cost of the goods/cargo concerned and all expenses up to the point when they have been loaded onto a ship in Rotterdam.

4.2 Cost, insurance and freight, commonly abbreviated as 'cif', is term of trade that must be accompanied by a named port of destination. For example, a price quoted as 'cif Singapore' includes the cost of the goods/cargo concerned, insurance, freight and all expenses up to the point when the ship has docked in Singapore.

Because imports are purchases of goods and services by domestic consumers, we expect them to be influenced by current income in the same general way that domestic consumption is influenced by current income. Accordingly, imports are usually taken to be a positive (upward sloping) function of income. A second important determinant of imports is the relative price structure of domestic and foreign goods, the demand for domestic goods will rise for all the products and services where domestic and foreign goods are important substitutes. The relative prices of foreign and domestic goods are influenced not only by the selling prices of these goods in the respective nations, but also by the rate of currency exchange.

By similar reasoning, exports may be thought of as largely dependent upon the level of income available in the groups of nations that are the domestic nation's trading partners, since domestic exports are imports for foreign nations (Elliott, 1979: 259-260).

5. Balance of Trade

A country's trade balance is the excess of visible exports over visible imports. This is the major, but far from the only, component of the balance of payment on the current account (Black, 1997: 22).

Background

Some information is now given about the two countries considered in our comparative study.

1. Thailand

Location: Located in the heart of Southeast Asian and as a gateway to Indochina, Thailand is bordered by Laos to the north east, Myanmar to the west, Cambodia to the east and Malaysia to the south.

Area: Thailand covers a land area of 511,770 square kilometers, extends about 1,620 kilometers from north to south and 750 kilometers at its widest point from east to west. Coastline approximately 3,219 kilometers on the Gulf of Thailand and 865 kilometers along the Indian Ocean.

Population: The country has a population of 59.5 million (July, 1997 est.) of which around 10 million live in the capital city, Bangkok. The most important ethnic minority is Chinese. Other minority groups include Malays, Kampuchians, Mon, Lao and various hill tribes.

Government: Thailand has been a democratic constitutional monarchy since 1932. Under the present constitution, the parliament is composed of 270 appointed senators and 360 elected representatives. There were seven Prime ministers from 1983 to 1996.

Economic Overview: One of the more advanced developing countries in Asia, Thailand depends on exports of manufactures including high-technology goods and

the development of the service sector to fuel the country's rapid growth, averaging 9% since 1989. Most of Thailand's recent imports have been for capital equipment and raw materials, although imports of consumer goods are beginning to rise.

Industries: Thailand's main industries are tourism, textiles and garments, agricultural processing, beverages, tobacco, cement, light manufacturing, such as jewelry, electric appliances and components, integrated circuits, furniture and plastics.

Agriculture: Products comprise rice, cassava (tapioca), rubber, corn, sugarcane and coconuts.

Exports:

Commodities: The commodities in exports are as follows: manufactures, agricultural products, fisheries, raw material and fuels.

Partners: The proportions of the value of exports in Thailand to other countries are as follows: USA 21%, Japan 17.1%, Singapore 13.6%, Hong Kong 5.3%, Germany 3.5%, UK 3%, Netherlands 2.8% and Malaysia 2.4%.

Imports:

Commodities: The commodities in imports are as follows: manufactures, fuels, raw materials and foodstuffs.

Partners: The proportions of the value of imports in Thailand to other countries are as follows: Japan 30.4%, USA 11.9%, Singapore 6.3%, Germany 5.8%, Taiwan 5.1%, Malaysia 4.9%, South Korea 3.7% and China 2.6% (Carpenter, 1994: 338-339).

2. Malaysia

Location: Located in the Southeast Asia peninsula and northern one-third of the island of Borneo, bordering Indonesia and the South China Sea and Thailand.

Area: Malaysia has total area of 329,750 square kilometers, including a land area of 328,550 square kilometers, and a water area of 1,200 square kilometers.

Bordering countries are Brunei 381 kilometers, and Indonesia 1,782 kilometers, Thailand 506 kilometers.

Population: The country has a population of 21.3 million (1997). The ethnic groups are Malay and other indigenous 58%, Chinese 26%, and Indian 7%.

Government: The Federation of Malaysia, formed 9 July 1963, is nominally headed by the paramount ruler (king) and a bicameral Parliament. The Prime Minister is Dr. Mahathir bin Mohamad (since 1981).

Economic Overview: The Malaysia economy, a mixture of private enterprise and public management, has posted a remarkable record of 9% average annual growth in 1988-1996. This growth has resulted in a substantial reduction in poverty and a marked rise in real wages. In 1996 manufactured goods exports expanded less rapidly than in previous years because of the global slump in electronics. Nonetheless, foreign investors continue to commit large sums in the economy. The government is aware of the inflationary potential of this rapid development and is closely monitoring fiscal and monetary policies.

Industries: Malaysia's main industries are rubber and oil palm processing and manufacturing, light manufacturing, electronics, tin mining and smelting, logging and processing timber, and petroleum production.

Agriculture: Products comprise natural rubber, palm oil, rice, subsistence crops, rubber, timber, coconuts and pepper.

Exports:

Commodities: The export commodities are as follows: electronic equipment, petroleum and petroleum products, palm oil, wood and wood products, rubber and textiles.

Partners: The proportions of the value of exports in Malaysia to other countries are as follows: USA 21%, Singapore 20%, Japan 12%, Hong Kong 5%, UK 4%, Thailand 4% and Germany 3%.

Imports:

Commodities: The commodities in imports, namely machinery, equipment, chemicals and food.

Partners: The proportion of the value of imports in Malaysia to others countries are Japan 27%, USA 16%, Singapore 12%, Taiwan 5%, Germany 4% and South Korea 4% (1995) (Carpenter, 1994: 333-334).

Objectives

The objectives of this study, which includes:

1. To investigate the elementary character and pattern in economic indicators in Thailand and Malaysia in the period from 1983 to 1996.
2. To compare the economic indicator means between Thailand and Malaysia.
3. To compare the differences in economic indicators between Thailand and Malaysia by using time series analysis.

Research Hypotheses

1. The patterns and trend of economic indicators should be similar in Thailand and Malaysia.
2. The means of economic indicators may not be different in Thailand and Malaysia.

Review of Literatures

Atukeren (1995) presented the Granger-causality between exports, imports, and economic growth in 32 developing countries. The role of the imports variable in the investigation of exports-output causality was emphasized, enabling one to test for

the cases direct causality, indirect causality, and spurious causality between export growth and output growth.

Felipe (1995) studied an empirical analysis of the determinants of long-run growth and technical progress in five Southeast Asian countries, Indonesia, Malaysia, the Philippines, Singapore, and Thailand, i.e., the ASEAN countries, during the last three decades. He had tested different endogenous growth models, and had analyzed whether the determinant of technical progress proposed by each of the models. His empirical finding indicated that an important determinant of long-run growth in the ASEAN countries was imports of foreign technology. The role of exports, except in Singapore, was not so clear. Education, exports of machinery and GDP growth was important determinants of growth in all five ASEAN countries.

Ibrahim (1996) showed that relationship between exports and growth of GDP of countries in the Asian region seems stronger than within countries of the Western Hemisphere region. The relationship between the growth of GDP and exports appeared stronger where there was an outward trade orientation. Other factors that appeared to be associated with the performance of exports include the diversity of exports and the level of processing for the export products. In the study of externality effect of the export sector on the non-export sector, it was found that the composition of export products was probably one of the major factors that determine the extent of the externality. Positive externalities from the export sector were found in countries that export products with linkages to other ancillary industries.

Levy (1993) found a relationship between the variance in growth of the money supply and the volatility of interest rates and money demand. This research also found that monetary policies, which were not sufficiently sensitive to changes in interest rates, were likely to result in higher expected interest rates and a higher variance of interest rates in the long term.