

Industrialisation and Inequality in Thailand*

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Introduction

Although Thailand has of late been regarded as a newly industrialising economy (NIE) by international organisations such as the World Bank (1993), the Thai people face acute problems that are rarely seriously discussed. Indeed, it might be too early to cite Thailand as an NIE. Thailand's economic development over the last three decades has obviously not been successful in the areas of human development and income distribution (in contrast, it might have failed in enhancing the quality of life as a whole) in the rural areas. Economic growth in particular seems to be impressive, but income inequality is rising. In fact the uneven development can invariably be seen as a *trade-off* between the agricultural and industrial sectors or between the rural and urban sectors or between Bangkok and the provinces. For years, the rural poor have been trying to solve their present difficulties by persistent migration from rural areas to seek work in Bangkok and other big cities, principally in the so-called "informal sectors". However, the picture of Thailand painted by some international organisations, namely the World Bank and the IMF, seems to be blurred by high economic growth. The severe effects and externalities of the industrialisation process have been paid less attention. The terrible fire at the Kader factory, in May 1993, in which nearly 200 workers were killed and

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hundreds were injured is only one example. Thai safety measures have been unable to protect workers sufficiently and it is also clear that the Thai safety standard has lagged far behind the country's rapid economic growth. In fact, the production structure is characterised by the hallmarks of an agrarian country.

Although manufactured exports have been growing rapidly, at a rate similar to those of the East Asian NIEs in the 1960s and 1970s, population and employment structures are overwhelmingly rural-based. The share of the labour force engaged in agriculture appeared to be 70 per cent in 1986, declining to about 65 per cent in the 1990s. A very high proportion of the labour force in agriculture suggests that a long-term deterioration of rural living standards is quite likely, in particular a low consumption rate at a low level of economic development. The prevalent unresolved problems are presented in the next section. In addition, it is pointed out that any attempts made by the Thai state to alleviate poverty in rural areas remain ambiguous.

The aim of this chapter is to analyse whether the economic policy reforms of the early 1980s may have been too few and too late to solve a rising unbalanced growth, to eradicate poverty in rural areas and to lessen depletion of natural resources that is certainly a hazard of industrialisation. The *neo-institutional economics* regarding the state will be applied in the Thai case. This paper also tries to adapt economic theories, to learn from economic history and to understand the key institutions with regard to the Thai economy. In a discussion of *the role of the state*, it will take up the point that major institutional changes are the most essential and critical to bring about agricultural modernisation and determine how far Thai industrialisation can proceed. In other words, the country can further set back high sustainable economic growth if the squeeze from the agricultural sector still persists. Rapid increases in the productivity of agriculture will be of major importance for domestic demand to absorb manufactured goods from a modern industrial sector. The agricultural sector should in turn be subsidised by the state to improve its productivity and living standards. These points are identified through a comparison with the experience of the East Asian NIEs in economic policy reforms and the role of the state.

A Conceptual Framework

Thailand began its integration into the world economy in the middle of the 1880s and has emerged as the major supplier of rice to the rest of the world, in particular the ex-colonies of Great Britain (Ingram, 1971). Modern Thai economic growth, however, only began in the late 1950s (see Falkus, 1992, Ingram, 1971; Muscat, 1994, Warr, 1993; Yoshihara, 1995). Most of the Thai leaders clearly show their interest in modernising the country from agricultural to industrial and yet the Thai state might be considered somewhat inclined to being predatory to the extent that Thai leaders may have taken out so much of the scarce resources, but put back so little in the way of public or collective goods; very low productivity in agriculture, weak human capital development and miserable poverty in the rural areas. There is thus ample reason to cite the Thai state as not developmental but predatory.

First of all, the outcome of economic development in the last four decades suggests that the Thai state was entirely controlled by the ruling elite; the military, vested-interest groups (mostly ethnic Chinese), and bureaucrats who seem to plunder without providing adequate welfare to their citizens in the terms of education, health care, the provision of pure water supply and adequate sanitation and the like.

Second, the Thai state seems to be unique in the sense that it has been rather weak in making any coherent policy effective. The most crucial stated policies (e.g., land reform or income distribution policy) have always been implemented, but in a somewhat diverse direction which has proved insufficient in the end. This is very likely intertwined with the unbounded power of bureau which might have led to arrogance, overconfidence and a perception of anti-democracy that often results in chaos and disorder. Any demonstrations were kept minimal or prohibited in order to make the country peaceful enough to attract foreign investment. The East Asian NIEs (except Hong Kong) were very strong (in terms of a degree of relative autonomy from vested-interests in decision-making) and effective while civil society or other social and economic forces were weak. On the contrary, the Thai state has been shown to be relatively weaker as it has been unable to *insulate* itself from vested-interest groups who have reinforced their political power. The assumption of the neo-classical economists that the state is well-intentioned, well-informed and competent appears to be a little off the mark. In reality, the state might be manipulated and incompetent; however, in the case of Thailand government failure is indeed the case. *Nevertheless, the Thai case is fascinating in the sense that in the 1930s the armed-forces have*

never held absolute power as they has in Indonesia, South Korea or Taiwan. The Thai monarchy, being the absolute source of legitimacy, is above politics and makes Thai political economy unique.

Third, the main failure emerges from the fact that the Thai bureaucracy, which evolved from a *Thai Sakdina (feudal) autocracy*, has turned out to be huge and clumsy as a monster (see Riggs, 1966; 1993). The rigidity of the hierarchical system of Thai bureaucracy has made it a *klepto-patrimonial* instead of a *meritocratic bureaucracy* since World War II (see Evans, 1989, 1992, 1995). In fact, there has been no substantial change in the Thai civil servant system since King Rama V reformed it. Power was exercised by the King in the past, but by *elected* ministers, technocrats and bureaucrats in the present day. The embedded merit system in the Thai bureaucracy has been gradually deteriorating to the system's disadvantage in that material incentive (its salaries) are rather low despite a very rapid transformation of the country's economic development (see Christensen and Siamwalla, 1993). It is said that a bureaucrat's class has dropped to the status of the new poor and the morale of organisation has been weak, but the power structure is still entrenched. The administrators have held the power to administer the country under a very long authoritarian regime. Public law was implemented by bureaucrats who could easily abuse their power due to the absence of the constraints of accountability to a civil society. The legal authority for administrative measures and the operation of the bureaucracy as determined by the King in the old days have been divorced from public liability and accountability (Rosenbergs, 1958). This is very prevalent in the Thai political structure which has remained little changed after 60 years of semi-democracy or the so-called "soft-authoritarian regime" (Chamarik, 1981; Samudavanija, 1989; 1992). The military, the technocrats and their business (sino-Thai) and academic allies have repeatedly been appointed to the senate in this period and are instrumental in maintaining *kleptocracy*. Hence, discretionary power and arbitrariness were mostly untouched by administrative law. Although royal servants were broken up after the people's coup in the 1932, civil servants have been taking over and manufacturing obedience.

Fourth, it is worth noting that the Thai state has been unable to foster long-term entrepreneurial perspectives among indigenous private elites, thereby lacking the one crucial type of state action in Gerschenkron's typology; the state must create the so-called "state entrepreneurial actions to substitute for missing

entrepreneurship." In reality, transformation has somehow been impeded rather than promoted by the Thai State and the consequence is that there are relatively few Thai entrepreneurs in commerce and industry. *Moreover, commercialisation in the Thai countryside is extremely insignificant and dominated by ethnic Chinese middlemen who are seldom autonomous, but subservient to an autocrat, aristocrats, and later, the military.* Some Thai left-wing writers go further by characterising them as parasites or ersatz capitalists.

Fifth, the political regime has been mostly authoritarian (soft) in nature, albeit the very short period of a full democracy during 1973-1976 and after the 1990s. The agricultural sector (rice farmers) has been heavily squeezed to lend support to the industrial sector in Bangkok and the peripheries. Productivity in the agricultural sector appears to have been stable and increasing at a very low level due to the resource endowment; land-abundant until the late 1970s (Siamwalla, 1989; Siriprachai, 1995). If Thailand had not had plenty of unused land, agricultural productivity would not have been severely set back. A neo-Malthusian ghost seems not to threaten in Thailand. The population in Thailand was only 11 million in 1929, 17 million in 1947 and 26 million in 1960, while the size of the country is about that of France. This *initial condition* of rich natural resources made it possible for the Thai state apparatus to take out and dissipate unproductive rents when industrialisation was getting started. In other words, Thai peasants could exhaust natural resources longer compared to scarce-resource countries like the East Asian NIEs. However, the agricultural sector could have contributed well to economic growth without turning forest land into cultivated areas, if the Thai state had generated rapid technological progress. The so-called "green revolution" has never had a chance to take root in the Thai economy owing to the deficiency of irrigated water. Existing dams, drainage and reservoirs are rather insufficient for success in developing and disseminating the new technologies. Furthermore, the infant industries such as those producing fertilisers and agricultural machines, sold at high prices to the agricultural sector, are protected by a high tariff wall. Thus, high economic growth was extensive rather than intensive. Besides, economic growth has been concentrated in Bangkok which is often cited as the world's leading primate city, and today houses about 8 million. This concentration of growth and industrialisation in the metropolitan area has inevitably been giving rise to *uneven development and inequality* leading in turn to an income's gap. *The performance of industrialisation suggests that intersectoral conflict and accumulated rural-urban antagonism will be occurring* (Aeusrivongse, 1993; Samudavanija, 1992).

The developmental states of the East Asian NIEs, especially South Korea and Taiwan, cannot simply be emulated by the Thai state because the state and institutional settings are so much different in historical and social contexts. Both historical and institutional factors do matter, but how and why they do matter will be put forward in this article. It is also argued that there is *no immunity* to the rent-seeking activities in Thailand that will be analysed at length below.

The Thai state might have functioned well in protecting individual rights, persons and property and enforcing voluntarily negotiated private contracts, but it has failed to create a strong domestic market and eradicate poverty in the rural areas. The strategy of the developmental state is quite difficult to achieve in Thailand and this is closely attributed to a relatively backward agricultural economy. The Thai state has been playing a contradictory role, compared to South Korea or Taiwan, in not closing the productivity gap between agriculture and industry. Thus, a backward dualistic economy continues to exist, although the Thai state, since the late 1950s, has attempted to industrialise with import-substituting industries that seemed unlikely to be successful in adapting new technological skills and absorbing surplus labour. This shortcoming is further constrained by an inflexible institutional factor, particularly in its *key* institutions; the lack of a hard state or relative state autonomy to give birth to the threat of penalising unproductive firms (see Amsden, 1989; Evans, 1995; Grabowski, 1994; Kohli, 1994; Wade, 1990). *Moreover, it has been forgotten that the experience of the East Asian NIEs lay not so much in foreign investment and multinational corporations, but in national capital and national industrialists as well as in building up an educated populace rapidly. This entails fostering internal articulation and achieving technological autonomy.* In fact, import-substitution industrialisation might not have failed if it had been inseparable from substantial improvements in agricultural productivity and income distribution that could in turn absorb domestic manufactured goods. *Such a process has always been taken for granted by the Thai ruling elite who were obsessed with a market mechanism in a neo-liberal paradigm which could have been a great help in linking the import-substituting industries to the relative backwardness of agriculture.* The point is that productivity in the agricultural sector has not been substantially upgraded as opposed to the industrial sector. In fact, Thai agriculture was dominated by the vestiges of *Sakdina* (Thai feudalism) with cultivation techniques dating back to the previous century. In addition, the Thai bureaucracy is not professionally competent enough to prevent the ruling elite and entrenched interest-groups from extracting and distributing

unproductive rents. It is undeniable that rent-seeking in the Thai society is always closely linked to public policy and allocation of scarce resources. Thus, the increased social injustice and income inequality not only remain unchanged, but also rise over time and space. In other words, that income is distributed more unequally in Thailand than in the East Asian NIEs is a fairly safe proposition to cite. In view of this, it is surprising that there has never been a major peasant uprising in this country.

Since the middle of the 1970s, the Thai state has been turning its strategy to export-led industrialisation, but the fundamental obstacles, i.e., the shortage of infrastructure, the lack of skilled labour and low secondary enrolment, the low productivity in the agricultural sector and impoverished rural inhabitants who are mostly farmers, are seldom overcome. Although the new development strategy seemed to keep economic growth high mainly with the influx of direct foreign investment from Japan, the East Asian NIEs and Western countries in recent years, the basic failure of the industrialisation process, as mentioned above, still prevailed under the same institutional setting. In fact, the institutional arrangements appear to have become worse off in so far as the rise of money politics and vote-buying has been encouraging corrupt politicians. In addition, the relative backwardness of the agricultural sector has resulted in presenting an unintended opportunity to not only urban bourgeoisie and ex-technocrats, but also local capitalists and influential persons who rallied to Parliament. Thus, electoral politics is believed to have paved the way for them to legitimise their power and plenty under the money politics. However, to understand the political economy of industrialisation in Thailand, we must turn back to import-substitution policy in the late 1950s which has had an impact on the present and future Thai economy.

State Promotion of Industrialisation

Under the Sarit government, industrial promotion policy was renewed by the Promotion of Industrial Investment Act of 1959. The Board of Investment (BOI) was set up in the same year. In addition, the Budget Bureau (1959) and the Office of Fiscal Policy (1960) were also established. This period saw the second rudimentary institutional change after the Chakri Kings had undertaken political and economic reforms in the mid-nineteen century. The multiple exchange rate regime and large-scale state enterprises came to an end. The former was replaced by export taxes and a fixed exchange rate while the latter

was concerned with infrastructure development. *The role of the Thai state was also believed to be a social guardian or a benevolent dictator and to provide a stable investment environment for the private sector* (Chaloemtiarnana, 1979). Investment incentives were given to selected import-substituting industries. The three, inconsistent, stated objectives were expected to reduce Thailand's dependence on the import of foreign goods, to raise the level of income through increasing value added and to save foreign exchange on import expenditure (Santikarn and Isrankura, 1988). Moreover, the Thai state began to engage in a massive campaign to attract foreign entrepreneurs to Thailand. The state even guaranteed and granted licences to foreign companies. In addition, labour unions were also suppressed by means of a martial law for years.

There is little doubt that the first easy stage of import substitution was inevitably successful in the late 1960s and the small domestic market was also easily exhausted. Nevertheless, a high protection rate and a set of incentives provided by BOI gave rise to inefficient, promoted manufacturing firms. One simple reason for this is that Thai authority was rarely concerned with discipline. The new bureaucrats were not modern civil servants, but worked for themselves. They were dynastic rather than public servants. The possession of legal and social privilege permitted them to seek economic rents from public policy. Performance standards were loosely imposed by the strongly entrenched officers in BOI on the recipients of protection. It is worth noting that the Sarit idea of industrialisation is believed to have come from his reading of the Beitzel Report in 1959 and other similar reports supported by American advisers (Beitzel, 1959, Loftus, 1956; 1962; Patamanan, 1985). The report resulted in the Thai government revision of the investment promotion law in 1962. American advisers were keen to manipulate the Thai policy-making process, in particular the first three national economic development plans (1961-1976), and were supported by Thai technocrats (see Stifel, 1976; Thanapornpun, 1990). Sarit was very keen to mitigate the role of the state-owned enterprises playing a significant role in the preceding period, but only shifted these privileges to the market. Ironically, new groups, of course, began to benefit from the new circumstances. Sarit and his associates did not refrain from carrying on their own private business outside the state-enterprise arena. In fact, his private business was tightly bound to government projects in the form of concessions and contracts for most public infrastructure such as transportation and communication. However, road building, for strategic reasons in the Sarit era, partly contributed to economic growth and integrated the Thai economy into the world market. The

bureaucratic polity remained prevailing, but the Sarit-Thanom-Prapath regime turned it into a patronised local capitalism instead. This system is claimed by some scholars to contain unfair competition, rent-seeking and corruption and can be seen as a predatory state.

In this period, the Thai state took away the invisible foot and put back the invisible hand of a market mechanism into the field of production, permitting private enterprises to develop. Fortunately, Field Marshall Sarit stayed in power only for a very short period. After his death in 1963, the size of his estate revealed that he had acquired a vast amount of money (more or less \$ US 130-150 million) from his patronage political position. The result of the Sarit regime use of the Revolutionary party had a major impact on the power structure of modern Thai political economy, namely, the monarchy, the bureaucracy and the military. In politics, it essentially interrupted and weakened parliaments and political parties. Thus, Thailand has hardly had social and economic bases for democratic development. The middle class, which was predominantly Chinese and therefore treated as alien, allied itself to the ruling elites. Very few Thai parliaments completed their terms (4 years). They often had to adapt their role to new circumstances (Meesook, et al., 1988). From 1932 to 1963, the military or the Revolutionary party (most of the period) was seldom accountable to civil society (Paribatra, 1993). However, the legacy of Sarit to Thai economic history was the concern with the increased role of technocrats. (Nak Wichakarn).¹ There is little doubt that, to a certain degree, the stable macroeconomic performances, notably economic growth and low inflation rate, were partly brought about by these dwindling, able and honest technocrats (Christensen, et al., 1993; Thanapornpun, 1990). The increased role of technical analysts appears to have influenced a number of policy-making bodies such as the Bank of Thailand, Ministry of Finance, and the Prime Minister's office. Nevertheless, technocrats need to go in for planning and suggesting, while bureaucrats who can approve and grant rights are the very patrimonial officials. This is a sharp distinction in modern Thai bureaucracy.

The 1960s began with a new investment law (Promotion of Industrial Investment Law Act 1960). BOI was empowered to encourage domestic and foreign investments in industry or negotiate conditions of investment agreements subject to the cabinet's approval. However, there were evaluations pointing out that the incentives were not enough to induce foreign firms to invest in Thailand. BOI Act was amended in 1962, 1965, 1968 and 1972.

Judged by the structure of production, ISI in the 1950s to the 1960s could not be regarded as successful. Heavy protection was by means of a high tariff wall, import quotas and other quantitative restrictions, especially import surcharges that were implemented by *ad hoc* sectoral policy. *However, it is misleading to take for granted that the high tariff barriers were made available as a tool for industrial policy protection under a strategic industrial policy regime. In contrast, it has from time to time been deployed as a source of government revenues by the Ministry of Finance* (Patamasiriwat, 1993; Zuzuki, 1993). ISI should have substituted for the imported goods through increased production within Thailand to fill the vacuum in the markets, but resources were instead transferred to the preferred industries by BOI (Promotion certificates) through the provision of relatively cheap machinery and intermediates, mostly capital and inputs from abroad. This was not uncommon in Third world countries due to the simple fact that foreign firms were prone to use their comparative advantage in labour-saving technology. Furthermore, the high wall of tariffs imposed on finished products under ISI inevitably induced them to import more and more capital and intermediate products for assembly only. Thailand has neither been guided by industrial sectoral planning nor had any industrial targeting strategy like the East Asian countries. This is indicated by the fact that :

The Thai State does not control the markets for credit and foreign exchange, thus depriving policy makers of perhaps the key tools for conducting industrial targeting. Furthermore, there has been little co-ordination or coherence in the use of existing industrial policy instruments, tariffs, investment promotions, capacity controls and local content regulations (Christensen and Siamwalla, 1994: 18).

BOI, being one of the main authorities to implement industrial policy, did not establish a coherent import-substitution policy *per se*; nor did it build up a clear-cut framework to enforce promoted firms to meet BOI's requirements. Punishment has never been the case in the Thai context. The one explicit principle of BOI is to encourage foreign companies to invest more and more in Thailand no matter the kind of industry. Later, some more serious criteria such as labour absorption was included. The obvious evidence is that no performance standards and follow-up have been imposed on the recipients of promoted certificates. The pre-requisite to make ISI successful in the East Asian manner rests heavily on four crucial factors; the strength of the state, the competent bureaucrats, independent technology learning capacity and increased productivity in agriculture prior to export-oriented industrialisation. This

implies that income distribution must be more equal to consume manufactured goods in exchange. Such a process properly raises rather than lowers standards of well-being. Consequently, the favourable caveats in industrial policy pursued by the Thai BOI, namely granting of tax holidays (8 years), exemption from import duties on machinery, components, raw materials and the imposition of bans and surcharges on competing imports enabled BOI to seek economic rents rather than enhance productivity through adapting modern knowledge.

Bribery started to play a significant role when industrialists, both foreign and local, applied for promotion certificates. However, BOI is by no means a rent-seeker (Christensen, et al., 1993; Meesook, et al., 1988). Not surprisingly, most incentives (taxes) offered by BOI to firms are opportunity costs to all Thais. Scarce resources distributed to promoted firms will be increased twofold unless these firms succeed in adapting and mastering new technological skills. Linkages became weak an expanding manufacturing sector was not able to generate activity throughout the entire economy. Hence, the import-substituting industries are at best foreign enclaves as long as the agricultural sector is left behind.

The share of consumer goods of the total amount of imports declined considerably from about 30 per cent in the middle of the 1960s to 10 per cent in the middle of the 1970s. The first easy stage of ISI was apparently quickly achieved, but the evidence suggests a more complicated story. The share of imported parts and intermediate goods required for the domestic production of consumer goods increased rapidly during the same period.

By 1970, the import of industrial products, especially chemicals and machinery was still substantial. ISI adopted by the Sarit government and its successors led the economy into structural difficulties and a large raw material and capital goods import bill was gradually created by the newly promoted industries (mostly joint-venture firms). The investment promotion act was now seen as a hindrance to industrial development because it gave birth to a high degree in price distortion of the factor market. Between the 1950 and 1960s It encouraged promoted firms to use more capital-intensive techniques that obviously had unmatched factor endowments in the Thai economy. What is more important, the Thai ISI is likely to have stressed a *high import content* due to the unilateral incentive system that was open to duty exemptions on imports of machinery and capital goods (De Rosa, 1986; Meesook, et al., 1988). It can be concluded that Thailand's BOI has played an active role in the allocation of the nation's

productive resources by encouraging specific sectors and discouraging others through the tax system.² However, BOI is clearly biased against agriculture and this is contrary to the experience of the East Asian NIEs. Again, a package of incentives seemed not to stem from a coherent strategic industrial policy (Siamwalla, 1993).

It has been argued that the East Asian NIEs also provided plenty of incentives like Thailand. The question emerges; why is the performance of manufacturing sectors in Thailand by comparison inadequate in terms of labour absorption and technological content compared to them? A closer look at the *contextual and institutional factors* seems to be essential for an understanding of the course of the Thai industrialisation process. As a matter of fact, a high degree of discretion and selectivity in the granting of incentives for a wide range of objectives without any accountability to civil society, accompanied by little monitoring or follow-up of promoted enterprises made it different. (see Christensen and Siamwalla, 1994). The implication is that technology is more than tools, plants or machines; it is very complex and embedded in key institutions. It also becomes clear that the Thai state has not created an indigenous technological capacity to support technological transfer from foreign firms.

As pointed out by Marzouk (1972), the encouragement of capital-intensive (or labour-saving) techniques with a low contribution to employment led to inefficiencies in the allocation of scarce capital resources. (To some extent) ISI rarely enabled the Thai economy to avoid a constantly increasing trade balance and deteriorating balance-of-payments. In particular, the labour absorptive capacity of this strategy in the context of the Thai economy appears to have been rather weak. This has adversely affected progress in agricultural modernisation and has erratically resulted in an accumulation of urban poor. As Watanabe (1992) rightly pointed out, despite an increase in the rate of industrialisation in the Southeast Asian countries, especially in Thailand, employment did not seem to correspond with an increment in the rate of industrialisation in production.³ The period of the Sarit regime (1959 to 1963) was treated as a decisive period in modern Thai economic history, since its emphasis on private entrepreneurship was perpetuated to the benefit of both economic growth and wealth of its successors. Again, there is a consensus that Thai industrial policy under the umbrella of the *muddled* ISI by way of BOI was indifferent to the means of rent-seeking which did not promote transformations in agriculture, nor enhance

technological capacity in industry (Christensen, et al., 1993; Meesook, et al., 1988).

This is entirely opposed to the industrial policy adopted in Japan, South Korea and Taiwan (Amsden, 1989; Chang, 1994, Graboswki, 1994; Wade, 1990). One explanation is intimately related to the relative autonomy of the state and the role of a strong national development ideology in these countries (see Siriprachai, 1993). However, it should be mentioned that the three East Asian NIEs underwent lengthy periods of agricultural improvement before ISI. They also succeeded in establishing relatively large growing domestic markets for manufactured goods linking to higher productivity and dynamic agricultural sectors. *What is the most essential contributor is the state capability to build up numerous literate populations with few natural resources in a short time.* The pattern of industrialisation is in fact remarkably similar to Great Britain's experience in the First Industrial revolution in the eighteenth century. It can as well be concluded that domestic-led growth industrialisation had brought about the changes in agricultural sectors before they shifted to export-oriented strategy. This success is highly dependent on the role of activist state or developmental state (Grabowski, 1994; Gunnarsson and Lundahl, 1994; Leftwich, 1994; 1995).

Export Promotion, the Legacy of ISI and the Squeeze on Agriculture

Before coming to the outward-looking strategy, it might be fruitful to comment on the legacy of inward-looking strategy. Import-substitution industrialisation in Thailand left many problems to be resolved. However, while the growth of the manufacturing sector had contributed substantially to GDP, it had very little impact on total employment as mentioned above. The incentives of BOI have been active in encouraging new investments in what it deems to be sunrise industries. The structure of tariff rates was quite high, ranging from 30 to 90 per cent between 1960 and 1979. Nevertheless, the structure of foreign trade has changed dramatically since 1960, reflecting the change in the structure of production. The export of manufactured goods became increasingly important, in particular from the light and agro-industries, while a decline in the relative importance of primary exports had been occurring. In imports, the share of consumer goods declined significantly while producer goods increased over time as is common. To a certain degree the share of the expansion of the manufacturing sectors, whether for the domestic or export markets, has been

associated with an increased import of components, raw materials and capital goods. In exports, Thailand has had a wide range of primary products for export. The diversification in agricultural products took place from the late 1950s to the middle of the 1960s and the expansion of the agricultural area occurred in upland crops, especially in the Northeast. Maize output grew most rapidly from the late 1950s, kenaf in the first half of the 1960s, sugar-cane in the 1960s and early 1970s and cassava in the late 1960s and throughout the 1970s. The rapid growth of agriculture during the 1960s and 1970s allowed Thailand to enhance its exports considerably.⁴ Rice production is still increasing and quite stable. The main factor explaining this expansion lies in plentiful unused land enabling Thailand to have a strong comparative advantage until the late 1970s. In fact, impetus for economic growth from the 1950s to the 1970s, came from the agricultural sector while the industrial sector in urban areas reaped most benefits from abundant cheap labour from rural areas under ISI policy. The intersectoral transfer of resources appears to have been one-way; a marketed surplus from rural to urban. The prices of rice have been kept lower than the border price by the rice premium and other measures since 1955 (Siamwalla and Setboonsarng, 1987). Thus, rice is the main staple good and is also treated as a wage good for urban labourers. By the early 1970s, the Thai leaders begun to turn away from ISI and adopt Export-Oriented Industrialisation (EOI). The question is, why did the Thai state decide to make a turnabout? A World Bank mission recommendation to the Thai government in 1970 might be the explanation:

Thailand's industrialisation is thus now at the cross-roads. The current trend of import substitution is toward more electrical products and vehicle assembly, gradually increasing the Thai-made content in these products, and towards petrochemical industries. Tariff increases would be necessary for all of these industries. An alternative approach would be to move towards a less protected, more competitive industrial structure with more attention to increased efficiency in primary processing, added emphasis on mass consumption goods, and vigorous promotion of export oriented manufacturing protection (IBRD, 1970 cited from Meesook, et al.,1988).

In fact, in 1963, the Bank of Thailand had warned of the many problems of ISI. However, with economic growth during the first two decades of its post-World War II history, the Thai economy was quite satisfactory, but not outstanding; GDP growth averaged 5.2 per cent in the 1950s, rising to 7.4 per cent during the

1960 to 1972 period. As the World Bank mission stated, ISI began to come across problems of excess capacity as the market became saturated in the late 1960s.

ISI, in reality, became the preferred strategy in Thailand not because of the rational arguments recommended by the World Bank (IBRD, 1959: Chapter 3), but rather because of expeditious policy actions to meet balance of payment crises. Needless to say, there was a common interest in ISI on the part of the bureaucratic authoritarian state, urban manufacturing entrepreneurs and multinational corporations. However, how much ISI and how long it should continue to support protection is often debatable.

The infant industry argument was implicitly used. It was widely known that ISI in Thailand was not *targeted* according to systematic economic criteria like in the East Asian NIEs, but was pursued in an incoherent, inefficient manner and for too long by BOI (Christensen and Siamwalla, 1994; Ingram, 1971; Meesook, et al., 1988; Silcock, 1967). The fact is that Thai technocrats were aware of this strategy in the early 1960s. Nevertheless, strong pressure to retain the apparatus of ISI might have come from nationalists and populists within the military, manufacturers and powerful new industrial and banking conglomerates. The idea of outward-oriented trade policies was being discussed publicly among Thai technocrats in National Economic and Social Development Board (NESDB) in the late 1960s. ISI strategy was perceived to be eventually fatal or at best self-defeating without liberalisation of industrial policy and conversion to export competitiveness.

In the early 1970s and the early 1980s, the world economy was full of disturbing events. The first oil shock severely affected the Thai economy owing to heavy reliance on imported oil and industrial materials. Though the first oil crisis in 1973 and 1974 took place almost simultaneously with the world commodity boom, rising prices of major exports, including rice, maize, rubber and tin helped to prevent a balance of payment's crisis. The first oil crisis appeared to have affected Thailand less compared to other developing countries, but its direct impact gave rise to high inflation in 1973 and 1974 and economic growth fell considerably in 1974 and 1975. Moreover, all the macroeconomic indicators were more satisfactory than most in other developing countries. The inflation rate was brought down quickly after the petroleum price increase. The Thai government showed an initial indication of moving from ISI to EOI in 1972 (Akrasanee, 1980). Export incentives provided by BOI, aimed to offset the cost-increasing

effect of protection on domestic prices of intermediate goods, are regarded as protection offsets insofar as exports are able to refund the full duties and business tax on import inputs since 1972.⁵ Duty drawbacks in the 1970s and BOI's export incentives seem to have been ineffective largely because of poor administration (Akraanee, 1980). In the late 1970s, Thailand was adversely affected again by the second oil shock and the subsequent world-wide recession, partly because the country had become quite open to the world economy. Balances of payments were in deficit for five consecutive years from 1975 to 1979, while the rate of inflation jumped to double-digits and accelerated to 19.7 per cent in 1980. However, Thailand did not rush into export liberalisation immediately, not because Thai technocrats were wise, but the red-tape within Thai bureaucracy made it impossible. Thus, Thailand's gradual shift to EOI was not the result of good planning. Rather, it was obstructed by the bureaucratic state because its official regulations and procedures were superfluous and cumbersome. The instruments of import protection existed simultaneously with instruments of export promotion, although a given set of policy interventions that systematically promoted ISI or EOI might not have been in force. Nonetheless, the revision of the Investment Promotion law in 1972 was designed to offset the disincentive effects of import protection.

Domestically, the middle class began to make its voice heard in politics and the business class, and ethnic Chinese business groups in particular started to assume a more explicit role in policy-making after 14 October 1973.⁶ The 1973 student uprising significantly affected the Thai political economy as a whole, and the patronised capitalism under the long authoritarian regime (1958-73) was partly demolished. In other words, the parasitic relationship of clientelism seemed to have been weeded with time and then the independent private sector was able to run businesses under the impersonal relationship of market forces. However, the patron-client relationship is very powerful and dynamics in the Thai society are not dead, but alive and adaptive. The military never regained the same level of unity or political dominance despite the overthrow of the civilian government in 1976 and the establishment of a new regime in 1977 (Boonmi, 1988; Chamarik, 1981; Elliot, 1978; Girling, 1981; Samudavanija, 1989; 1992). Between 1979 to 1981, when the OPEC countries raised oil prices dramatically, the government could not carry out its macroeconomic policy regardless of favourable external conditions. The Thai economy entered a period of stagflation, experiencing for the first time twin deficits. Several austerity measures urgently adopted by the government resulted in slower growth in the

country. This economic recession partly came from the fact that the exports of primary products did not continue to supply foreign exchange. In fact, Thai policy-makers had decided to adjust their strategy and put greater emphasis on promoting manufactured exports in the Third National Economic and Social Development Plan (1972-1976). Moreover, the country shifted to an outward-looking strategy, again with the lack of a coherent industrial policy. The main stated objective to promote manufactured exports rested heavily on foreign direct investments and multinational corporations (Christensen and Siamwalla, 1994; Santikarn 1992; UNIDO, 1992). The backbone agricultural sector, regardless of improving productivity, has the same duty to supply cheap labour and raw materials to export sectors.

Nevertheless, in the fourth five year plan (1977-1981), the export promotion policy was significantly revised to reduce the anti-export bias resulting from ISI. BOI still played a leading role in authorising and granting exemptions and privileges. Fiscal deficits began to soar, sustained by the newly found access to foreign commercial banks. Large-scale foreign indebtedness started in 1976; the Defence Loans Act enabled the government to borrow more for defence purposes, subject to a limit of 20,000 million baht.⁷ The Thai conservative monetary policy seemed appropriate in the 1950s and the 1960s, but in the late 1970s the dollar began to appreciate against other major currencies and a fixed baht/dollar parity became untenable. The Bank of Thailand is well-known for keeping the foreign exchange rate stable and for 26 years (1955-1981), the baht/dollar exchange rate remained between 20 and 21 baht per dollar. In fact, the Thai government delayed a devaluation and decided not to increase domestic oil prices following the second oil shock in 1979, despite a severely increased current account deficit. In July 1981, the Prem government had to devalue by 10 per cent and again in 1984 by about 15 per cent. The latter devaluation was coupled with the change in the exchange rate system, whereby the baht was tied to basket of major trading partners instead of being solely linked to the US dollar. The two devaluations cannot be interpreted as an initiative of sound exchange rate policy, but were implemented by the forced necessity to offset a rampant situation.

Economic Policy Reforms, Industrialisation and Poverty

By 1970, the Thai government was beginning to reassess its commitment to ISI in the light of growing financial difficulties. It was clear that the majority of the promoted firm's products were aimed at the urban enclave market rather than

the mass rural market (Richter and Edward, 1973). Over time, the infant industry argument became increasingly evident (Akrasanee, 1980; Akrasanee and Atjanant, 1986). However, the Thai industrialisation process seems to have acquired little new technology owing to the lack of skilled labour (UNIDO, 1992). A promoted firm was required only to export a certain share of its output (percentage) to get promotion support, but the lack of effective monitoring and information to enforce performance criteria made industrial policy less effective. As a result, export-oriented manufactured goods were at best *footloose*. In addition, the slowdown of the world economy and reduction of American economic and military aid presented Thailand with a widening balance of payments and budget deficits which made the situation worse. Even though exports had been fairly diversified since the late 1950s, the heavy hallmarks of primary products remained with the country. The small size of the domestic market with consequent low effective demand could not absorb the excess capacity from the manufacturing sectors. It should also be pointed out that the poor and undeveloped agricultural sector has been both a cause and a consequence.

By the early 1980s, the Thai economy faced a set of economic crises similar to the ones that hit other developing countries. She had to undertake a major change in economic policy, especially the so-called Structural Adjustment Loans programmes (SALs) actively advocated by the World Bank and the Stand-by-Arrangements supported by the IMF. In short, some scholars may have overstated the extent to which the SALs helped Thailand to become more efficient in resource allocation (e.g., Akrasanee and Wattananukit, 1990; James, et al., 1989; Loathamatas, 1992a; Pongpaichit, 1992, Robinson, et al., 1991). A closer look and a more critical analysis of the role of SALs can be found in Thanapornpun (1990).

The World Bank and Thai technocrats agreed to shift the emphasis towards EOI. The objective was to increase exports and to reduce not only the balance of payment's deficits but also the import-competing industries. The decade of the 1980s even witnessed major economic crises in many developing countries including Thailand. Adjustment programmes were required to undertake major tax reform to raise more revenue and to make the tax system more efficient. In general, if structural adjustment refers to the restoration of equilibrium, i.e., providing a firm foundation to withstand further shocks and facilitate development (Goldin and Winters, 1992), then structural adjustment loans

programmes in Thailand during the 1980s appeared to have been less satisfactory for a package of economic reform.

Since the early 1980s, the Thai economy has suffered severely from continuous economic crises. Ironically, Thailand cannot be classified as being successful in the implementation of major economic reforms in at least three important policies, i.e. trade, tariffs and tax policies.⁸ Furthermore, most *ad hoc* sectoral policies continue to prevail. The question arises; why has Thailand been able to sustain high economic growth and to maintain positive macroeconomic indicators? Trade policies in Thailand are still full of quantitative restrictions, but a clear plan for a subsequent reduction in tariffs to quite low and uniform levels was strongly proposed by the Ministry of Finance in the early 1990s (Richupan, 1990). The early 1980s economic policy reforms of raising energy prices and devaluing the baht appear to have had only a part of the desired effect. The growth of manufactured exports has increasingly been the result of sound exchange rate policy rather than only export subsidies. Two successful devaluations in 1981 and 1986 did substantially help Thailand to reduce the trade deficit in 1985 without affecting domestic levels of inflation (see Ranis and Mahmood, 1992). Devaluations were used to reduce the *anti-export bias*, and to achieve competitiveness of tradable goods. In the Thai context, BOI has often strictly followed a one way route by granting subsidies and privileges both in ISI and EOI. Promoted firms that did not fulfil the conditions were never threatened with punishment.

Judging by the conservative financial policy of the Bank of Thailand, the developments were undoubtedly regarded as major economic policy reforms. Clearly, disturbances in the world economy urged Thai monetary policy to depart from the traditional exchange rate policy. The volatility of the world financial system in the 1970s and 1980s also caused these policy adjustments, if seen in contrast to the stable period of the 1960s. Nevertheless, an exchange rate policy is not a commercial policy *per se*. This distinction is relevant in the Thai context regarding *ad hoc* sectoral policy. Commercial policy affects import-substituting and export-oriented interests (Rodrik, 1992). Bureaucratic autonomy, discretion and patronage have been shaped or guided by incoherent policies, in particular by those of the Ministry of Commerce. In 1982, Thailand became a contracting party of GATT; it is widely perceived that a commitment to integrate into the world economy would incite a country to keep pace with sound macroeconomic

policy, but my contention is that this does not necessarily make the Thai state developmental.

In essence, the lack of consistency in *ad hoc* sectoral policy (Grindle and Thomas, 1989, 1991; Christensen, et al., 1993) can be attributed to the characteristics of a rent-seeking society prevailing in Thailand since the 1950s. The most important hindrance is the discretionary legal mandates of individual departments. Ministerial discretion in trade and industrial policies, quotas, licensing and factory promotions are often deployed to seek economic rents to such an extent that some of the rents are or have to be kicked back to the bureaucrats and their political masters (Christensen and Siamwalla, 1993; Siamwalla, 1991; Thanapornpun, 1990). The trend has been increasing since the 1990s, and vote-buying politics might contribute to it. It should be made clear that the East Asian NIEs might have had a rent-seeking to a considerable extent, but the social benefits of high productivity in agriculture and export-led industrialisation surpassed the social costs of rent-seeking activities.

It is evident that export licensing, either automatic or non-automatic, affects about 150 product categories, mainly textiles and clothing which have rapidly become the country's highest foreign exchange earning commodity group. They also contributed substantially to manufacturing value-added and absorbed approximately three-fourths of employment, especially female workers in the manufacturing sector. Other items cover certain agricultural commodities, fuels, metal and metal products, wood and wood products, wild animals and their carcasses, pesticides, paper and sacred statues and images. Export quotas are still in place for sugar, cassava and textiles. Formal institutions, in particular the Import and Export Commodity Act of 1979, give absolute power to the Ministry of Commerce or the Permanent-Under Secretary of the Ministry to promulgate scores of subordinate legislation for imposing quantitative restrictions and other regulations on trading without the approval of the cabinet or Parliament (Sathirathai, 1987; Siriprachai, 1990). This can easily lead to corruption and rent-seeking activities if the bureaucrat is not a benevolent social guardian. In the Thai context, the bureaucrat can easily restrict supply with very low risk of detection or punishment from above. Rather, the clientelism encourages corrupt officials to expand their activities. It is very common that their bosses often share in the on-going process (Shleifer and Vishny, 1993). The low salary is often cited, but the story might be more complicated in the sense that the institutions can not keep the most honest and talented people in their

organisations. What is more important, Thailand has never had administrative courts (Conseil d' etat) to deter corrupt bureaucrats. They would serve to curb malfeasance, impropriety and abuse of power on the part of state officers (Klausner, 1989). Hence, legal and public cessation of corruption and rent-seeking is highly unlikely to come about.

In addition, under an existing electoral regime and elected coalition government after 1975, politicians who have to be re-elected and desire to be ministers need to spend a lot of money on a patronage fund to keep an elected member of Parliament in office. The clientelistic fashion has become pervasive (Christensen and Siamwalla, 1993; Christensen, et al., 1993; Samudavanija, 1989; Siamwalla, 1991; Thanapornpun, 1990). It is often stated that trade quotas, capacity control and factory permits created resources for the military elite in the past, but for political parties and individually elected politicians in the present. Furthermore, the serious shortage of infrastructure since the middle of the 1980s has even created an opportunity for the various ministries (elected politicians) to carry out a big project. Economic rents (in the form of commissions, permits, licences, etc. were repeatedly appropriated by bribery, "palm-oiling" or other corrupt means. However, in many cases the allocation system is not based on competitive rent-seeking, but is used covertly instead by the politicians in power to generate income for themselves or for their party. It is almost impossible to believe that this occurs in really the most Buddhist country in the world. Hence, commercial policy, to a greater extent than that of *ad hoc* sectoral policies in Thailand, has seldom been reformed through the structural adjustment loans programmes.⁹

It has been argued that both SALs of the World Bank and the Stand-by-Arrangement programme of the IMF in the early 1980s did rescue the Thai economy which readjusted towards greater efficiency enhancing measures at the macroeconomic level, but that it might have been too little and too late to enhance balanced growth and equal distribution of income and opportunities for the rural poor and unskilled labour. Several studies have shown that the nominal exchange rate of the baht had been over-valued for years, (Siamwalla and Setboonsarng, 1987) and caused by imposing high import duties to protect promoted firms. In other words, the agricultural sector was squeezed by the modern sector for a long period and as a consequence, Thai peasants had to pay the high prices of protected goods. It is manifest that both *ad hoc* sectoral policies, for example, in rice and an over-valued exchange rate during the 1961 to 1980 period, eminently discriminated against export producers, in particular

exporters of primary commodities. To a certain extent the fact that it directly impeded the transformation of the agricultural sector is undeniable. Not surprisingly, the agricultural sector, which is the poorest sector in the country, has been left in poverty. As rightly observed by Timmer:

Thailand did not use similar trade and pricing for key commodities in an effort to protect domestic farmers from the very low prices that occur from time to time in the world market. Although the strong performance of Thailand with rising labour productivity argues that such free trade policies promote growth, Thailand paid a price for rural poverty (Timmer, 1991: 138).

During the readjustment in the 1980s, the Thai government seems to have been reluctant to implement the structural adjustment programmes fully. Development policy instead aimed at alleviating poverty in the agricultural sector and government expenditures as well as the tax system were firmly moved towards the creation of an environment suitable for export-oriented industries in urban areas, especially in the proximity of Bangkok. The industrial policy seems not to have been enormously changed to develop rural industries thoughtfully. It is often forgotten that in the East Asian NIEs' experience the domestic market was a crucial prerequisite before manufactured export goods could compete on the world market (Adelman, 1982; Gunnarsson, 1985, 1991). This simple fact might not have been discussed among the Thai technocrats in the NESDB.

It is also obvious that the scale of land reform was very limited and ineffective at keeping poor farmers from becoming indebted. Previous attempts to limit private land ownership were never successful due to vested-interests until the Agricultural Land Reform Act was enacted in 1975. The revision of land reform in 1993 under the Chuan government is a good example in support of this assessment. The recent land reform scandal in many provinces, particularly in Phuket in late 1994 suggests that discretionary power and rent-seeking activity were deployed as instruments to seek economic rents from scarce resources, while the Thai state still strongly supported a policy of growth maximisation. The equalisation of regional and personal income levels is believed to have received even lower priority than had been expected during the 1980s.

It should also be noted that the high or impressive growth since the 1960s has, of course, trickled down some benefits to the poor. Absolute poverty declined steadily from 57 per cent in 1962-1963 to 24 per cent in 1981. Nevertheless, income inequality has in contrast increased in every region, both in rural and

urban areas. It is true that a decline in the incidence of absolute poverty can be quite consistent with an unchanged or even worsening income distribution (Williamson, 1991). Worsening income distribution over three decades in Thailand has remained ubiquitous (Huntaserini and Jitsuchon, 1988; Sussangkarn, 1992; Tinakorn, 1992).

The income shares of the richest 20 per cent of households increased from 50 per cent of total household income in 1975/76 to 55 per cent in 1988/89, while the share of the poorest 20 per cent declined from 8 per cent to 4.5 per cent during the same period (Sussangkarn, 1992). However, recent data from the National Statistical Office (1993) shows that the share of the richest 20 per cent of households decreased to 42.81 in 1990, while the share of the poorest 20 per cent jumped to 8.52 per cent. This fact simply suggests that development enriched the urban rich relatively than the rural poor.

Rising income inequality both between industrial and agricultural sectors and between regions partly reflects the nature and competence of the Thai state to cope with fundamental problems. It remains apparent that rising income equality and real wages in the rural areas cannot be manifested through *laissez-faire policy*. Economic growth did partly trickle down, but not enough to improve living standards as a whole. In addition, both import-substituting and export-oriented industrial sectors mostly concentrated in Bangkok (Santikarn, 1992), have been inadequate for sufficient labour absorption. An attempt in the 1980s to restructure the Thai economy seems to have offered little stimulus to industrial labour absorption (Ezaki, 1990). In addition, a recent study done by UNIDO has shown that the output elasticity of employment in the manufacturing sector in Thailand was very low and declining in the 1980s compared to the 1970s, noticeably falling from 0.74 to 0.39 (cited from Ghose, 1993; table 4.11). *Employment conditions almost certainly deteriorated regardless of the development strategy adopted. It has been argued that export-oriented industries are significantly more labour-intensive than import-substituting industries, but this was not the case for Thailand.* What factors can explain the very low output elasticity of employment in the manufacturing sector in the 1980s will have to be gone into. The monsoon weather tremendously affected seasonal fluctuations in labour demand. In the very long slack season, hundreds of thousands of able bodied men and women migrated to work in Bangkok and its vicinities, partly because there were not enough rural industries. Having only low skill and education (due to a weak and predatory

state), they often worked in informal sectors and lived in slums in Bangkok. The formal sector, led by multinational and joint-venture firms, did not have a sufficient capacity to absorb labour. Migration provided essential means to escape from poverty as the migrant workers could only get jobs in the informal sector with its easy entry and low need of skills. Small income earnings from hard work were deployed to support their families in their rural homes. The push factor rather than a pull-type of urbanisation was of greater importance since it led to deficiency of employment opportunities stemming from the collapse of the rural economy which pushed agricultural workers out to Bangkok.

Nevertheless, by the middle of the 1980s, commodity prices on the world market were depressed and the substantial number of farmers remaining in agriculture received very low incomes. It is not surprising that the price support programmes have hardly ever had adequate funds to raise the general level of farm-gate prices for rice (Thanapornpun, 1980). In the case of cassava, the quota system causes a large source of rent-seeking and rent-dissipation (Siamwalla, 1986, Siriprachai, 1988), except for the case of sugar-cane in which the mills' and farmers' associations are strong and can collude to bargain with the government. What is responsible for the successful structure of subsidy in the sugar-cane industry is the nature of the production line.

It is commonly known that the Thai economy has undergone rapid economic transformation as the share of agriculture in the gross domestic product (GDP) has been shrinking rapidly and as export promotion has replaced import substitution as a development strategy. However, Thailand's tax system has remained very regressive compared to the East Asian NIEs (Richupan, 1990; Tanzi and Shome, 1992) and has lacked transparency. The tax structure itself is rather complex, resulting from many special allowances and high standard deductions (allowed for different sources of incomes), in particular through BOI and by the failure to tax fringe benefits. It has been argued that tax policy has historically depended heavily on domestic consumption and trade taxes. By 1992, the seven per cent value-added tax was confusedly replaced by complex, inefficient business taxes by the Anand government. Thailand has tinkered with its tax system over the years without any major policy reform (Pathamasiriwat, 1993). The existing tax policy does not provide for an equitable income distribution or opportunity. It is small wonder that while the Thai state has been playing a key role in enhancing economic growth, tax policy has not served to generate social justice and human rights (Tinakorn, 1992). Increased disparity in

income partly mirrors these phenomena. Although the signal that the Thai government has put out over the years to stimulate exports of manufactures is still effective, income redistribution or the achievement of special social goals is a long way off. Not surprisingly the role of social security with transfer payments has been very limited in Thai society (Tanzi and Shome, 1992). It has been clearly shown that taxes to discourage speculation in land have never been put forward. An unintended consequence is, of course, highly related to the urban poor by raising their living costs. Again, the rural poor tried to escape from poverty by moving to seek jobs in Bangkok. At the end of a long journey, being unable to rent cheap accommodation, they commonly crowded into very densely populated areas. We are not taken aback that the slums in Bangkok are voluminous with both permanent and temporary migrants.

The question arises of why industrialisation seems to inhibit poverty eradication. Recent data suggests that high economic growth did diminish absolute poverty in all regions over the two decades until 1981. In terms of relative poverty, high economic growth enlarged income inequality both in the regions and economic sectors. That made the poor poorer. However, commercialisation has gradually taken place since the 1980s and increased numbers of agricultural wage-earners and unskilled workers are vulnerable to becoming poor in Thailand (Siamwalla and Setboonsarng, 1987; Sussangkarn, 1992; Tinakorn, 1992), partly because the land frontier has been closed. In addition, recent expeditious high land prices have given rise to unproductive expenditures and social waste from speculation, while tax incentives granted by BOI have led to prevalent rent-seeking by a public bureaucracy made up of low paid, poorly trained, dishonourable but powerful elite (Christensen and Siamwalla, 1993). Recently, BOI has kept up with an odd policy again to grant subsidies to luxury hotel and townhouse investors. The stated reason claimed want to provide the urban poor with accommodation. The main objective of establishing BOI to protect and help infant industry is fading. The social cost of distortions has always been treated as negligible, but is in fact substantial.

It must be emphasised that South Korea, Taiwan and Singapore were rather unusual. The beneficial effects of incentives will not develop if incompetence, corruption or various forms of rent-seeking activities become the norm. Since the late 1950s, incentive legislation, especially in ad hoc sectoral policy that is based on discretionary decisions, has provided a perfect instrument for enriching a few members of the military elite, bureaucrats and elected ministers by permitting

some investors (some traders) to evade taxes (to get quotas or licences). The loser is, of course, public interest.

The tariff reform in the 1980s seems to have had little effect (Zuzuki, 1993). The Thai government will need to focus on reducing the wide dispersion of its 34 nominal tariff rates ranging between one and 200 per cent and the excessive rates of effective protection. In fact, a major tariff reform was attempted in 1982 and if some progress was made in equalising rates of protection within individual industries such as textiles, the result for the industrial sector as a whole was modest. In effect, some of these gains were reversed when tariff rates were raised again in 1985. The import tax was still essential for increasing government revenue when the budget remained in deficit (Zuzuki, 1993). This left Thailand with the highest average nominal rate of tariff protection (34 per cent) of any of the Pacific Basin developing countries (Noland, 1990). The Thai government again began to reform tariffs in the early 1990s as a result of a commitment to the Asean Free Trade Area (AFTA) to do so within 15 years (1 January 1993 to 31 December 2008). Export duties have been of less importance since the 1980s, while import duties have remained high at 18 per cent of government revenues.

The Thai state seems to have been incapable of dealing with these problems in the past (Phipatseritham, 1993). It is not easy to draw a conclusion on the failure to privatise. The national or security interest is often cited for the necessity of keeping on the loss-making state-owned enterprises. Both civilian and military governments alike have distributed economic patronage by appointing their supporters and friends to control state-owned enterprises. In other words, the strong clientelistic relationships have been strengthened again and used to seek economic rents to finance political parties in the next general election.

The early 1980s witnessed the slowdown in infrastructure investment in a Thailand facing twin deficits. Most government projects were postponed to keep the economy stable. Nevertheless, after the middle of the 1980s the economy rapidly recovered. The Thai state has been inviting foreign private enterprises to invest in huge infrastructure projects by granting concessions on a build-operate-transfer (BOT). It stems in fact from the ideology of privatisation. It is interesting to mention that it has undoubtedly led to a war of rent-seeking among the elected politicians, government officials, state enterprises and private investors (foreign and local), because each mega-project can easily constitute a gigantic rent for those who can exert the most political muscle (Mueller, 1989). A

simple explanation lies in the political economy of privatisation which was started without attempting to draft any standardised legal framework to regulate (Christensen and Siamwalla, 1994). Hence, bribery and "palm-oiling" have been flourishing. In the Thai context, it is commonly known as "tea" or "coffee-money".

In May 1990, Thailand announced plans to dismantle its remaining capital controls and maintain a fully convertible currency under Article VIII of the IMF Articles of Agreement. It is understandable that financial reform might be more easily achieved than privatisation of state-owned enterprises. Not only has the sector been developed very quickly over the last three decades, it has also been suitable for financial firms to become competitive on international financial markets.

The Thai State: Between Rent-seeking and Inequality

Thailand has a number of administrative laws that grant the authority to implement various aspects of national policy, especially in international trade and internal affairs. Political pressure and vested-interest groups have been the exporters, industrialists and bankers, while a large number of peasants are less powerful and thereby unable to bargain with bureaucrats and vested-interest groups. The fragmented political party systems and vote-buying remain evident. It is no secret that Thai political parties got financial support from urban vested-interest groups. There is no sign that Thai political parties are consolidating their bases in the countryside. In fact, bureaucrats and ministers usually found it prudent to consult formal interest groups namely trade, industrial and banker associations on various technical aspects of state intervention. As pointed out by Siamwalla and Setboonsarng (1991) and Laothamatas (1992b), this has provided the vested-interest groups with the means of entry into the policy-making process, whereas the farmers are never informed of any of the consequences of state discretionary policies. However, some trade associations are more skilful in lobbying policy-makers than others. Not surprisingly, inside information has allowed interest groups, for instance exporters, to obtain large speculative profits through trading. It is worth noting that insecure government since 1973 has tended to concentrate resources in urban and industrial sectors in the interests of maintaining its own power and winning international recognition. However, rural insurgency in the Northeast of Thailand in the 1960s and the 1970s

compelled the Thai elite in Bangkok to pay more attention to them and to distribute some resources.

Reliable and accurate data on the standard of living is notoriously difficult to collect, but trends in poverty and labour productivity by the rural sector reflect the underlying economic environment in which these people live and work. The rural poor in Thailand, not just in the Northeast but also in other regions, are very destitute and have only little education, usually discontinuing their studies after the compulsory level. It is often forgotten that the Thai government got round ISI under the unbalanced growth strategy in the 1950s and 1960s and tried to change to EOI in the early 1970s; but the rural sector has in this regard generally been treated as a supplier of cheap food, raw materials and low wage labourers (Jansen, 1991; Siamwalla and Setboonsarng, 1987). This has been mirrored in both macroeconomic policies (exchange rate policy and *ad hoc* sectoral policy) and in infrastructure developments. It is fair to say that part of the infrastructure development by the central government in remote rural areas helped to improve the living conditions. Nevertheless, the economic surplus in the rural sector has been squeezed and used to subsidise urban industrial development; the rice premium was one such case between 1955 to 1986. After enacting the Farmers' Aid Fund, the government still kept the domestic prices of rice down through rice reserve requirements adopted by the Ministry of Commerce (Siamwalla, 1975; Thanapornpun, 1985). This inexorably led to a drop in the cost of living in urban areas, reduced the pressure by urban workers to increase wages, encouraged exports and enabled export-oriented promoted firms to compete in the world market. In conclusion the experience of industrialisation in Thailand over the last 40 years seems to have bred corruption and rent-seeking activities as well as unbalanced growth.

High, impressive growth over more than four decades could also have taken place at the expense of poverty and the depletion of natural resources in rural sectors. It is noteworthy that rural poverty and low agricultural productivity in the rural sectors of Thailand are reinforced, thus restricting purchasing power and limiting the domestic market for manufactured goods. If industrialisation in urban areas had been able to bring about modernisation in agriculture, it would have been possible for Thailand to become a newly industrialising country. Again, the East Asian countries have grown at a very high rate and have promoted high technological industries presumably by tax incentives under a strong activist and developmental state (e.g., Chang, 1994; Evans, 1995;

Grabowski, 1994; Kohli, 1995). The essential difference in conduct is that the Thai state has not come out with threats to punish promoted industries for not being competitive or efficient. Furthermore, the technological transfer process, being one of the most important linkages of late industrialisation, is the missing link of industrial policy. The nationalist policy in the Phibul era might be close to the insulated developmental states in South Korea (Haggard and Moon, 1983), but under the Thai bureaucratic capitalism of state-owned enterprises, it turned into an import-substitution strategy in which inefficient industries needed to be protected from foreign competition for many years. What made it so different will be discussed below.

The redirection of policies reflects an emerging consensus that countries following an outward-oriented, market-based development strategy achieve relatively higher rates of growth and living standards. It might be too early to confirm this in the case of Thailand. The most important factor behind the East Asian miracle may not lie in what industrial policy they pursued, but rather on the kind of state.

Nevertheless, there still remain some difficulties and restricting conditions that must be remedied to secure continued growth of the Thai economy. One immediate problem is bottlenecks in the infrastructure and the other is the quality of the labour force. Infrastructure investment needs are enormous, but in part because of large government budget deficits in the early 1980s that surpassed six per cent of GDP, Thailand has saved and invested somewhat less than some other East Asian countries. Even though the government has run a surplus since 1988, the share of investment in GDP has risen only to about 26 per cent. Additional increases to around 30 per cent would be desirable for the long run (Noland, 1990). In the coming 1995 budget it might be more than 30 per cent. However, since the early 1990s, this has gradually increased to approximately 30 per cent, made possible by high sustained economic growth.

Lack of adequate investment in infrastructure is still one major constraint on future growth and development. As a result of corruption in government contracting, the flow of investment in infrastructure has been adversely limited. Additional investment in human capital is also urgent, including an expansion of secondary education in general, and of technical and vocational education in particular. Sciences and engineering need to be strengthened at university level and research and development activities encouraged domestically. The main point is to create *equal opportunities* for the lower classes. The consecutive

surpluses in government budgets make it a propitious time for the Thai government to carry out reform in economic policy and in education.

The Thai state has been centering on more economic growth than on a fair income distribution. Even without external debt and balance of payment crises in the early 1980s, the prospects for the poor in Thailand can hardly be satisfactory. For the period from the 1960s to the 1980s, the data tells us that the trade-off paradigm between the speed of economic growth and the share of income of the poor was so little mitigated that the deterioration in the share of income of the poor was quite substantial. The conclusion is that in the foreseeable future the path of development does not give much hope for attaining the goal of poverty eradication in Thailand through economic growth (Aldelman, 1992).

Using the subtle framework of Roemer and Radelet (1991), Thailand might have been able to achieve stabilisation in macroeconomic policy, in particular high economic growth, a low inflation rate, a surplus in government budgets, etc. The outward-looking strategy, for which export expansion was the engine of recently sustained economic growth, is often cited (James, et al., 1989; Robinson, et al., 1991, World Bank, 1993). Structural adjustment aimed at correcting imbalances in foreign payments, government budgets, and the money supply with the aim of controlling inflation and maintaining macroeconomic stability is obviously successful. However, economic reform, liberalisation, privatisation and institutional reform were open to question. Economic reforms which in this context refer to changes in institutional structure or administrative procedures that were designed to alter economic activity and improve performance were hardly ever carried out. Recent attempts at Constitutional amendment in late 1994 of articles 198-199 on the issue of decentralisation to local government have failed entirely. Liberalisation through the removal of government interventions in *ad hoc* sectoral policy, namely incentives for investment, export quotas, export licensing and other barriers to entry was not seriously implemented either. Such a policy is known to foster patronage and rent-seeking, rather than to dismantle it. A case in point is the Commerce Ministry corruption scandal in allocating quotas of cassava in 1993-1994 to the European Union. Privatisation through the sale of government-owned enterprises to private investors and the contracting of formerly governmental functions to private firms was negligible in the past.¹⁰ Now, evidence of a policy change are mega-projects such as the sports complex for the Asian Games which was contested between Bangkok Land Plc and

Thammasat University at Rangsit campus. Estimated costs of the total project ran to more or less 10,000 million baht. Institutional reforms, meaning changes in government institutions that make it possible for economic reform to work and predominantly involves shifts away from administered control towards mechanisms that reduce transaction costs of administration, have been rare (Paribatra, 1993; Samudavanija, 1989; Samudavanija and Paribatra, 1991).

In conclusion, the Thai economy needs economic, political, and institutional reforms. Rent-seeking and corruption should be kept at a minimum by making administrative regulations clear, transparent and accountable. In fact, Thai society absolutely needs good governance as synonymous with sound development management (Leftwich, 1994; 1995). Accountability, a legal framework for development, public information and transparency should be fully provided to warrant democracy. Lacking a mechanism for effectively controlling and countering discretionary power is a serious drawback of a regime of patron-client relationships which might have become a major barrier to any reforms.¹¹ (Christensen, et al., 1993; Samudavanija and Paribatra, 1991) As has taken place in some countries with well-developed clientelistic governments, economic reform can be both politically costly and irrational (Grindle and Thomas, 1991). *Most neo-classical economists (the Washington Consensus) seem to conceive that export-oriented policies will be likely to reduce inequality within developing countries, but the Thai case appears not to have supported this proposition. The main contribution to the successful East Asian NIEs comes from a rapid expansion of higher education in which the relative supply of skilled labour has been increasing.* Thus, more expansion of manufactured exports to the world market does not necessarily lead to reduction of inequality. The last point that should be added is simultaneously related to the institutional constraint that shapes the Thai society into being neither a strong nor minimal interventionist state. The predatory-cum-soft authoritarian state might be an apt description of Thailand.

Notes

¹ The prestige is given to academicians or experts (Nak Wichakarn). Thai technocrats often include professionals/experts working at the NESDB and the Bank of Thailand, the Ministry of Finance.

² Siamwalla and Setboonsarng (1987) rightly observed that BOI emphasised the promotion of big industry with tariff protection, exemption from import tariffs on machinery and income tax holidays. Unfortunately, most agro-processing industries like rice milling and rubber processing (small and medium-scale) are entirely ignored in terms of access to BOI promotion privileges. BOI is clearly biased against agriculture.

³ The rate of industrialisation in employment is simply defined as the share of industrial workers in the total labour force employed.

⁴ Recent improvements in transport, both by road and by rail, have increased the possibility of switching from subsistence agriculture to both export crops and cultivation of fruits and vegetables for the home markets (Silcock, 1967).

⁵ In fact, this system was established in the late 1950s under the control of the Fiscal Policy Office of the Ministry of Finance, but the law allows for a partial refund of duties and business taxes on inputs.

⁶ This was a popular uprising of university students against the military government which resulted in the downfall of the Thanom-Prapath regime (the Sarit's legacy).

⁷ In 1981 the Act was revised to empower the government to borrow from foreign sources for defence purposes as long as the sum of defence borrowing plus external borrowing for other purposes did not exceed 10 percent of the budget expenditures each year.

⁸ The World Bank classifies the conditional content of structural adjustment loans programmes in ten items: exchange rate, trade policies, fiscal policies, budget/public spending, public enterprises, financial sector, industrial policy, energy policy, agricultural policy and other (see Greenaway and Morrissey, 1993).

⁹ The main policy recommendations of the World Bank for Thailand were: (i) to raise domestic energy prices to international level; (ii) to develop strong deflationary monetary and fiscal policies; (iii) to end the import substitution policy for industry; (iv) to emphasise export-oriented industries; (v) to reduce import tariffs and remove all export restriction and taxes; (vi) to increase and make more effective personal taxation, (vii) to end restrictions on the level of domestic interest rates, (viii) to make a comprehensive review of government organisation and expenditure in order to eliminate waste, etc.

¹⁰ There were indeed two state enterprises selling to private firms during the 1977 to 1991 period, four expired, two were rented by private enterprises, one received a concession, four become joint-ventures, and four were permitted into the private sectors to run businesses (see Phipaserithum, 1993). There were 61 state-owned enterprises at the end of January, 1993.

¹¹ Irwan (1989) argues that the old patron-client relations in business started to declined rapidly. I shall argue that this conclusion is premature.

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