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FINANCE AND DEVELOPMENT IN THAILAND

by

Alek A. Rozental

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Alek A. Rozental

CONTENTS

VOLUME I

I. FINANCIAL MARKETS AND DEVELOPMENT PLANNING--A CONCEPTUAL FRAMEWORK

Relevance of Financial Markets	I- 2
Financial Markets in the Saving-Investment Process	I-11
Economic Efficiency	I-21
Development Goals and Priorities	I-24
Prolegomena to the Growth Theory of Dualistic Open Economies	I-28
Organized and Unorganized Financial Markets	I-38
Alternatives to Financial Intermediation--A Digression	I-50
Financial Markets as Vehicle of Economic Growth	I-55

II. THE FINANCIAL NEXUS AND THE THAI ECONOMY

Introduction	II- 1
The Thai Economy--Record of Recent Years	II- 3
The Thai Economy--Prospects	II-10
Monetary Accounts	II-21
Financial Intermediation	II-31
Intersectoral Resource Transfers	II-38
Uses of Funds in Thai Agriculture	II-40
Sources of Funds in Thai Agriculture	II-43
Agricultural Savings and Intersectoral Transfer	II-44
Intersectoral Flow of Funds	II-46

III. FINANCING OF RURAL HOUSEHOLDS

Introduction	III- 1
Financial Markets and Rural Households	III- 2
Agricultural Credit and Mobilization of Voluntary Saving	III- 3
The Market for Lendable Funds in Thai Agriculture	III- 7

Unorganized Markets--Supply III- 10
Unorganized Markets--Demand III- 19
The Terms of Loans III- 31
Repayment Record III- 46
Other Aspects of the Unorganized Markets III- 50
Organized Markets in Agricultural Credit III- 58
The Cooperative Institutions III- 60
Cooperative Credit--Performance and Prospects III- 74
Bank for Agriculture and Cooperatives III- 89
Cooperative Movement and Voluntary Savings III- 92
Government Departments and Rural Credit III- 96
Commercial Banks and Agricultural Credit III- 98
Implications for Developmental Planning III-105

IV. COMMERCIAL BANKING

The Growth of Commercial Banking in Thailand IV- 3
Assets and Liabilities of Commercial Banks IV- 8
Time Series Analysis of the Composition of Commercial Banks' Balance Sheets IV- 23
Time Series Analysis--Commercial Banks' Expansion of Credit IV- 29
Cross-Section Analysis, July 1962 and 1966, for Banks Operating in Thailand IV- 38
Commercial Banks and Unused Capacity IV- 66
The Operational Policies of Thai Commercial Banking IV- 79
Commercial Banking in the Saving-Investment Process IV- 90

V. BRANCH BANKING

The Extent of Branch Banking in Thailand V- 3
Operational Characteristics of Branch Banks V- 9
Thai Branch Banking in the Development Process V- 20
Implications for Development Planning V- 29

VOLUME II

VI. CENTRAL BANKING

Introduction	VI- 1
Assets and Liabilities of the Bank of Thailand	VI- 6
Provision of Credit	VI-21
Rediscount Facilities of the Bank of Thailand	VI-22
Debt Management and the Bank of Thailand	VI-38
Government Bonds	VI-40
Treasury Bills	VI-57
Central Banking and the Financial Nexus	VI-67
Relations with Financial Institutions	VI-68
Central Banking in the Development Process	VI-80

VII. FINANCING URBAN BUSINESS ENTERPRISE

The Nature and Scope of Unorganized Financial Markets in Thailand	VII- 3
Sample Survey of Urban Credit	VII-17
The Scope of the Survey	VII-19
The Composition of the Sample	VII-24
Sources of Initial Capital	VII-38
Sources of Current Funds	VII-48
Terms of Loans	VII-67
Urban Credit Survey and the Unorganized Financial Markets	VII-80

VIII. THE CAPITAL MARKETS

Introduction	VIII- 1
The Government Savings Bank	VIII- 4
The Loan Office for Small Industries Development	VIII-19
The Industrial Finance Corporation of Thailand	VIII-26
Life Insurance Companies	VIII-47
Employee Benefit Funds	VIII-66
The Stock Market	VIII-75

IX. FINANCIAL MARKETS IN THAILAND--CONCLUSIONS AND RECOMMENDATIONS

Summary of Empirical Findings IX- 1
Development Strategy and the Structure of Financial Markets IX-10
Suggestions for Increasing the Efficiency of the Financial Markets IX-12
Suggestions for Channelling Resources into Development Priorities IX-13
Suggestions for Expanding the Scope of Organized Financial Markets IX-15
National Investment Consortium--A Proposal IX-16
Financial Structure and Economic Growth IX-28

APPENDIX: URBAN CREDIT SURVEY QUESTIONNAIRES A1

CHAPTER I

FINANCIAL MARKETS AND DEVELOPMENT PLANNING--A CONCEPTUAL FRAMEWORK

The significance of financial markets to a country's economic development derives from three widely held beliefs.[1] In the first place it is believed that these markets can play an important role in mobilizing voluntary saving and directing these savings into development outlets. In the second place it is frequently asserted that such a role is not played to the full in the less developed countries or else is discharged ineffectively. Finally, it is contended that in a country such as Thailand with its export oriented, largely agricultural economy, there exist distortions in the structure of financial markets which impede progress toward industrialization and diversification--the economic course the country has apparently set for itself.

In this chapter these beliefs and assertions will be examined, although not all of them will be fully studied since certain of the issues raised can best be examined in the light of empirical findings reserved

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[1]Financial markets, as the term is used in this context, pertain to the complex of institutions and instruments which bring together lenders and borrowers. Financial markets is a less comprehensive concept than financial nexus in that the latter includes foreign saving and government finance. Here, no attention is paid to foreign saving; and government finance is treated only tangentially to the extent that government monetary and fiscal policies and its debt management influence the structure, the level, and the direction of voluntary saving and private investment.

for later chapters. More particularly, this chapter will focus its discussion on the nature of the connection between financial markets and development planning and will endeavor, in the light of this discussion, to develop an outline of a conceptual framework for developmental planning strategy in the area of finance designed to facilitate and to speed up the rate of economic growth.

Relevance of Financial Markets

It would seem rather obvious that there is some relationship between a country's financial structure and its stage of economic growth. Any definition, whether formal or operational, of a stage in the development of a country's economy includes some mention of the money and capital markets and of financial institutions. In general, more complex and, hence, more "developed" financial markets are associated with "higher" stages of growth. But such an association is by no means either clear or unambiguous. It begs the rigorous definition of both financial structures and stages of economic growth which is capable of furnishing even a weak ordering relation.

At its extremes such an ordering does not present much difficulty. Very poor countries will usually have very simple financial structures, however measured. Very rich countries will show a converse relation. For example, one of the simplest ways of measuring the complexity (or the degree of development) of a financial structure is to look at the proportion of demand deposits to the gross national product. While this index pertains only to the spread of the "commercial banking habit" in a country, commercial

banks have been found, historically to be the precursors of all other institutions operating in the money and capital markets.[2] This index will be low for countries with low per capita incomes and high for the rich, hence, presumably more developed countries. But for a number of countries this index will give surprising results. Even a cursory scrutiny of these deviations from the expected trend will suggest that the relationship is strongly affected by the political organization in a country. To cite one example: Soviet Russia may have a lower index than India, not because the former country is less developed, but because it chooses to limit severely the role of demand deposits in its economy.[3]

Similar irregularities will appear no matter how sophisticated the indices of financial structures are being devised. Indeed, such a sophisticated index has recently been developed by Goldsmith, and its value is severely affected by circumstances having little to do with the stage of economic growth as commonly understood.[4]

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[2]"A monetary system and especially its commercial banking component has commonly been the first significant financial intermediary..."J. G. Gurley and E. S. Shaw, "Financial Aspects of Economic Development," American Economic Review (September 1955), p. 520.

[3]See Raymond W. Goldsmith, "The Determinants of Financial Structure," Organization for Economic Cooperation and Development, (Development Center Studies No. 2 Revised ; Paris: OECD, July 1965), p. 2, mimeo.

[4]Goldsmith's index measures the relation between the value of total financial assets and national wealth. This "financial interrelations ratio" (FIR) is a composite of several determinants which include GNP, a monetization ratio, a capital formation ratio, the ratio of new issues of non-financial units to their capital formation, the ratio of new issues of financial instruments by financial institutions to new issues by non-financial units, the ratio of total issues of financial instruments to the issues of non-financial units and others. Ibid., pp. 6-7.

The significance of these deviations from expected values goes beyond statistical difficulties. These deviations strongly suggest that financial structures can play a varying role in moving a country from a "lower" to a "higher" stage of growth and, indeed, that a given level of economic development can be reached through an entire gamut of financial structures, from simple to complex. Complementary to this is the observation that there exist policy alternatives in the degree of sophistication of financial markets in reaching a higher growth stage.

It appears then that the relationship between the financial structure and a stage of economic growth will be strongest in those countries which, for historical or ideological reasons, do not reject commercial banking, financial intermediaries, or equity instruments. But even in these countries, which fall within the broad range of "mixed" economies, it is not immediately clear whether the relationship is causal or merely symptomatic.

The problem may be restated. Granted that there is an observable correletion between, for example, the ratio of financial assets to GNP and per capita income, is the accumulation of these assets merely a reflection of higher levels of income or did the process of asset accumulation, by itself, in some yet to be explained fashion, help bring about these higher per capita incomes?

For example, in most of the "mixed" economies enjoying high levels of income and consumption, a large proportion of the population hold claims on financial intermediaries, saving and loan accounts, pension funds, and

shares in mutual investment companies.[5] In what way did these holdings act as catalysts in the development process and in what fashion did the acquisition of these claims help to raise the level of per capita income?

The question is a crucial one. If, indeed, financial structure is simply a fortuitous reflection of a level of economic development already reached by a country, then the study of this structure, while of academic interest, is of little value to those concerned with developmental planning. If, however, it is true that financial institutions and instruments can serve as catalysts, if not outright determinants of economic growth, then such a study acquires operational significance. This is so because if one understands the ways and means by which a financial structure accelerates or impedes economic growth, one can, in principle, devise a structure which enhances the acceleration of growth while minimizing the impediments.[6]

The preceding discussion can perhaps be clarified by means of a crude illustration. Laos probably does not need an organized stock exchange

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[5] In the United States, in 1962, 40 per cent of family units earning less than $5000 a year held claims against life insurance and pension funds, compared with 85 per cent of families with annual income over $25,000 holding such claims. With respect to stocks and other investment assets, 17 per cent of those earning under $5000 and 90 per cent of those earning over $25,000 held them. For all families the percentages holding claims against life insurance and pension funds and stocks and other investment were 58 and 29 respectively. See Paul B. Trescott, Money, Banking and Economic Welfare (New York: McGraw-Hill, 1965), p. 293.

[6] On the importance of "financial innovation" in economic development, see Rondo Cameron et al, Banking in the Early Stages of Industrialization (Oxford: Oxford University Press, 1967), pp. 1-9.

(nor does it have one). For one thing, there are no corporate issues in existence. For another, there is little prospect of productive domestic corporations seeking capital at large in the near future. It would be preposterous to set up a stock market in Laos on the grounds that more advanced countries have one. But neither does Laos have a network of savings banks, and its voluntary domestic savings are pitifully low. Does this mean that the establishment of savings banks in the Lao countryside would use resources that could be more efficiently employed in alternative occupations? The answer is by no means clear.

Statistical evidence which bears on the issue raised in the preceding paragraphs, while not conclusive, is highly suggestive. Two studies of economies not vastly different from that of Thailand provide concrete evidence that there is a high degree of correlation between such a universally accepted determinant of capital formation and growth as the ratio of saving to income, on the one hand, and the proportion of savings held in the form of financial paper (a ratio which reflects the sophistication of financial markets), on the other. The first of these studies analyzes the results of saving surveys in a number of ECAFE countries conducted in the second half of the last decade.[7] This study shows a clear relationship between the percentage of household saving to personal

[7] United Nations, Economic Bulletin for Asia and the Far East (Bangkok: Department of Economic Affairs, ECAFE, December 1962). Unfortunately Thailand was not one of the countries which have conducted saving surveys in response to the ECAFE request.

disposable income and the ratio of saving in financial assets to tangible assets (see Chart I). The other study pertains to a survey of saving in the Philippines and is much more emphatic than the former study in asserting that:

> "Financial activities are not simply a mirror image of real activities. They can and do lead an independent existence: and can and do influence real variables."[8]

In this study of Philippine saving, which is of special interest to Thailand because of similarities between the two countries in their strategy of economic growth, Hooley found that growing availability and accessibility of outlets for saving has contributed to a rise in the rate of saving. These outlets were associated with the growth of banks and other financial intermediaries which provided the households with instruments into which an increasing amount of these savings was converted.[9] Savers seek outlets which combine an attractive return with other characteristics of value to the savers, such as liquidity, safety, or diversification. It is the essence of financial intermediation that specialized institutions of the financial markets can offer such instruments to the savers as otherwise

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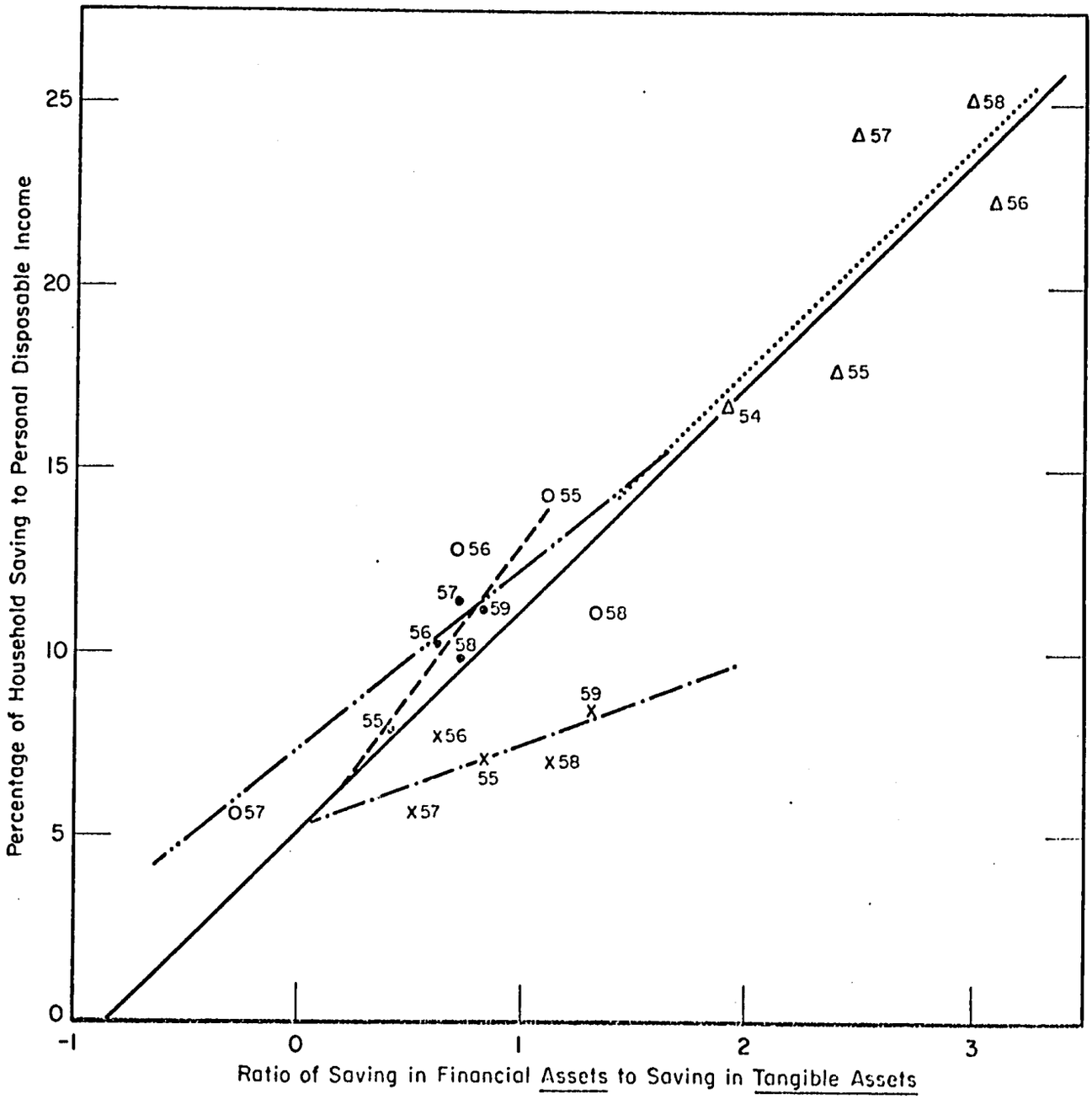
[8] R. W. Hooley, "Implications of Saving Structure for Economic Development," The Philippine Economic Journal (Second Semester, 1962), p. 130.

[9] "The rate of domestic saving is not simply the result of psychological qualities usually called thrift. The rate of saving is inextricably tied up with the structure of saving, and in order to explain the former, one is compelled to analyze the latter." (R. W. Hooley, op. cit., p. 115); and, "There would be strong reasons for devising a change in composition of saving toward financial claims even if the rate of saving remained constant. Therefore, if the rate of saving is positively correlated to composition, the argument for encouraging the growth of financial structure becomes even stronger." (R. W. Hooley, op. cit., p. 114).

Chart I

Rate and Form of Household Saving in Four Ecafe Countries 1954-1959



Key:

- CEYLON - X
- FEDERATION OF MALAYA - O
- JAPAN - Δ
- PHILIPPINES - •
- FOUR COUNTRIES

Source: United Nations, Economic Bulletin for Asia and the Far East, December 1962, p. 9

would not be available. Thus, a saver may not be willing to share in the equity of a new corporation but he may be willing to buy a unit in an investment trust. A building society certificate may be a more effective means of tapping voluntary saving than a real estate bond, and so on.[10]

Even more suggestive is a recent study which attempts to provide a set of objective criteria to determine a country's development potential, and, by implication, to indicate the kind of indicators which are associated with rapid economic growth.[11] Seventy-three developing countries were divided into three categories, based on past performance, of high, moderate, and low growth countries. Using the technique of discriminant analysis, 29 complex indicators were used to determine the factors (groups of indicators) which best explain the differences between these groups of countries. It was found that a single discriminant function of only four variables accounted for 97 per cent of the discriminable variance between groups. Of these four variables, the degree of improvement in financial

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[10] An important concomitant of financial intermediation (other than commercial banking) is the creation of money substitutes which satisfy liquidity preference but prevent the interest rate from going as high as would be the case if business financed its expansion by borrowing directly from the households. (See Gurley and Shaw, op. cit., p. 533).

[11] Irma Adelman and Cynthia Taft Morris, "Performance Criteria for Evaluating Economic Development Potential; An Operational Approach," Quarterly Journal of Economics (May 1968).

institutions was the most important.[12] One possible implication of the study is that an improvement in the performance of financial institutions would have the effect of placing a given country in a higher growth category.[13] Still, the available statistical information cannot yet be said to prove rigorously that a greater spread of financial intermediation leads to a higher rate of voluntary saving[14] or what is even more important, to indicate the sort of institutions and instruments which would bring about a higher rate of capital formation. One has to accept the limitations of quantitative data in this respect and agree that:

> "...one cannot infer that a change in the rate of saving is brought about by increase in the share represented by financial forms. The rate and form of savings may both be influenced by other variables, both financial and non-financial."[15]

---

[12] The normalized version of the discriminant function (D') was equal to 127F plus 65K plus 108M plus 72L, where F is the degree of improvement in financial institutions, K is the degree of improvement in physical overhead capital, M the degree of modernization of outlook, and L the leadership commitment to development. Ibid, p. 273.

[13] This point will be developed further in Chapter IX.

[14] Voluntary savings are to be distinguished from compulsory saving (e.g., through taxation, pricing policies, and inflation) and from contractual saving (via contracts for life insurance, pensions, and similar arrangements) in that they come to the market without coercion on the part of the political authorities and are supplied in response to market stimuli. While data for Thailand are lacking, voluntary savings in this country are likely to be at the upper end of the range for ECAFE countries, which extends from a minimum of 70 per cent to 90 per cent of all household saving (ECAFE Bulletin, p. 9).

[15] Even though statistical evidence cannot fully demonstrate as yet that a greater degree of financial intermediation will raise the ratio of saving to income, there is by now ample evidence that it facilitates the flow of savings into investment. (ECAFE Bulletin, p. 9.)

Financial Markets in the Saving-Investment Process

Inasmuch as both statistical evidence and intuitive understanding appear inadequate to make precise the role that financial structures play or could play in the development process, it is necessary to fall back on the analytical framework of economic theory. In this theory economic growth is closely associated with capital formation. The accumulation of capital assets over time is a necessary, if not a sufficient, condition for raising the levels of income and consumption. To a large extent, even in countries with a substantial influx of foreign capital, the rate of capital accumulation will depend on the volume and disposition of domestic savings. Saving can be mobilized in a number of ways. They can be extracted from national output forcibly and compulsorily by taxation, inflation, and confiscation, or they can be diverted from consumption to investment voluntarily by offering various inducements to consumers to part with current control over resources in exchange for a claim over a greater volume of resources in the future.

The literature on development planning abounds in discussions of the reasons for low levels of voluntary saving in less developed economies. While the most important explanation lies in low levels of real income, a multitude of social, psychological, and attitudinal obstacles have been adduced, and doubts are expressed whether these obstacles can be removed

by the mere improvement in economic organization.[16] One tends to be somewhat skeptical of these non-economic impediments, if only because countries which have achieved impressive rates of capital formation were at one time or another said to operate within a similar set of constraints to voluntary saving. This is not to say, of course, that it suffices to change some financial instrument or to create a financial institution in order to augment the flow of voluntary saving, but rather that social mores and attitudes do change, sometimes quite rapidly, and that in this process of change, financial structures and their adaptations can play a part. Indeed, to the extent that a given financial structure is accepted in a society it will, of necessity, influence the beliefs and attitudes of the population. An insurance company is a social institution as well as a financial one. It used to be maintained by some, for example, that the Chinese would not tolerate soliciting for life insurance policies, both because of their

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[16] Almost every book on economic development has a section dealing with inadequacy of voluntary saving stemming from social and political, as well as economic, conditions prevailing in the less developed countries. Among the more assertive in stressing the effect of non economic factors on voluntary saving are: Ragnar Nurkse, Problems of Capital Formation in Underdeveloped Countries (Oxford: B. Blackwell, 1953), pp. 50ff; W. Arthur Lewis, The Theory of Economic Growth (London: Allen & Unwin, 1955), and Marion J. Levy, "Some Social Obstacles to Capital Formation in Underdeveloped Countries," in National Bureau of Economic Research, Capital Formation and Economic Growth: A Conference of the Universities (Princeton: Princeton University Press, 1955), pp. 441-520; A notable exception to the view that saving is the main limiting factor in capital formation and economic growth is propounded by Albert O. Hirchman, who holds that it is the "ability to invest" rather than to save which is holding back a more rapid rate of growth. See The Strategy of Economic Development (New Haven: Yale Univeristy Press, 1958), pp. 35ff.

attitude toward death and because of the role of surviving kin in relation to deceased family members. The life insurance business is now, however, a thriving one in Taiwan. Total assets of all life insurance companies rose from some 16 million N. T. dollars at the end of 1959, to over 600 million at the beginning of 1965.[17]

A major problem in development finance is that such savings as do exist tend to go to less productive uses. Traditional theory has never dealt very satisfactorily with the concept of "productive" versus "non-productive" investment, but if the aim of development planning is to maximize the rate of accumulation of capital assets over time, then one should distinguish between such investment as dwellings which do not generate further capital assets, and machine tools which do.[18] While both initial outlays may be classed as investment, it clearly matters which type predominates. Thus posed, the task of creating an appropriate financial structure for rapid development is not only to augment the flow of voluntary saving but also to channel it into a more productive

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[17] The Central Bank of China, Taiwan Financial Statistics Monthly (June 1965), p. 56. Moslems have found a way to overcome objections to collection of interest by calling such interest on productive loans "participation in profits." See R. Firth and B. S. Yamey, Capital Saving and Credit in Peasant Societies (London: Allen & Unwin, 1964).

[18] "It is at least conceivable that under conditions of forced economic growth and industrialization, capital and hence capital formation may be viewed as limited to plant, equipment, and inventories that are directly serviceable as tools." Simon Kuznets, "International Differences in Capital Formation and Financing," Capital Formation and Economic Growth: A Conference of the Universities (Princeton: Princeton University Press, 1955), pp. 19-111.

investment mix.

It is convenient to approach the issue by disaggregating the flow of savings into three components: real, directly transferred, and indirectly transferred.[19] Real savings are coterminous and simultaneous with real investment. A farmer who builds a fence around his plot saves and invests at the same time. The decision to save and to invest are lodged in the same agent.

Directly transferred savings are those where the saver deals directly with the investor (borrower). Only in the case of indirectly transferred savings does the financial market intervene between the saver and the investor.

Much of real saving and investing is believed to be optimal or at least not detrimental to the goal of capital formation.[20] In any case much of this type of saving is hardly capable of monetization and hence

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[19] See Raymond W. Goldsmith, "The Supply of Savings," in M. D. Ketchum and L. T. Kendall (eds.), Readings in Financial Institutions (Boston: Houghton Mifflin, 1965), p. 257.

[20] Self-use of savings is considered optimal within its limitations of size and scope mainly because it is believed that in most cases the act of saving would not occur without the concurrent prospect of direct investment by the saver. Most of such saving takes place in tangible assets and the act of saving is indistinguishable from that of investment. A farmer who constructs a fence around his plot is a case in point. ECAFE Bulletin (December 1962) estimates that for most of the countries in the region, except Japan, the proportion of saving retained for self-use (within the sector) was at least 50 per cent in the period surveyed (1954-59). In agriculture the proportion of retained savings in tangible form is probably much higher. De Vries puts the proportion at 80 per cent in E. K. Bauer, Proceedings of the International Conference on Agricultural and Cooperative Credit (Berkeley: University of California Press, 1952), p. 91.

of indirect transfer to investors. On the other hand, there is a good deal of evidence that a substantial proportion of directly transferred saving goes into uses remotely connected with productive investment. Much of it goes into current consumption, or into construction of luxury dwellings, the social cost of which appears much higher than the social benefit of maintaining the productivity of the labor force. Frequently the direct transfer merely shifts the composition and distribution of monetary assets without adding perceptibly to the stock of capital goods.[21]

This being the case the function of financial markets would seem to be to reduce the scope of direct transfer and, pari-passu, extend the scope of indirect transfer of saving into investment.[22] This contention merits a more extended discussion.

Fundamentally, the contention that indirect financing is more conducive to capital formation than direct saver-borrower relationships is an extension of the division of labor argument. The horizon facing the individual saver and the individual borrower is a limited one, both

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[21] See, for example, U Tun Wai, "Role of the Money Market in Supplementing Monetary Policy" in David Kruine (Ed.), Rehovath Conference on Fiscal and Monetary Problems in Developing States (New York: F. A. Praeger, 1967), pp. 161-179; also Douglas S. Paauw, Financing Economic Development (Glencoe, Illinois: The Free Press, 1960), pp. 125-30.

[22] "Economic development is retarded if only self-finance and direct finance are accessible and if financial intermediaries do not evolve." J. G. Gurley and E. S. Shaw, "Financial Aspects of Economic Development," American Economic Review (September 1955), pp. 518-19.

in terms of their skills and knowledge and in terms of their resources. Specialized financial institutions extend significantly this horizon in all dimensions.

At any given point of time there is an array of investment opportunities with corresponding returns to saver which range from the more to the less attractive in terms of return. When the saving-investment relation is a direct one, the resources of the saver will fall short of those required for some more attractive investment. The process of indirect finance extends substantially the range of choice.

It will be noted that the specialization, or division of labor, argument would suggest greater intermediation in the saving-investment process even were the two parties involved in direct transfer from saver to investor primarily concerned with maximizing the accumulation of capital assets. In fact, as suggested above, this is often far from being the case. More often than not, direct transfer takes place to facilitate the consumption of those who tend to consume more than their current income or else such transfer takes place in order to convert the excess of income over current consumption into assets of low productivity over time.[23]

Intermediation in the saving-investment process appears to be a necessary concomitant of economic development because of the very nature of

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[23] See Hugh T. Patrick, "Financial Development and Economic Growth in Underdeveloped Countries," Economic Development and Cultural Change (January 1966), pp. 178-79.

the supply of investible funds and the mechanics of growth which takes place in the less developed countries, at least in those of the "mixed" variety. The very useful distinction between "surplus" units and "deficit" units or economic sectors, applies with special cogency to the less developed countries where bulk of saving originates in households but where most of the investing is done by other sectors.[24] The process of economic growth is associated with industrialization. This, in turn, suggests the growing requirement for outside funds both because of the increasing needs for fixed capital and because of the spread of the corporate form of business organization. Thus the importance of an efficient mechanism to transfer funds from the surplus to the deficit units becomes apparent.[25]

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[24] See Gurley and Shaw, op. cit. Deficit units are those which at end of accounting period find that their increment in debt exceeds the increment in financial assets. The opposite is true for the surplus units. In most ECAFE countries more than two-thirds of total saving comes from households, but the proportion of those savings held in financial claims is low and is positively correlated with both the level of per capita income and the ratio of household saving to disposable personal income (ECAFE Bulletin, pp. 8-10).

[25] In principle, the increasing needs of corporations and government could be satisfied not only by financial intermediation but also by instrumentalities of direct finance, whereby claims against business and government are sold directly to households. But the thinness of capital markets in the less developed countries, together with the whole complex of social forces militating against this type of finance, make this extremely unlikely. It is only at a very advance stage of development that direct financing via stocks and bonds becomes truly significant. For the ECAFE countries surveyed the proportion of household saving directly transmitted to users in other sectors in 1959-60 ranged from less than 4 per cent in Ceylon to 13 per cent for Korea (ECAFE Bulletin, p. 11). In 1946-54, the corresponding proportion in the United States was 23 per cent, and this proportion actually declined sharply from the 1920s. (R. W. Goldsmith, "The Formations of Saving in the U.S.," Proceedings of the Second International Savings and Investments Congress [Brussels: Secretariat of the Congress 1959] p. 44).
Financial markets in performing their transfer function also extend the availability of entrepreneurial talent by enabling people to obtain funds other than their own.

That more efficient financial institutions facilitate the channeling of investible funds into a more productive mix has long been recognized in the literature on economic growth.[26] In commenting on their findings, Adelman and Morris have this to say:

> "The importance in D_1 of the variables representing the degree of improvement in financial institutions (F) is perhaps not surprising. It will be recalled that this indicator is an overall measure of the success of the economy in increasing the flow of domestic resources through financial institutions and the extent to which these financial organizations provide medium and long-term credit for investment in the major sectors of the economy. The degree of improvement in financial institutions, therefore, describes one fundamental aspect of successful economic performance in a developing country, the loosening of the saving-investment constraint through domestic effort. It is interesting to note that this general indicator of the effectiveness of institutions for saving and lending was chosen by the discriminant analysis in preference to the more specialized index offered by the rate of investment itself."[27]

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[26] See, for example, Charles P. Kindleberger, Economic Development (New York: McGraw Hill, 1958), p. 191. In this leading text on the subject, the author states: "One of the major tasks of the monetary authorities in development is to support the gradual expansion and proliferation of the machinery--commercial banks, saving banks, investment banking, insurance companies, government bond market, private bond and share markets, etc.--which link surplus and deficit spending units."

[27] Adelman and Morris, op. cit., p. 269.

It would thus seem that financial markets can, and should, play a positive role in development planning. Far from being merely mirror images of a given stage of economic growth, they can contribute significantly both to the level of voluntary saving and to their more efficient allocation. From this position it is but a step to see whether principles and techniques could not be evolved whereby the structure of financial markets is better adapted to that dual task. On a purely pragmatic level this has, of course, long been recognized. The record is replete with proposals for the establishment of financial institutions which are designed to improve the allocation of investment, augment the flow of voluntary saving, and accelerate capital formation. But these proposals are usually not rooted in any clear-cut concept of the way in which financial markets should be structured so as to achieve a higher rate of growth.[28] A conceptual framework capable of supporting a structure of financial markets designed to speed up the rate of economic growth can be constructed in three layers. The first of these layers is composed of those criteria of economic efficiency which have to do with optimum allocation of resources, full utilization of these resources, and reduction of constraints to competition.

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[28]For an earlier attempt in this direction see: Alek A. Rozental, "Internal Financing of Economic Development," American Journal of Economics and Sociology (August 1958); and "Mobilization of Domestic Saving," in Proceedings of the Asian Section of the International Chamber of Commerce (Karachi, 1960). Reprinted in Center for Development Planning, National Planning Association, Reprint Series # 6, Washington D. C. 1967.

Classical economic theory enables one to detect deviations from economic efficiency, if not necessarily to eliminate them. But to the developmental planner bent on accelerating the rate of growth, improvements in the efficiency of existing institutions and instruments of the financial markets may not be of overriding importance. In fact, such improvements may actually be counterproductive in those cases where the market arrangements facilitate the flow of funds into channels which have very low priority from the standpoint of developmental strategy. Hence, the second layer of the conceptual framework should include an implicit or explicit set of developmental goals and priorities against which the performance of the existing markets can be tested and towards which it can be structured. Finally, and this is particularly true in the developing countries, only a portion of the financial markets is actually or potentially amenable to developmental guidance. Many of the financial flows take place outside the purview and the scrutiny of developmental authorities, who, even when armed with the knowledge required to reform the financial markets and the power to do so, may still not be able to influence the vast volume of financing which flows through the so-called unorganized markets.

Each one of these conceptual layers will be discussed in turn.

Economic Efficiency

Those criteria which deal with resource allocation and the relation of the market structure to allocation efficiency are an integral part of the economist's intellectual baggage and need not be discussed here. Certainly the financial markets in the less developed countries have their share and more of the inefficiencies brought about by monopolistic practices, by under-utilization of resources, by lack of knowledge and skills, and by all the other circumstances which cause institutions to operate below the optimum.

One convenient index of the extent of these market inefficiencies is the discrepancy between the rewards offered to the savers and the costs to be borne by investors. While these rewards and costs need not be confined to purely financial ones, they tend to be reflected in the rates of return, on the one hand, and the cost of capital, on the other.[29] This is illustrated in the following diagram.

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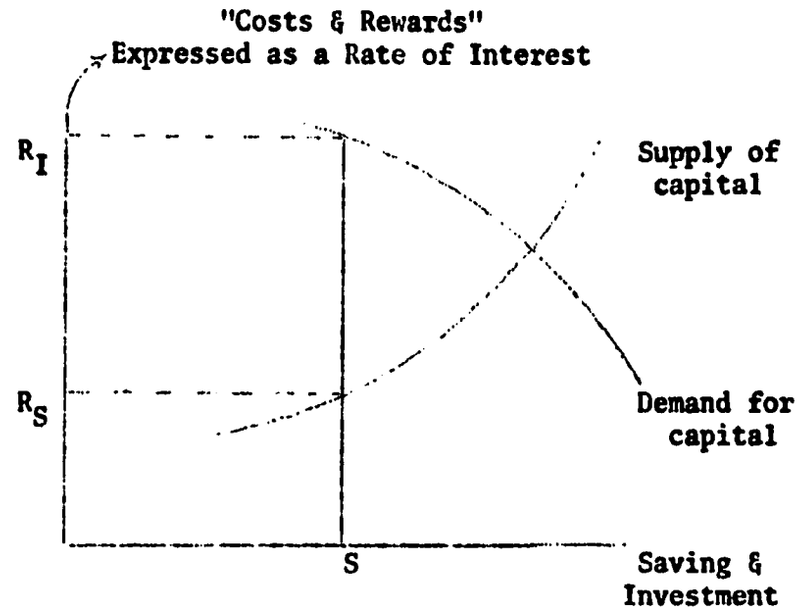
[29] See Tibor Scitovsky, Welfare and Competition: The Economics of a Fully Employed Economy (Chicago: Richard D. Irwin, 1951), pp. 223-25; and John A. Buttrick and H. Williamson, Economic Development: Principles and Patterns (New York: Prentice Hall 1954), pp. 178-82.



Given the demand and supply for lendable funds, it is seen that the market clears at S because the extra return $R_I R_S$ does not accrue to the savers. Thus, not only is the flow of saving less than it would be in the absence of the "gap" but also the cost of investment is greater than it would be otherwise. A gap measured by the distance $R_I R_S$ probably exists in all countries but is said to be particularly great in the less developed countries. This follows from the contention that in these countries not only are financial markets imperfect but, in addition, nonpecuniary factors affect both the "costs" and the "rewards."[30]

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[30]For a discussion of these non-pecuniary factors, see: D. M. Wright, "Econometric Models in Relation to Social Setting," American Economic Review (May 1952); Marion J. Levy, op. cit.; Henry G. Aubrey, Industrial Enterprise in Underdeveloped Countries (New York: National Bureau of Economic Research, November 1953) mimeo; United Nations, Formulation and Economic Appraisal of Development Projects (United Nations, 1951), pp. 90ff.; R. I. Crane, Aspects of Economic Development in South Asia, (New York: International Secretariat, Institute of Pacific Relations, 1954), p. 47.

Moreover, in the underdeveloped countries, the variance in the distribution of interest rates is larger than in the advanced countries. In many countries, the rates of interest prevailing in the money market for certain limited purposes compare favorably with those obtaining in much more advanced countries. On the other hand, capital for other purposes, particularly those connected with the acquisition of durable assets, is either completely unavailable or available only on prohibitive terms. Furthermore, the interest rates announced by the existing institutions obscure the existence of much higher rates prevailing outside the orthodox banking and financial institutions.[31]

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[31] In India, moneylenders exact interest rates varying between 12 and 50 per cent with rates of loans by the pathans reported to be as high as 300-400 per cent. See International Monetary Fund, Financial Institutions in India (February 1950), pp. 39-45. In Cuba, rates on loans for processing of sugar range from 2.5 to 4 per cent as compared with mortgage loans of from 9 to 12 per cent. More significant is the fact that a small industrial producer is unable to obtain bank accommodation at any price. See IBRD, Report on Cuba (Baltimore: The Johns Hopkins Press, 1953), p. 586. In Burma, legal rates range to a maximum of 12 per cent on secured loans and 18 per cent on unsecured loans. In Thailand, maximum rates charged by banks are 15 per cent. In Indonesia, the maximum bank rate is about 7 per cent, but industrial loans charged by a government corporation are 9 per cent. See Mobilization of Domestic Capital, p. 38. In Greece, interest rates on industrial loans reach 30 per cent. See Hollis B. Chenery, "Application of Investment Criteria," Quarterly Journal of Economics (February 1953). At the same time, rates of interest paid to savers, bondholders, and others who hold monetary claims to income are very low, with few exceptions. Thus, the rate paid on saving deposits is in the range of from 2 to 3 per cent. See Formulation and Appraisal of Development Plans, p. 306, and Mobilization of Domestic Capital, p. 55. In many countries, commercial banks either discourage savings deposits or pay as little as one-half of 1 per cent (Ibid., p. 36). The yield on government bonds seldom exceeds 4 per cent in Asia (on long-term bonds) and is about 8 per cent in Latin America. See United Nations Yearbook, 1954, p. 448. In Thailand commercial banks pay a maximum of 7 per cent per annum on deposits but charge 14 or 15 per cent per annum to ordinary borrowers. Rate payable on government bonds is currently 7 per cent per annum.

One possible strategy then, which pertains both to the efficiency of the market structure and to developmental objectives, would be to reduce the spread between the reward to the saver and the cost to the investor, particularly if the investor is one anxious to obtain long-term assets.

Developmental Goals and Priorities

The developmental bias towards the accumulation of capital assets and, hence, toward long-term finance is, as stated previously, firmly established in the literature and often finds expression in the dictum that capital formation is a necessary, if not a sufficient, condition of economic growth.[32] This helps but little in devising an ordering of goals and priorities. It tells nothing as to which segment of the economy should have first claim on resources, whether it should be public infrastructure, agriculture, or industry, or what should be the emphasis within each of the segments. More importantly, it tells nothing about the requisite shift in priorities, both sectoral and structural, which correspond to the stages of growth of the entire economy. Yet, unless there exists some theoretical underpinning for developmental goals and priorities, however broadly defined, the structuring of financial markets

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[32] Thus, for example, Adelman and Morris, in devising indicators of the performance of financial institutions in the developmental context, attach considerable importance to the way in which these institutions transfer long-term capital to agriculture and manufacturing. See Society, Politics and Economic Development (Baltimore: Johns Hopkins Press, 1967).

will be done in a conceptual vacuum and will have to be confined to ad hoc exercises which may often be at cross purposes.

It thus seems necessary to give a tentative outline of a "theory" of growth of an open dualistic economy, such as Thailand, if only to derive some overall guiding principles which could underlie the structuring of its financial markets. Unfortunately, there is no rigorously defined, universally agreed upon, optimal path of development for Thailand.

There are, at best, certain hunches whose quantitative expression lacks precision but whose direction is clear enough. These directional hunches suggest that Thailand's former reliance on exports and trade as the primary vehicles of growth will have to be decreased in favor of greater emphasis on manufacturing capacity if the country is to continue to grow in the future.

During the past several years, the ratio of total investment to GNP approximated 20 per cent annually in Thailand, but less than one-fourth of capital formation can be attributed to "manufacturing."[33]

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[33] In 1965, for example, of the Gross Domestic Product of 81 billion baht, capital formation accounted for 18.5 billion. Of this amount, only 4.2 billion can conceivably be attributed to manufacturing, and even this figure is grossly inflated by the inclusion of construction equipment in the subtotal for "machinery imports" and of automobile assembly in that of "value added to transportation equipment."

While the rate of growth of value added in manufacturing has, in recent years, been in excess of the growth rate of the GNP, much of this growth appears to have been either of the "packaging" variety--imported manufacturing components are assembled and labelled in Thailand--or else devoted to the production of building materials and components which fed the construction boom in urban areas. Both types of manufacturing activity add relatively little to the expansion of the productive base of the economy and do little to enhance its ability to increase the production of goods and services over time.

Those concerned with the country's development strategy think that increased emphasis on manufacturing, which relies more on local entrepreneurship and local resources and less on imported skills and equipment, describes the best path for Thailand's development to follow. Thus, the Minister of National Development said in 1966:

> "First, while the proportion of total investment to Gross National Product has reached a highly respectable level of 21 per cent, only a small portion of this investment is being channeled into the manufacturing industries. During the past five years, real manufacturing output increased at the annual rate of only 7.6 per cent. If we are to fulfill the annual target of a 10 per cent increase in manufacturing products in our next Five-Year Plan, and if we are to reach the industrial take-off stage in the foreseeable future, inducement must be provided to shift the emphasis from investment for short-term commercial gain to the so-called growth investment. That is to say, the government will encourage only the type of capital

> outlay which is based on long-term profits involving the establishment of permanent undertaking with an eye toward future expansion."[34]

In the second five-year plan (1967-71) the target for the manufacturing sector is an annual growth rate of about 11 per cent (compared with the GNP target of some 9 per cent). In the words of the authors of the plan:

> "Accelerated industrial development is an objective of the Second Plan which has been adopted in order to realize a structural change in the economy, with the manufacturing sector growing, creating employment opportunities, and utilizing greater supplies of indigeneous raw materials."[35]

These statements are little more than value judgments. Even so, they do not appear unreasonable. In the succeeding section an attempt will be made to clothe these hunches in what may be a first approximation to the growth theory of the small, export-oriented economy, where

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[34] Speech delivered at the Seminar on Economic Development and Investment Opportunities sponsored by the Thailand Council of the Asia Society at the Plaza Hotel, New York, October 5, 1966.

[35] National Economic Development Board, The Second National Economic and Social Development Plan (Bangkok: National Economic Development Board, 1967), p. 165.

agriculture still continues to be the primary occupation of the vast majority of the population.[36]

Prolegomena to the Growth Theory of Dualistic Open Economies[37]

A theory purporting to explain the growth of a dualistic, open economy has to show how an economic entity, with most of the characteristics of underdevelopment, reaches a stage of self-sustaining growth. For the purposes of this discussion we can define self-sustaining growth as a situation where, without any change in the value of the behavioral and/or institutional parameters, output, per capita income, and per capita savings continue to increase, although not necessarily monotonically. In

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[36] It will be remembered that this monograph is part of a larger study of developmental strategy of open dualistic economies (see Introduction). The final results and findings of this team effort are not yet available; therefore, the statements in the text should not be taken as representing these conclusions and findings. The author, as a member of the research team, did, however, benefit from many discussions and arguments with his colleagues.

[37] As stated in the text, the purpose of this section is to provide a rationale for the developmental priorities, very broadly conceived, and, hence, for policy guidance in the area of finance. No attempt will be made to present this theory in a rigorous fashion, nor is it proposed to defend its premises and method of reasoning. The writer considers the hunches of the Thai developmental authorities sufficient justification for orienting the financial markets toward the provision of long-term capital to manufacturing for export markets and merely appends his own hunches to those of the planning authorities. It is for this reason that this section is not documented even though it should not be too difficult to find, both in the descriptive literature and in the statistical data, much to support the ideas expressed. As suggested in the preceding footnote, the forthcoming studies of the Center for Development Planning address themselves more directly and far more rigorously to the problems raised in this section.

addition, an adequate theory must explain the path leading to the stage of self-sustaining growth in terms of both dualism and openness. Finally, such a theory must account for the fact that some open, dualistic economies which do begin the growth process somehow never reach the self-sustaining stage.

Merely for illustrative purposes, it could be assumed an open, dualistic economy which starts its growth process with, say, crop exports amounting to 10 per cent of its GNP (or more) will have reached self-sustaining growth when such exports fall to 5 per cent of GNP with the other 5 per cent being replaced by exports of manufacturing goods.

If the above approach is accepted, then it would follow that the process of growth of dualistic, open economies is, in essence, that of transferring resources from the crop-producing sector to that producing manufacturing goods for the export markets.

Before we can discuss how this process is triggered and what are its dynamics, we should consider the basis for the contention that growth will be maximized by a shift of resources from agriculture to manufacturing, in general, and manufacturing for exports, in particular.

With respect to manufacturing, in general, there is, first of all, the impressive historical evidence. All developed countries have increased their share of manufacturing relative to total output at the expense of agriculture. But historical evidence is seldom conclusive. A number of standard explanations have been advanced in the literature, all to the effect that manufacturing, being more efficient or more productive, is more

growth-conducive than agriculture. Thus, manufacturing is supposed to be more able to take advantage of capital-intensive inputs, to be more adapted to the establishments of large plants which, through indivisibilities, produce a range of increasing returns to scale, to be more amenable to better technology, and so on. But there are other reasons for the superiority of manufacturing in the growth process which either are specific to the type of economies under study here or else have not received adequate attention in the relevant literature. Given the kind of production function which exists in monsoon agriculture, for example, it is very difficult to utilize labor fully throughout the year. A shift to manufacturing thus tends to increase productivity per man even with little addition to capital stock and/or technology. Basically, even though agriculture can gain a lot from capital-intensive methods and better technology, its scope on these counts appears limited as compared with manufacturing. Fundamentally, the horizons for more roundabout methods of production, for deepening the production process, and so for taking advantage of division of labor, seem to be much higher in manufacturing. It also seems that manufacturing is much more able to organize its production so as to exercise control and to provide incentives. This last point may appear somewhat nebulous, but the ability to "punish" bad performance and to "reward" superior performance seems to be inherently much greater in a factory than in a field. The ability to control and to offer clearly perceived incentives is far from

insignificant. Finally, manufacturing is more capable to generate external economies and linkages. Agricultural production is less prone to generate backward linkages.

But even though a good case can be made for shift of resources from agriculture to manufacturing, it does not follow that this manufacturing activity should emphasize manufacturing for export markets. In open economies, however, there is a prima facie case for maintaining, if not increasing, the level of export earnings. If resources are shifted out of agriculture, other exports must fill the gap. But there are other, perhaps m re important, reasons why a dualistic, open economy should maintain its growth impetus by developing manufacturing for exports. When manufacturing is mainly of the packaging variety and serves chiefly to substitute for imports of consumer goods, it must contend with limitation of the market for these consumption goods, a market which in low income countries is necessarily limited. The interaction of the accelerator and the multiplier would cause an absolute fall in investment in manufacturing when consumption demand slows down its rate of increase. In contrast, demand may be expected to continue to increase when goods are produced for world market. "Import substitution" manufacturing faces a demand curve of low price and income elasticity. "Export promotion," on the other hand, faces an almost infinitely elastic demand curve, particularly when the product is one in which the country has a competitive advantage and when its total output of that product is a small fraction of the world output.

The comparative cost advantage of the type of economies represented here by Thailand would seem to lie in processing foods, fibers, and forest products. Manufacturing for exports based on processing these items benefits from abundance of cheap labor force, specificality (in climatic terms) of the raw materials, proximity to large population centers, and the fact that the long-range outlook for the world demand for these products seem to be great.

Granted that self-sustaining growth is associated with the development of manufacturing exports, what is the developmental path which the open, dualistic economies should follow in order to reach that objective?

It would seem that the growth curve has three steps, or thresholds, in it. All three "thresholds" must be crossed before the economy reaches the fragment of the curve which would insure a self-sustaining growth rate. It further appears that while many countries manage to cross one or two of these thresholds, few penetrate the last segment of the curve.

The first of these thresholds has to do with creating a surplus of resources in the agricultural sector, available for investment in sectors outside the crop-producing one. The second threshold is one where resources are transferred outside of agriculture and invested in trade, real estate, and substitution of consumer imports via domestic packaging and assembly. The last threshold is one where a further transfer of resources takes place. This time, however, in addition to the continuing, albeit diminishing, transfer out of agriculture, savings are invested in development of

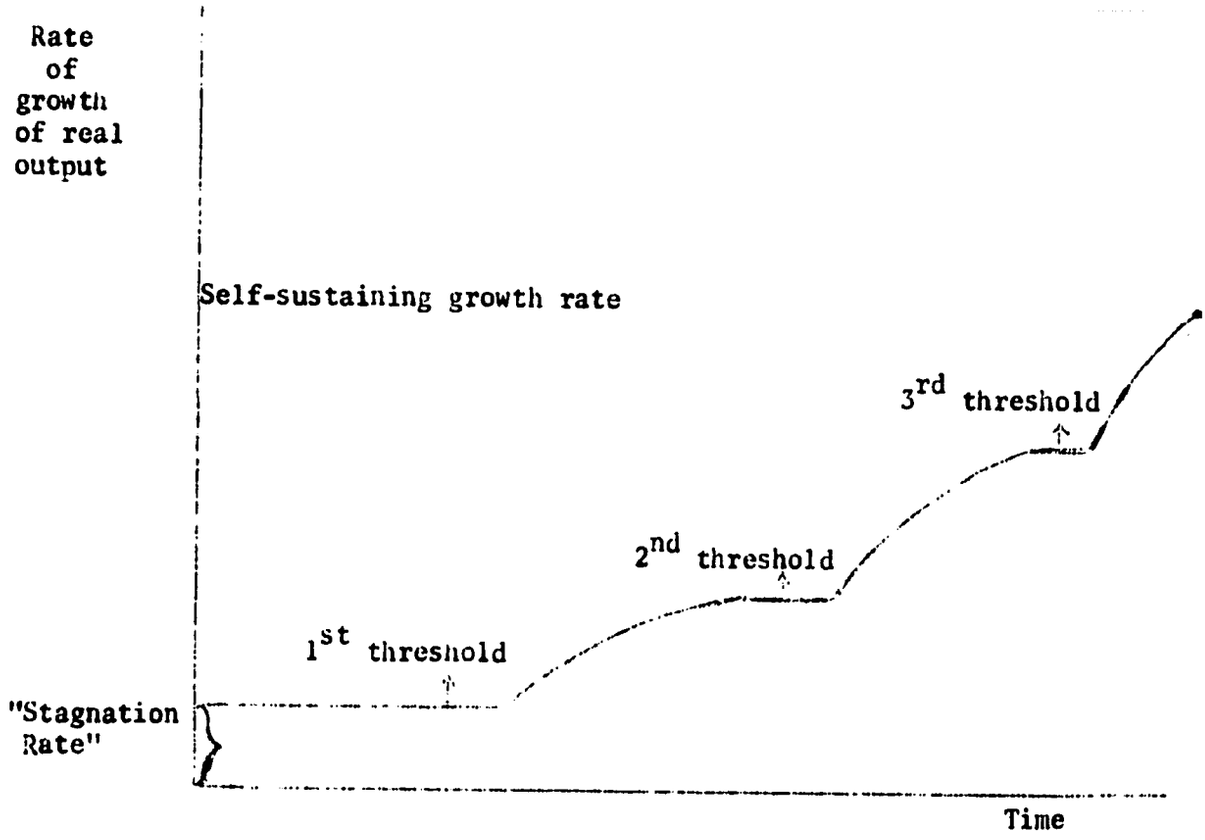
manufacturing capacity, the substantial proportion of which produces for the export markets.

It should be noted that almost every economy, even a fairly primitive one, will always devote some of its resources to real estate construction in urban areas and, for that matter, to manufacturing for a foreign market. The concept of threshold is designed to indicate some quantitatively definable proportion of GNP (or total exports) which markedly changes the structure of the economy and puts the country on a segment of its growth curve which has a steeper slope throughout most of its range (see Chart II).

Historically, the crossing of the first threshold came about when export earnings of a staple agricultural crop rose sharply. Generally, this increase was brought about by the emergence of a strong foreign demand rather than by a technological breakthrough in the production of the crop or crops. It also seems that the increase in the output of the crop, necessary to produce a large export surplus, was a function not only of the price but also of the stability of the foreign market. That is, a large increase in output was sustained over the years when the producers had a reasonable expectation that demand would continue strong. Given the economic and political structure in many of these countries, a substantial proportion of these sharply increased export earnings tended to accrue to persons outside agriculture: traders, merchants, and processors. Whenever it so happened that these persons had a high propensity to save, on the one hand, and the opportunities to derive quick

Chart II

Hypothetical Growth Curve - Open Dualistic Economies



profits in rapid pay-off activities on the other hand, the stage was set for the crossing of the second threshold.

While the crossing of the first threshold can, in most instances, be traced back to some point of time when export earnings were sharply augmented, the crossing of the second threshold is more difficult to ascribe to a single phenomenon in time. It would seem that the gradual accretion of such things as the cumulation of entrepreneurial skill, the effects of tax laws and tax administration, the political and social situation of the country, and the influx of foreign know-how and capital eventually combine in creating a state of affairs where the rate of growth of sectors such as trade and services, real estate, and even "manufacturing" exceeds that of GNP, as a whole, and certainly that of agriculture. Even so, in a number of countries the stepping across the second threshold has been accentuated and accelerated by governmental policies, especially those pertaining to tax structure, foreign exchange policy, and foreign trade generally. But these policies appear, in retrospect, often to have been mutually inconsistent or else leading to an end result other than the one sought or achieving an end that proved, ultimately, inimical to the continued growth of the economy. To cite one instance, in some of the open, dualistic economies the government simultaneously followed policies of both protection and "indigenization." The former policy tended to favor the type of import substitution policy for which the growth curve flattened out after a few years, and the latter policy tended to eliminate or sharply reduce the quality and the

quantity of the entrepreneurial talent.

The crossing of the first two of the three thresholds could and did, in fact, occur in many countries more or less haphazardly. Sooner or later some crop became subject to strong demand abroad, and sooner or later there arose profitable opportunities for investing the trade surplus in luxury hotels, automobile assembly plants, or in packaging pharmaceuticals. Sooner or later, too, the export earnings diminished, the demand for luxury hotel accommodation fell off, and the number of traders, landlords, and other nouveaux riches able and willing to buy motorcars or oral contraceptives was exhausted. The growth curve did flatten, and the last threshold was never surmounted.

What are the necessary and sufficient conditions for crossing the last threshold? In looking at historical evidence, one is attracted to what may be called the "windfall" explanation. It would seem that in order to attract talent, capital, and other resources into that sector which produces manufactured goods for export, a concatenation of circumstances had to be created where immediate and substantial gains could be realized by those traders, merchants, and processors who ordinarily are not particularly interested in projects of long gestation periods. In such projects the pay-off is remote in time even though a rational calculus would indicate that the discounted stream of income is greater than that obtainable from their current activities. Again, such a windfall seldom comes about as a result of a single event. Rather, it

appears to be a vector of such things as tax laws, other legislation, exchange rates, and trade and investment policy. Key legislative or financial events do play a part, but that part can only be comprehended against the entire economic fabric. One can speculate, for instance, that in Taiwan such a threshold was crossed when the Japanese industrialists began to use Formosa as an extension of their own manufacturing plants, but one may wonder if this would have been sufficient were it not for the imminent stoppage of U. S. aid and, indeed, for the possession of a large and skilled labor force obtainable at a low real wage. In the case of Korea, the windfall may appear to result directly from the Vietnamese war and the peculiar interpretation of U. S. procurement regulations, but, again, one may question whether the threshold could have been crossed as a result of these developments alone. As will be shown in the succeeding chapters, Thailand is well over the second threshold. Whether it will successfully cross the third one depends, in part at least, on the ways in which the conditions in its financial markets will be adjusted to facilitate rather than impede the occurrence of the "windfall" conditions.[38]

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[38] One final hunch. It would seem that once a country succeeds in inducing its traders, speculators, builders, and others to engage in manufacturing there is little danger of regression. Once in manufacturing, the entrepreneurs seem to like it and to stay with it. They find their social status enhanced, their opportunity to exploit fringe benefits even greater than in trade, and, most of all, their political and economic security better assured. One does not wish to belabor this point, but it is one of considerable significance in countries such as Thailand or Malaysia. A manufacturer employs a considerable amount of people. He uses inputs which are manufactured by other large employers of labor. Any threat to his position must be weighted in terms of its effects on those workers, technicians, and suppliers whose livelihood often hinges on the continued prosperity and peace of mind of the threatened manufacturer.

Organized and Unorganized Financial Markets

Armed with a set of developmental priorities which, in the case of Thailand, emphasize the formation of small- and medium-scale manufacturing plants which produce for export those goods and services in which the country has a comparative cost advantage, the planning authorities can begin to improve the efficiency of the financial markets and to attempt reforms and modifications of these markets so as to make them more responsive to those developmental needs. But the effectiveness of these modifications and reforms is restricted by the fact that in most of the developing countries a good deal of financial transactions are done outside the formally organized markets. In many sectors of the economy the financing of enterprises is outside the purview and scrutiny of developmental authorities. In fact, it may be convenient to consider those markets over which the authorities do not exercise supervision to be coterminous with the unorganized ones.[39] Inasmuch as the unorganized

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[39] "All this is merely another way of stating our argument that we need to have a more systematic study of how the market forces actually work or fail to work in the different types of underdeveloped country. Applied to the majority of the underdeveloped countries at the earlier "pre-take-off" stages of economic development, this now assumes a special significance. The degree of effective control that the government of such a country can exercise over the rest of the economy depends more clearly than elsewhere on the growth of suitable monetary, fiscal, and market institutions through which it can extend its control." Hla Myint, "Economic Theory and the Underdeveloped Countries," Journal of Political Economy (October 1965), p. 494.

markets tend to be amorphous, informal, and unofficial, there is little legislation and regulation which covers their operation: hence, not much is known about the institutions and instruments comprising the unorganized markets beyond the widespread conviction that their scope and importance is indeed wide.[40]

The very term "unorganized markets" is a misnomer. Such markets as those for moneylending, the rotating credit societies, and trade credit or mortgage credit are often highly organized, if frequently in a somewhat clandestine fashion. To the extent that these unorganized markets account for a substantial proportion of the total value of transactions in an economy, they tend to deflect one individual's savings into another's consumption or into those investments which have a low priority, given the societal desire to accelerate capital formation. This is one reason why the participants in these markets are anxious to remain outside the organized orbit and why the activities in these markets are often shrouded in secrecy. The lenders find the outlets for their surplus funds attractive in terms of the return offered and the timing of the payoff. The borrowers

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[40] Almost every study of the economic structure in the less developed country devotes a few pages to the unorganized markets. However, little hard information can be gleaned from these descriptions besides confirming one's impression that they are indeed significant. See particularly the various writings of U Tun Wai, infra and supra, Paauw, op. cit., and ECAFE Bulletin. Much of the discussion in the text is based on the present writer's field study in Thailand. In Chapter VII are given the empirical and quantitative results of a Survey of Urban Credit which the writer conducted under the auspices of the Bank of Thailand and which gives much information on the Thai unorganized markets.

find themselves compelled to resort to this market for a variety of reasons, of which one of the most important is that, given the purpose of the loan and the character of the available collateral, the unorganized market is the only place where they can obtain funds. No doubt other considerations also play a part. For example, in the organized money markets the degree of disclosure required, the danger of tax or other liability resulting therefrom, and the sheer administrative cumbersomeness of indirect transfers operates as a powerful constraint on would-be borrowers and lenders who choose to operate outside them.

But it should not be thought that the unorganized market is entirely composed of shady lenders and destitute or furtive borrowers with a generous sprinkling of tax dodgers, smugglers, and gamblers. Many of the transactions taking place in the unorganized markets are among kin, close friends, and business associates. Such transactions will occur in any society, however well organized. Yet other types of transactions are simply not amenable to the discipline of the organized money market, or amenable only at a heavy administrative cost. Many forms of trade credit, for example, can hardly be institutionalized through the traditional mechanisms of the money and capital markets.

Such things as discounts for prompt payment, for instance, are a form of financing which falls into this category. Much of agricultural credit will probably always remain outside the orbit of formal organizations inasmuch as the lender-borrower relation in the countryside frequently

involves the lender acting as a shopkeeper, extension agent, crop buyer, and miller at one and the same time while the borrower acts simultaneously as a consumer, entrepreneur, and laborer.

It remains true, however, that unorganized markets in most of the less developed countries act as a brake on economic growth in a number of important respects. They hold down the rate of capital formation by diverting a portion of saving to consumption. They lead to an investment mix that tends to be less productive over time than would be the case if allocation of saving to investment were determined by responsible and specialized institutions concerned with expanding the productive base of the economy.[41] They insulate a large portion of the economy from public

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[41] This is not to suggest that institutions typically operating in the organized financial markets are invariably responsible and competent. In fact, it is quite possible that some direct financing takes place in the unorganized markets because an institution under public scrutiny has been discredited in the eyes of would-be borrowers. Inasmuch, however, as it is true that the bulk of unorganized financing is for the purpose of consumption and speculation, and to the extent that there is awareness that such financing deflects resources to less productive uses, there is little that responsible authorities can do about it as long as these transactions remain outside the orbit of public policy. To quote U Tun Wai, "In the unorganized money markets of the developing countries, most of the borrowings are for financing consumer expenditures. About 80 or 90 per cent of the supply of funds is from non-institutional sources such as professional money lenders, traders, shopkeepers, landlords, relatives, and friends who charge exorbitant rates of interest. Furthermore, the link between the unorganized and the organized money market is poor, and central banks are unable to influence the terms and conditions of loans in the former." (U Tun Wai, op. cit., p. 1.) See also, I. Adelman and C. T. Morris, Society, Politics and Economic Development, pp. 118-19.

control and policy. They deprive the fisc of some revenue and, hence, of control over real resources. They create a pattern of interest rates which weigh heavily on those least able to bear the explicit or inputed costs of borrowing. Finally, they perpetuate forms of behavior not conducive to social discipline and responsibility.

On the other hand, it should be recognized that unorganized markets fulfill many needs which are not being satisfied elsewhere. Some of the practices in these markets have evolved from deeply held custom and have roots in primal organization and mores. In some cases, furthermore, a segment of the unorganized money market has developed practices and forms which turn out to be remarkably efficient in relation to their purposes.

Nevertheless, it would seem that one way in which financial markets can enhance development would be by enlarging the scope of the organized money and capital markets and correspondingly reducing the size and the scope of the unorganized markets. To the extent that this is done by adapting the institutions and instruments in the organized money markets to the functions hitherto performed outside them, it must be concluded that real progress has been achieved.

It should be emphasized at this juncture that the mere prohibition or elimination of some of the activities performed in the unorganized markets is not likely to do much good. The very existence of such activities under the common handicaps attached to them demonstrates their vigor and their acceptance. To remove them by decree or policy action

would either not be effective or, if effective, would merely leave unattended a deeply felt economic need. The latter can be justified only in those relatively rare cases where it can be shown that such activities are detrimental to important social goals and values. Rather, the task of the organized financial markets is to take over and absorb those activities which, for one reason or another, thrive in the unorganized markets.

Such a task, while difficult, is clearly not one impossible of achievement as witness the historical experience of many of the developed and developing countries.

The task may be facilitated by the fact that transactions in the unorganized markets are subject to a number of handicaps. On the one hand, these handicaps cause the interest rates and other costs of borrowing to be high, but, on the other hand, the risks, administrative costs, and lack of legal redress may make the real return to the lender much less attractive than would appear on the surface. By the same token, organized transactions could, under certain circumtances, become more attractive to lenders and borrowers hitherto reluctant to handle them for a variety of reasons. To cite one possible situation in which functions of the unorganized market could be taken over, at least in part, by the organized institutions, one could look at agricultural

credit.[42]

It is then possible to consider the organized market as the medium through which financial structure can be brought to bear on the developmental process, provided such an extension is relative to the size of the unorganized market, and provided also that the relative shrinkage of the latter does not lead to elimination of services with detrimental effects on the level of business activity and eventually on the level of the national product. Thus posed, the issue becomes one of devising measurements of the relative sizes of the two types of markets and of developing indices capable of judging whether the above aims are being achieved. This is a complex undertaking to achieve with any degree of precision, but it should not be difficult to develop some broad indicators which gauge the direction, if not the exact pace, of the interaction of the organized and the unorganized markets.

One very crude way of estimating the sizes of the two markets is to assume that the flow of cash transactions occurs principally in the unorganized markets, while those transactions settled by check

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[42] "But in most ECAFE countries the organized capital market is only a part of the capital market--the larger segment being the unorganized market. The unorganized market is centered in the rural areas." (ECAFE Bulletin, p. 23.) See Chapter III for a detailed discussion of the existing pattern of financing of rural households in Thailand and for specific suggestions for reducing the scope of unorganized markets in financing these households.

take place in the organized markets. As a strict proposition the above is certainly not true. The two types of markets are both complementary and competitive. Moneylenders borrow from the banks by writing checks on their demand deposits, and many transactions taking place within the unorganized markets employ postdated checks or similar devices as collateral. Nor is it true that indices related principally to the commercial banking system exhaust the contribution of the organized markets to total flow of finance. Still, in most of the developing countries commercial banks are by far the most important component of the organized financial markets, and they also indirectly finance other institutions. One index has been suggested by U Tun Wai which seeks to measure the size of the organized markets (and thus, by implication, that of the unorganized market) by calculating two ratios over time, the ratio of currency held by the public to total money supply and the ratio of commercial bank credit to domestic national income[43] (see Charts III and IV).

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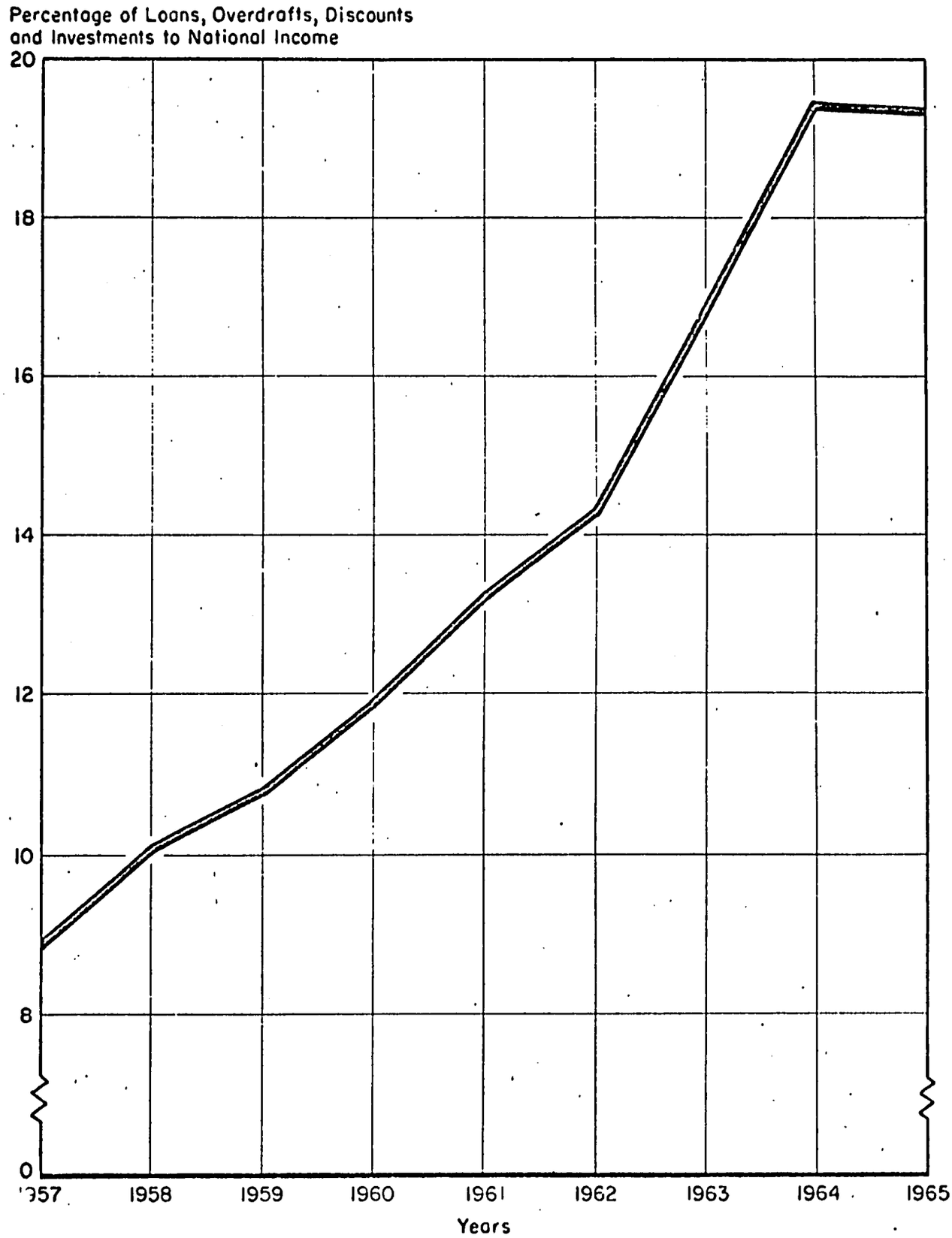
[43] U Tun Wai (Role of the Money Market..., p. 2) uses the ratio of demand deposits to money supply rather than that of currency. This ratio considers matters from the liability side of the bank's balance sheet, while the ratio of bank's credit to DNI (loans, overdrafts, discounts, and investments) relates to the asset side. Wai suggests that the ratio of bank risk assets to national income is a more reliable index of the two. However, given the commercial banks' assets and liabilities, it is quite simple to relate both indices. Thus, if M is money supply, Y national income, D demand deposits, C risk assets, A and L total assets and liabilities, then:

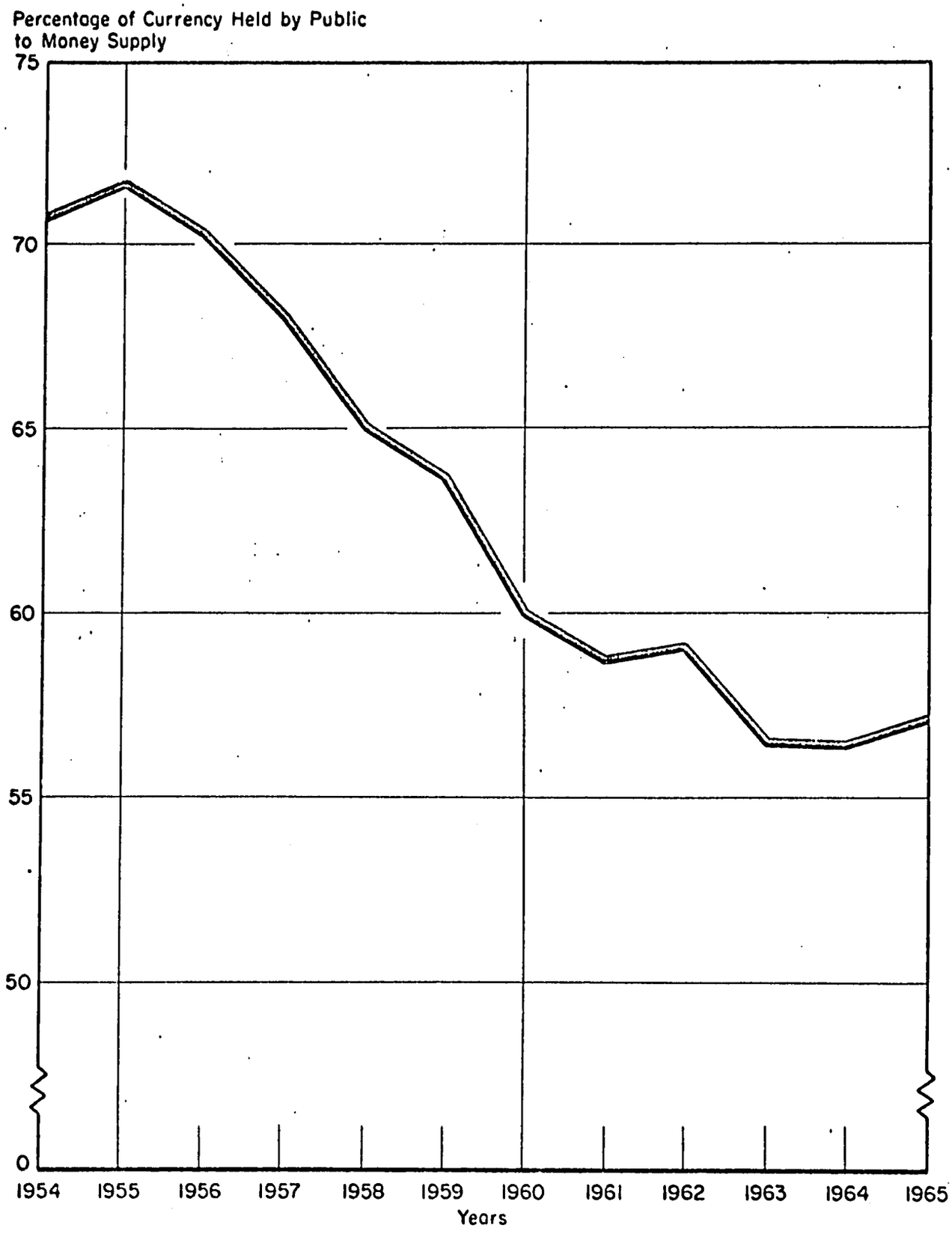
$$D/M \quad [\ M/Y \quad (\frac{C}{A}/\frac{D}{L})\ ] = \frac{C}{Y}$$

CHART III



Sources: Bank of Thailand Monthly Report, March 1966
N.E.D.B. National Income of Thailand 1957-1965

CHART IV



Source: Bank of Thailand Monthly Report, March 1966

In most developing countries the ratio of currency to money supply is about 50 per cent, compared with 20 or 30 per cent in the developed countries. The ratio of bank credit to national income hovers around a median of 28 per cent for all less developed countries. In 1963 this ratio was in the range of 40 to 45 per cent for such countries as Argentina, Brazil, Ceylon, Greece, Philippines, Tunisia, and the UAR but was less than 20 per cent for Ghana, Jamaica, Jordan, Korea, Malaysia, Mexico, Nicaragua, and Sudan. For the highly developed countries, the ratio ranged from 47 to 148 per cent.[44]

For Thailand, the ratio of currency to money supply appears to be within the range for countries in similar stage of development; i.e., about 57 per cent. Somewhat more surprising is the rather low ratio of bank credit to national income. In 1963, this ratio was slightly higher than 16 per cent, which would put Thailand substantially below such countries as Ceylon, the UAR, and the Philippines. While this may be indicative, it has already been pointed out that the crude ratios are influenced by many considerations having little to do with either the stage of economic growth or the relative importance of unorganized markets.[45] For example, in some countries, such as Ceylon, Burma, or the UAR, a high ratio of bank credit to national income represents the large

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[44] U Tun Wai, op. cit.

[45] Ibid., p. 3.

amounts of loans made by the banking system to the government, whether for doctrinaire reasons or under the pressure of deficit financing. More interesting is the fact (shown in Charts III and IV) that both ratios suggest a steady decline of the share of unorganized markets over time, a decline which, however, seems to have been arrested in recent years.

However imperfect such crude indices may be, when employed over a number of years, they do certify that an extension of the scope of the organized markets does, in fact, take place. This, however, is not sufficient in itself. Such an extension should not occur at the expense of eliminating or neglecting functions hitherto performed in the unorganized markets. One indication whether such neglect or elimination has taken place comes from the structure and pattern of interest rates, particularly in those markets which are known to be largely outside the organized ones. A sharp rise in the rate of interest on agricultural loans, for example, even when accompanied by the increase in the ratio of bank credit to national income, cannot be considered to be a movement in the desired direction. Only when over a period of years there is a perceptible trend in the ratio which suggests an increase in the scope of the organized markets, accompanied by a shift to the right of the schedule of lendable funds, can it be asserted that there has been an improvement in the efficiency of the financial markets.

The task of the development planner in the area of financial markets is thus seen as one of devising ways and means by which activities handled by the unorganized markets are gradually taken over by the

organized markets without impairing the level of economic activity and without causing social unrest.[46] The extent to which he is successful can be broadly gauged by indicators which, however crude, do provide a reliable guide when observed over a period of years.

Alternatives to Financial Intermediation--A Digression

Prior to summarizing the diverse strains of thought on the role and potential of financial markets in developmental strategy which have been discussed in the preceding sections, it may be useful to consider alternatives to financial intermediation.

Financial markets have to do with augmenting the flow of voluntary savings and channeling them into investments on the basis of decisions of specialized buyers and sellers of lendable funds. A country may play down these functions of financial markets, either because it wishes to rely on forced rather than on voluntary saving or because it wishes to remove decision-making on investment allocation from the money and capital markets, organized or not. While it appears to be true that most often the de-emphasis of financial intermediation is associated with a priori ideology or political commitment to maintain a highly centralized and controlled regime, on occasions such events as inflation or a collapse of an important financial institution may cause a country to veer sharply

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[46] "Unorganized finance that survives effective competition is worth preserving." J. G. Gurley, H. T. Patrick, and E. S. Shaw, The Financial Structure of Korea (Seoul: United States Operation Mission/Korea, 1965), p. 85.

away from reliance on money markets as the primary catalyst of saving and the chief allocator of investments.

Hence, it may be appropriate to review some of the potential and actual drawbacks of financial intermediation or, as Gurley calls it, the "dark side of finance."[47]

In the first place, under certain circumstances, financial markets as a vehicle for more rapid capital formation may be inefficient in the sense that resources so mobilized and allocated will yield less than if the same resources were employed differently. Inflation is a case in point. A country undergoing inflation, or one where inflation is either a vivid memory or an ever present possibility, will find it very difficult to mobilize saving for productive uses via the institutions and instruments of the traditional financial markets. Similarly, reliance on financial intermediation will be seriously handicapped by scarcity of securities and monetary claims of all kinds.

Secondly, even if inflation is held in check and a country has produced sufficient monetary claims to permit reasonable diversification, financial markets may prove less efficient than the alternatives of central planning or forced saving through inflation or severe taxation.

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[47] See J. G. Gurley, "Financial Structures in Developing Economies" in David Kruine (Ed.), Renovath Conference on Fiscal and Monetary Policies in Developing Economies (New York: F. A. Praeger, 1967), pp. 92-120.

Financial markets work through the interaction of manifold decisions to buy or to sell claims to resources. They are, in fact, decentralized and subject, by and large, to private time preferences and tastes of the persons acting in their individual capacity. Again, this may prove inefficient when social benefit diverges sharply from private benefit because current prices, for example, do not fully account for the fact that current output may well become a future input,[48] or when, because of the Pigovian "impatience," current consumption is valued much more highly than accumulation of capital assets.[49]

Thirdly, finance may lead to less than optimal allocation of resources not only over time but in any current period because of elements of monopoly or monopsony in the markets or because total resources are inadequate not only in terms of totality of existing claims but also in terms of skills, facilities, or managerial talent.

In the case of financial markets, such inefficiency will not necessarily correct itself. In fact, it is a characteristic of financial markets in a number of less developed countries that they can continue to be vastly profitable even though they lead to inefficient use of scarce

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[48] See J. E. Meade, "External Economies and Diseconomies," Economic Journal (March 1952), and Tibor Scitovsky, "Two Concepts of External Economies," Journal of Political Economy (April 1954).

[49] See A. C. Pigou, A Study of Public Finance (London: Macmillan and Co. 1948), pp. 97ff.

resources in terms of long-run social objectives. Given existing tastes and preferences, as well as prices, such activities as trading, speculation, and consumption loans do little to expand the productive base, but, for a while at least, they offer large rewards to financial entrepreneurs.[50]

These are telling criticisms, and much evidence drawn from a variety of countries could be adduced to attest to their cogency. But it should be borne in mind that, however valid these drawbacks of finance may be, they do not establish the superiority of alternatives. Indeed, while decentralized decision-making may lead to a slower rate of capital formation than a perfect plan, such perfection is seldom achieved. Decentralization serves to mobilize resources even more scarce than saving; namely, the skills and incentives of many persons not ordinarily subject to control by planners. Financial intermediation may be inefficient because of a narrow base or because of inadequate resources, but, in principle at least, growth in financial organization brings economies of scale and/or external economies and thus enhances the efficiency of finance. The same can hardly be said for ever-growing plan organizations in controlled societies.

As for inflation, it is seldom deliberately and successfully used as a method of accelerating progress. Even in terms of its effect

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[50] See Gurley, Financial Structures, pp. 6ff. These structures apply with special force to the unorganized markets. See Gurley, Shaw, and Patrick, Financial Structures of Korea.

on capital formation, it is a dangerous device, and, to the extent that it is effective in reducing consumption, its social and political dangers preclude its continued use.

The listing of shortcomings of financial intermediation does point out one important lesson. Financial markets, in a society determined to accelerate its growth, cannot be left entirely to their own devices. This is especially true of preindustrial societies no matter how committed they may be to the freedom of the individual or the primacy of market decisions. Some government action is clearly called for on at least two fronts. It behooves the government to intervene in order to reduce the inefficiencies of markets arising because of the inadequacy of resources and also to correct misallocation of scarce resources through financial markets. In the former case, the government will attempt to broaden the operating base of the financial institution by such devices as issuing its own securities, by guaranteeing certain loans, and by establishing under its sponsorship certain specialized institutions. In the latter case, government actions will be mainly those of regulation, supervision, and control. Inasmuch as resources may be misused by government no less than by financial markets, care should be taken lest the control does not stifle those dynamic elements which have made most of the richest countries opt for financial intermediation in preference to collectivist planning. But even in the most laissez faire economies, government action in the realm of finance has always taken place. Central bank rediscounting,

for example, is an action designed to broaden the resource base of commercial banks. Reserve requirements, on the other hand, illustrate the realization that the short-run interests of commercial banks may deviate from those of the society as a whole.

In the long run, however, the profitability as well as the efficiency of financial markets depend on the expansion of the productive base of the economy. This, of course, is realized by the operators in the financial markets themselves. It is an interesting possibility that judicious governmental control and restraint may actually be welcome by those on whom it is imposed since it insures that abandoning certain lucrative but dubious practices will simultaneously affect all participants so that no unfair advantage accrues to the least scrupulous competitors.[51]

Financial Markets as Vehicle of Economic Growth

For a country such as Thailand there are certainly no ideological or cultural obstacles to reliance on financial markets as the primary vehicle to augment savings and to channel them to more productive uses. If anything, the role of government in insuring that financial institutions perform to full potentiality has not yet been fully defined. Not only has Thailand been able to achieve an impressive record of economic performance

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[51] Gurley, Financial Structures.

with little collectivist planning and little constraint on economic freedom but also, in that country, two additional factors provide an added incentive to avoid the alternative of centralized direction of the saving-investment process. The first of these factors is the considerable investment the country already possesses in financial institutions and instruments of all kinds. The other is the circumstance that foreign capital available to Thailand now, and in the foreseeable future, can best be transmitted through the financial institutions of the kind prevailing within the country. It is possible that these same factors would operate in other small, export-oriented economies provided ideological considerations do not override the importance of these economic advantages.

It would thus appear that in Thailand, at any rate, financial markets can be structured so as to speed up the rate of economic growth. The conceptual framework developed at some length in the preceding sections suggests the following broad strategic principles:

1. The efficiency of the existing institutions and instruments of the financial markets will be improved to the extent that the cost of long-term capital is lowered and the spread between the reward to the saver and the cost to the investor narrowed.

2. Availability of capital to finance the small- and medium-size manufacturer should be increased, particularly when such a manufacturer is engaged in the production of commodities in which the country has (or could

acquire) a competitve cost advantage in world markets. One way to increase the availability of such capital would be to deflect the financing flows from those channelled into trade, construction, and speculative activities.

3. Organized financial markets should be so modified and reformed as to be able to compete successfully with the unorganized ones. In particular, organized markets should try to enlarge significantly the scope of their operations in financing productive activities by developing imaginative institutions and instruments able to attract lenders and entrepreneurs in hitherto confined to the unorganized markets. These broad strategic guidelines may be deemed too imprecise to provide a blueprint for a reform of the Thai financial markets. But this need not necessarily be a drawback, from an operational standpoint, for at least two reasons. In the first place, the Thai economy has had an excellent record of growth, particularly in the last decade, and there is no proof that the imperfections of its financial structure had the effect of preventing this growth from reaching a high rate. In fact, it could be argued that the structure and the orientation fo the Thai financial markets have mirrored the efficient growth path of the economy in the past with its institutions and instruments adapting themselves remarkably well to the financing of trade and related activities. In the second place, while, as had been argued on the preceding pages, the time may have come when Thailand needs to shift its developmental emphasis to the establishment of a manufacturing base and to expand markets for its manufacturing output, no rigorous case has been made for such a shift in developmental strategy.

It would, therefore, be inappropriate to adopt a "holistic" philosophy and to attempt a major revision of the Thai financial markets. Instead, the approach should be that of "piecemeal social engineering."[52] The main structure of the financial markets in the Kingdom should be taken as a datum, and such modifications and improvements as seem to be called for should be cautious and moderate rather than major and drastic. To this end, the three broad principles enunciated above appear quite adequate.

In short, the position taken here is that it is both possible and desirable to modify the structure of the Thai financial markets without perfect knowledge about the exact magnitudes prevailing either before or after the change, provided the direction of the change is known and provided that the change leads to results implicit in the conceptual framework developed in this chapter.[53]

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[52] See Karl Popper, "The Poverty of Historicism III," Economica, Vol. XII, No. 6 (May 1945), pp. 69-89.

[53] In welfare economic terms, the proposition is that the present situation is short of the optimal point-set boundary. Given both uncertainty in the dynamic sense and lack of firm knowledge about the precise position of this boundary, a movement in the northeast direction is best calculated to avoid gross errors and eventually to reach the desired goal.

CHAPTER II

THE FINANCIAL NEXUS AND THE THAI ECONOMY

INTRODUCTION

The financial nexus reflects the results of manifold decisions taken within the sectors associated with the nexus. The significant fact about the financial nexus is that it is a collection of economic decisions pertaining to saving and investment which are commonly considered to be of crucial significance in the process of capital formation.

In the detailed exposition of the financial nexus presented in the work of Cookson,[1] seven sectors are distinguished: households, business, state enterprises, foreigners, government, financial intermediaries, and the Central Bank. The selection of these sectors was based on the belief that significant differences in behavior exist among them with respect to the decisions affecting the fraction of current income not consumed, with respect to preferences regarding assets, and with respect to ways and means of financing excess of investment over saving and excess of consumption over income.

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[1]Forrest E. Cookson, "The Dynamics of the Thai Economy--An Application of the Open, Dualistic Economy National Income Accounting Framework" (Field Work Report #7; Washington: National Planning Association, Center for Development Planning, July 1966), pp. 22-32.

In this chapter an attempt will be made to analyze the flow of saving and investment among the sectors comprising the financial nexus. Due to the limitations of statistical information and to the lack of basic knowledge about key behavioral parameters, this attempt will be confined to four sectors only: government (including state enterprises), rural households, all other households, and rest of the world. Neither the national income accounts nor other available information enables a distinction to be made between the corporate and unincorporated business and between business and other households. On the other hand, the separation of rural households from all other households (which include all forms of business) was motivated by the belief that in an open, dualistic economy the transfer of resources from agriculture to other sectors of the economy is of key importance in understanding the dynamics of growth.[2]

Before proceeding with the attempt to analyze intersectoral resource transfers, as these are reflected in the flow of funds through the financial nexus, it is necessary to provide a broad picture of the Thai economy, its performance in recent years, the volume and trend of aggregate savings and investment, and other pertinent background information.

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[2]See Chapter 1.

The Thai Economy--Record of Recent Years

Tables II-1 through II-4 give, in capsule form, the basic information about the Thai economy. As seen in Table II-1, Gross Domestic Product has been increasing at an annual rate of 7.5 per cent in the period 1961-1965, compared with the 4.5 per cent rate in the preceding five years. In the more recent period the higher rate of growth was due to rapid increases in value added of most sectors of the economy, with the notable exception of agriculture, services, ownership of dwellings, and administration (including defense).

Agriculture, even though increasing far more slowly than the other segments of the economy, still accounts for over a third of the national income, with trade second in importance in proportion of total value added. Table II-2 shows that exports account for nearly a sixth of the gross domestic product, with gross investment running, in recent years, at some 14 per cent of total expenditures on goods and services.

Table II-3 brings out the most remarkable fact about the recent performance of the Thai economy. In spite of its high rate of growth it was able to generate an internal rate of saving which was more than adequate to finance private capital formation by voluntary savings and which contributed to the saving shortfall in the public sector. The excess of public investment over public saving was financed in the main by private and public capital inflow from abroad.

Thus, during the last decade Thailand has managed to sustain a high rate of growth, both aggregate and per capita (annual population

Table II-1

GROSS NATIONAL PRODUCT BY INDUSTRIAL ORIGIN
(in billion baht ; at constant 1962 market prices)

	1957	1958	1959	1960	1961	Change 1957-1961 in % p. a.
Agriculture	20.7	18.4	20.7	21.8	23.5	3.2
Crops	14.2	12.1	14.2	15.1	16.6	4.0
Livestock	3.7	3.7	3.9	4.0	4.1	2.6
Fisheries	1.0	0.8	0.8	0.9	1.0	-
Forestry	1.8	1.8	1.8	1.8	1.8	-
Mining, Quarrying	0.8	0.6	0.7	0.9	0.9	3.0
Manufacturing	6.2	5.5	6.4	6.9	7.1	3.4
Construction	1.6	1.6	1.9	2.2	2.4	10.7
Electricity, Water Supply	0.1	0.2	0.2	0.2	0.3	32.0
Transport, Communication	2.7	2.5	3.3	3.9	4.0	10.3
Wholesale, Retail Trade	9.5	8.5	9.6	10.7	10.8	3.3
Banking, Insurance, Real Estate	0.8	0.8	1.1	1.3	1.6	19.0
Ownership of Dwellings	2.4	2.5	2.6	2.7	2.8	3.9
Public Administration, Defense	2.6	2.5	2.5	2.8	3.0	3.6
Services	4.1	4.3	4.9	5.2	5.4	7.1
Gross Domestic Product	51.5	47.4	53.9	58.6	61.8	4.7
Net Income from Abroad	-0.3	-0.2	-0.1	-0.1	-0.1	
Gross National Product	51.2	47.2	53.8	58.5	61.7	

Source: Based on World Bank compilations derived from information provided by the National Economic Development Board.

Note: The exchange rate is currently 20.80 baht to the U.S. dollar.

(continued)
Table II-1

GROSS NATIONAL PRODUCT BY INDUSTRIAL ORIGIN
(in billion baht ; at constant 1962 market prices)

	1961	1962	1963	1964	1965	Change 1961-1965 in % p.a.
Agriculture	23.5	23.9	25.8	27.4	27.7	4.2
Crops	16.6	17.1	18.3	19.8	20.2	5.0
Livestock	4.1	3.7	3.9	3.6	3.5	-3.5
Fisheries	1.0	1.2	1.5	1.8	2.0	19.0
Forestry	1.8	1.9	2.1	2.2	2.0	2.7
Mining, Quarrying	0.9	1.0	1.0	1.1	1.3	9.6
Manufacturing	7.1	7.4	8.6	10.0	11.2	12.1
Construction	2.4	2.7	3.4	3.6	3.9	12.9
Electricity, Water Supply	0.3	0.4	0.4	0.5	0.5	13.6
Transport, Communication	4.0	4.4	4.6	5.3	5.9	10.2
Wholesale, Retail Trade	10.8	11.5	12.8	14.5	15.5	9.5
Banking, Insurance, Real Estate	1.6	1.9	2.1	2.4	2.8	15.0
Ownerships of Dwellings	2.8	2.9	3.0	3.1	3.2	3.4
Public Administration, Defense	3.0	3.0	3.3	3.4	3.8	6.1
Services	5.4	5.7	6.1	6.3	6.7	5.5
Gross Domestic Product	61.8	64.8	71.1	77.6	82.5	7.5
Net Income from Abroad	-0.1	-0.1	-	-0.1	-	
Gross National Product	61.7	64.7	71.1	77.5	82.5	

Table II-2

EXPENDITURE ON GROSS DOMESTIC PRODUCT
(in billion baht ; at current market prices)

	1957	1958	1959	1960	1961	Change 1957-1961 in % p.a.
Consumption	39.2	40.6	42.7	45.5	49.6	6.1
Private	35.0	36.4	38.2	40.8	44.3	6.1
Public	4.2	4.2	4.5	4.7	5.3	6.0
Gross Investment	7.1	6.6	7.8	9.3	9.7	8.1
Private	5.6	5.2	5.8	6.8	6.7	4.7
of which: Fixed Capital	(5.1)	(5.0)	(5.2)	(6.0)	(6.3)	(5.4)
Public	1.5	1.4	2.0	2.5	3.0	19.0
of which: Fixed Capital	(1.2)	(1.1)	(1.7)	(2.2)	(3.0)	(25.8)
Expenditure on Consumption and Gross Investment	46.3	47.2	50.5	54.8	59.3	6.4
Exports of Goods and Services	8.6	7.1	8.1	9.3	10.9	6.1
Expenditure on GDP and Imports	54.9	54.3	58.6	64.1	70.2	6.3
Less: Imports of Goods and Services	8.9	8.4	9.3	9.9	10.7	4.7
Expenditure on GDP	46.0	45.9	49.3	54.2	59.5	6.7
Statistical Discrepancy	1.8	0.1	1.4	1.1	-	
Gross Domestic Product	47.8	46.0	50.7	55.3	59.5	5.6

Source: See Table II-1.

Table II-2

EXPENDITURE ON GROSS DOMESTIC PRODUCT
(in billion baht ; at current market prices)

	1961	1962	1963	1964	1965	Change 1961-1965 in % p. a.
Consumption	49.6	53.0	56.3	60.6	63.7	6.5
Private	44.3	47.2	50.3	53.8	56.7	6.3
Public	5.3	5.8	6.0	6.8	7.0	7.2
Gross Investment	9.7	12.2	15.2	16.9	17.7	16.2
Private	6.7	9.2	11.5	12.2	12.6	17.1
of which: Fixed Capital	(6.3)	(8.6)	(11.3)	(11.8)	(12.3)	(18.2)
Public	3.0	3.0	3.7	4.7	5.1	14.2
of which: Fixed Capital	(3.0)	(3.0)	(3.7)	(4.7)	(5.1)	(14.2)
Expenditure on Consumption and Gross Investment	59.3	65.2	71.5	77.5	81.4	8.2
Exports of Goods and Services	10.9	10.7	11.0	13.8	14.8	7.9
Expenditure on GDP and Imports	70.2	75.9	82.5	91.3	96.2	8.2
Less: Imports of Goods and Services	10.7	11.9	13.2	14.7	15.8	10.2
Expenditure on GDP	59.5	64.0	69.3	76.6	80.4	7.8
Statistical Discrepancy	-	0.9	-0.9	-2.5	-0.7	-
Gross Domestic Product	59.5	64.9	68.4	74.1	79.7	7.6

Source: See Table II-1.

Table II-3

SAVING AND INVESTMENT IN THE PUBLIC AND PRIVATE SECTORS

(in billion baht; at current prices)

	1957	1958	1959	1960	1961	Change 1957-1961 in % p.a.
I. PUBLIC SECTOR						
1. Current Surplus of Government[1]	0.5	0.8	0.9	1.5	1.5	
1.1 Current Revenue	5.1	5.5	5.9	6.8	7.4	9.7
1.2 Current Expenditure	4.6	4.7	5.0	5.3	5.9	6.4
2. Current Surplus of State Enterprises	0.2	0.2	0.3	0.6	0.6	
3. Current Surplus of Local Governments	-	-	0.1	0.1	0.1	
4. Total Public Saving	0.7	1.0	1.3	2.2	2.2	33.1
5. Public Capital Formation	1.5	1.4	2.1	2.5	3.0	19.0
6. Sector Balance	-0.8	-0.4	-0.8	-0.3	-0.8	
II. PRIVATE SECTOR						
7. GDP (adjusted)[2]	46.0	45.9	49.3	54.2	59.5	
8. Transfer[3]	0.4	0.5	0.5	0.6	0.6	
9. Govt. Revenue, Surplus of State Enterprises, Local Government	-5.3	-5.7	-6.3	-7.5	-8.1	
10. Disposable Income	41.1	40.7	43.5	47.3	52.0	6.1
11. Private Consumption	-35.0	-36.4	-38.2	-40.8	-44.3	6.1
12. Private Saving	6.1	4.3	5.3	6.5	7.7	6.0
13. Private Capital Formation	5.7	5.2	5.8	6.8	6.7	4.1
14. Sector Balance	+0.4	-0.9	-0.5	-0.3	+1.0	
III. WHOLE ECONOMY						
15. Balance of Resources Current Account of Balance of Payments[4]	-0.4	-1.3	-1.3	-0.6	+0.2	

[1] Fiscal year data converted to calendar years by using quarterly averages.

[2] As estimates of gross domestic product and of expenditures on gross domestic product are independently derived, statistical discrepancies between the two series appear. For clarity of exposition, these discrepancies have been eliminated from this table. For this purpose, expenditure data were substituted for product figures because it appeared that despite their shortcomings they gave, on the whole, a somewhat better indication of year-to year changes.

(continued)
Table II-3

SAVING AND INVESTMENT IN THE PUBLIC AND PRIVATE SECTORS
(in billion baht; at current prices)

	1961	1962	1963	1964	1965	Change 1961-1965 in % p.a.
I. PUBLIC SECTOR						
1. Current Surplus of Government	1.5	1.9	1.9	2.4	2.9	
1.1 Current Revenue	7.4	8.2	8.8	10.0	11.4	11.4
1.2 Current Expenditure	5.9	6.3	6.9	7.6	8.5	9.5
2. Current Surplus of State Enterprises	0.6	0.7	0.7	(0.8)	(0.8)	(est.)
3. Current Surplus of Local Governments	0.1	0.1	0.1	(0.2)	(0.2)	(est.)
4. Total Public Saving	2.2	2.7	2.7	3.4	3.9	15.4
5. Public Capital Formation	3.0	3.0	3.7	4.7	5.1	14.2
6. Sector Balance	-0.8	-0.3	-1.0	-1.3	-1.2	
II. PRIVATE SECTOR						
7. GDP (adjusted)[2]	59.5	64.0	69.3	76.6	80.4	
8. Transfers[3]	0.6	0.5	0.9	0.8	1.5	
9. Govt. Revenue, Surplus of State Enterprises, Local Government	-8.1	-9.0	-9.6	-11.0	-12.4	
10. Disposable Income	52.0	55.5	60.6	66.4	69.5	7.5
11. Private Consumption	-44.3	-47.2	-50.3	-53.9	-56.7	6.3
12. Private Saving	7.7	8.3	10.3	12.5	12.8	13.5
13. Private Capital Formation	6.7	9.2	11.5	12.2	12.6	17.1
14. Sector Balance	+1.0	-0.9	-1.2	+0.3	+0.2	
III. WHOLE ECONOMY						
15. Balance of Resources Current Account of Balance of Payments[4]	+0.2	-1.2	-2.2	-1.0	-1.0	

[3] Derived as the difference between current expenditures of the Central Government and general Government consumption expenditure, except for 1959 and 1960 where transfers were estimated directly from the Government accounts.

[4] Current account of the balance of payments defined as consisting of the net balance of goods and services, including private transfers, but excluding investment income.

increase is estimated to be in the neighborhood of 3 per cent per annum), while maintaining a very stable level of internal prices and while acutely accumulating foreign exchange reserves (See Tables II-4 and II-5).

In the period 1963/64, the most recent for which comparative data are available, Thailand's ratios of saving and investment to income were the highest among the developing nations of Asia and the Far East, while its compound growth rate for the decade 1956/64 was exceeded only by that of Taiwan (See Table II-6). Moreover, among the nine nations included in Table II-6 Thailand is the only one that, throughout the entire decade, has maintained a stable level of prices and has avoided any foreign exchange problems.

The Thai Economy--Prospects

It was hinted in the preceding chapter that the impressive record of the Thai economy to date has been associated with the crossing of the second "threshold" to self-sustained growth and that continuing high growth rates may not be maintained unless the economy develops a more viable manufacturing base with substantial proportion of manufacturing output going to export markets. The past performance was the product of many circumstances, some of them fortuitous and some of them possibly non-recurrent.[3]

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[3] For a summary of these circumstances, of which the rapid growth in export markets appears to have been the most significant, see Forrest E. Cookson, "Prospectus--The Development of the Economy of Thailand, 1950-1965" (Washington: National Planning Association, Center for Development Planning, January, 1968), mimeo.

Table II-4

BALANCE OF PAYMENTS
(millions of U. S. dollars)

	1957	1958	1959	1960	1961	1962	1963	1964	1965
1.0 Goods and Services									
1.1 Receipts	428.2	350.1	399.9	459.1	543.3	538.8	558.6	702.9	765.1
Merchandise exports, f.o.b.	390.1	307.0	357.4	405.0	473.3	453.9	460.5	584.8	607.1
Transportation & Insurance	8.5	10.3	5.9	9.5	12.5	14.2	15.1	20.3	24.8
Foreign travel	2.7	4.2	5.2	5.4	7.7	8.8	9.9	11.6	17.0
Investment Income	5.7	6.0	4.9	6.6	8.9	10.3	12.7	18.7	25.5
Direct Investment	..	..	..	(0.2)	(0.1)	(0.3)	(0.6)	(0.7)	(0.7)
Other	..	..	..	(6.4)	(8.8)	(10.0)	(12.1)	(18.0)	(24.8)
Government n.i.e.	10.4	12.0	13.2	17.2	21.4	30.9	35.2	44.5	64.4
of which military	..	..	..	(0.8)	(2.7)	(8.9)	(15.1)	(21.1)	(33.8)
Other services	9.0	8.4	8.3	10.5	12.6	13.6	15.8	13.7	15.1
Sub-total: Services	36.3	40.9	37.5	49.2	63.1	77.8	88.0	108.8	146.8
Sub-total: Goods & Services	426.4	347.9	394.9	454.2	536.4	531.7	549.2	693.6	753.9
Private donations	1.8	2.2	5.0	4.9	6.9	7.1	9.4	9.3	11.2
1.2 Expenditures	473.8	430.1	466.8	496.6	536.0	603.6	668.4	755.7	813.0
Merchandise imports, c.i.f.	404.7	385.5	424.4	447.4	479.9	540.7	603.2	673.9	723.0
Non-monetary gold	5.1	1.1	-	2.9	6.2	7.5	7.1	5.3	6.2
Transportation & Insurance	8.8	6.2	5.4	5.7	6.6	5.5	4.3	5.7	7.7
Foreign travel	12.7	10.2	10.0	12.7	12.2	16.2	17.1	22.1	24.1
Investment Income	117.5	13.2	11.4	11.3	13.0	15.0	14.7	22.4	26.2
Direct Investment	..	..	..	(8.1)	(9.1)	(9.4)	(8.4)	(8.9)	(10.6)
Other	..	..	..	(3.2)	(3.9)	(5.6)	(6.3)	(13.5)	(15.6)
Government n.i.e.	4.6	2.9	3.9	5.3	5.0	4.4	7.4	8.7	7.2
Other services	9.3	7.5	9.8	8.9	10.9	12.3	12.2	14.5	15.3
Sub-total: Services[1]	52.9	40.0	40.5	43.9	47.7	53.4	55.4	73.4	80.5
Sub-total: Goods & Services	462.7	426.6	464.9	494.2	533.8	601.6	666.0	752.6	809.7
Private donations	11.1	3.5	1.9	2.4	2.2	2.0	2.4	3.1	3.3

(For footnotes see end of table)

Table II-4
(continued)

BALANCE OF PAYMENTS
(millions of U.S. dollars)

	1957	1958	1959	1960	1961	1962	1963	1964	1965
1.3 Net Goods and Services	-45.6	-80.0	-66.9	-37.5	7.3	-64.8	-109.8	-52.8	-47.9
2.0 Errors and Omissions (net)	-5.0	21.5	10.9	29.2	9.6	16.4	28.8	11.6	25.5
3.0 Loans and Official Donations									
Private Sector (net)	3.0	4.0	10.0	9.3	14.6	19.0	43.7	59.0	46.1
3.1.0 Drawings	..	..	..	13.0	26.0	35.4	66.6	100.8	93.3
Direct long-term	2.4[3]	3.3[3]	3.4[3]	3.4	6.5	9.6	17.8	20.3	28.3
Medium and long-term loans	-	-	4.6	5.3	11.0	23.1	43.6	68.0	51.6
Short-term trade loans and advance payments for exports	..	..	..	4.3	8.5	2.7	5.2	12.4	12.8
IFCT	-	-	-	-	-	-	-	0.1	0.6
Repayments	..	..	..	3.7	11.4	16.4	22.9	41.8	47.2
Direct long-term	..	..	..	0.5	0.8	2.1	0.8	2.2	1.5
Medium and long-term loans	-	-	-	1.7	5.5	11.9	15.8	29.0	37.7
Short-term trade loans and advance payments for imports	..	..	..	1.5	5.1	2.4	6.3	10.6	8.0
3.2 Public Sector (net)	54.7	36.1	51.9	48.0	48.1	91.4	84.0	52.4	58.3
3.2.0 Donations (net)	35.0	25.3	41.3	34.1	21.4	38.8	47.7	31.0	44.0
U.S. grants	31.4	20.7	37.5	32.0	19.4	26.8	30.6	19.0	29.2
Colombo Plan, UN Special Agencies, etc.	0.6	1.6	0.8	2.1	2.0	12.0	14.3	9.2	12.0
Japanese war debt settlement	3.0	3.0	3.0	-	-	-	2.8	2.8	2.8

(For footnotes see end of table)

Table II-4
(continued)

BALANCE OF PAYMENTS
(millions of U. S. dollars)

		1957	1958	1959	1960	1961	1962	1963	1964	1965
3.2.1.0	Drawings	28.5	14.7	23.7	28.3	41.4	64.7	51.8	48.4	36.9
	IBRD	8.2	4.1	12.2	11.2	12.4	16.7	11.5	14.7	10.4
	ICA/AID	6.0	0.6	1.9	4.0	7.3	1.7	0.6	3.3	4.0
	DLF	-	-	-	5.4	5.8	2.9	3.0	3.0	2.1
	Export-Import Bank	0.3	-	6.6	5.4	1.7	7.5	2.4	0.1	-
	Germany	-	-	-	-	-	-	0.8	7.4	7.4
	Loans from private sources	14.0	9.2	3.0	2.2	9.2	33.5	24.3	9.6	) 13.0
	Short-term loans	-	-	-	0.1	5.0	2.4	9.2	10.3	)
3.2.1.1	Repayments	6.1	3.9	13.1	14.4	14.7	12.1	15.5	27.0	22.6
	IBRD	1.4	1.5	2.5	2.6	2.7	2.8	3.9	5.4	6.2
	ICA/AID	-	-	-	-	-	0.2	0.2	0.2	0.2
	DLF	-	-	-	-	-	0.1	0.1	0.1	0.5
	Export-Import Bank	0.1	0.1	0.1	-	0.1	1.2	1.3	1.5	2.1
	Germany	-	-	-	-	-	-	-	-	-
	Loans from private sources	4.6	2.5	10.5	11.8	8.9	6.1	4.6	9.2	) 13.5
	Short-term loans	-	-	-	-	3.9	1.7	5.4	10.6	)
4.0	Miscellaneous (net)	0.6	-1.0	0.3	-7.8[4]	-1.2	-0.2	-1.1	-1.1	-1.0
5.0	Foreign Assets Net (-increase)	-7.7	19.4	-6.2	-41.2	-78.4	-61.8	-45.6	-69.1	-81.0

1
2 Excluding Non-Monetary Gold.
3 Before 1959, estimated; from 1959, based on exchange records. Excludes banks.
4 Net.
Of which: Baht liabilities to U.S. Government for surplus agricultural commodities 1.8, and payments to IBRD and IDA 4.2 .

Source: Compiled by the World Bank from IMF and Bank of Thailand.

Table II-5

PRICE INDICES

	1960	1961	1962	1963	1964	1965	December 1964	December 1965
WHOLESALE PRICE INDEX (1958 = 100)								
Agricultural products	92.4	93.1	97.8	99.3	77.5	83.9	79.9	94.7
Foodstuffs	87.3	99.7	109.6	101.5	94.7	97.7	92.3	106.9
Condiments	107.5	112.6	106.8	97.3	108.2	105.4	114.3	106.9
Leather	135.2	131.6	121.6	106.4	90.4	101.5	97.9	111.8
Cloth	100.1	100.9	101.8	101.4	106.9	112.3	112.6	111.9
Fuels	104.0	104.5	104.5	104.3	104.1	104.2	104.2	104.3
Metals	112.5	108.8	102.8	99.1	105.5	107.3	111.7	100.3
Construction Materials	100.6	100.7	111.6	110.9	111.7	111.1	112.1	111.4
Chemical Products	94.0	88.7	91.8	89.6	104.1	95.9	105.4	86.4
Miscellaneous	108.8	121.3	118.6	112.0	108.8	104.2	107.7	104.8
Wholesale Price	92.3	99.7	106.0	99.3	93.4	96.0	92.6	103.8
II. **CONSUMER PRICE INDEX**[1] (1962 = 100)								
Food	94.7	96.8	100.0	99.9	104.2	104.8	103.1	106.1
Clothing	97.2	98.2	100.0	99.8	97.9	96.9	96.7	96.9
Housing	95.6	96.0	100.0	105.2	105.6	107.5	106.0	108.0
Personal & Medical Care	99.2	99.5	100.0	101.0	101.0	102.2	101.4	102.2
Transportation	100.2	100.8	100.0	100.0	100.6	102.1	100.5	101.9
Recreation, Reading, Education	100.6	100.4	100.0	99.3	101.1	101.9	101.6	102.2
Tobacco, Alcoholic Beverages	99.9	99.9	100.0	100.0	100.0	100.0	100.0	100.0
Consumer Price	96.4	97.6	100.0	100.9	102.9	103.3	102.5	104.5

[1]For Bangkok-Thonburi metropolitan area.
Source: Department of Commercial Intelligence, Ministry of Economic Affairs.

Table II-6

Gross Domestic Saving: Ratio to GNP
Two-year averages of 1955-56, 1959-60 and 1963-64[a],
Asian and Selected Far East Countries

	Annual compound rate of growth of GNP[b] at consistent prices 1956-1964	Saving ratio						Gross capital formation as a percentage of domestic resource absorption	
		1955 + 1956		1959 + 1960		1963 + 1964			
		A	B	A	B	A	B	1955-56	1963-64
Burma.....	4.7	18.2[e]	16.8[c]	17.7	16.1	20.7[d]	19.2[d]	20.8	20.3
Ceylon.....	3.8	16.7	16.3	12.2	11.4	11.2	10.4	13.3	13.3
China (Taiwan)....	7.5	14.7	8.2	17.7	11.6	19.3	17.9	14.5	18.5
India.....	4.0	15.4	14.1	16.1	15.8	15.6[d]	15.1[d]	15.6[e]	16.1[d]
Korea, Republic of	5.5	9.5	-1.2	10.0	3.8	13.5	7.2	9.6	14.4
Malaya, States of	5.6	17.8		20.8[f]	20.3[f]	16.8[e]	16.7[a]	12.2	19.0
Pakistan.....	4.3	5.7	5.0	9.8	8.0	14.9	11.3	7.8[h]	16.5[h]
Philippines.....	4.5	7.4	6.7	9.8	9.3	17.5	17.4	8.9	14.7
Thailand.....	6.7	14.9	12.9	15.5	14.0	21.1	20.0	16.8	21.8

Source: United Nations Economic Survey of Asia and the Far East 1966, Bangkok, 1967.

Notes to Table II-6

Notes:

(1) Savings A. Indirectly estimated as the algebraic sum of gross domestic capital formation and balance of payments on current account. To assure comparability, the balance of payments on current account inclusive of transfer payments was used, irrespective of the procedures followed by different countries in compiling the Finance of Gross Domestic Capital Formation accounts. Burma, India, the Republic of Korea and Malaya in their national accounts or savings statistics eliminate a part of transfer payments from the balance of payments on current account. The series of Savings A therefore yields higher savings ratios for these countries than do the national computations.

Savings B. Indirectly estimated as the algebraic sum of gross domestic capital formation and the balance of payments on current account exclusive of grant assistance. Grant assistance which enters the Transfer Payments section of the balance of payments was estimated on the basis of information in the IMF Balance of Payments Yearbook, Volumes 13-17.

Gross capital formation as a proportion of domestic resource absorption. Resource absorption equals the difference between GDP and the balance of payments on goods and services, all taken at current market prices. This difference equals the sum of national expenditures on consumption and gross domestic capital formation.

[a]Calendar year except for Burma (fiscal years ending 30 September), India (fiscal years beginning 1 April) and Pakistan (fiscal years beginning 1 July).

[b]GNP at dominant market prices except for Burma and Malaya (GDP), India (national income) and Pakistan (GNP at constant factor cost).

[c]1956-57. [d]1962-63.

[e]The estimate of resource absorption is based on national domestic product at current factor cost. For 1955 and 1960 the trade balance had to be used instead of the balance of goods and services.

[f]1960. [g]1962. Series A average of 1962 and 1963: 16.6 per cent.

[h]The estimate of resource absorption is based on gross product at current factor cost.

Of the slightly over 12 billion baht worth of exports in 1964 nearly 10 billion consisted of crop and related exports. Less than one and one-half per cent of the value of total exports consisted of manufactured goods and a listing of these goods in Table II-7 shows that most of them were of the low capital intensity type.

While manufacturing has been increasing faster than GNP in recent years (Table II-1), its higher rate of growth seems to be the result of several rather special developments. Thus, the establishment of a major oil refinery in 1963 has not only added some 7 per cent to total value added in manufacturing but has also contributed substantially to the overall growth rate for the period 1961-65 (Tables II-8 and II-9).

Similar effects were due to establishment of a tin smelter in 1965. Moreover, items such as those of "machinery and equipment" or "chemicals and chemical products" include a very high proportion of assembly (automobiles) and packaging (pharmaceuticals) plants.

The same pattern of reliance on activity which is primarily for the purpose of satisfying the consumption demand of the urban middle class in the intermediate rather than the long run, and which does relatively little to develop the native productive base, emerges from a breakdown of capital formation by type of capital goods. Construction accounts for over 40 per cent of all capital formation in recent years and that proportion is understated in that some of the imported "capital goods" are directly related to construction activity (e.g., cranes, drills, and possibly elevators). Much of the "transport equipment" is passenger vehicles or parts for them,

Table II-7

Value of Exports of Principal Commodities, 1955-1964
(in million baht)

	1955	1956	1957	1958	1959	1960	1961	1962	1963	1964
Merchandise Exports f.o.b.	7,705	7,558	8,067	6,413	7,734	8,542	9,923	9,435	9,490	12,165
Food Crops and Products	3,640	3,619	4,373	3,443	3,350	3,725	4,997	4,667	5,236	7,016
Other Crops and Products	2,429	2,104	1,967	1,575	2,577	2,969	2,944	2,947	2,507	2,844
Minerals	537	596	621	296	469	580.2	656	718	772	1,022
Manufactured Goods (Total)	51.3	68.7	72	59	66	85	131	150	159	159
1.Wood products, including Plywood	0.3	0.7	1	3	3	6	7	8	6	9
2.Textiles, Yarns and Fabrics	6	33	23	11	10	23	24	28	35	36
3.Sarongs, Shawls,etc.	-	-	1	2	4	6	13	12	16	17
4.Cement	3	5	15	13	15	14	53	63	55	36
5.Precious Stones, Silverware	42	30	32	29	34	36	34	39	47	61

Note: Components do not add to total because several export categories have been omitted from the table, i.e., Re-exports, Fishing, Forestry, Livestock and Products, and Miscellaneous.
Source: Compiled by the World Bank from various sources including Annual Statements of Foreign Trade and the Bank of Thailand.

Table II-8

GROSS DOMESTIC PRODUCT ORIGINATING FROM MANUFACTURING

(Millions of baht)

		1961	1962	1963	1964	1965	1966
1	Food	2,370.8	2,705.1	2,510.8	2,402.6	2,529.8	3,279.5
2	Beverages	689.3	794.9	880.8	927.3	995.5	1,190.7
3	Tobacco	865.9	996.8	1,008.5	1,031.3	1,235.4	1,348.3
4	Textiles	170.7	191.3	254.9	372.5	457.2	542.0
5	Footwear, other wearing apparel and made-up textile goods	279.0	287.3	296.8	306.9	317.2	330.2
6	Wood and cork products, except furniture	293.8	348.4	472.0	558.9	620.4	609.1
7	Furniture and fixtures	86.4	100.1	100.5	104.9	108.1	116.7
8	Paper and paper products	21.5	18.8	24.4	44.9	48.8	55.8
9	Printing, publishing and allied industries	148.3	148.7	176.4	213.7	227.2	262.1
10	Leather and leather products except footwear	120.6	120.5	124.7	131.4	135.2	140.5
11	Rubber products	239.2	210.5	219.9	216.2	223.5	228.2
12	Chemicals and chemical products	459.1	467.1	521.6	621.9	734.3	854.6
13	Petroleum refining	-	-	-	166.5	637.5	795.9
14	Non-metallic mineral products except products of petroleum and coal	373.1	424.4	486.8	579.8	715.9	840.9
15	Basic metal industries	18.1	16.6	8.0	8.7	13.0	24.6
16	Electrical machinery, apparatus, appliances and supplies	32.5	40.4	29.1	26.3	27.2	32.9
17	Machinery and equipment	253.3	245.9	442.7	630.0	668.0	736.8
18	All other	220.4	320.4	316.2	360.5	372.7	393.7
19	Total value added	6,642.0	7,437.2	7,874.3	8,704.2	10,066.9	11,782.4

Source: N.E.D.B., National Income of Thailand, 1966 Edition (Bangkok, 1967).

Table II-9

GROSS DOMESTIC PRODUCT ORIGINATING FROM MANUFACTURING
Index (1961=100)

	1961	1962	1963	1964	1965	1966
1. Food	100	114.10	105.91	101.34	106.71	138.33
2. Beverages	100	115.32	127.78	134.53	166.43	172.74
3. Tobacco	100	115.12	116.47	119.10	142.67	155.71
4. Textiles	100	42.07	149.33	218.22	267.84	317.52
5. Footwear, other wearing apparel and made-up textile goods	100	102.97	106.38	110.00	43.69	118.35
6. Wood and Cork products, except furniture	100	118.58	160.65	190.23	211.16	207.32
7. Furniture	100	115.86	116.32	121.41	125.12	135.07
8. Paper and paper products	100	87.66	113.49	208.84	226.98	259.53
9. Printing, publishing and allied industries	100	100.27	118.95	144.10	153.20	176.74
10. Leather and leather products except footwear	100	99 92	103.40	108.96	112.11	116.50
11. Rubber products	100	88.00	91.93	90.38	93.44	95.40
12. Chemicals and chemical products	100	101.74	113.61	135.46	159.94	186.15
13. Petroleum	-	-	-	100	382.9	478.0
14. Non-metallic mineral products except products of petroleum and comp.	100	113.75	130.47	155.40	191.88	225.38
15. Basic metal industries	100	91.71	44.20	48.07	71.82	135.91
16. Electrical mach, apparatus, appliance and surplus	100	124.31	89.54	80.92	83.69	101.23
17. Machinery and equipment	100	97.08	174.77	248.72	263.72	290.88
18. All other	100	145.38	143.47	163.57	169.10	178.63
19. Total value added	100	111.97	118.55	131.05	151.56	177.39

Source: See Table II-8.

thus overstating even further the relative share of "capital goods" in capital formation (Table II-10).

In any case, and even if the view that Thailand should shift its strategic emphasis from crop exports to manufacturing based on local resources and oriented towards world markets is not accepted, there are reasons to believe that continuing rapid growth of the economy, on the lines followed in the past, cannot be taken for granted. As Cookson puts it:

> "For the past ten years the Thai economy has made remarkable progress; the society has achieved an internal economic equilibrium in which development could proceed at a rapid pace. At present, however, it appears that a variety of factors, some inherent to the economy and some external, are converging in such a way that internal equilibrium could be seriously upset and continued growth threatened."[4]

Monetary Accounts

Turning from the broad picture of the Thai economy to a somewhat more detailed account of its monetary aspects, it may be convenient to begin by presenting a consolidated statement of the monetary system (Tables II-11-II-15).

A consolidated monetary statement is useful on at least two counts. It gives a summary of the assets and liabilities of the organized money market and thus a glimpse into the nature of the financial instruments

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[4] F. E. Cookson, "Prospectus," p. 15.

Table II-10

GROSS FIXED CAPITAL FORMATION BY TYPE OF CAPITAL GOODS AT 1962 PRICES

(Millions of baht)

	Type of capital goods	1961	1962	1963	1964	1965	1966
1	Imports of capital goods	2,633.4	3,041.5	4,013.1	4,525.2	4,899.6	5,465.4
2	Transport equipment	793.7	947.6	1,022.7	1,270.6	1,347.2	1,519.9
3	Machinery and other equipment	1,075.8	1,304.1	1,882.3	2,220.4	2,396.7	2,716.5
4	Industrial raw materials	763.9	789.8	1,108.1	1,034.2	1,155.7	1,229.0
5	Construction	5,031.0	5,982.0	7,783.2	8,475.3	9,292.7	9,893.6
6	Private construction activity	3,087.8	4,001.3	5,118.5	5,546.5	5,967.8	6,137.1
7	Construction in urban area	1,965.3	2,932.4	4,050.9	4,399.7	4,747.9	4,912.0
8	Construction in rural area	741.5	706.8	753.8	874.3	941.7	948.9
9	New lands	381.0	362.1	313.8	272.5	278.2	276.2
10	Public construction activity	1,943.2	1,980.7	2,664.7	2,928.8	3,324.9	3,756.5
11	Public construction	1,936.6	1,971.9	2,654.7	2,919.4	3,315.3	3,746.8
12	Cost of reafforestation	6.6	8.8	10.0	9.4	9.6	9.7
13	Other domestic capital formation	2,254.0	2,615.6	3,281.2	3,763.4	3,992.3	4,238.1
14	Agricultural tools of dom.origin	215.8	215.1	243.2	234.3	245.6	250.0
15	Value added of transport eqpt.	221.1	244.6	304.8	398.5	481.3	513.9
16	Trucks, buses and cars	89.9	117.1	164.0	290.3	363.2	389.2
17	Domestic vessels	102.7	100.0	110.5	78.3	86.2	93.0
18	Rolling stock	28.5	27.5	30.3	29.9	31.9	31.7
19	Other tools & eqpt. domestically produced	42.0	39.4	61.4	60.6	68.5	71.9
20	Office eqpt.domestically produced in the public sector	145.6	173.3	115.9	155.2	152.7	169.3
21	Additional costs(import duties,insurance, transportation,mark-ups,installation, sale and municipal taxes.)	1,629.5	1,943.2	2,555.9	2,914.8	3,044.2	3,233.0
22	Gross fixed capital formation	9,918.4	11,639.1	15,077.5	16,763.9	18,184.6	19,597.1

Source: See Table II-8.

Table II-11

Consolidated Statement of the Monetary System

(Million of Baht)

Assets and Liabilities	End of Period									
	Dec. 1956	Dec. 1957	Dec. 1958	Dec. 1959	Dec. 1960	Dec. 1961	Dec. 1962	Dec. 1963	Dec. 1964	Dec. 1965
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
Foreign assets (net)	6,261.5	6,384.6	5,985.1	5,943.4	6,834.4	8,406.0	9,653.2	11,010.0	12,447.9	13,991.9
Net IMF Position	62.5	62.5	62.5	225.0	225.0	225.0	225.0	234.0	234.0	395.2
Claims on government	5,093.9	5,552.0	5,974.4	6,520.0	4,545.6	4,379.2	5,184.4	5,026.0	5,580.3	6,587.4
Claim on private sector	3,219.3	3,712.5	4,353.6	4,912.7	5,761.7	6,586.6	7,791.6	8,908.1	10,553.7	12,611.6
Unclassified assets	428.7	519.0	695.5	695.0	1,031.8	1,166.5	1,135.4	1,277.2	1,465.7	1,580.5
Assets = Liabilities	15,065.9	16,230.6	17,071.1	18,296.1	18,398.5	20,763.3	23,989.6	26,455.3	30,281.6	35,166.6
Money	7,728.4	8,196.6	8,451.9	9,076.1	10,088.4	11,075.4	11,093.3	11,881.0	12,919.0	14,332.1
Quasi - money	1,191.9	1,473.1	1,769.9	1,899.0	2,312.1	2,945.0	4,632.1	5,881.0	7,151.3	8,568.6
Government deposits (including official entities)	596.3	656.9	703.3	908.1	1,469.9	1,800.3	2,566.0	2,234.3	3,369.7	4,560.0
Bonds (Savings Bonds etc.)	71.3	86.8	105.4	133.7	168.4	213.7	301.6	430.7	590.6	712.5
Counterpart funds	351.8	452.7	375.5	451.1	464.9	544.0	566.6	483.9	382.8	162.4
Exchange difference	3,178.4	3,163.0	3,163.0	3,163.0	1,004.3	-	-	-	-	-
Capital Accounts	1,583.0	1,868.1	2,152.5	2,268.9	2,505.7	3,728.0	4,064.1	4,606.2	4,791.9	5,317.8
Unclassified liabilities	364.8	333.4	349.6	396.2	384.8	456.9	765.9	938.2	1,076.3	1,513.2

Source: Bank of Thailand.

Table II-12

Consolidated Statement of the Monetary System - Index 1956 = 100

End of Period

	Dec. 1957	Dec. 1958	Dec. 1959	Dec. 1960	Dec. 1961	Dec. 1962	Dec. 1963	Dec. 1964	Dec. 1965
Foreign assets (net)	101.97	95.59	94.76	109.13	134.25	154.17	177.43	198.84	244.06
Net IMF position	100.00	100.00	360.00	360.00	360.00	360.00	374.40	374.40	632.32
Claims on government	108.99	117.28	128.0	89.24	85.97	101.78	98.93	109.56	129.13
Claim on private sector	115.31	134.64	152.60	178.98	204.60	242.03	276.70	321.90	393.03
Unclassified assets	121.06	162.12	162.23	240.68	272.10	267.18	295.59	341.89	367.41
Assets = Liabilities	107.73	113.35	121.49	122.17	137.88	159.29	175.67	201.07	233.84
Money	105.74	109.30	115.28	130.14	142.87	143.11	153.27	166.66	185.57
Quasi - Money	122.86	154.61	158.38	192.83	245.62	386.32	490.48	596.42	720.16
Government deposits (including official entities)	110.36	118.16	152.56	246.95	302.45	431.09	375.36	566.03	764.66
Bonds (Savings Bonds etc.)	121.78	147.88	187.58	236.27	299.82	423.15	604.27	828.61	1,006.59
Counterpart funds	129.57	106.64	127.11	132.63	154.40	140.92	137.63	108.72	46.16
Exchange difference	99.64	99.64	99.64	31.64	-	-	-	-	-
Capital Accounts	118.07	136.04	143.40	158.36	234.91	256.85	291.11	302.85	333.64
Unclassified liabilities	86.02	90.20	102.22	100.28	117.88	197.60	242.06	277.89	434.02

Source: Bank of Thailand.

Table II-13

Consolidated Statement of the Monetary System (Percent distribution)

	End of Period									
	Dec. 1956	Dec. 1957	Dec. 1958	Dec. 1959	Dec. 1960	Dec. 1961	Dec. 1962	Dec. 1963	Dec. 1964	Dec. 1965
Foreign assets (net)	41.58	39.43	34.83	32.81	37.11	40.52	40.16	41.62	41.20	39.82
Net IMF position	.42	.39	.37	1.24	1.22	1.09	.94	.89	.78	1.12
Claims on government	33.83	34.20	35.01	36.00	23.58	21.11	21.57	19.00	18.47	18.67
Claims on private sector	21.38	22.87	25.51	27.12	31.29	31.75	35.52	33.67	34.93	35.91
Unclassified assets	2.85	3.20	4.08	3.84	5.60	5.62	4.73	5.63	4.98	4.47
Assets = Liabilities	100	100	100	100	100	100	100	100	100	100
Money	51.23	50.59	49.51	49.67	54.78	53.39	46.15	44.91	42.76	40.71
Quasi - money	7.91	9.08	10.36	10.38	12.56	14.21	19.27	22.23	23.67	24.36
Government deposits (including official entities)	3.22	4.04	4.12	4.96	7.98	8.68	10.68	8.45	11.16	12.94
Bonds (Savings Bonds etc.)	.47	.53	.61	.73	.92	1.03	1.26	1.63	1.96	2.04
Counterpart funds	2.33	2.78	2.19	2.46	2.53	2.62	2.36	1.83	1.28	0.46
Exchange difference	21.09	19.48	18.52	17.83	5.45	-	-	-	-	-
Capital Accounts	10.51	11.51	12.61	12.40	13.61	17.97	16.91	17.41	15.86	14.99
Unclassified liabilities	2.42	2.05	2.05	2.16	2.09	2.20	3.20	3.54	3.56	4.49

Source: Bank of Thailand.

and institutions of that market, and it also provides some insight into the elements which underlie changes in the money supply.[5]

Table II-11 gives assets and liabilities of the monetary system for the period 1956-65 arranged by three sectors, foreign, government, and private. The difference between the assets of the system and its non-monetary liabilities is the money supply, consisting of coins, paper currency, and demand deposits held by the private sector.[6]

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[5]Actually, the Thai consolidated statement comprises assets and liabilities of the Bank of Thailand, certain Treasury accounts, the commercial banks, and the Government Savings Bank. The last institution is more properly classified as a part of the capital market (see Chapter VIII).

[6]Foreign Assets (net) consist of gold, foreign exchange assets held by the Bank of Thailand, the Exchange Equalization Fund, and the net foreign exchange position of the commercial banks and certain authorized agents. The foreign exchange assets are mainly held in Pounds Sterling and United States dollars.

Prior to the establishment of the par value of the baht on 20 October 1963, foreign assets holdings of the Bank of Thailand and the EEF were valued at a uniform rate of 20 baht per U. S. dollar; since that date, the par value of 20.80 baht per U. S. dollar has been used. The foreign exchange holdings of the commercial banks and authorized agents have always been valued at the current market rate.

Claims on Government include the Bank of Thailand's overdrafts (up to November 1960) to the government, the Bank's balance at the Provincial Treasuries, and Thai Government securities held by the Bank of Thailand, the commercial banks, and the Government Savings Bank. The data include Treasury coins in circulation.

Claims on Private Sector comprise discounts, loans, and overdrafts granted by the commercial banks and the Government Savings Bank to the private sector.

Money consists of the banking system's demand liabilities "Currency" and "Deposits" which are held by the private sector. Currency consists of notes issued by the Bank of Thailand and coins issued by the Treasury Department, Ministry of Finance. Deposit money comprises mainly demand

[6] (continued)
liabilities (these also include a small account of the private sector's deposits at the Bank of Thailand, of the commercial banks, and the Government Savings Bank).

Quasi-Money comprises mainly time and savings deposits of the government and official entities held at the Bank of Thailand, the commercial banks, and the Government Savings Bank.

Government Deposits consist of demand and time deposits of the government and official entities held at the Bank of Thailand, the commercial banks, and the Government Savings Bank.

Bonds consist of Savings Bonds and Premium Savings Bonds issued by the Government Savings Bank with a maturity ranging from 3 to 5 years.

Counterpart Funds are the baht deposits, consisting of the Thai Government's baht contribution and the baht proceeds from the sale of U. S. dollars received under aid programs.

Claims on Government consist of:

1. Bank of Thailand (B.O.T.)
   - -Government bonds and Treasury bills
   - -Balances at provincial treasuries
   - -Less: Currency holdings of provincial treasuries
2. Treasury coins in circulation
3. Deposit Money Banks
   - -Government bonds and Treasury bills
   - -Loans and overdrafts to Government
4. Less: E.E.F. net liabilities to Government and Treasury net I.M.F. position

Claims on Private Sector consist of:

1. Commercial Banks
   - -Loans and overdrafts to the private sector
   - -Bills discounted
   - -Investment in shares and debentures
2. Government Savings Bank
   - -Loans and advances

Exchange Difference is an account of profits made by the Bank of Thailand in the course of purchases and sales of foreign exchange during the period of the Multiple rate system. In October 1960, 2,159 million baht from the Exchange Difference Account was used to retire some Government debts owed to the Bank of Thailand. The remaining 1,004 million baht was transferred to the Bank's own reserves in January, 1961.

[6] (continued)

Capital Accounts equals Net Worth.

Unclassified Assets consist of:

1. Bank of Thailand (B.O.T.)
   - -Bank premises
   - -Loans to staff
   - -Sundry debtors
2. Deposit Banks (including G.S.B.)
   - -Bank premises, furniture and equipment
   - -Other immovable properties and other assets
   - -Profit and loss account
   - -Less: Other assets

Unclassified Liabilities consist of:

1. Bank of Thailand
   - -IBRD and IMF deposits
   - -Sundry creditors
2. Deposit money banks

   Commercial Banks
   - -Other liabilities (Total)
   - -Profit and loss account
   - -Total demand and time deposits of B.O.T. (in local and foreign currencies)
   - -Rediscounts--other banks in Thailand
   - -Loans, overdrafts and advances--other banks in Thailand
   - -Less: Cash and balances with other banks in Thailand
     Other assets--branch adjustment
     Total loans and advances--other banks in Thailand
     Margin and surety fund

   Saving Banks
   - -Current deposits of commercial banks
   - -Other liabilities
   - -Less: Balance at commercial banks and items for collection
     Bills discounted for commercial banks
     Loans and advances of commercial banks

Table II-12 shows that in the period 1956-65 all items, with the exception of counterpart funds, increased substantially in amount. The greatest increase took place in government bonds and in quasi-money. But, as shown in Table II-13, bonds still account for a minor proportion of total liabilities, whereas quasi-money (time and saving deposits) rose in relative importance from 8 per cent in 1956 to over 24 per cent in 1965.

The nature and significance of the various assets and liabilities will be examined in detail in later chapters. What will be briefly discussed here is the changes in the money supply.[7]

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[6] (continued)
In preparing its consolidated statement Thailand follows the International Monetary Fund conventions. Items which are assets of one monetary sector and liabilities of another are excluded from both sides of the account. Thus, for example, commercial banks' holdings with the Bank of Thailand are excluded and so are their borrowings.

It is almost impossible, in practice, to derive the consolidated statement from the component series published independently in Thai statistics. A lot of careful reconciliation is necessary to come fairly close. See Paul B. Trescott, "The Structure of the Thai Monetary Accounts," unpublished mimeo paper (circa 1967).

[7] As mentioned before, in the period 1957-65 Thailand's price level was so stable that, for all practical purposes, it could be taken as given, thus dispensing with the need, so urgent in analysis of the financial structures of other countries to distinguish between "real" and "nominal" financial flows and stocks. The stability of the price level can be traced directly to the management of the country's money supply.

Money supply rose during the period under discussion by 86 per cent, but its share in total liabilities actually fell from 51 per cent in 1956 to 41 per cent at the end of 1965.

As a matter of fact, the increase in money supply barely kept pace with the growth of the GNP.[8]

Indeed, such increase in money supply as did take place was due entirely to the increase in foreign exchange assets. In both the public and the private sectors increases in some assets were more than offset by increases in liabilities with the net result that these two sectors actually contributed negatively to the changes in money supply. In the public (government) sector an increase in government indebtedness to the Bank of Thailand was more than offset by a sharp increase in the public deposits at the banking system. In the private sector, while loans and advances of the commercial banks increased substantially over the period under discussion, the sector's time and savings deposits increased at nearly twice the rate of loans and advances. The increase in quasi-money, combined with what appears to have been a deliberately deflationary policy of accumulating large idle balances, has kept the money supply to a level

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[8] A simple linear regression of money supply on GNP shows that a 10 per cent increase in GNP was associated with a 9 per cent increase in money supply (and 8 per cent increase in currency, 15 per cent increase in demand deposits).

which prevented prices from rising.[9]

Financial Intermediation

The stability of the price system together with the rapid growth of the economy in a climate favorable to trade played a part in generating a high level of voluntary savings and a corresponding high rate of private capital formation. Yet only a small fraction of these savings and investment can be traced through the financial intermediaries of the organized financial markets.

As seen in Table II-14, financial assets holdings by the private sector were some 25 billion baht at the end of 1965, an increase of 3 billion from the preceding year. In 1965 total savings in the private sector amounted to nearly 13 billion baht (see Table II-3). Thus the proportion of private sector savings reflected in holdings of financial assets was less than 25 per cent.[10]

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[9] This deliberate policy of preventing the money supply from expanding faster than GNP (in spite of, presumably, the extension of the degree of monetization in the economy and a greater volume of transactions), has been often attacked by some of the more aggressive elements of the Thai economy on the grounds that it holds back the rate of expansion of the economy and prevents greater economic progress. See, for example, Bangkok Bank, Ltd., Annual Report, 1966, pp. 66-71.

[10] Tables II-14 through II-17 understate somewhat the amount of financial assets held in the organized portion of the markets. These tables are based on official statistics which do not give data on various provident funds and other institutions of the organized markets, the liabilities of which can be estimated. Such estimates will be given below. But the fact remains that the bulk of voluntary savings is channelled through the unorganized financial markets.

Table II-14

Outstanding Amounts of Private Sector Savings as Represented by Financial Asset Holdings
(million baht)

Claims on Year	Monetary System Cash	Monetary System Demand Deposits	Government Savings Banks	Commercial Bank Time Deposits	Govt. Bonds & Bills	Life Insurance Fund	Total
1956	5,420.7	2,275.1	730.0	349.4	189.3	225.5	9,190.0
1957	5,568.2	2,593.6	867.0	438.5	222.7	263.7	9,953.7
1958	5,543.2	2,917.5	949.0	621.7	261.0	290.7	10,583.1
1959	5,779.9	3,267.9	1,023.0	774.6	338.6	314.3	11,498.3
1960	6,043.9*	4,022.7*	1,248.0	1,025.7	480.5	328.1	13,148.9
1961	6,511.7*	4,563.7*	1,448.0	1,485.3	655.0	325.3	14,989.0
1962	6,573.4*	4,519.9*	1,698.0	3,140.0	770.9	333.5	17,034.8
1963	6,711.8	5,167.2*	1,975.0	4,253.0	921.0	366.8	19,394.8
1964	7,202.9	5,535.8*	2,311.8	5,614.3	1,227.2	386.9	22,278.9
1965	8,183.5	6,168.2	2,773.0	6,406.8	1,372.8	430.1	25,334.4

*Includes Cash on hand and deposits of life insurance companies.
Source: Based on data obtained from the Bank of Thailand.

Table II-15 brings out the overriding importance of the commercial banking system in organized financial intermediation. In 1965 demand and time deposits of the commercial banks accounted for half of all the liabilities, with currency accounting for an additional 32 per cent. Other liabilities were less than 20 per cent of the total outstanding. As seen in Tables II-16 and II-17, an increasing proportion of private sector savings was channelled through the commercial banks while the proportion going through other intermediaries was declining throughout most of the period 1957-65.

Table II-18 shows, however, that the commercial banks, even though they are by far the most important intermediary of the organized financial markets, account for less than 20 per cent of the volume of private investment.

In calculating the sources of private capital formation during the Second Plan period, the planners allotted less than 10 per cent of total requirements to the organized financial institutions of the total estimated requirement of some 93 billion baht. Foreign sources are estimated to provide 10 billion, financial institutions 9 billion, and the remainder to come from "self-finance."[11]

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[11] National Economic Development Board, The Second National Economic and Social Development Plan 1967-1971 (Bangkok: N.E.D.B., 1967), p. 69, mimeo.

Table II-15

Outstanding Amount of Private Sector Savings as Represented by Financial Asset Holding (Percentage)

Claims on Year	Monetary System Cash	Demand Deposits	Government Savings Bank	Commercial Bank Time Deposits	Govt. Bonds & Bills	Life Insurance Fund	Total
1956	58.98	24.76	7.94	3.80	2.06	2.45	100
1957	55.94	26.06	8.71	4.41	2.24	2.65	100
1958	52.38	27.57	8.97	5.87	2.47	2.75	100
1959	50.27	28.42	8.90	6.74	2.94	2.73	100
1960	45.97	30.59	9.49	7.80	3.65	2.50	100
1961	43.46	30.45	9.66	9.91	4.37	2.17	100
1962	38.59	26.53	9.97	18.43	4.53	1.96	100
1963	34.61	26.64	10.18	21.93	4.75	1.89	100
1964	32.33	24.85	10.38	25.20	5.51	1.74	100
1965	32.30	24.35	10.95	25.29	5.42	1.70	100

Includes Cash on hand and deposits of life insurance companies.
Note: Details may not add up to total because of rounding.
Source: Based on data obtained from the Bank of Thailand.

Table II-16

Financial Saving Flows in Thailand - Annual Changes in Private Holdings of Selected Financial Assets, 1957-1965
(million baht)

Claims on Year	Monetary System Cash	Monetary System Demand Deposits	Government Savings Banks	Commercial Banks Time Deposits	Govt. Securities	Life Insurance Fund	Total
1957	147.5	318.5	137.0	89.1	33.4	38.2	763.7
1958	-25.0	323.9	82.0	183.2	38.3	27.0	629.4
1959	236.7	350.4	74.0	152.9	77.6	23.6	915.2
1960	264.0	754.8	225.0	251.1	141.9	13.8	1650.6
1961	467.8	541.0	200.0	459.6	174.5	-2.8	1840.1
1962	61.7	43.8	250.0	1,654.7	115.9	8.2	2134.3
1963	138.4	647.3	277.0	1,113.0	150.1	33.3	2359.1
1964	491.1	368.6	336.8	1,361.3	306.2	20.1	2884.1
1965	980.6	632.4	461.2	792.5	145.6	43.2	3055.5

Source: Based on data obtained from the Bank of Thailand.

Table II-17

Financial Saving Flows in Thailand - Annual Changes in Private Holdings of Selected Financial Assets, 1957-1965
(Percentage)

Claims on Year	Monetary System Cash	Monetary System Demand Deposits	Government Savings Banks	Commercial Banks Time Deposits	Govt. Securities	Life Insurance Fund	Total
1957	19.31	41.70	17.94	11.67	4.37	5.00	100
1958	-3.97	51.46	13.03	29.11	6.09	4.29	100
1959	25.86	38.29	8.09	16.71	8.48	2.58	100
1960	15.99	45.73	13.63	15.21	8.60	0.84	100
1961	25.42	29.40	10.87	24.98	9.48	0.15	100
1962	2.89	2.05	11.71	77.53	5.43	0.38	100
1963	5.87	27.44	11.74	47.18	6.36	1.41	100
1964	17.03	12.78	11.68	47.20	10.62	0.70	100
1965	32.09	20.70	15.09	25.94	4.77	1.41	100

Note: Details may not add up to total because of rounding.
Source: Based on data obtained from the Bank of Thailand.

Table II-18

Selected Indicators of Investment Flows
(amounts in billion of baht)

	1957	1958	1959	1960	1961	1962	1963	1964	1965
Gross Investment	7.1	6.6	7.8	9.3	9.7	12.2	15.2	16.9	17.7
Private	5.6	5.2	5.8	6.8	6.7	9.2	11.5	12.2	12.6
Public	1.5	1.4	2.0	2.5	3.0	3.0	3.7	4.7	5.1
GDP (Gross Domestic Product)	47.8	46.0	50.7	55.3	59.5	64.9	68.4	74.1	79.7
Index of GDP	100.0	96.2	106.1	115.7	124.5	135.8	143.1	155.0	166.7
Gross Investment as % of GDP	14.9	14.3	15.4	16.8	16.3	18.8	22.2	22.8	22.2
Private Gross Investment as % of GDP	11.7	11.3	11.4	12.3	11.3	14.2	16.8	16.5	15.8
Index of Gross Investment	100.0	92.9	109.9	131.0	136.6	171.8	214.1	238.0	249.3
Index of Private Investment	100.0	92.8	103.6	121.4	119.6	164.3	205.4	217.9	225.0
Gross Private Sector Borrowing from Banks	0.49	0.64	0.56	0.85	0.83	1.20	1.12	1.64	2.10
Index of Private Sector Borrowing from Banks	100.0	130.6	114.3	173.5	169.4	244.9	228.6	334.7	428.6
Private Sector Borrowing as % of Private Investment	8.8	12.3	9.7	12.5	12.4	13.0	9.7	13.4	16.7

Source: Compiled by the World Bank from data provided by the National Economic Board.

Intersectoral Resource Transfers

Following the overview of the Thai economy and its monetary system, it is now time to broach what was to be the main purpose of this chapter; namely, a description of the way in which intersectoral transfers are channelled through the financial nexus. As mentioned at the outset, the attempt to trace resource transfers between sectors through changes in financial assets and liabilities will be a crude one at best. Thailand is one of the few countries in the region for which the Economic Commission for Asia and the Far East did not even attempt to estimate sectoral savings in its special study of development finance conducted in 1966/67.[12]

The nature of the difficulties (statistical, conceptual, and other) can best be inferred by indicating the method by which financial transfers out of agriculture (rural households) were estimated in one recent year.[13]

Agriculture is defined in the Thai national accounts as the value added from crops, livestock, fisheries, and forestry.[14] It provides employment and income for at least three-fourths of the Thai labor force and, although its relative share of the Gross Domestic Product shows a declining trend, it still accounts for about a third of the annual domestic

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[12] See United Nations, Asian Center on Agricultural and Allied Projects, Economic Survey of Asia and the Far East (Lahore: Punjab Government Printing Press, 1951), especially Section 4, "Sectoral Savings," pp. 17-21.

[13] See Alek A. Rozental, "A Note on the Sources and Uses of Funds in Thai Agriculture," Economic Development and Cultural Change, (forthcoming).

[14] Office of the National Economic Development Board, National Income of Thailand, 1965 (Bangkok: N.E.D.B., June 1966), p. 87.

output.[15] Savings out of this sector can be estimated either by calculating the difference between its income and expenditure or, as it is attempted here, by estimating net changes of assets over time.

Assets can be either real (acquisition of capital goods) or financial. An increase in financial assets in one sector must correspond to an increase in liabilities elsewhere. However, no such correspondence exists for increases in real assets; i.e., there are no financial liabilities in other sectors equal to the increase in real assets. Consequently, the difference between total assets and total financial liabilities gives changes in real worth or in saving of a sector for a given period of time. In this sense, saving is treated as a source of funds analogous to borrowing, to dishoarding, or to sale of assets. Similarly, funds, however acquired, must be used for acquisition of real assets, acquisition of financial assets, hoarded, or lent out. When some of these financial flows are netted out, the simple sources and uses of funds table will look as shown below:

Table II-19

Simple Sources and Uses Table for a Sector

Uses	Sources
Capital Formation	Savings
(Change) Financial Assets	
(Change) Hoarding	(Change) Borrowing

[15] See Table II-1.

Capital Formation and Saving, being national income or flow concepts, are given for a period of time. Financial assets and liabilities which are balance sheet or stock concepts are given as changes between two points of time.[16]

In attempting to fit estimated values to the items shown in the above table so as to construct a sources and uses statement for the Thai agricultural sector, the years 1962 and 1963 were chosen because some key data could not be estimated for any more recent year. Data for capital formation were those for 1963, and other data were taken as the difference between end-of-year figures for 1963 and 1962.

Uses of Funds in Thai Agriculture

The value of real assets has been assumed to be equal to gross fixed capital formation in agriculture during 1963. Estimates of capital formation in Thailand rely heavily on foreign trade statistics and, for inventory changes, on income tax returns. For these and other reasons, the figure of capital formation in agriculture, with its predominance of small operators who save and invest at the same time, cannot be considered to be much more than an approximation, and it probably understates somewhat the actual amount of investment taking place in agriculture. It should also be noted that the figure of gross capital formation in Thai agriculture in 1963,

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[16] See: Lawrence S. Ritter, "An Exposition of the Structure of the Flow-of-Funds Accounts," Journal of Finance (May 1963); and, John P. Powelson, National Income and Flow-of-Funds Analysis (New York: McGraw-Hill, 1960), pp. 215-308.

2,460 million baht at current prices, includes public as well as private capital formation. In spite of these reservations capital formation is the only item in the to-be-constructed sources and uses table which is directly obtainable from the national income data.

In order to estimate changes in financial assets it was assumed that the amount of insurance, stocks, bonds, and other instruments issued by predominantly urban institutions and purchases by agricultural households was insignificant.[17] Thus, changes in financial assets of the agricultural sector were confined to three types of instruments: commercial banks deposits (both time and current), various liabilities of the Government Savings Bank, and the deposit liabilities of various agricultural credit institutions.

Data on commercial bank deposits do not provide information on the origin of these deposits. It was assumed that the share of agriculture in the net increase of bank deposits between 1963 and 1962 was equal to the share of agricultural capital formation to total gross capital formation in 1963, or some 17 per cent, giving a figure of 298 million baht.

Data on Savings Bank liabilities are published monthly in the Bank of Thailand Bulletins, but, again, these figures do not give any indication as to the origin of these deposits. Here, the assumption was made that the share of agriculture in the increase of Government Savings Bank's liabilities

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[17] The amount may be insignificant but is most certainly positive. In particular, there is some evidence that landlords have been buying some government bonds of late.

between 1963 and 1962 was equal to the share of agriculture in the Thai Gross Domestic Product, or 36.5 per cent in 1963. This yielded a figure of 98 million baht.

Finally, it was assumed that the entire net increase in the deposit liabilities of agricultural cooperatives and other public and private institutions operating in the countryside accrued to agricultural households.[18]

With respect to hoarding, the assumption was made that only hoarding of currency is significant. It was assumed that the agricultural sector adds to its cash balances the same proportion of the increase in currency in circulation as its share in the Gross Domestic Product. This is almost certainly an understatement. While the Thai farmer has had no recent experience of inflation, the very reluctance to convert his assets into more sophisticated financial instruments suggests that his preference for currency may be greater than that of his urban counterpart.[19]

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[18] For sources of data see Chapter III, pp. 84-85.

[19] The preference of agricultural households for holding cash balances may be a factor contributing to price stability. In neighboring Vietnam, until 1965, considerable increase in the currency in circulation was barely reflected in the price index. Some of the reasons for this high liquidity preference were similar to those that presumably obtain in Thailand: lack of attractive alternative instruments, reluctance to convert cash into visible evidence of taxable capacity, and uncertainty about the future. In Vietnam, however, another special factor was operative. As the direct control of the Viet Cong over the countryside diminished, they tended to hold more currency in order to enter the market no longer subject to physical coercion.

Sources of Funds in Thai Agriculture

If the estimates of uses of funds appear to rest on slender statistical foundations, those of the sources of funds in Thai agriculture are little better than guesstimates. Here the problem hinges on deriving some estimate of the net change in agricultural borrowing. If such a figure could be obtained, the difference between the aggregate of uses of funds and the change in borrowing will give agricultural saving for the year.

The most recent estimate of agricultural indebtedness in Thailand is given in a publication entitled Agricultural Credit in Thailand, Theory, Data, Policy.[20] This publication is in the nature of a preliminary report of a sample survey of agricultural credit in the whole of Thailand, undertaken in 1962 and 1963. Total agricultural debt of farm families was estimated at some 9,122 million baht.

Inasmuch as no comparable estimates exist for other years,[21] annual changes in total farm debt can only be derived on the basis of assumptions regarding the relationship between the farm debt and other known economic magnitudes. Assuming that the ratio of such debt to sector income remains

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[20] Pantum Thisyamondol, Virach Arromdee and Millard F. Long, Agricultural Credit in Thailand, Theory, Data, Policy (Bangkok: Kasetsart University and the Kasetsart/Hawaii University 1965), Contract in Cooperation with USOM/Thailand, Chapter III.

[21] Estimates were, in fact, made for the years 1933-34 and 1952-54. The methods used and the scope of the earlier surveys are not, however, comparable with the 1962-63 survey.

relatively constant from year to year, i.e., that net indebtedness changes no faster and no slower than output, annual change in the value of farm families debt approximates 404 million baht between 1963 and 1962, or about 174 baht per debt-incurring family.[22]

Agricultural Savings and Intersectoral Transfer

The crude sources and uses compilation presented in (Table II-20)[23] derives a figure of saving in Thai agriculture for the year 1963 of 2,576 million baht. It should be emphasized most strongly that this figure has to be regarded with the utmost caution. In particular, the table, even apart from the inadequacy of primary data and the simplicity of method employed, cannot be said to reflect the totality of resources available for transfer out of agriculture. The sources and uses approach employed here cannot deal with transfers other than voluntary; i.e., those associated with the tax structure or, even more importantly in Thailand's case, with

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[22]This assumption would become untenable were farm income to fall as a result of unanticipated crop failure or some other mishap following borrowing by farm households. As it happens, however, farm income in 1963 was substantially higher than in 1962. This in itself does not make the assumption fully plausible, but it removes one of the more telling objections to its use. At the time of writing, no better alternative was available. The total number of farm families in Thailand was 3,410,309 in 1960 according to the 1960 Population Census (See Central Statistical Office, Thailand Population Census 1960, p. 3). In the sample survey 68.6 per cent of the 742 sample families were found to be in debt. See Pantum Thisyamondol et al., op. cit., p. 2.

[23]For a more sophisticated approach and yet one using a similar conceptual framework and techniques, see W. E. Davies and P. J. Drake, "Flow-of-Funds Social Accounting: A Malayan Example," The Malayan Economic Review (October, 1964). Davies and Drake do not, however, sector out agricultural households.

Table II-20

Sources and Uses of Funds, Thai Agricultural Sector, 1963

(Million Baht)

Real Assets	2,460	Saving	2,576
Cash Balances	213		
Commercial Bank Deposits	298		
Savings Banks	98	Borrowing	404
Agricultural Credit Institution	11		

Source: See text.

discriminatory price structure. To cite one such possible transfer--is the rice premium (a tax paid by exporters of rice) a form of forced saving on the part of the paddy farmer by compelling him to accept a for his crop which is presumably below one which would prevail in the absence of the premium?

Intersectoral Flow of Funds

In spite of the rudimentary techniques applied in calculating sources and uses of funds in agriculture, the very tentative nature of the data, and the rather questionable assumptions employed in allocating aggregates to agriculture, there is reason to believe that the main conclusion stemming from Table II-20 is a valid one; i.e., there has been, in 1963, a transfer of resources from agriculture to the rest of the economy. The table is so constructed that, so long as the net change in monetary assets exceeds the net change in borrowing, there must be an excess of saving over capital formation. For reasons touched upon in the preceding sections, it is almost certain that the net increase in financial assets was underestimated while that of debt was overestimated, if only because the figure for net change in debt included some intrasectoral borrowing. Thus, irrespective of the estimates of capital formation, a portion of agricultural saving was used to finance capital formation outside agriculture. This conclusion becomes even stronger when it is remembered that many forms of transfers which take place out of agriculture were not even considered in Table II-20. These included discriminatory

prices, incidence of certain taxes, and so on.

Indeed, preliminary results of Cookson's work on the dynamics of the Thai economy suggest that "historically and for some time in the future, the economy has been dependent upon the saving out of income originating from agricultural production."[24]

As a matter of fact, Cookson's estimates of savings together with independent estimates of investment by sector make it possible to construct a primitive flow-of-funds table for a recent year. In constructing such a table the sectoral saving and investment estimates will be taken as given and the available statistical information regarding financial assets and liabilities alloted to the four sectors in a way to make them consistent with these estimates.

In constructing the flow of funds given below in Table II-21 the procedure followed was similar to that used in Japan.[25] Sectoral savings were those estimated by Cookson,[26] while estimates of capital formation by sector were developed independently from national income accounts and other information. Increases in financial assets were allocated to the four sectors by the techniques suggested in the preceding section (from totals given in Table II-16), supplemented by estimates of holdings in

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[24] F. E. Cookson, "Prospectus," p. 11.

[25] See United Nations, "Savings in the Economic Growth of Postwar Japan," Economic Bulletin for Asia and the Far East (September 1960).

[26] Forrest E. Cookson, "Resource Transfers and the Dual Economy with Special Reference to Thailand," (Bangkok, 1968), unpublished mimeo paper Table V.

Table II-21

Flow of Funds - Saving and Investment by Sector, Thailand, 1964
(in million of baht)

	Total	Agriculture	Industry	Government	Foreign
Non-financial Transaction					
Gross Investment	17,700	3,284	10,916	2,690	810
Gross Savings	16,890	4,234	9,410	1,327	1,919
Statistical Discrepancy	810	126	340	235	109
Financial Transactions					
Increase in Financial Assets	2,967	1,106	1,610	196	55
Cash	491	196	270	20	5
Demand Deposits	367	73	257	18	18
Government Savings Bank	337	202	135	-	-
Time Deposits	1,361	544	681	136	-
Government Securities	306	61	214	-	31
Other Securities	10	-	9	-	1
Life Insurance	20	4	15	1	-
Provident Funds	70	22	27	21	-
Others	5	3	2	-	-
Increase in Financial Liabilities	2,967	30	2,776	1,324	-1,163
Net Increase or Decrease (-) in Financial Assets	0	1,076	-1,166	-1,188	1,218

Source: See text.

provident funds and other assets. Increases in financial liabilities were calculated as residuals. The four sectors in Table II-21, agriculture, industry, government, and foreign, correspond to rural households, all other households, government (net of state enterprises), and the rest of the world.

It thus appears that in 1964, the "industry" and government were deficit sectors and the agriculture and foreign sectors were the surplus ones.

There are reasons to believe that a similar pattern prevailed throughout most of the decade 1956-65.

CHAPTER III

FINANCING OF RURAL HOUSEHOLDS

INTRODUCTION

It was brought out in the preceding chapter that agricultural saving has exceeded capital formation in agriculture, at least in recent years. The available data suggest that, given the capital formation, the excess of saving over investment and, hence, transfer of savings out of agriculture will take place whenever annual changes in acquisition of these assets are greater than net borrowing. Indeed, the role of debt in the financing of rural households is crucial. Much of the income generating activity in the countryside would not be possible were it not for inputs coming from other sectors and obtained through the use of the facilities of the financial nexus. Even when borrowing is used for purposes of consumption, it often indirectly finances the productive process by providing the rural households with the wherewithal during the period of production of agricultural output. Thus, borrowing, by affecting both the level of agricultural income and the level of consumption, influences the level of saving. Moreover, inasmuch as rural households do have some choice in the form or in the timing of loans, agricultural credit affects not only the level but also the composition of rural saving. For those reasons, much of the discussion in this chapter revolves round the magnitude, composition, and distribution of agricultural credit.

Financial Markets and Rural Households

Rural (or farm) households will be used coterminously with the sector "agriculture," as defined in the national income statistics. Even though the share of agriculture in the Thai economy shows a decline when measured as a proportion of GNP, agriculture continues to provide employment and income for at least three-fourths of the labor force; and agricultural output provides much of the wherewithal to the export and financial nexi. The rhythm of the monsoon still permeates the cycle of credit throughout the economy. In centers remote from primary agricultural production, credit continues to be tightest in June and July, just before the planting season, and eases considerably in the last quarter of the calendar year when the rice harvest is being gathered. The primary agricultural producer may borrow little from the commercial banks directly, but those who sell to him and who buy from him depend on bank credit to varying extents.

In no other sector of the economy does the unorganized market play such an overriding role as in agriculture. Most of the financial transactions between farmers and others, be they buyers or sellers, are handled outside institutions subject to regulation, supervision, and control of the public. Most of these transactions are in cash, and most of them are done on the basis of private agreement, often implicit rather than explicit, and frequently sanctioned by many years of usage and still adhered to, even though the original rationale may be but dimly perceived or has disappeared

altogether.

It is in agriculture that the pattern and the structure of interest rates appear to be the most irregular and discontinuous. Side by side with the substantial proportion of loans carrying a zero interest charge there will be others, which, when imputed in money and translated into annual rates, would show fantastically high interest charges, upward of 600 or 800 per cent per annum. It is also in agriculture that the many imperfections of the financial markets in the less developed countries appear in their most acute form and seem least capable of speedy improvement and least amenable to rational planning for economic development. Capital markets in the urban centers may be in embryonic stage, but they are well-nigh non-existent in the countryside. In the cities there is, prima facie, a substantial degree of competition among lenders, but such competition is much weaker among those who supply credit to the farmer.

As mentioned previously, the concepts "agriculture" and "rural households" will be used interchangeably except as otherwise noted. Thus, for example, shopkeepers and traders residing in the countryside will be considered to be within the farm household sector and so will landlords, even though they may physically reside in the city.

Agricultural Credit and Mobilization of Voluntary Saving

The relation between voluntary saving and the structure of the markets for lendable funds in agriculture is a complex one. Care must be taken to go beyond a partial equilibrium analytical framework and to

consider the effects of such things as an inflationary expansion of the total supply of credit on saving and investment in the entire economy. Similarly, a distinction must be made between a transfer of resources from one sector to another and an increase in the aggregate flow of voluntary saving or else a more efficient use of these savings for developmental purposes. Thus, a policy designed to scale down the volume or the cost of rural debt would, prima facie, tend to increase the disposable income of the peasant but reduce that of the landlord, the village moneylender, and the indigenous banker. If it is true that the marginal propensity to save of the higher income groups is greater than that of the debt-burdened farmer, the total of the saving available to the economy would fall rather than increase, even assuming that a part of the (now higher) income of the farmer will be saved. On the other hand, to the extent that the poor farmer, the village laborer, or the plantation worker finds it easier to borrow at less onerous terms, he may increase his productivity, particularly if he begins to perceive the possibility of increasing his income substantially through greater effort.[1]

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[1]One of the principal findings reported in a study by G. T. Castillo, "Sociological Factors in Savings and Capital Accumulation: Some Research Findings," Philippine Economic Journal (Second Semester, 1964), pp. 193-96, is that investment orientation increases with increases in actually or potentially available saving.

Moreover, even if it is granted that rural creditors with their accumulated assets, higher absolute incomes, and greater range of economic horizons are able to save a greater fraction of their incremental income than their debtors, it does not necessarily follow that they actually do so or that the assets they accumulate are readily available for developmental purposes. As a matter of fact, there are reasons to believe that the very existence of high rents and high interest rates in rural areas tend to deflect the potential savings of these higher income groups into speculative acquisition of land, liquid hoards of cash, and other assets of little direct developmental value.[2]

Of all the measures designed to increase the flow of voluntary saving from farmers, the most fruitful appear to be those which increase their productivity and their income and which clearly relate the increase in the latter to the rise of the former.[3] Investment and saving in agriculture are low because "Incentives to work more...are weak because the marginal productivity of labor is very low; and incentives to save

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[2]See United Nations, FAO Regional Office, Measures for Mobilizing Rural Savings (E/CN. 11/1 & T/WP. 1/L.4) (Bangkok: United Nations, 1953).

[3]This is not to say that institutional and other arrangements are not capable of increasing the flow of saving at any given level of income or of channeling such savings into more productive uses. Such arrangements are not, however, within the purview of agricultural credit, as here discussed. See pp. III-83-III-87.

more...are weak because the marginal productivity of capital is also very low.[4] If this is granted, the function of agricultural credit should be to foster borrowing for productive purposes on terms which are consistent with the average productivity of capital in agriculture and which discourage borrowing which is not of this type.[5] The structure of agricultural credit conforming to the preceding criteria should not be such, however, as to lead to inflationary price rises in the rest of the economy or to a perceptible decline in capital formation in sectors other than farm households.

The difficulties, conceptual and statistical, involved in calculating in advance whether a given change in the markets for lendable funds in agriculture will have a net inflationary impact on the general price level or whether it will result in an increase in the aggregate income of farm households in excess of a net loss in the aggregate income of, say, landlords, suggest that, in the field of agricultural credit only modest suggestions for developmental planning can be absolved from the full burden of proof. That is, one should avoid suggesting grandiose schemes involving injection of large amounts of credit in a short period of time. When the addition to aggregate demand resulting from addition to the supply of lendable funds

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[4]See T. W. Schultz, Transforming Traditional Agriculture (New Haven: Yale University Press, 1964), p. 28. See also the implications of the sample survey discussed in the text.

[5]See in this connection the discussion of supervised credit in the last section of this chapter.

in agriculture is modest in relation to the supply of aggregate goods and services, the danger of a significant rise in the general level of prices recedes, particularly when the additional supply of credit is directed to uses which are calculated to add to the aggregate output within a short span of time. This approach is consistent with the concept of "piecemeal engineering," alluded to earlier.[6]

The Market for Lendable Funds in Thai Agriculture

There is a dearth of reliable information regarding almost every significant magnitude of the market for lendable funds in agriculture. Even the previously cited estimate of total debt outstanding in 1962/63 of 9.1 billion baht, while in many respects superior to similar estimates made for earlier years, is little more than an informed guess.[7] For 1934/35 total rural debt outstanding was said to have amounted to a mere 100 million baht, but in 1952/54 this figure is said to have risen to over 2 billion. Moreover, there is absolutely no information with respect to the relation of debt outstanding to the annual volume of borrowing.

The chief reason for this statistical hiatus is the fact that in agriculture, the bulk of borrowing and lending is done outside institutions subject to public scrutiny and control. This situation is far from being

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[6]See Chapter I, pp. III-51-III-53.

[7]See Chapter II, p. II-43.

unique to Thailand.[8]

U Tun Wai has devised a series of indicators relating the size of rural debt outstanding to a variety of economic variables. Table III-1 applies these indicators to Thailand and extends them to the years 1962/63. The figures fail, however, to give a clear idea of the size of the unorganized markets, as well as of changes in its size over time. For Thailand, at any rate, no perceptible trend emerges from the table.

Table III-1

Indices of Farm Household Debt in Relation to Economic Variables, Thailand, 1962-1963

Debt as Per Cent of	1934-35	1952-54	1962-63
Commercial Banks Loans, Overdrafts, and Discounts	29	143	113
Currency in Circulation in Private Hands	69	56	136
Income (output) Originating in Agriculture	23	14	34
Net National Income at Factor Prices	12	8	15
Debt (Amount in Millions Baht)	100	2059	9122

Sources: For earlier years, based on: U Tun Wai, "Interest Rates Outside the Organized Money Markets of Underdeveloped Countries," IMF Staff Papers (November 1957), Table 8.
For 1962-63, computed by the writer.

[8]See the relevant data for India, Pakistan, the Philippines, and other countries in Udhis Narkswasdi, Agricultural Credit Systems in Certain Countries (Bangkok: Kasetsart Univeristy, 1963), pp. 48-53. Even in the USA some 40 per cent of agricultural credit is from non-institutional sources.

In the sample survey of agricultural credit in Thailand for 1962-63, the proportion of loans contracted by farmers from institutions of the organized markets is estimated at 7.9 per cent of the number of loans and 5.5 per cent of their value. Details are given below.[9]

A scrutiny of Table III-2, made in conjunction with that of Table III-3, confirms the impression that institutional credit is relatively more important in areas where total flow of funds is less. Thus, the proportion of credit extended to farmers by institutions is highest in the South where both total debt and the average debt per family are lowest. The opposite is true for the Central Region. A given institutional effort will, of course, result in a higher proportion of the total when the total is low.

Even though it is not possible to mark off clearly the boundaries of the unorganized market in Thailand agriculture, it is difficult to escape the impression that it is the dominant force on both the supply and the demand side in the market for lendable funds in the countryside.

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[9] This proportion is less than the estimate of 12 per cent made in 1953 (see Udhis Narkswasdi, op. cit., p. 52). However, there are reasons to believe that the figure given in the text does, if anything, overstate the proportion of loans by value made by institutions of the organized market in Thailand. This would follow from a bias in sample design which probably led to over-emphasizing the importance of cooperative credit in at least one region of Thailand, the Northeast (see Narkswasdi, op. cit., p. 3). The entry of at least one commercial bank into the field of agricultural credit since 1963 is not believed to have altered the situation significantly.

Fortunately, the sample survey does provide some valuable information about the characteristics and the operations of the unorganized markets and thus gives a factual background to a discussion of its nature and its role in the development process. Much of the discussion in the succeeding section will be based on this survey.

Unorganized Markets--Supply

As seen in Table III-2, non-institutional lenders to farm households are about equally split between commercial and non-commercial purveyors of resources represented by neighbors and relatives. Relatives are the single most important type of lender in every region when the value of loans is taken into consideration. The percentage of loans extended by relatives ranges from a low of 22.5 per cent in the Central Plain to a high 58.5 per cent in the Northeast. It is assumed, although this is by no means universally true, that loans extended by relatives are made on terms and conditions vastly different from those extended by other lenders. In particular, it is alleged that these loans are often made without security and without any interest cost to the borrower.[10] It is unfortunate that the published results of the sample survey do not present data which would

[10] This, while a frequent assertion in the literature, is not explicitly stated in the sample survey. Implicitly, however, it follows from other data given in the survey, particularly those relating to interest rate by region, the type of lender, and the duration of the loan by type of lender. Further discussion is found in the section on "Terms of Loans."

Table III-2

SOURCES OF CREDIT BY REGION

Type of Lender	Central Plain		North		Northeast		South		Total	
	Number	Value	Number	Value	Number	Value	Number	Value	Number	Value*
					-- Per Cent --					
Relatives	17.8	22.5	44.8	47.0	50.0	58.5	40.2	43.0	39.9	32.5
Neighbors	14.0	16.7	24.1	19.9	12.1	4.3	15.1	12.9	15.7	15.5
Commercial Lenders	65.9	57.8	20.6	23.3	30.5	26.4	31.8	30.6	36.5	46.5
Local Stores	39.2	13.9	4.1	3.0	12.1	4.6	12.1	10.9	16.5	
Crop Buyers	8.2	7.9	5.2	10.1	9.1	6.5	13.7	13.8	8.6	
Landlords	6.6	10.7	0.0	0.0	1.5	5.2	0.0	0.0	2.1	
Money Lenders	8.0	14.3	7.8	8.9	3.3	7.5	3.0	1.5	5.4	
Other	3.9	11.0	3.5	1.3	4.5	2.6	3.0	4.4	3.9	
Institutional Lenders	2.3	3.0	10.3	9.8	7.6	10.8	12.9	13.7	7.9	5.5
Credit Cooperatives	1.4	2.0	10.3	9.8	7.6	10.8	12.1	12.9	7.5	
Other Government Agencies	0.9	1.0	0.0	0.0	0.0	0.0	0.8	0.8	0.4	
Commercial Bank	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: Pantum Thisyamondol, Virach Arromdee, Millard F. Long Agricultural Credit in Thailand, Theory, Dates, Policy (Bangkok: Kasetsart University, 1965), p. 37.

*In the published study the figures following the decimal point were missing whether as a result of printing error or some other reason with the result that the addition of the component percentages yielded 98% rather than 100%. Hence the addition of 0.5 to each of the four components shown.

Table III-3

ESTIMATED TOTAL DEBTS BY REGION

Region	No. of Sample Families	Total Debts (Baht)	Average per Family	No. of Farm Families in each Region	Estimated Total Debt per Region (Baht)
Central	311	2,163,543	6,956.73	789,632	5,493,256,623.36
North	147	202,481	1,377.42	833,856	1,148,569,931.52
Northeast	148	206,911	1,398.04	1,300,460	1,818,095,098.40
South	136	185,017	1,360.42	486,361	661,655,231.62
Total & Weighted Average	742	2,757,952	3,716.92	3,410,309	9,121,576,884.90

Source: Agricultural Credit, p. 20.

enable separating these zero interest, no security, no fixed maturity loans from others. As it is, the inclusion of these in the aggregate compilations distorts the picture of the "markets" (cost-free loans are in the nature of free resources and perhaps not properly a part of the market).[11]

Neighbors are often the more prosperous farmers and not infrequently part-time landlords. In some parts of the country those with greater acreage will let others work their land at certain times of the year and will advance cash or supplies at other times. The proportion of loans made by neighbors to the total value of loans is highest in the North with 19.9 per cent and lowest in the Northeast with slightly over 4 per cent. The low figure for the Northeast is in part explained by the high ratio of loans made by relatives and partly by the presumed infrequency of better-to-do farmers. It is in the North where the practice referred to above is the most widespread owing to the prevalence of multicropping in that area and the correspondingly lesser emphasis on the production of annual staple crops.[12]

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[11] The published results are meant to be preliminary. It is intended to process the data further and publish the results in a somewhat tighter form. IBM cards have been prepared for some 1100 loans included in the sample made to 68 per cent of the 742 respondent farm families. (Information contained in a personal communication to the writer).

[12] That neighbors may double as part-time landlords in the North because of the importance of intermediate crops in the area, such as garlic, fruit, and soybeans, is a point made here to account for the puzzling fact, shown in Table III-2, that no loans by landlords were found in the sample.

The various categories of commercial lenders[13] show a more differentiated picture regionally. Local shopkeepers are the most numerous commercial lenders in the country, as a whole, and in two of the four regions. As a proportion of value of loans, however, credit extended by shopkeepers diminishes in importance, suggesting that, while they make numerous and frequent advances to the farmers, these advances are generally for small sums or, what is actually the case in most instances, that the aggregate value of the commodities which they sell for credit is relatively small. This is seen in Table III-4.

Table III-4

Sources of Credit By Type of Commercial Lenders

Type of Lender	Number of loans as % of total loans	Average size of loan (in baht)
Shopkeepers	16.5	782
Crop buyers	8.6	1921
Landlords	2.1	3531
Moneylenders	5.4	3425
Other	3.9	1328
All Loans	36.5	1727

Source: Derived from Narkswasdi Agricultural Credit, pp. 37-38.

[13] These include shopkeepers, crop buyers, landlords, moneylenders, and others. Commercial lenders are distinguished from relatives, neighbors, and institutional lenders.

Somewhat surprising is the finding presented in Table 2 showing the relatively minor role played by crop buyers as suppliers of credit to farmers. Non-institutional suppliers of credit were often alleged to force the farmer into disadvantageous commercial relationships of various kinds.[14] Thus, for example, in Thailand, the practice of "rice baiting," whereby the farmer borrows against the security of his crop with the proviso that the crop, or a fraction of it, will be sold to the lender, was believed to be not only widespread but resulting in gross exploitation of the farmer. Leaving aside the determination of what constitutes "exploitation," Table III-5 brings out clearly the fact that repayment of both principal and interest in kind is not an important method of settling debts.[15]

Landlords play a minor role in the supply of credit to farmers except in the Central region where some 10.7 per cent of the value of all loans is provided by them (Table III-2). In other regions tenancy is not widespread, and the landowners are often farmers themselves.

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[14] See, for example, Frank J. Moore, "Moneylenders and Cooperators in India," Economic Development and Cultural Change (June 1953), pp. 140-43. See also Udhis Narkswasdi, op. cit., p. 2.

[15] The practice of borrowing from crop buyers is most widespread in the Central region, which is both the most commercialized of all regions in Thailand and one where cultivation of annual crops, notably rice, predominates. Forty-five per cent of Central Plain farmers reported borrowing from this source. Of those, however, only 7 per cent were obligated to sell the crop to the buyer. Udhis Narkswasdi, op. cit., p. 42.

The catch-all category of "other" lenders includes itinerant traders and peddlers who, in certain areas, are important sources of credit to the farmers. They are the most important exception to the general situation which seems to be peculiar to Thailand, where moneylenders not only reside in villages but are, for the most part, ethnically Thai.[16]

As shown in Table III-6, two-thirds of all loans extended to farmers were of less than one-year maturity. Among non-institutional lenders only relatives could be counted on to wait longer than one year for repayment, and in this case it is probable that the duration of the loan was determined less by the initial contract than by the willingness of the lender to wait.

The foregoing discussion of the structure of the supply side of the unorganized market for agricultural credit is believed to provide a fairly reliable picture of the situation in Thailand, even though the methodology employed by the survey would suggest the exercise of considerable caution in interpreting the specific percentages.[17] While

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[16]For a variety of reasons this cannot be demonstrated statistically, but it is asserted by a number of qualified observers. During the present writer's visits to the provinces all those interviewed made the same assertions and many cited the case of a Chinese lender who tried to establish himself in a village but gave up after a year or so. U Tun Wai (op. cit., p. 88) claims that Chettiars were at one time important suppliers of credit in Thailand, but little trace of them could be found, at least in the North. A number of Indian lenders (Malabars and Peshavaris) do, however, operate in towns and cities.

[17]See Udhis Narkswasdi, op. cit., p. 38.

Table III-5

METHOD OF REPAYMENT BY TYPE OF LENDER

	Principal			Interest		
	Cash	Crop	Crop Sales	Cash	Crop	Crop Sales
	--Per Cent--					
Relative	95.4	1.6	3.0	83.2	12.6	4.2
Neighbor	92.1	4.0	3.9	77.3	17.9	4.8
Commercial Lender	76.5	8.9	14.6	69.2	16.1	14.6
Local Store	77.4	8.9	13.7	71.5	13.5	15.0
Crop Buyer	67.4	5.1	27.5	64.1	12.8	23.1
Landlord	73.7	8.8	17.5	62.0	18.0	20.0
Money Lender	75.0	15.5	9.5	65.8	26.6	7.6
Other	93.0	4.7	2.3	79.5	17.9	2.6
Institutional Lender	98.8	1.2	0.0	98.7	1.3	0.0
Credit Cooperative	100.0	0.0	0.0	100.0	0.0	0.0
Other Government Agency	88.9	11.1	0.0	80.0	20.0	0.0
Commercial Bank	-	-	-	-	-	-
All Loans	84.8	6.3	8.9	75.4	15.0	9.6

Source: Agricultural Credit, p. 41.
See, for example, Frank J Moore, "Money Lenders and Cooperators in India," Economic Development and Cultural Change (June 1953), pp. 140-43. Also, Udhis Narkswasdi, op. cit. p. 2.

Table III-6

Duration of Loans By Type of Lender

Type of Lender	Duration	
	Less Than One Year	More Than One Year
	Per Cent	
Relative	45.4	54.6
Neighbor	60.2	39.8
Commercial Lender	73.5	26.5
Local Store	86.8	13.2
Crop Buyer	70.2	29.8
Landlord	62.4	28.6
Moneylender	52.9	47.1
Other	43.5	43.5
Institutional Lender	7.0	93.0
Credit Cooperative	2.6	97.4
Other Government Agency	44.4	55.6
Commercial Banks	-	-
All Loans	68.8	31.2

Source: Narkswasdi, Agricultural Credit, p. 39.

comparison with the surveys made in other countries is difficult, owing to different definitions employed, and cannot be conclusive because of quite different conditions prevailing in such countries as India, Pakistan, Taiwan, and the Philippines, the findings for Thailand appear to be consistent with the findings elsewhere when modified by the specific conditions existing in Thailand. The emerging picture is that of a variety of lenders, thus providing some choice to the farmer, however limited such a choice may be in practice, with landlords playing a much

smaller role than in other countries but relatives, a much greater role. Most important, crop buyers apparently exercise a lesser degree of monopsony power than is commonly believed. The relative importance of the various types of lenders seems to be geographically heteregenous with commercial lenders predominant in areas of commercialized agriculture and of relatively high income per farm household (which is, in turn, correlated with area cultivated per farm) and with relatives more significant in areas where overall debt is low. Finally, the bulk of the supply of loans from commercial lenders is of relatively short duration with only 26.5 per cent of loans from this source available for periods exceeding one year.

Unorganized Markets--Demand

It was asserted in the preceding paragraph that it is in the more prosperous regions that commercial moneylenders predominate rather than, as may have been expected, in the poor areas. It would seem that in the prosperous, commercialized areas the demand for credit is greater than the available supply from the preferred sources--institutions, relatives, friends, and neighbors. Conversely, in areas where total demand for credit is low, the preferred sources supply a larger proportion of the total. This suggests an important aspect of the demand for credit; namely, that it is strongly correlated with both income and area cultivated.

Table III-7, deals with potential rather than effective demand for lendable funds. Farmers' responses indicate that the desire to borrow

increases continuously and directly with respect to both area cultivated and net income. The proportion of farmers wishing to borrow (or saving so) would seem to be substantially greater than of those actually borrowing.[18] After all, the willingness to borrow has to contend with the availability and the cost of funds and with other requirements of lenders which, on occasion, are beyond the capacity of the borrower to meet. Hence, an unexpected finding of the Thailand sample survey is that

Table III-7

Thailand--Agricultural Credit Sample Survey
Proportion of Borrowers Needing Loans by Income and Area Cultivated

Proportion Requiring Loans			
By Net Income (Baht)		By Area Cultivated Per Farm (Rai)	
Income	Per Cent	Area	Per Cent
1 - 1,999	56.64	49.09	1 - 5
2,000 - 4,999	61.33	54.00	5 - 10
5,000 - 9,999	75.86	57.39	10 - 20
10,000 - 19,999	76.79	72.49	20 - 50
20,000 - and over	87.50	90.85	50 and over
Total	68.19	68.19	Total

Source: Derived from data contained in Narkswasdi Agricultural Credit.

[18] Thus, an investigation of farm loan requirements in Taiwan indicated that 89 per cent of the farmers surveyed required credit, but only 69 per cent actually contracted to borrow. (Udnis Narkswasdi, op. cit., p. 28.)

the proportion of all farmers desirous of borrowing is almost exactly the same as the proportion of farm households who actually borrow, 68.19 per cent versus 68.06 per cent. There is a strong presumption that "desire to borrow" was construed as tantamount to actively seeking a loan.

Tables III-8 and III-9 show that, for those who actually incur debts, the size of the debt increases with income as well as with area cultivated per farm. It is worth noting that the relationship between the size of debt and each of the other two variables is not entirely symmetrical. The modal loan size for the richest farmers is in excess of 20,000 baht, and the corresponding figure for farmers with the largest farms is between 5,000 and 10,000 baht. The impression given by the Tables III-7, III-8, and III-9 is that the more prosperous the farmer, the more he is willing to borrow and the greater the amount of debt he will contract.

While the sample survey did not explicitly relate the purpose to which the loan proceeds are devoted to indices of farmers' prosperity, there are indications that here, too, the correlation is positive; i.e., the more prosperous the farmer, the more productive the purpose for which he borrows.[19]

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[19] This seems to be implied in the relation of such purposes as purchase of productive inputs to size of loan, loan duration, and loan frequency in regions which are relatively more commercialized and more prosperous. See Narkswasdi, op. cit., Chapter 3. The relationship asserted in the text is not stated explicitly. The general proposition that it is the more prosperous farmer who is likely to borrow, to borrow more, and to do so increasingly for purposes relating to increased output is also borne out by Castillo, op. cit.

Table III-8

NET CASH INCOME IN RELATION TO SIZE OF LOAN

Net Cash Income (Baht)	Amount of Loan in Baht and Percentage of Total Debts							
	1-499	500-999	1,000-1,999	2,000-4,999	5,000-9,999	10,000-19,999	20,000+	Total
1 - 1,999	25.42	13.56	22.04	16.95	18.65	1.69	1.69	100
2,000 - 4,999	22.26	12.10	16.56	32.47	9.55	5.73	1.27	100
5,000 - 9,999	5.68	6.82	19.31	38.07	22.16	4.55	3.41	100
10,000 - 19,999	5.81	2.33	6.98	26.75	29.07	23.55	5.81	100
20,000 - and over	7.14	-	7.14	14.29	21.43	25.00	25.00	100
Total	13.24	8.10	16.01	30.63	18.97	8.89	4.16	100

Source: Derived from Agricultural Credit.

Table III-9

AREA CULTIVATED IN RELATION TO SIZE OF LOAN

Area Cultivated (rai)	Amount of Loan in Baht and Percentage of Total Debts							
	1-499	500-999	1,000-1,999	2,000 4,999	5,000 9,999	10,000 19,999	20,000- and over	Total
1 - 5	29.63	29.63	7.41	11.11	11.11	3.70	7.41	100
5 - 10	31.49	9.26	22.22	20.37	9.26	3.70	3.70	100
10 - 20	22.77	9.91	14.85	36.63	8.91	4.95	1.98	100
20 - 50	8.20	6.67	20.00	35.90	21.03	6.15	2.05	100
50 and over	2.33	3.88	10.07	26.36	29.45	19.38	8.53	100
Total	13.24	8.10	16.01	30.63	18.97	8.89	4.16	100

Source: Derived from Agricultural Credit.

Table III-6 indicated that over two-thirds of loans contracted by Thai farmers are short-term in nature, of less than one year's duration.[20] Given the seasonal nature of needs for funds under annual crop cultivation, the type of cultivation still preponderant in the country, one would expect that the peak of demand for loans will take place during the planting season and the bottom will be reached during the harvest season.[21] It is, therefore, somewhat surprising to find, as did the sample survey, that cash loans were fairly evenly spaced over time. As shown in Table III-10, the proportion of loans contracted during the planting season, 26.5 per cent, was only slightly higher than the 22.2 per cent contracted during the harvest season. This suggests, among other things, both greater liquidity and lesser dependence on annual staples than commonly supposed. For loans contracted in kind,

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[20] Data in Table III-6 pertain to number of loans. To the extent that loans of longer duration tend to be greater in size, the proportion will shift in favor of long-term loans. In fact, 76 per cent of all loans were for sums under 2,000 baht; and of those above 2,000 baht, only 13 per cent were for over one year or "indefinite." Narkswasdi, op. cit., p. 29.

[21] Four seasons, each one of about three months duration, can be distinguished in the rice cycle of cultivation in Thailand. The harvest season extends roughly over the first three months of the calendar year, followed by the dry, the planting, and the growing seasons.

Table III-10

Date of Borrowing By Type of Loan

Type	Quarter 1	2	3	4	Total
	Per Cent				
Cash	22.2	23.6	26.5	27.6	100
Kind	6.8	12.5	58.6	22.1	100
All Loans	17.3	20.2	36.6	25.9	100

Source: Agricultural Credit, p. 27.

however, the seasonal pattern is very much pronounced. During the peak demand season, 58.6 per cent of all loans are incurred, compared with a mere 6.8 per cent following the harvest.[22]

[22] It should be borne in mind, however, that Table III-10 deals with number of loans rather than with their value. Inasmuch as loans in kind are much smaller, on the average, than cash loans, the overall impression is that of remarkable seasonal stability of demand for credit. (The average size of loans extended by shopkeepers, a category of lender with the highest proportion [71 per cent] of loans in kind, was 782 baht as compared with the 1,727 baht for all loans. See Table III-4.)

If the demand for cash loans, taken for the country as a whole, does not diverge very much from a moving average, the purpose for which the loans are made tends to differ considerably both spatially and temporally. In general, in areas where the farmers have to wait a full year for the bulk of their earnings to come in, loans for consumption purposes predominate. These are contracted during periods preceding the rice and corn harvests. In other areas, where intermediate crops provide a considerable part of farmers' income throughout the year, loans for variable inputs play a more important role and are contracted throughout the year. In Tables III-11 and III-12, the purposes for which loans are contracted are numbered from one to ten and stand for the following:

1. Purchase of tools, machinery, and livestock
2. Labor, seed, fertilizer, feed, and other variable inputs
3. Housing, irrigation, and other construction
4. Purchase of land, housing, or other assets
5. Living expenses
6. Social expenditures (weddings, funerals, etc.)
7. Educational expenses
8. Relending
9. Purposes other than farming
10. Miscellaneous

Table III-11

SHORT TERM LOANS : PURPOSE OF LOANS*

Purpose of Loans	Central		North		Northeast		South		Total	
	Baht	Percent	Baht	Percent	Baht	Percent	Baht	Percent	Baht	Percent
1	81,090	7.72	3,800	5.75	7,986	16.94	3,950	15.73	96,826	8.15
2	195,225	18.60	19,124	28.83	5,660	12.00	3,500	13.94	223,509	18.85
3	5,980	0.56	4,450	6.71	1,595	3.38	2,700	10.75	14,725	1.23
4	58,350	5.56	7,050	10.63	17,379	36.84	4,300	17.15	87,079	7.35
5	290,780	27.73	6,577	9.91	5,075	10.76	6,240	24.86	308,672	25.98
6	37,150	3.54	6,280	9.47	3,310	7.01	2,900	11.55	49,640	4.17
7	25,970	2.41	3,000	4.52	200	0.42	300	1.19	28,870	2.43
8	720	0.06	8,000	12.06	-	-	-	-	8,720	0.73
9	15,950	1.54	-	-	5,600	11.87	-	-	21,550	1.81
10	338,660	32.26	8,030	12.12	360	0.76	1,210	4.83	348,260	29.30
Total	1,049,875	100	66,311	100	47,165	100	25,100	100	1,187,851	100

*Details may not add up to totals because of rounding.
Source: Agricultural Credit, p. 23.

Table III-12

LONG TERM LOANS : PURPOSES OF LOANS*

Purpose of Loans	Central		North		Northeast		South		Total	
	Baht	Percent	Baht	Percent	Baht	Percent	Baht	Percent	Baht	Percent
1	127,062	11.39	54,200	39.80	36,710	22.98	11,300	7.07	229,272	14.59
2	230,445	20.66	14,700	10.80	24,141	15.11	25,100	15.70	294,386	18.73
3	30,000	2.69	3,700	2.72	5,200	3.26	15,185	9.50	54,085	3.47
4	225,900	20.26	20,000	14.69	58,355	36.53	48,662	30.42	352,917	22.48
5	226,611	20.32	5,440	3.99	16,670	10.44	13,020	8.14	261,741	16.65
6	11,700	1.05	29,500	21.66	2,700	1.69	10,350	6.47	54,250	3.45
7	25,500	2.27	2,000	1.47	820	0.51	9,400	5.88	37,700	2.40
8	77,000	6.91	-	-	-	-	-	-	78,000	4.96
9	43,500	3.90	-	-	4,050	2.54	4,700	2.94	52,250	3.32
10	116,550	10.46	6,630	4.87	11,100	6.94	22,200	13.88	156,480	9.95
Total	1,114,268	100	136,170	100	159,746	100	159,917	100	1,571,081	100

* Details may not add up to totals because of rounding.
Source: Agricultural Credit, p. 23.

In the North, where intermediate crops are perhaps more important than rice, loans for living expenses constitute less than 10 per cent of the value of short-term loans and less than 4 per cent of the value of long-term loans. In the Central region, on the other hand, with rice still dominating the regional economy (and with little double cropping), some 28 per cent of short-term borrowing was for consumption purposes and over 20 per cent of long-term borrowing was used to pay for current living expenses. Conversely, the North uses the greatest proportion of its short-term loans for variable inputs even though, when long-term loans are included, it is the Central region which forges ahead.[23]

One aspect of Tables III-11 and III-12 deserves mention. Social expenditures account for only 4.17 per cent of short-term borrowing and 3.45 per cent of long-term. These are rather insignificant proportions for purposes which, allegedly, account for much of farmer indebtedness in other countries.[24] This low proportion does not mean that the Thai

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[23] The reasons for this are not absolutely clear and are not given in the published results of the sample survey. It is likely that the more prosperous farmers of the Center are in a position to borrow long-term loans for purchases of better seed, fertilizer, and so on, to an extent greater than the generally smaller and less affluent farmers in the North.

[24] See Udhis Narkswasdi, op. cit., p. 29; Castillo, op. cit., p. 196; and Frank J. Moore, "A Note on Rural Debt and Control of Ceremonial Expenditures in India," Economic Development and Cultural Change (June, 1954), pp. 408ff.

farmer does not spend much on weddings, funerals, or "bouns" but rather suggests that the Thai rural society has developed means other than borrowing to cope with these expenditures.[25] Thus, for example, in the Northern provinces, in the event of a death in the family, fellow villagers each contribute 3 or 4 baht toward the funeral expenses of the bereaved. Elsewhere, a communal fund will be established, often made up of unsold paddy, out of which certain emergency expenses of villagers will be met.[26]

From the sample survey, as well as from other sources, the impression is gleaned that the demand for loans increases as the farmer becomes more oriented toward commercial agriculture and as he learns that an increased effort to enhance his productivity will result in substantially higher cash income. The extent to which this orientation will actually be translated into effective demand depends on the supply of funds available to him and the terms at which he can borrow.

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[25] An earlier survey of rice farmers in the Central region established that the proportion of ceremonial expenses to total consumption expenditures was 13 per cent (Ministry of Agriculture, Report on Economic Survey of Rice Farmers in Nakorn Pathom Province, 1955-56 [Bangkok: Agricultural Research and Farm Survey Station, 1959]).

[26] Information developed during the writer's field trips.

The Terms of Loans

In this section two aspects of the terms of credit in the unorganized market will be discussed: the pattern of interest rates and the security for a loan. The method of repayment and the duration of loans were briefly discussed in other contexts.[27]

While it is true that all aspects of rural credit are related and that the terms at which lendable funds are being transferred are both the product and the influence behind the demand and supply schedules, the connection between the collateral and the interest rate is particularly intimate, even though the relationship is not necessarily a simple one.[28] For example, while, in general, the better the quality of the collateral the borrower can muster, the lower the interest rate he has to pay, other things being equal, it is not unusual to find that the most favorable terms are offered borrowers who proffer no collateral whatsoever. This is not surprising when it is realized that the need to produce a security with which to supplement a promise to repay is in itself an admission that one's credit standing is not of the highest order. It is, after all, only the triple-A American corporation which can sell unsecured debentures to the public. In the majority of cases, however, the credit rating of

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[27] See above.

[28] See Anthony Bottomley, "The Premium for Risk as a Determinant of Interest rates in Underdeveloped Rural Areas, "Quarterly Journal of Economics (November 1963), pp. 637-47.

rural borrowers is such that the quality and the kind of collateral he is able to offer is an important determinant of the rate of interest he will be asked to pay. It is difficult to establish this proposition empirically, however, because the data are not collected in a way which relates rigorously the quality of collateral to the interest rate under ceteris paribus conditions. Moreover, in practice, it is well-nigh impossible to preserve these conditions when dealing with aggregates. In the sample survey of Thai agricultural credit there appears, however, some indirect confirmation (in Tables III-13 and III-14) that the quality of the collateral influences the rate of interest. In Table III-13, security of land, considered the best of all securities, is given for most larger loans. As seen in Table III-14, it is the largest loans which carry the lowest interest rate. Conversely, as seen in these two tables, the greatest proportion of the smallest loans (up to 2,000 baht) involves no collateral whatsoever. Among these loans 54 per cent are unsecured while for larger loans (over 5,000 baht) only 16 per cent are unsecured.[29]

[29] The 16 per cent of unsecured loans for sums in excess of 5,000 baht suggests that the number of farmers able to borrow against their credit rating alone, at relatively favorable rates of interest, is by no means negligible.

Table III-13

SECURITY BY SIZE OF LOAN

Size of loan	Type of Security								Total
	Land	Crops	Farm Capital	Jewelry	Note	No Security	No Answer	Other	
--Baht--	--Per Cent--								
1-1,999	8.1	1.2	1.1	1.4	1.6	53.7	32.0	0.9	100
2,000-4,999	37.2	1.0	1.0	0.3	3.4	40.5	15.6	1.0	100
5,000 and over	75.0	2.2	-	-	2.2	16.3	2.2	2.2	100
All Loans	17.3	1.3	1.0	1.1	1.9	49.1	27.3	1.0	100

Source: Agricultural Credit, p. 28.

Table III-14

RATE OF INTEREST BY SIZE OF LOAN

Size of Loan	Mean Interest Rate	Interest Rate (Monthly)						Total
		0.0-0.9	1.0-1.9	2.0-2.9	3.0-4.9	5.0-9.9	10.0 and Over	
--Baht--		-- Per Cent --						
1 - 499	3.2	51.1	4.3	8.5	12.8	15.6	7.7	100
500 - 999	2.6	34.9	10.8	19.9	19.9	13.3	1.2	100
1,000 - 2,999	2.3	34.3	14.7	27.4	14.7	8.1	0.8	100
3,000 - and over	1.9	26.3	26.8	30.8	11.1	4.0	1.0	100

Source: Agricultural Credit, p. 32.

Table III-13 shows that land as a security constituted only 17.3 per cent of all loans. Nearly half of all loans granted were made with no security whatever. The picture is slightly clouded by the high proportion of loans, particularly small loans, where no indications were given with respect to collateral, but it is more than not likely that many loans in this category were made between parties related by kinship and other ties. The high proportion of unsecured loans is a circumstance found in a number of other countries and reflects the poverty of the borrowers and a shortage of marketable assets.[30] Of some interest is the very low proportion of loans secured by jewelry in Thailand. In other countries, particularly India, gold and jewelry are much more important forms of security.[31]

The high regard in which land mortgage is held in the eyes of the lenders is in itself a reflection of the scarcity of transferable assets in the hands of the farmers. In Thailand, however, land is considered the superior type of collateral for yet other reasons. It is preferred security by commercial banks and other institutions; it is required by the primary cooperative credit associations; and it is an asset, the value of which has been appreciating over time. This preference

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[30] See Udhis Narkswasdi, op. cit., pp. 41-43.

[31] Ibid., p. 42. The small proportion of crop collateral shown in Table III-13 probably understates the real position. It is likely that many of the smaller loans are, in fact, secured by crops in one way or another but shown in the "no answer" column.

for land mortgage is a limiting factor in the development of rural credit both because of supply conditions and also because of the cumbersome procedures involved in the valuation and registration of real estate mortgages. On the other hand, rural lenders in unorganized markets are, in Thailand, rather reluctant to acquire land for themselves, to start eviction proceedings and to bring about repossession. Their preference for land mortgage derives from their knowledge that a borrower who pledges an asset several times the value of the loan will do his utmost to repay it rather than risk proceedings against his land. In fact, moneylenders and others are much more flexible than institutions of the organized market in the way they deal with this collateral.[32]

The inverse relation between the size of the loan and the interest rate is a well known phenomenon of rural credit in the less developed countries. In part, as argued previously, this relation is a function of the collateral available to small borrowers, but it also has much to do with the higher administrative cost of collection and with the nature of small loans, which implies a greater risk of delay or an inability to repay. The mean interest rate according to the size of the loan ranges, as shown in Table III-14, from 3.2 per cent per month for loans under 500 baht to 1.9 per cent for those in excess of 3,000 baht. The extent of this range is almost certainly telescoped by the inclusion in the Thai

[32] See section on Organized Markets.

sample of interest-free loans from relatives and others. It is this which accounts for the high proportion (51.1 per cent) of loans under 500 baht paying less than 1 per cent per month. In a 1957 study in the Philippines, which involved a large sample of farm families and a total of 1,914 short-term loans, interest-free loans were excluded. The range of interest rates, all of which were inversely related to the size of the loan, extended from 55.4 per cent per annum for the smallest loans to 14.4 per cent for the largest.[33]

The inclusion in the Thai sample survey of loans from relatives, landlords, and others which carry a zero interest rate is also responsible for the murky appearance of the relationship between the income of the borrower and the rate of interest. Contrary to what may have been expected, those with incomes of 20,000 baht and over (annually), a high net income by Thai standards,[34] pay a mean monthly interest rate of 2.7 per cent, compared with the 2.3 per cent rate paid by those with net annual incomes in the 2,000 to 5,000 baht range (see Table III-15). It is reasonable to assume, however, that a substantial number of the loans contracted by the latter and bearing a monthly interest charge under 1 per cent (57.6 per cent of all loans made to this income group) were, in fact, zero interest loans.

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[33] See Leopoldo P. De Guzman, "An Economic Analysis of the Methods of Farm Financing Used on 5,144 Farms: 1955," The Philippine Agriculturist, Vol. 41 (1958).

[34] The per capita GNP in 1963 is estimated at slightly over 7,300 baht.

The inverse relationship between the rate of interest and the size of the loan stems from the incidence of "sound" collateral, from the fact that administrative overhead is relatively invariant with respect to the size of the loan, and from the presumption that small loans are those demanded by the less provident farmers.

No such readily apparent connection exists for the relationship, brought out in Table III-16, between the duration of the loan and the rate of interest. Again, the high proportion of loans between relatives, apparently not subject to market considerations, tends to distort the relationship somewhat. Table III-16 shows that the rate of interest tends to be lower for loans made for periods in excess of one year than for shorter-term loans.[35]

Now, the relationship between the short-term and long-term interest rates has been very unstable even in countries where there exist quite reliable time series of homogeneous claims. On theoretical grounds, one would expect higher rates to be attached to claims with longer maturity, if only because of longer forbearance of liquidity such loans entail. In fact, however, in the United States since 1900 there have been about as many periods in which short-term rates were above long-term rates as when

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[35] The De Guzman study brings out the relationship between the duration of loans and the interest rate in greater detail. In the nine categories into which De Guzman divides his sample (by average interest rate per annum and by average period of loans in months), the inverse relationship is, with only one exception, a monotonic one.

the opposite was true.[36] Nevertheless, it is not only theoreticians but also hard-headed money and capital market practitioners who widely believe that short-term rates tend to be lower than long-term rates.[37] Yet, in the less developed countries, especially in the domain of agricultural credit, it generally costs more to borrow money for short-term loans than it does for long-term loans.[38]

The reasons for the inverse relation between the duration of loans and the interest rate are somewhat conjectural. Shorter-term loans have been shown to be often made for less productive purposes than loans of longer duration. Shorter-term loans are associated with borrowers who are, on the whole, less provident, less prosperous, and, hence, less reliable than borrowers for longer-term loans. It is the longer-term loan that most often is associated with collateral in the form of a land mortgage. Last but not least, an interest charge, when computed on an annual basis, makes little sense to an anxious borrower who needs the use of a loan for only two or three months.[39] The lender finds it easier to charge a higher rate of interest when the absolute amount added to the principal is still a

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[36] U.S. Board of Governors of the Federal Reserve System, Federal Reserve Historical Chart Book, (Washington 1962), p. 21.

[37] See Roland I. Robinson, Money and Capital Markets (New York: McGraw-Hill Co., 1964), p. 82.

[38] See Udhis Narkswasdi, op. cit., p. 41.

[39] See U Tun Wai, op. cit., p. 104.

Table III-15

RATE OF INTEREST BY NET INCOME OF BORROWER

Net Income	Mean Interest Rate	Interest Rate (Monthly)						Total
		0.0-0.9	1.0-1.9	2.0-2.9	3.0-4.9	5.0-9.9	10.0 and Over	
		-- Per Cent --						
1 - 1,999	3.6	31.8	11.5	13.6	15.9	22.7	4.5	100
2,000 - 4,999	2.3	57.6	6.4	15.2	6.4	9.6	4.8	100
5,000 - 9,999	2.8	34.5	17.2	16.1	17.8	10.9	3.5	100
10,000 - 19,999	2.8	28.1	13.2	30.6	16.5	9.1	2.5	100
20,000 - and over	2.7	33.3	19.4	25.0	5.6	13.9	2.8	100

Source: Agricultural Credit, p. 33.

Table III-16*

RATE OF INTEREST BY DURATION OF LOAN*

Duration of Loans	Mean Interest Rate	Interest Rate (Monthly)						Total
		0.0-0.9	1.0-1.9	2.0-2.9	3.0-4.9	5.0-9.9	10.0 and Over	
		-- Per Cent --						
One-six Months	3.1	45.4	9.9	13.5	9.6	14.5	7.1	100
Six-Twelve Months	3.1	21.9	13.4	26.8	22.2	12.7	2.9	100
More Than one year	1.9	56.7	7.9	17.7	9.8	7.3	0.6	100
Indefinite	2.2	38.9	17.7	22.5	12.9	6.8	1.3	100

Source: Agricultural Credit, p. 32.

*Details may not add up to totals because of rounding.

small sum.

According to the sample survey of agricultural credit in Thailand, the mean monthly rate of interest on all loans and for all regions was 2.4 per cent in 1962-63. The breakdown by regions and by frequency distribution is given in Table III-17. Unlike certain other data contained in the published results of the sample survey, Table III-17 weighs the number of loans by their baht value. The data given in Table III-16 appear to be consistent with the findings in other countries.[40]

Even a brief scrutiny of Table III-17 will suggest that there can be no simple explanation of the determinants of the interest rate. Thus, the Northeastern region, considered to be the poorest and the most depressed area of Thailand, enjoys a lower mean rate than the relatively prosperous North. The highly commercialized and relatively well-to-do farmers in the Central Plain pay more, on the average, than farmers in the South. A very high proportion of Southern borrowers pay less than 1 per cent a month, suggesting a high incidence of interest-free borrowings

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[40] U Tun Wai states: "weighted average rates of interest...in rural areas of underdeveloped countries...[are] usually between 24 and 36 per cent per annum" (Ibid., p. 102). See also: Reserve Bank of India, Report on Rural Credit Follow Up Survey, 1956-1957 (Bombay: Reserve Bank of India, 1960); N. B. Tablante, "Implications of Credit Institutes and Policy for Savings and Capital Accumulation in Philippine Agriculture," Philippine Economic Journal, III (Second Semester, 1964), pp. 208-25; and F. H. King, "Agricultural Finance and Credit in Taiwan," n.d. (mimeo).

Table III-17

RATE OF INTEREST BY REGION*

Region	Mean Interest Rate	Rate per Month							Total
		0.0-0.9	1.0-1.9	2.0-2.9	3.0-3.9	4.0-4.9	5.0-9.9	10.0 and over	
		-- Per Cent --							
Central Plain	2.2	30.1	15.6	28.1	8.3	6.5	9.4	2.2	100
North	3.3	39.7	9.5	4.3	15.5	13.8	13.8	3.4	100
Northeast	2.7	56.8	2.4	8.8	3.2	2.4	17.6	8.8	100
South	1.5	63.6	12.9	6.8	5.3	0.8	7.8	3.0	100
All Loans	2.4	38.5	12.9	20.6	8.1	6.1	10.6	3.2	100

*Details may not add up to totals because of rounding.
Source: Agricultural Credit, p. 30.

from relatives and landlords (plantation owners).[41] The Northeast, which also enjoys a high proportion of this kind of loan, has a substantial percentage of loans with very heavy monthly interest costs.

In the absence of data which would permit a more rigorous statement regarding the determinants of interest rates, only observations of a general character can be made here.[42]

In the first place, it is a truism that the rate of interest is given by the intersection of the demand and supply functions. For any given supply of lendable funds for a specific kind of loan, it will be the quantity demanded of this type of loan which will determine its price. The implication of this is that in the South the mean cost of lendable funds is lower than in the Center because the demand for loans is much greater in the latter region. Of course, it is more than likely that the supply of funds is also unequal, but it is presumably the relation of demand to supply which is determining. This tautology abstracts from differences in risk, which is in itself a composite of many complex factors.[43] It does, however, help to explain the high rate in the North.

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[41] One possible reason for the low mean rate in the South is the substantial proportion of Moslems living in that region.

[42] The authors of the Thai sample survey were hoping to run a multiple regression of the relevant factors. At the time of writing, however, the results of the analysis were not yet available. See, however, R. C. Blitz and M. F. Long, "The Economics of Usury Regulations," Journal of Political Economy (December, 1965).

[43] Some of these will be discussed in the following section.

By all standards, Northern borrowers seem to be the most credit worthy of all, yet they pay more for loans than those in the Northeast. There must be something in the nature of the demand for funds in the North which exerts upward pressure on the level of interest rates and which, to the extent that it persists over time, is not fully alleviated by temporal and spatial arbitrage on the supply side. In fact, as suggested earlier, it would seem that the nature of the cultivation in the Northern provinces, with main reliance on the production of subsidiary cash crops and the importance of long-maturing fruit crops, puts particularly heavy demand on the market for lendable funds. For one reason or another, the suppliers of funds have not yet adjusted to a situation where above-average profits could be made.

For Thailand as a whole the highest rates of interest are those charged by the local shopkeepers and, somewhat surprisingly, by landlords. The lowest rates are those obtained by relatives, although the rate of 1.8 per cent per month given in Table III-18 is the weighted mean of all loans made by relatives, including the substantial, if unknown, proportion of loans made without any interest charge. The pattern of regional dispersion from the mean rates, according to the source of loans, shows no particular surprises. One would expect moneylenders to charge a much higher rate of interest to farmers in the Northeast than to those in the Central plain. Both the risk and the limitations on supply are greater in the former region.

Table III-18

MONTHLY INTEREST RATES BY REGION AND TYPE LENDER

Type of Lender	Region				Mean for all Areas
	Central Plain	North	Northeast	South	
Relative	1.7	2.6	1.8	1.1	1.8
Neighbor	2.4	3.3	3.3	2.3	2.6
Commercial Lender	2.3	4.8	4.3	2.0	2.9
Local Store	2.7	5.4	6.2	2.7	3.5
Crop Buyer	2.4	4.7	3.9	1.3	2.9
Landlord	3.8	-	1.8	-	3.5
Money Lender	2.1	5.0	7.3	3.6	3.3
Other	1.6	3.4	7.0	2.2	2.5

Source: Agricultural Credit, p. 40.

If one abstracts from the loans made among relatives, it would seem that the modal rate of interest for loans in the Thai countryside is between 36 and 48 per cent per annum. This compares with the 24 to 30 per cent modal rate in the unorganized markets in the urban areas.[44] It is superfluous to argue whether this differential is "justified." The very nature of the unorganized market is such that elements of monopoly exist and some degree of "exploitation" does take place.[45] Perhaps the most significant finding of the sample survey is that the commonly employed forms of exploitation play but a minor role in Thailand. Thus, in general, farmers have access to more than one lender; rice baiting and other types of borrowing and repayment in kind are relatively unimportant; few farmers feel lenders take undue advantage of them; and so on.[46]

Assuming a given level of effective demand for loans, the interest rate will vary with the availability of funds in an area, with the cost of administration, and with the degree of risk. The fact that rural rates are higher than those in the urban areas must be primarily the function of higher relative administrative costs and higher risks. It cannot be due to lesser demand because this, if anything, would militate against higher rates.

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[44]See Chapter VII.

[45]See, in this connection, R. C. Blitz and M. F. Long, op. cit.

[46]See U. Narkswasdi, particularly pp. 42-43.

It can attributed only partly to availability of funds because one would expect funds to flow to the countryside, were other factors comparable with those prevailing in urban areas.[47]

There can be little question that unit costs of administration are greater in the case of agricultural credit than for comparable urban loans. Rural loans are for smaller amounts and are made to a widely dispersed clientele which has little in the way of easily assessable collateral and little sophistication in financial dealings. But, on the other hand, rural lenders have developed a number of techniques to reduce the unit costs of processing, of collection, and of recovery. Most moneylenders are located in the villages, right among their actual and potential clients. They have developed simple and flexible procedures and have adjusted in other ways to the peculiarities of their metier. Nevertheless, the administrative costs of rural loans remain probably higher than those in urban centers, even though their influence on the level of the rates of interest should not be exaggerated.

Repayment Record

One indication of the creditableness of rural borrowers and, hence, the degree of risk in agricultural credit may be obtained from the examinations of the repayment record of farmers. Unfortunately, data on

[47]This assertion clearly assumes a degree of rationality and knowledge among lenders which probably does not obtain in fact. There may also be various institutional and other constraints inhibiting free movement of funds to the countryside in spite of higher profits there.

this point contained in the sample survey suffer from a number of drawbacks. The published figures do not specify whether "non-repayment" means a delay or a repudiation. If a delay, how long and at what point does it become a bad debt? The published results also are not clear whether the percentages refer to the number of loans alone or whether these are weighted by the amounts. Table III-19 summarizes such data as are available. It is seen that for the country as a whole 18 per cent of farmers failed to pay interest (on time?) but 43 per cent did not pay back principal (on time?).

The higher proportion of those repaying interest on time is not surprising. Even though in many cases the terms of loans do not explicitly separate the interest from the principal, lenders make sure thay any partial repayment is first credited to interest, with successive payments being applied to the capital value of the loan. What is surprising, however, is the very high proportion of those who do not pay back principal.

Were the figures in Table III-19 to be taken as pertaining to the actual loss experience of the lenders (rather than to a delay), then it would seem that the rates of interest exacted in the Thai countryside are far from being exorbitant, a loss ratio on both interest and principal of the order of 20 per cent effectively reduces the nominal interest rate[48]

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[48] Nominal rate is the rate agreed on, either implicitly or explicitly, between the borrower and the lender.

Table III-19

Repayment Performance of Borrowers

Region	Percentage Repaying Principal	Percentage Repaying Interest
Central	49.6	77.6
North	77.8	95.8
Northeast	64.4	91.1
South	50.7	70.4
Total (465 borrowers)	57.0	81.9

charged on a loan by more than half. Thus, with a nominal rate of 50 per cent per annum and with a bad debt ratio of 20 per cent (one in five borrowers fails to repay both interest and principal), the effective return to the lender is only 20 per cent per annum.[49]

[49] If R is the nominal rate, ϕ the bad debt ratio, and E the effective rate, then $E = R - \phi - \phi R$.

Table III-20

Nominal and Effective Rates of Interest

Bad Debts as Per Cent of Loan Value	Effective Rates of Interest				
	10	15	25	50	
10	22.22	17.78	38.89	66.67	Nominal Rates
15	29.41	35.29	47.06	76.47	
25	46.67	53.33	66.67	100.00	
50	120.00	130.00	150.00	200.00	

Source: See Footnote 50.

Table III-20 shows the effective interest rates under various assumptions regarding the bad debt ratio and the nominal rate.[50] In order for the lender to realize an effective annual rate of 25 per cent per annum, for example, he would have to charge the borrower 66.67 per cent if he believes that one out of four farmers will fail to pay back the interest and the principal.

In fact, however, the proportion of those who repudiate the debt is almost certainly lower than that shown in Table III-19. Rural lenders

[50] $E = \frac{R \text{ plus } \phi}{1 \text{ minus } \phi}$ The formula does not consider compound interest, a minor consideration in the case of agricultural loans which are typically of short duration.

do extend the maturity of the loan, particularly when non-repayment is attributable to natural causes. All the same, uncertainty regarding these and other causes of non-repayment do result, in the case of rural credit, in considerable disparity between nominal and effective rates of interest.

Other Aspects of the Unorganized Markets

The picture which emerges from the available empirical data suggests a large potential demand, on the one hand, and a limited supply of funds on the other. That a large need for funds exists is demonstrated both by the results of various surveys and by the published observations of keen students of agricultural credit who point out low levels of income of farmers, little savings, uncertainties due to vagaries of weather and market, the seasonal nature of production--particularly of monsoon agriculture--and the desire to maintain consumption at a scale dictated by custom and prestige.[51]

Due to the unavailability of collateral, to limitations on the supply side, and to other constraints, both institutional and cultural, effective demand is substantially below the potential need for funds. In particular, not enough credit is extended for purposes which will tend to enhance the productivity and the income of the farmer and particularly for purposes which would make the loan a self-liquidating one, in the sense of its proceeds adding to the value of output an amount in excess of

[51]See, for example, U Tun Wai, op. cit., p. 81.

the value of principal plus interest. To quote a passage from the Thai sample survey: "Actually, in an underdeveloped country, the agricultural credit problem is more likely to be too few debts than too many; the inability to obtain credit on terms they can afford may limit the farmer's possibilities of expanding output.[52]

The contention that the volume of credit demanded would have been greater had the terms been more favorable to the farmer suggests that the elasticity of demand in terms of price (interest rate) is greater than unity. There is some evidence to suggest that this indeed is the case.[53]

In any event, whatever the shape of the demand function in the market for lendable funds in agriculture, a shift to the right of the supply function would lower the cost of capital and increase the quantity of rural credit. As it is, it is contended that the existing supply schedule has low elasticity. Those who lend funds in the countryside are often persons aware of alternative uses of capital which, given the relative risks, they may find more attractive. The institutional framework in which rural lenders operate does not offer short-run possibilities of expanding credit in a way possible in a fractional reserve banking system. The links with the large, urban, organized market for funds are weak and

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[52] Narkswasdi, op. cit., p. 19.

[53] Thus, defective demand for credit is greater in those areas where the rate of interest is lower and where there is a greater degree of monetization of the economy. See Udhis Narkswasdi, op. cit., pp. 37ff, and the cross-section data cited therein.

uncertain.[54]

An examination of the conditions under which lenders operate, however, lends little firm evidence to support the contention that the prevailing terms of credit are the results of some conspiracy rather than the results of economic forces over which the lenders themselves have but limited control. Even when lenders in the unorganized markets insist on land mortgage, they are often willing to accept the sort of document which is not acceptable to the commercial banks. In Thailand, one reason why relatively good credit risks will borrow in the unorganized market rather than from banks or from an officially sponsored institution is the more relaxed attitude of the unorganized market lenders toward this question of land collateral.[55]

Frequently moneylenders will waive collateral but will exact a higher

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[54] It is probable, however, that scarcity of data tends to understate the extent of the linkage. In export-oriented economies, in particular, organized markets do supply credit to agriculture, albeit indirectly. Banks finance exporters of crops, and bank-financed importers finance shopkeepers in the hinterland. See, in this connection, U Tun Wai, op. cit., pp. 94ff, and Narkswasdi, op. cit., p. 43.

[55] In Thailand there exist three types of titles to land. One is really a temporary squatter's permit, unacceptable to all lenders; the second is a deed of sale, which is not acceptable to organized market lenders but accepted by moneylenders; and the third is a duly registered title, acceptable to all. The moneylenders will not insist on registration, on appraisal, and on other formalities which farmers find not only irksome and time consuming but, equally important, sometimes impairing their dignity and standing in the community.

rate of interest. Indeed, the prevalence of some very high annual rates of interest can, in the majority of cases, be traced to loans made for small sums to farmers not noted for their creditworthiness and devoid of any security. Such loans are usually made for either emergency or current consumption, and there is little in the proposed use of the loan which would diminish the risk to the lender.[56]

The flexibility in the practices with respect to collateral and the willingness to advance funds, at a price, to less creditworthy farmers for consumption purposes are among the two important reasons which account for the fact that, in a country like Thailand, perhaps 95 per cent of all loans are contracted outside the organized markets.[57]

Other reasons for the prevalence of unorganized markets in agricultural credit are found throughout the vast literature dealing with rural conditions in the less developed countries.[58] Moneylenders dispense with

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[56] One subsidiary reason, not hitherto mentioned, for the existence of high rates of interest is the fact that many lenders in the unorganized markets ("moneylenders" for short) lend out their funds for only a few months in a year, there being no demand for credit during the remainder of the year. Monthly interest thus has to compensate for funds being idle during, say, harvest months and yet provide an annual rate of return which warrants the use of capital in agriculture.

[57] See above, Table III-2. Commercial bank loans to agriculture from January 1962 to January 1964 rose by only 70 million baht (Bank of Thailand, Annual Economic Report, 1964). Not many of these loans were made directly to farmers.

[58] In addition to the sources cited on the preceding pages, the most comprehensive and in many ways indispensable reference is the Reserve Bank of India, All India Rural Credit Survey, Vols. I and II (Bombay: Reserve Bank of India Publications, 1954, 1956, and 1957).

many cumbersome procedures and with much paperwork. They grant loans tailored to fit the borrower's need of the moment. Most important of all, they can disburse funds quickly and without recourse to an authority other than their own. Also, as mentioned previously, they are amenable to delays and postponements of repayment and will, on occasion, grant an additional loan to a debtor in temporary straits. Finally, moneylenders are ubiquitous, as contrasted with sporadic institutional lenders, know their customers well, and are well known to them. Indeed, the relationship between the borrower and the lender outside the organized markets often involves a broader range of services with the lender performing valuable economic functions in the area of technical advice, storage, and marketing.

Be that as it may, elements of monopoly certainly exists, and many abuses do take place. Even in Thailand where, in recent years at any rate, dispossession and loss of land through debt have been rare occurrences, there are reasons to believe that farmers are not fully aware of the implicit cost of borrowing in such practices as sales of green paddy or repayment of loans in kind in farm produce. Moneylenders employ various techniques to hide the true cost of a loan from officialdom, and some of these techniques rebound to the disadvantage of the less sophisticated and less alert borrowers.[59]

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[59] These include such devices as lumping principal and interest in one promissory note with only one sum showing; deducting interest from the funds disbursed; postdating checks which again lump interest and principal; issuing two promissory notes, one for interest, the other for principal, but both claiming to be for principal; etc. See U Tun Wai, op. cit., p. 98.

Even though moneylenders will frequently dispense with any security against the loan and will advance funds to improvident borrowers, they are not without recourse with respect to balky and recalcitrant debtors. In fact, while many of the methods employed to secure recovery shun courts and legal redress, they may appear to the farmer to be on occasion more ruthless than repossession proceedings.[60] Yet, by all accounts, defaults do take place, and they do so in a significant proportion of all loans granted.

But, if the often made assertion about the scourge of money lending and the plight of the farmer who falls prey to them appears greatly exaggerated, when not beside the point, it does not follow that the status quo in agricultural credit is either desirable or incapable of improvement. Much of the desirable productive activity does not take place because either supply of finance is limited or its terms are unacceptable. Yet much lending in the countryside is for purposes which do little to improve the lot of the farmer over time. The existing structure of credit tends to impede the flow of voluntary savings on the part of the farmer in a variety of ways. Farmers are compelled to borrow for a few months every year merely to survive, and the very necessity to do so inhibits

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[60] These methods rely on social compulsion and "exploit" the farmer's concern about "face" and status in the village. See A. Bottomley, op. cit.

accumulation of cash savings, let alone entrusting them to a specialized financial institution. The fact that most farmers are perennially in debt robs them of an incentive to save more, or indeed to work harder or more efficiently. There is little in the structure of unorganized markets which would encourage longer-term productive credit designed to increase the farmer's income and thus his ability to save. Short-term consumption loans are certainly more risky, but the risk is compensated by the high interest rate; and the lender who values liquidity prefers the existing pattern of credit. To the extent that these lenders accumulate profits, they seldom use them for development of productive enterprise but, rather, for ultimate enjoyment of consumption.

In short, the unorganized markets in agricultural credit fulfills a static purpose.[61] It supplies high-cost, high-risk credit to many who otherwise would not have been able to tide themselves over from one year to the next. It is designed to maintain the existing asset structure with little growth of either output or profits allowable over time. Given the limited supply and a very large need for funds for frequently non-productive purposes, the unorganized market does its job reasonably well, at prices which appear consonant with conditions prevailing in that market.

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[61] See Horace Belshaw, Le Credit Agricole Dans Les Pays Economiquement Sous-Developpes (Rome: FAO, 1959), pp. 59ff.

Given the nature of these unorganized markets, it can hardly be expected that they will of and by themselves gradually abandon their emphasis on consumption and short-term "asset maintenance" loans and shift their emphasis into provision of loans for productive purposes. Yet, as argued previously, it is the latter type of loan which is most likely to increase the farmer's income over time and to generate voluntary saving capable of being channeled into further productive uses. This being so, attention should be devoted to devising ways and means of either changing the character of these unorganized markets or, alternatively, transferring some of their functions to markets which respond to developmental priorities. Some of these ways and means are suggested in the concluding sections of this chapter. But, as will be seen in the succeeding pages, the mere extension of the scope of the organized markets as they perform at present is not likely to be very fruitful. The organized markets require a considerable amount of social engineering if they are to become more efficient and to increase their share in the market for lendable funds in agriculture.

Organized Markets in Agricultural Credit

Little is known about the inner structure of the unorganized markets in agricultural credit even though this market provides the vast bulk of all the funds to farmers.[62] On the other hand, there is no dearth of information about the structure of the institutions comprising the organized market, even though only a fraction of total agricultural credit flows through them. This situation is, of course, implicit in the fact that the latter institutions, being subject to public scrutiny, supervision, and control, are surrounded by legislative enactments, administrative statutes, and accounting requirements. They have to publish financial statements at regular intervals; they have to submit reports; and they are frequently the subject of official discussions and memoranda.

In no small measure these organizational constraints are responsible for the minor role which the organized markets play in agricultural credit. The constraints limit the area of operations, preclude actions and policies which could extend the scope of the institutions, and inhibit their flexibility and freedom of movement. Yet, the basic motivation of these constraints, to direct the flow of funds in agriculture to developmental

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[62] Among the unknown aspects of what one is tempted to call the "organization of unorganized markets" are the interrelations of various lenders, their sources of funds, the tie-in with commercial banks and other institutions, the degree of formal or informal collusion, and so on.

ends consistent with the national resources and objectives, is a sound one. Hence, a study of the institutions in the organized markets must bring out which of these constraints are unavoidable and a necessary price to be paid for social control, and which are expendable or could be reworked so as to provide maximum efficiency consistent with developmental aims.[63]

The organized market for agricultural credit consists of three unequal parts. The bulk of credit comes from the cooperative institutions. A small proportion is provided by various governmental departments and, in recent years, a small but growing amount of lendable funds to the farmers have been made available by at least one commercial bank. In the aggregate the institutional loans to farm households have not, in recent years, exceeded 100 million baht annually, which according to the sample survey represented in 1962-63 some 5.5 per cent of all loans made to farmers.[64]

Of the three components of the organized market, the most highly structured is the cooperative institutional complex. At its base it consists of nearly 10,000 primary cooperative credit societies, of unlimited liability type. At its apex it was represented by the Bank for Cooperatives.[65] The structure is, however, far from being a formal pyramid.

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[63] See, Chapter I.

[64] Bangkok Bank, Ltd. did not start its program of loans to farmers until 1963. In 1965, its annual loan volume approached 10 million baht. See below.

[65] Until 1967 when it was replaced by the Bank for Agriculture and Cooperation Credit. See below.

In fact, between the apex and the base there are only two district agricultural banks or, rather, federations of credit cooperatives, and some seven production credit societies, a rather new and promising form of dispensing credit to the Thai farmer.

The supply of agricultural credit emanating from governmental departments is uneven, intermittent, and directed to achieve ad hoc goals. It is confined to one or two ministries and is concentrated in the Ministry of Agriculture.

So far, the commercial banks' direct loans to farmers are limited to the activities of the Bangkok Bank Ltd., and some preliminary explorations on the part of one or two others. However, commercial banks do, of course, make loans classified as agricultural, which are usually confined to accommodation extended to processors, distributors, and exporters of agricultural crops.[66]

The Cooperative Institutions

At the end of 1964 there were in existence 9,915 village credit cooperatives, by far the most important direct source of institutional credit to the farmer. The membership of these cooperatives covers only

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[66] See below.

about 8 per cent of farm households.[67]

The introduction of cooperatives into Thai agriculture dates back to 1916. It was originally meant to be an experiment, and their enactment was through an amendment to the existing law on associations. By 1928, when the cooperative movement was already well on its way, a cooperative statute was promulgated. This statute, subject to minor amendments, is still in force.

From its very beginning the stimulus, direction, and control of the cooperative movement was in the hands of the government. Initially, the unit of government in charge of cooperatives was located at the Ministry of Agriculture. From there it shifted to the Ministry of Cooperatives, now defunct, and since 1963, to the Ministry of National Development and its Department of Credit and Marketing Cooperatives. The latter unit of government is, however, only one of three departments dealing with cooperative societies under the direction of the Registrar of Cooperative Societies, who is concurrently Deputy Secretary of the Ministry of National Development. The Registrar is in charge of the organization, registration, liquidation, supervision, and audit of all types of cooperatives. In the field, the Registrar operates through nine regional

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[67] There were, in addition, six production credit cooperatives, 263 farm products marketing cooperatives, and 457 land cooperatives. (NDEB, Agricultural Credit and Cooperatives in Thailand [May, 1965], mimeo.) Only the production credit cooperatives will be discussed in this chapter.

inspectors who, in turn, control 63 provincial and 182 district supervisors.[68]

In the history of the cooperative movement in Thailand, there emerge three distinct stages. From its formation until the Revolution of 1932 the cooperative movement was an experimental, emergency device to protect the farmer from the imminence of dispossession and loss of land. Only after 1932 did the government undertake to promote actively the spread of cooperatives (including other than credit cooperatives), albeit still mainly on what may be termed welfare principles. In this, the second stage of the cooperative development, the formation of the Bank of Cooperatives in 1947 gave a fillip to the movement which lasted until about 1954 and which witnessed a vigorous growth of credit societies. Since 1954, the cooperative movement remained rather stagnant. The number of societies and the volume of loans outstanding remained roughly constant.[69] Between 1947 and 1954 the number of village credit societies rose from 5,385 to 9,580, and loans outstanding to members expanded from 39 to 256 million baht. From 1955 to 1963 the number of societies oscillated around the

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[68] See Chamsien Saranaga, The Role of Government in Cooperative Development of Thailand (Bangkok, January, 1966), mimeo.

[69] There are no reliable data on the operations of the village credit cooperatives beyond 1963. Since about 1961 the number of primary societies has actually declined, partly as a result of a deliberate policy to consolidate the village societies and to weed out the least efficient ones.

9,850 level, and loans outstanding to members rose only by 18 per cent to under 300 million baht (See Table III-21).[70]

Even though the village credit cooperatives have accumulated a little over 90 million baht of reserves and some 34 million of deposits, the bulk of its funds for lending came from the Bank for Cooperatives. As shown in Table III-21, by the end of 1963 the cooperatives owed the Bank for Cooperatives some 218 million. These funds are borrowed at 7 per cent and are relent to members at 10 per cent per annum with the differential covering the costs of operation and accruing or contributing to the cooperative reserve fund or else used for other functions the village cooperatives are supposed to perform, such as farm and cooperative education.

The 10 per cent rate charged by the village cooperatives to their members is a single rate irrespective of the duration of the loan or its purpose. In the past, the bulk of the loans were for medium and long duration, up to 10 years, and to a large extent for the purpose of acquisition of land and debt consolidation. In recent years, however, a greater emphasis has been put on the provision of loans for the purchase of farm machinery and land improvements, and short term loans for general

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[70] As shown in Table III-22, the volume of loans outstanding remained constant even though loans disbursed annually rose from some 20 million baht in 1955 to 83 million in 1963. Repayments of principal since 1961 began to exceed disbursements, however, increasing the ratio of repayments to loans outstanding from 8 per cent in 1955 to 28 per cent in 1963.

Table III-21

AGRICULTURAL COOPERATIVE CREDIT SOCIETIES
(Unlimited Liability Credit Coops.)

CONSOLIDATED BALANCE SHEETS 1955 - 1963
(in thousand baht)

	1955	1956	1957	1958	1959	1960	1961	1962	1963
Number of Operating Societies	9,832	9,835	9,858	9,932	9,930	9,922	9,917	9,907	9,876
ASSETS									
Cash in hand and banks	2,994.5	3,595.7	2,951.8	3,199.4	2,820.2	3,326.2	4,128.9	5,253.8	6,422.3
Loans	254,152.3	259,538.4	274,400.3	295,862.3	300,648.5	307,794.7	306,723.7	300,349.7	299,219.2
Interests receivable	25,725.8	30,749.0	38,145.6	46,119.9	51,855.2	57,593.8	54,240.9	48,323.0	41,681.7
Investments	7,730.5	7,775.8	7,812.0	7,911.1	9,101.6	9,690.6	10,339.0	10,385.2	10,418.9
Other assets	26.2	35.0	36.0	160.0	542.3	412.9	592.5	3,406.7	128.9
Miscellaneous	365.4	251.1	264.4	539.3	1,052.4	1,034.5	1,047.5	1,777.8	1,676.6
Total	290,994.8	301,945.0	323,610.1	353,792.0	366,020.2	379,902.7	377,072.5	369,496.2	359,547.6
LIABILITIES									
Share capital	257.8	261.3	263.4	271.3	269.1	272.3	280.8	289.9	300.7
Reserves	32,006.6	40,278.6	46,641.3	53,316.0	60,415.9	67,753.4	75,522.7	83,277.5	91,462.6
Common-good fund	1,258.4	1,720.5	2,074.7	2,435.4	2,833.5	3,245.8	3,679.8	4,121.3	4,476.5
Borrowings	239,137.5	239,188.9	249,721.0	268,781.3	269,542.8	272,594.1	258,623.1	239,596.2	217,899.1
Deposits	9,005.9	13,351.4	17,341.8	20,774.8	24,095.1	26,906.3	29,788.0	32,346.8	34,518.6
Other liabilities	79.6	70.2	90.7	151.9	510.3	356.4	280.5	340.6	406.7
Profits	9,248.9	7,074.1	7,476.2	8,061.3	8,353.5	8,764.4	8,897.6	9,523.8	10,483.5
Total	290,994.7	301,945.0	323,610.1	353,792.0	366,020.2	379,902.7	377,072.5	369,496.2	359,547.6

Source: Department of Credit & Marketing Cooperatives, Ministry of National Development.

Table III-22

LENDING OPERATIONS OF UNLIMITED LIABILITY CREDIT COOPERATIVES
1955-1963 (in thousand bahts)

Year	Loans Disbursed	Repayments of Principal	Loans Outstanding	% of Repayments to Loans Outstanding
1955	19,635.7	20,219.1	254,112.3	7.95
1956	26,860.8	21,481.6	259,491.5	8.27
1957	36,533.4	21,638.9	274,386.1	7.88
1958	42,582.3	21,106.2	295,862.2	7.13
1959	48,179.0	43,392.7	300,648.5	14.43
1960	49,117.4	41,971.1	307,794.8	13.63
1961	56,312.0	57,383.0	306,723.8	18.70
1962	64,474.5	70,848.5	300,349.7	23.58
1963	83,317.6	84,448.2	299,219.2	28.22

Source: Ministry of National Development, Department of Credit and Marketing Cooperatives.

farm operation.

As mentioned previously, the village societies are of the unlimited liability type. Even though each loan must be secured by land mortgage, the borrower must attach two signatures of fellow villagers to his loan application. In addition, the board of directors of the society, around three or four members, must approve the application which is then submitted to the Bank of Cooperatives, whose officers, together with the officials of the Department, approve and disburse the loan. The village society membership then is supposed to see to it that the proceeds are spent according to the purpose set out in the application.[71]

The golden era of cooperative growth in Thailand, from 1947 to 1954, followed the establishment of the Bank for Cooperatives, and the injection of funds into rural credit from sources outside agriculture.

The Bank for Cooperatives was actually established under an Act passed in 1943, but it did not start operations until 1947. It was, in principle, an independent institution, even though the Minister of National Development and the Registrar of Cooperatives were ex-officio chairman and vice-chairman of the Board. The rest of the Board members, five in number, were elected by the shareholders.[72]

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[71] See Ministry of Cooperatives, Present Conditions of Agricultural Cooperation in Thailand (Bangkok,1962), mimeo.

[72] Much of the factual information regarding the Bank for Cooperatives is drawn from Bank for Cooperatives, Eighteen Years Progress of the Bank (Bangkok, 1965), mimeo.

In addition to initial capital of some 35 million baht transferred from the Department of Cooperatives which came from the sale of bonds and from capital stock, the bulk of the Bank's resources was borrowed from the Government Savings Bank, the Ministry of Finance, and from Counterpart Funds. Beginning in 1951, the Bank was authorized to accept deposits from the public. At the end of 1964, total resources of the Bank stood at some 273 million baht (See Table III-24).

The Bank for Cooperatives has borrowed, since its inception, a total of 156 million baht from the Government Savings Bank at rates of interest ranging from 4 per cent per annum in the early years to 7 per cent in 1962, the last recorded date. Since 1954, however, the amounts of loans granted by the Savings Bank have been declining; and recently, in spite of a rate of interest which eliminates any margin to the Bank for Cooperatives, no funds have been forthcoming from this source.[73] A similar situation obtains in respect to loans from the Ministry of Finance, the other major supplier of funds to the Bank for Cooperatives and, hence, to the village societies. Of the total amount borrowed since 1950, 125 million baht, only some 30 million came after 1954 and only

[73] Operation costs of the Bank for Cooperatives were covered out of the spread between the interest paid and received. The Bank received no budgetary allocation (other than that implicit in the low interest payable on government funds).

Table III-23

UNLIMITED LIABILITY CREDIT COOPERATIVES

LOANS DETAILED BY PURPOSE
1956-1963

	Percentage of Total							
	1956 %	1957 %	1958 %	1959 %	1960 %	1961 %	1962 %	1963 %
Long-Term								
Old debt refinancing	21.8	15.7	14.7	15.0	13.1	17.9	10.2	16.5
Land purchase	2.6	2.5	2.7	3.0	3.5	3.3	3.3	5.2
Reorganization of farm Operation	-	-	-	-	-	-	-	0.2
Medium-term								
Purchase of work animals	35.2	31.1	28.7	33.0	29.0	25.1	24.7	25.5
Land improvement	11.4	18.6	20.2	19.8	20.7	25.8	24.3	25.6
Farm machinery	3.0	4.0	4.0	6.1	5.1	6.6	6.7	6.5
Farm implement	3.3	3.2	3.2	2.3	0.8	1.8	0.2	0.1
Transport equipment	3.9	3.2	2.2	2.9	2.3	1.8	2.1	1.8
Animal husbandry	-	-	-	-	-	-	2.0	1.6
Plantation	-	-	-	-	-	-	1.2	1.1
Building of farm houses	-	-	-	-	-	-	9.7	11.0

Source: See Table III-22.

Table III-23 (continued)

UNLIMITED LIABILITY CREDIT COOPERATIVES

LOANS DETAILED BY PURPOSE

1956-1963

Percentage of Total

	1956 %	1957 %	1958 %	1959 %	1960 %	1961 %	1962 %	1963 %
Short-term								
Seed fertilizers and Agricultural Chemicals	0.7	0.8	3.5	0.7	3.1	0.1	1.0	0.6
Wages, rents, taxes	0.5	-	-	0.1	-	-	1.9	2.2
Household expenses	1.6	2.4	5.4	1.5	6.0	0.6	9.2	0.6
Ceremonial expenses	0.5	0.4	0.3	0.5	0.3	0.1	-	-
Food stuff	-	-	-	-	-	-	0.2	0.3
Others	15.5	18.1	15.1	15.1	16.1	16.9	3.3	1.2
Total	100	100	100	100	100	100	100	100
Total (in thousand bahts)	26,861.0	36,533.0	42,582.0	48,179.0	49,117.4	56,312.0	64,474.5	83,317.6

Source: Department of Credit and Marketing Cooperatives.

Table III-24

BANK FOR COOPERATIVES

COMPARATIVE BALANCE SHEETS 1956 - 1964
(in million baht)

ASSETS	1956	1957	1958	1959	1960	1961	1962	1963	1964
Cash in hand and banks	44.0	45.6	26.6	37.7	35.1	37.9	44.0	41.0	44.5
Advance to Coop. Societies	238.9	250.2	268.5	270.8	274.3	261.2	243.9	224.3	211.2
Loss: reserve for bad debts	0	0.1	0.2	0.2	0.2	0.2	0.2	0.3	0.3
Current Assets	238.9	250.1	268.3	270.6	274.1	261.0	243.7	224.0	210.9
Other Assets	-	0.1	2.0	2.5	2.2	1.5	2.1	2.2	0.6
Government Securities	-	-	-	-	-	9.0	15.9	23.9	16.9
Fixed Assets	0.3	0.3	0.4	0.3	0.3	0.4	0.3	0.4	0.4
Total Assets	283.2	296.1	297.3	311.1	311.7	309.8	306.0	291.5	273.3

Source: Eighteen Years Progress .

Table III-24 (continued)

BANK FOR COOPERATIVES

COMPARATIVE BALANCE SHEETS 1956 - 1964
(in million baht)

LIABILITIES	1956	1957	1958	1959	1960	1961	1962	1963	1964
Authorized paid-in-capital	10.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0
Reserves	7.7	11.5	15.2	19.4	24.6	26.2	32.8	38.7	43.7
Deposits	16.0	20.6	25.4	31.1	36.6	40.7	45.6	46.7	43.2
Other liabilities	3.7	4.7	4.5	7.5	7.5	5.5	7.6	7.7	7.5
Bonds and borrowings:									
4 1/2% Coop. Bonds	15.1	14.0	12.9	11.7	10.4	9.1	7.8	6.4	4.9
Government Savings Bank	113.6	113.7	110.0	112.5	104.4	103.3	95.7	84.7	72.3
Ministry of Finance	107.2	111.3	108.7	106.9	103.6	96.5	88.5	80.1	75.3
Counterpart funds	4.3	4.7	4.4	4.2	3.9	3.6	3.3	3.0	2.8
Dept. of Credit and Marketing Cooperatives, Revolving fund	-	-	-	0.9	3.8	4.8	6.5	7.3	7.4
Profit	5.6	5.6	6.2	6.9	6.9	10.1	8.2	6.9	6.2
Total Liabilities	283.2	296.1	297.3	311.1	311.7	309.8	306.0	291.5	273.3

Source: Eighteen Years Progress.

4 million after 1960. Interest rates payable to the Ministry of Finance were 4 per cent, with the exception of the last loan in 1964 at 2 per cent.

Table III-25 shows the effect of the drying up of the supply of outside funds. Repayments from village cooperatives actually exceeded new loans since 1954, and the total of loans outstanding declined since 1962.[74]

Before concluding the expository discussion of the cooperative structure in Thailand, mention should be made of the two District Cooperative Banks, one in Chiengmai and the other in Uttradit. These were set up in the early 1950s with funds provided by the Bank for Cooperatives and supplemented by a loan from counterpart funds. These district banks which, in reality, are federations of village credit cooperatives in the two northern provinces, were set up in the hope of tapping local funds for agricultural credit to supplement those available from the Bank for Cooperatives. Some 260 village societies belong to these two federations. The terms and conditions on which the federations finance their members are analogous to those of the Bank for Cooperatives. The cost of operation of these federations is covered out of a spread of 1 per cent which is the difference between the 6 per cent payable by the federations to the Bank for Cooperatives and the 7 per cent they charge their members.[75]

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[74] As seen in Table III-22, village societies could increase the volume of loans disbursed in spite of the trickle of funds from the Bank for Cooperatives, because in the last few years repayments were in excess of disbursement. As much of the loans outstanding are probably in default, this process will soon come to a halt.

[75] Only 4 per cent is payable on the 5 million baht borrowed from the counterpart fund.

Table III-25

Lending Activities of the Bank for Cooperatives
1947-1964

Year	New Loans	Repayment Including Interest	Total Loans Outstanding	Repayment as Percent of Loans Outstanding
	Baht			Percent
1947	25,069,053	9,213,405	38,471,751	23.94
1948	36,280,405	13,878,871	63,895,808	21.72
1949	41,868,845	18,423,209	92,196,719	19.98
1950	26,403,897	21,576,934	103,005,130	20.94
1951	44,055,176	27,531,867	126,299,111	21.79
1952	77,413,238	33,932,934	179,056,811	18.95
1953	74,686,505	37,542,525	228,953,358	16.39
1954	42,667,893	40,602,026	245,879,414	16.51
1955	20,079,773	44,291,640	236,964,789	18.69
1956	28,585,240	43,393,815	238,945,517	18.16
1957	38,749,019	44,583,475	250,198,937	17.81
1958	42,738,353	42,481,262	268,281,529	15.83
1959	28,293,953	45,116,535	270,369,260	16.68
1960	27,196,057	44,488,517	273,680,878	16.25
1961	26,740,941	60,257,345	260,385,308	23.14
1962	34,669,331	70,649,825	243,902,423	28.96
1963	50,308,138	88,014,140	221,096,650	39.80
1964	62,227,898	93,045,559	205,804,547	45.21

Source: Department of Credit and Marketing Cooperatives.

Table III-26 gives balance sheets for the two federations for the years 1955-65. There is little indication that the federations have succeeded in attracting local capital to any significant extent.

Cooperative Credit-Performance and Prospects

In spite of its relatively long history the cooperative credit remains of minor significance in the market for lendable funds in agriculture. It did little to enhance the income or the earning potential of its customers; its influence on inculcating thrift habits and voluntary saving was negligible;[76] and its impact on the unorganized market was barely perceptible.

A full discussion of the failure of the cooperative movement in Thailand to live up to its early promise is beyond the scope of this study. But overshadowing all economic, political, or social factors which account for the marginality of the cooperatives in rural credit is the fact that they owe their formation and their continued existence to the initiative of the government rather than to the expression of the economic need of the Thai farmer. The very concept of the cooperatives was borrowed from a different social and economic setting and transplanted to a soil which proved much less hospitable than that of Europe. In the 50 years of its operations the cooperative credit movement in Thailand has developed little

[76] See succeeding section for a discussion of the attempts of the cooperatives to augment the flow of saving in the countryside.

Table III-26

FEDERATIONS OF UNLIMITED LIABILITY CREDIT COOPERATIVES
Consolidated Balance Sheet as of June 30, 1955 - 65

(in thousand bahts)

Number Federations	1955 2	1956 2	1957 2	1958 2	1959 2	1960 2	1961 2	1962 2	1963 2	1964 2	1965 2
Liabilities											
Paid-up share Capital	667.1	683.5	688.0	695.8	697.1	699.0	700.2	674.6	713.8	739.3	755.1
Reserves	72.2	116.8	189.7	276.2	375.1	483.0	591.5	699.2	809.2	915.1	980.8
Share-Transfer Fund	-	-	-	-	-	-	-	-	-	0.5	35.8
Dividend Stabilization Fund	20.8	30.2	45.0	59.5	74.0	92.7	97.7	104.7	111.7	78.7	85.7
Common-Good Fund	10.4	15.1	21.0	26.7	32.5	38.3	41.3	40.8	40.5	36.3	37.4
Deposits	2,119.1	1,274.0	1,532.3	1,506.1	1,305.3	1,213.6	1,473.9	1,296.8	831.4	637.8	1,266.6
Loans from Bank for Coops.	7,699.1	7,900.7	8,271.1	7,720.4	7,785.7	7,621.1	7,583.4	7,439.2	7,702.5	9,198.5	9,144.0
Over Payments of Loans by members	-	-	-	-	-	38.0	65.9	50.0	64.8	72.9	115.9
Unpaid dividend on capital	0.3	0.3	1.7	7.8	0.6	9.3	2.3	2.4	2.6	3.7	5.5
Unpaid Contribution to Union Fund	1.0	-	-	-	1.0	-	0.7	-	0.9	-	1.3
Miscellaneous	-	0.1	0.2	-	6.4	3.4	0.5	-	1.5	37.0	-
Profit for year	131.2	179.3	197.0	414.1	226.6	213.2	200.2	209.5	208.8	183.6	143.2
Total	10,721.2	10,200.0	10,946.0	10,706.6	10,504.3	10,411.6	10,759.6	10,517.2	10,487.7	11,903.4	12,571.3

Table III-26 (continued)

FEDERATIONS OF UNLIMITED LIABILITY CREDIT COOPERATIVES
Consolidated Balance Sheet as of June 30, 1955 - 65
(in thousand baht)

Assets	1955	1956	1957	1958	1959	1960	1961	1962	1963	1964	1965
Cash in Hand	228.7	191.8	270.8	291.7	299.0	103.8	290.5	125.3	78.3	127.7	117.2
Deposits at Banks	1,021.6	177.0	647.0	413.3	700.7	385.9	527.0	721.0	840.8	1,140.0	1,376.3
Accrued interest on Deposits	-	-	-	-	-	-	3.3	6.8	3.7	4.2	-
Loans to Credit Cooperatives	9,137.0	9,338.9	9,595.5	9,409.4	9,106.4	9,506.7	9,525.6	9,269.8	9,184.2	10,181.2	9,927.8
Stationary	2.4	3.4	2.9	3.9	3.0	2.7	4.2	6.0	5.2	19.0	14.0
Furniture & Fittings	83.4	81.9	71.6	60.9	47.9	40.2	35.2	50.1	42.2	45.0	182.2
Office Building	133.0	126.0	119.0	113.1	107.4	102.3	97.2	98.2	93.3	88.7	409.7
Land	240.0	240.0	240.0	240.0	240.0	240.0	240.0	240.0	240.0	240.0	480.0
Miscellaneous	5.5	1.3	-	-	-	-	-	-	-	-	63.8
Total	10,851.6	10,160.3	10,946.8	10,532.3	10,504.4	10,381.6	10,723.0	10,517.2	10,487.7	11,845.8	12,571.0

Source: See Table III-22.

unofficial leadership, managed to tap very little of private resources, and, in fact, hardly ever ceased to be a governmental operation based on principles which proved of little vitality in Asia.

It is largely because farmers consider cooperatives to be government-imposed institutions that they often fail to repay loans, that they frequently misuse the proceeds of the loans, or that they simply show a lack of interest either in joining a cooperative or approaching it for loans.

One aspect of rural credit that is not sufficiently emphasized in the literature is the importance of speed in obtaining funds. The slow, deliberate, often irksome delays which farmers associate with officialdom helps explain not only the reluctance of some farmers to deal with cooperatives but also the instances of misuse of funds obtained. A farmer may have originally requested funds for a genuinely productive purpose, but because of delay he felt compelled to get the money from a moneylender. When the cooperative finally gets around to disbursing the loan, the farmer will, more likely than not, spend the money for a purpose other than originally intended. One of the reasons why the operations of the Bangkok Bank, Ltd. appear to compete successfully with government-sponsored institutions in those areas where both types of lenders operate is the belief of would-be borrowers that the commercial bank will handle the application and the disbursement of the loan made more promptly. Even when this impression is not warranted in fact (some production loan societies

have a good record in this respect), it effectively inhibits those farmers who have access to either type of lender.[77]

It is quite common for prime risks to approach moneylenders from time to time, even when the borrower is quite capable of obtaining a similar loan on better terms from the local bank. While other considerations play a part, an often-voiced explanation is the overriding desire to obtain funds quickly. Some moneylenders can actually disburse a loan (in cash) within a few minutes of the appearance of prime risk applicants.

The governmental sponsorship and control over credit cooperatives also accounts for the lack of drive and vigor that sometimes characterizes those entrusted with the task of fostering the cooperative movement in the credit field. A district supervisor has no special incentives to expand membership, to increase the volume of business, or to experiment with new ideas and practices. On the contrary, in many instances a man nearing retirement or anxious to maintain his civil service rating in the facet of shifting political winds will tend to minimize his risks and his effort. There are, to be sure, many officials in the cooperative movement who are well trained, well motivated, and anxious to introduce long-delayed reforms. As will be seen below, their efforts have borne fruit to some extent. But it remains true that the very nature of official control over the cooperative movement militates against venturesomeness, provides little incentive for expansionism and risk-taking, and tends to perpetuate the

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[77] See below a more extended discussion of production credit societies and of the operations of the Bangkok Bank, Ltd.

status quo ante.

The attachment to the unlimited liability, Raiffesen-type of credit cooperative, and to the ideology of the cooperative movement rooted in the concept of welfare rather than economic efficiency, has further impeded the growth of this type of credit. Most village cooperatives are too small and too understaffed to permit efficient management. Their amalgamation and consolidation is, however, made difficult by the existing legal structure. The interest rate exacted by village cooperatives bears no relation to market conditions and, in fact, is one of the primary reasons for the gradual drying up of funds. It is difficult for the Bank for Cooperatives to borrow at 7 per cent when the Treasury pays 8 per cent on its bonds. On the other hand, a farmer may prefer to pay a higher rate of interest provided he can get the money, get it faster, and without many cumbersome procedures.[78] In particular, the requirement that each borrower must pledge his land severely restricts the scope of village credit societies, in spite of certain relief given to cooperative mortgagors.[79]

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[78] This is the opinion of many keen observers interviewed during field trips undertaken by the writer. In fact, most loans contracted by farmers are at a much higher interest rate.

[79] For example, members of village credit societies do not have to pay a registration fee on land mortgages.

Other factors which help to explain the relative stagnancy of cooperative credit in Thailand can be listed.[80] They include the farmers' lack of understanding of cooperative principles and practices, lack of adequate cooperative education and training, insufficient attention to integration of credit with marketing, and shortcomings in legal provisions.[81]

As mentioned above, the continuing efforts of the more vigorous and better motivated leaders of the cooperative movement, albeit still within the government, began to bear some fruit. Beginning in 1961, more effort was expended to direct cooperative credit activities into accommodation for the purchase of productive inputs, to simplify procedures, to insure group supervision, and to orient the granting of the loan toward its purpose rather than the credit status of the borrower. In spite of legal difficulties, consolidation and amalgamation was pushed forward and the formation of multipurpose societies encouraged.[82]

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[80] In spite of the absolute increase in the loans disbursed annually, shown in Table III-22, it would seem that the share of cooperative credit in the market has declined over the years. It is not impossible, moreover, to treat, for accounting purposes, a delay in collection of a loan due as simultaneously a repayment of an old loan and the granting of a new loan.

[81] See Chamien Saranaga, op. cit. Mr. Chamien was the Deputy Director-General of the Department of Credit and Marketing Cooperatives. Of course, many of the shortcomings mentioned in the texts are prevalent throughout Asia and frequently more acute elsewhere. "Cooperation has failed, but Cooperation must succeed." (Government of India, Summary Report on All-India Rural Credit Survey [New Delhi, 1960], p. 8.)

[82] See Agricultural Credit andCooperatives in Thailand.

But the most promising development in the field of cooperative credit was the growth and apparent success of production credit cooperatives. They were originally launched in 1959, and by the end of 1965 six were in operation and flourishing. In spite of their modest scope to date, the production credit societies merit a more extended discussion.

In the first place, the new type of credit institution has an operating area which covers an entire district (amphur). It is, therefore, large enough to serve a larger membership, to employ paid personnel, and to man its own office.

A production credit cooperative operates on three fundamental principles: limited liability, supervised credit, and integration of credit with provision of inputs and the marketing of outputs. Not all of these principles are, as yet, fully operative in Thailand, but their gradual implementation seems to augur well for the future of this type of credit.

The principle of limited liability enables the formation of larger groups and restricts responsibility of the members to the amount of loans they underwrite. Typically, up to 4,000 baht can be borrowed by any member without any collateral other than the signature of fellow members. The interest rate is 12 per cent per annum.

The principle of supervised credit relates the granting of the loan to the purpose for which the money is borrowed rather than to the social status of the borrower. Technical advice is extended regarding the best utilization of the proceeds and the best means of disposing of the crop.

Throughout the entire process, from the time of application until the sale of the crop, supervision is exercised both informally by members of a group within the society and formally by the supervisor from the Department of Credit and Marketing Cooperatives.

Integration with provision of inputs and with marketing of output is still in its infancy in Thailand, but some of the societies do handle, on indent basis, fertilizers, improved seeds and other inputs. Other market members produce on an agency basis.

It appears that, in spite of the rather elaborate application procedures and the institution of careful checks incident to supervision, production credit cooperatives manage to approve and disburse loans within 15 days from the date of application. The repayment record to date has been excellent (See Table III-27).

Table III-28 gives a detailed breakdown of the loan composition of the production credit cooperatives. It is seen that loans for "household expenses" are but a small and diminishing share of total loans.

So far, the financing of the production credit cooperatives has been on a somewhat artificial basis, funds being provided to it partly out of budgetary allocations and partly out of counterpart funds. These funds have been obtained at a subsidized interest rate so as to insure a spread to the production credit societies sufficient to cover the rather high cost of operation of supervised credit. As shown in Table III-29, the production credit societies have shown a profit which, beginning in 1961, has increased

Table III-27

Lending Operations of Limited Liability Production Credit Cooperatives, 1961-1965
(in thousand baht)

Year	Loans Disbursed	Repayments of Principal	Loans Outstanding	Repayments as % of Loans Outstanding
1961	2,059.1	611.6	6,447.6	9.48
1962	2,983.6	2,063.3	2,367.9	87.13
1963	4,042.7	2,867.5	3,543.1	80.93
1964	4,952.0	3,933.4	4,561.7	86.22
1965	7,430.5	5,040.0	5,654.9	89.12

Source: Department of Credit and Marketing Cooperatives.

Note: A better measure of the repayment record than the proportion to loans outstanding would be of repayments in relation to loan maturities. Even though percentages are not available it appears that repayments in relation to loan maturities are pretty well near 100 per cent at present.

Table III-28

LIMITED LIABILITY CREDIT COOPERATIVES

Loans Detailed by Purpose and Maturity - 1961 - 1965

Type of Loan and Purposes	1 9 6 1	1 9 6 2	1 9 6 3	1 9 6 4	1 9 6 5
Short-term Loans	Baht	Baht	Baht	Baht	Baht
1. Seeds	15,970	14,575	11,415	4,070)	
2. Chemical fertilizers & other materials	9,240	192,380	347,265	437,180)	494,650
3. Cultivation & harvesting expenses	1,209,570	1,832,910	2,291,470	2,391,600	3,014,030
4. Household expenses	75,110	66,575	133,390	74,840	78,860
5. Other expenses	-	1,900	73,300	55,050	162,810
6. Livestock fattening	-	76,500	184,100	199,350)	
7. Repairs to chicken sheds	-	-	-	1,000)	
8. Purchase of chicken and feeds	-	19,650	25,600	52,300)	968,300
9. Purchase of fingerlings and feeds	-	7,900	7,900	4,500)	
10. Renovation of fish ponds	-	3,200	13,450	12,000)	
11. Repairs to farm houses	-	-	9,800	11,870)	101,150
12. Repairs to water facilities	-	-	3,000	4,000)	
13. Repairs to farm implements	-	-	-	6,250	12,050
14. Expenses on mushroom cultivation	-	-	-	4,000	-
15. Payment of shares	-	32,050	36,600	29,620	137,210
Sub-total	1,309,890	2,247,640	3,137,790	3,287,630	4,969,060

Source: Department of Credit and Marketing Cooperatives.

Table III-28 (continued)

LIMITED LIABILITY CREDIT COOPERATIVES

Loans Detailed by Purpose and Maturity - 1961 - 1965

Type of Loan and Purpose	1961 Baht	1962 Baht	1963 Baht	1964 Baht	1965 Baht
Medium-term Loan[1]					
1. Pig raising	127,350	201,650	1,500	100,900)	
2. Poultry farming	92,500	50,860	51,400	117,950)	373,960
3. Fish culture	82,150	25,450	30,700	75,840)	
4. Purchase of farm machinery	37,950	15,250	116,720	161,880	209,030
5. Purchase of work animals	39,050	53,900	218,330	520,930	710,970
6. Refinancing of old debts	26,000	17,590	46,960	14,700	99,760
7. Improvement of orchards	22,200	15,300	6,800	21,220	-
8. Building and remodeling of farm houses	5,000	14,000	15,500	45,900	142,830
9. Purchase of farm implements	14,250	159,850	143,150	43,700	99,710
10. Land clearance and improvement	246,460	137,600	191,610	357,850	668,140
11. Purchase of transport equipment	2,500	13,350	15,850	42,150	57,220
12. Payment of shares	53,800	31,150	66,410	152,390	99,860
Sub-total	749,210	735,950	904,930	1,664,410	2,461,480
GRAND TOTAL	2,059,100	2,983,590	4,042,720	4,952,040	7,430,540

[1]The duration of medium-term loans is up to three years, the loans may be repayable by installments.
Source: Department of Credit and Marketing Cooperatives.
Ministry of National Development

Table III-29

LIMITED LIABILITY CREDIT COOPERATIVES

Consolidated Balance Sheets as of March 31, 1961 - March 31, 1965
(Unit : baht)

	1961	1962	1963	1964	1965
Number of operating societies	2	2	3	4	6
Membership	492	639	1,011	1,336	1,966
ASSETS					
Cash in hand	32,115	2,974	14,416	195,497	218,493
Banks	72,035	150,214	324,828	890,523	944,337
Interest Receivable	3,876	6,204	19,318	37,406	69,549
Short-term loans	975,600	1,817,470	2,661,250	1,649,330	2,810,398
Medium-term loans	471,950	550,400	881,800	1,615,030	2,844,490
Other debtors (agricultural supplies)	-	-	-	-	62,276
Stationary	2,064	3,593	7,082	13,325	22,244
Stock of agricultural supplies	-	-	-	15,500	39,158
Building materials	-	-	2,659	2,659	2,299
Investment in Bank for Cooperatives	8,800	8,800	8,800	8,800	8,800
Furnitures and fittings	4,200	18,331	64,923	64,771	69,159
Premises	-	312,257	364,418	339,458	323,018
Miscellaneous	3,620	200	-	2,078	8,117
Total	1,574,260	2,870,443	4,349,494	4,834,377	7,422,338

Table III-29 (continued)

LIMITED LIABILITY CREDIT COOPERATIVES

Consolidated Balance Sheets as of March 31, 1961 - March 31, 1965

(unit : baht)

	1961	1962	1963	1964	1965
LIABILITIES					
Paid-up share capital	147,425	344,850	581,851	760,976	1,137,720
Reserve	170	200,246	281,839	355,295	461,087
Share-transfer fund	4	694	2,478	3,563	11,950
Common-good fund	5	1,005	4,683	11,259	14,156
Deposits	-	47,273	214,367	249,725	344,412
Loans from Bank for Cooperatives	1,385,864	2,145,271	3,112,074	3,191,367	4,943,323
Loans from other sources	-	-	-	100,000	200,000
Other liabilities	-	10,000	-	-	819
Profit for year	40,792	121,104	152,303	167,582	308,870
Total	1,574,260	2,870,443	4,349,595	4,839,767	7,422,337

Source: Department of Credit and Marketing Cooperatives.

every year.[83]

As shown by the experience of a number of countries which instituted supervised credit on principles analogous to those in Thailand, this type of credit is best calculated to achieve the objectives of increasing the productivity and income of the farmer, orienting him toward voluntary saving and toward acquisition of productive assets.[84] But it should be borne in mind that even though, in principle, production credit societies are designed to help the small farmer, the tenant farmer, and the poor farmer, in practice they effect principally the more prosperous and the more provident farmer. In the Lampoon society great pride was taken in the fact that the 280 members were carefully selected from many applicants in the amphur. While some tenants and some small farmers did belong to the Lampoon society (near Chiengmai in the north of Thailand),the emphasis was on insuring that the members are sound, reliable, and trustworthy farmers.

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[83] Most loan funds advanced to the production credit societies derived from revolving funds administered jointly by the Department and the Bank for Cooperatives. These funds total about 10 million baht and carry an interest cost to the societies of 3 per cent. Information about production credit societies was obtained from official sources, supplemented by the writer's visit to the Productive Credit Society of Lampoon.

[84] See Horace Belshaw, op. cit., pp. 243ff. The previously cited sources from the Philippines and Taiwan also stress the apparent success of supervised credit.

Bank for Agriculture and Cooperatives

The principles behind the formation and operation of the productive credit societies bode well for their future. The intensified formation and promotion of this type of credit will be one of the chief tasks of the newly formed Bank for Agriculture and Agricultural Cooperatives. The new institution came into operation in the second half of 1966.[85]

The new bank is to be the apex of a unified system of agricultural credit and will absorb the assets and the functions of the Bank for Cooperatives. The unified credit system, however, is not to exclude the participation of private financial institutions in the field of rural credit. In fact, the new bank is to insure coordination among the various government departments and the private institutions which are already in the business of lending to farmers or can be induced to enter it in the future.

The Bank for Agriculture adopts the principles of supervised credit as its operational policy. It proposes to extend credit to individual

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[85] The formation of the Bank for Agriculture and Cooperatives was the chief recommendation of the National Agricultural Credit Board established at the close of 1963 under the chairmanship of the Assistant to the Prime Minister. Its office is at the National Economic Development Board. The Board is, in the meantime, controlling certain minor funds which are being disbursed by various government departments in the form of loans to farmers and is also carrying out a training program for the staff of the nascent bank.

farmers directly but on a limited scale initially. These loans will be made through branches of the bank of which only seven are scheduled for 1966 and which will be established in those areas where cooperatives are weak or non-existent. The bulk of bank funds will, however, be channeled via the existing cooperatives and those which the bank hopes to encourage to form on production society lines. Existing village societies will be encouraged to amalgamate and to consolidate.[86]

The loans made either directly or through cooperatives will be primarily for short- and medium-term duration. The interest rate is to vary between 8 and 12 per cent per annum. The bank calculates a loan fund need, for the first six years of its activities, of some 900 million baht, of which 500 million is to come from budgetary appropriations and the rest from loans contracted outside by the bank.

It is hoped that by the end of 1971 some 11 per cent of farm households will be covered by the bank-directed credit system. In the meantime, great emphasis is being put on training of personnel of competence and integrity necessary to man a large scale system of supervised credit.

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[86] The Ministry of National Development is currently revising the existing law on cooperatives. This should facilitate the task of consolidation and of the merging of village credit societies.

In spite of its relatively modest objectives, the bank may find its goals to be rather difficult to reach even if its training program yields a sufficient number of reasonably competent and well motivated personnel. Thus, it may prove difficult for the new institution to raise 400 million baht of new money in the market, given its interest rate structure. If the farmers will borrow either directly or through their cooperative at 10 per cent, the bank could hardly pay more in the market than 5 or 6 per cent itself.[87] At this rate it may prove well-nigh impossible to secure unsubsidized funds. Furthermore, inasmuch as the bank will still appear to farmers as a government institution, it will encounter many of the same impediments and obstacles to growth which have plagued the existing institutions and which have been discussed above. In particular, the bank will find it hard to resist pressures for loans for longer duration but less productive purposes, not to mention other, less focussed but no less dangerous, pressures.

All the same, the tidying of the present system and the recognition of the need for supervised credit to be administered by viable primary units disposing of skilled personnel is a step in the direction of greater efficiency and vitality of the organized segment of the market for rural credit.

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[87]The Bank's planners are not yet convinced, however, that it would be politic for the new institution to charge higher rates.

Cooperative Movement and Voluntary Savings

As mentioned above, the cooperative movement in Thailand, as well as in other parts of Asia, has inherited the welfare orientation of its parent movement in Europe, which is only being gradually shed in favor of economic efficiency. An important part of this orientation is the belief that it is incumbent upon the credit societies to foster thrift, to inculcate the saving habit, and to reduce the farmers' dependence on private moneylenders.

The record shows that the efforts of the cooperatives to mobilize farmers' voluntary saving have had only very limited success. In Table III-30 the deposits of the cooperative institutions are shown since 1955. Only the village cooperatives and the Bank for Cooperatives show an accumulation of significant sums, but a closer look even at these reveals a less encouraging picture. Thus, the bulk of the deposits at the Bank for Cooperatives are not those of the cooperative societies at all but, rather, those of various official and eleemosynary institutions which, for one reason or another, hold their idle funds at the Bank for Cooperatives.[88] In recent years the annual increase in the members' deposits of the unlimited liability village cooperatives averaged some 2 million baht.

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[88] See Eighteen Years of Progress. At the end of 1964 deposits of cooperatives were only 6.5 million.

Table III-30

Deposits in Cooperative Institutions
(Thousands of baht)

Year	Village Coops	Bank for Cooperatives	District* Banks	Production Credit Societies
1955	9,009		2,119	
1956	13,351	16,000	1,274	
1957	17,342	20,600	1,532	
1958	20,775	25,400	1,506	
1959	24,095	31,100	1,305	
1960	26,906	36,600	1,213	
1961	29,788	40,700	1,473	
1962	32,347	45,600	1,297	47
1963	34,519	46,700	831	214
1964		43,200	638	250
1965			1,267	344

Source: Derived from Table III-21-29.

Note: It is possible to consider the net change in the reserves of the village Cooperatives as part of members deposits inasmuch as the cooperative membership has an equity claim against these reserves. This was the position taken in calculating uses of funds, earlier in this paper.

*In 1963 the name of district banks was changed to Federations of Village Credit Coops. They stopped accepting demand deposits and returned or transferred them to the savings (a/cs). This is the reason why deposits were reduced. Now the federations encourage more savings among farmers.

With aggregate membership of these cooperatives of some 175.000, this comes to some 12 baht of additional savings per member per year.

One reason for the poor performance of the cooperatives in mobilizing rural saving, apart from the basic one of low rural incomes, is the lack of attraction of the saving instruments proffered by them. With very few exceptions, the rates of interests offered are below those available either at commercial banks or at specialized saving institutions, such as the Government Saving Bank.[89]

It would appear that such saving deposits as the cooperatives did manage to accumulate in some 50 years of operation are due to the compulsory features inherent in the cooperative credit system. Thus, members of unlimited liability cooperatives have to "save" a minimum of 50 baht a year for 10 years. Members of the production credit societies are compelled to hold shares in the limited liability society equal to 5 per cent of the value of the loan and so on.[90]

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[89] Local cooperatives pay a maximum of 6 per cent for 12 months' deposits (Bank for Cooperatives pays 7 per cent) compared to 7 per cent payable by commercial banks. Cooperatives pay 4 per cent on current savings deposits which occasionally proves attractive but, more often than not, to non-members of the cooperatives. However, these so-called current deposits are in reality limited withdrawal deposits usually confined to four withdrawals a month. The Government Savings Bank can pay up to 5 per cent on similar facilities.

[90] Cooperatives pay 5 per cent per annum on these compulsory deposits.

The rather dismal record cannot be attributed entirely to lack of effort on the part of cooperative leadership or to a lackadaisical attitude of its official supervisors. For example, the two district federations have pioneered in the use of mobile vans which are sent into the villages and actively seek deposits from members. Yet, as seen in Table III-30, these federations have actually been losing deposits for a number of years. Nor can it be maintained that the task of garnering rural savings is a hopeless one. In some respects the Government Savings Bank has been moderately successful in the countryside. In Taiwan, from 1953 to 1961, members' deposits at farm associations increased nearly eightfold.[91] Given proper incentives and proper organizational efforts, it should be possible both to increase the volume of savings from the farm households and to channel it into developmental direction. The real question is whether cooperative institutions are necessarily the most efficient institutions to undertake that task. It would seem that implementing a program of supervised credit, with its high degree of technical overseeing required and with the requisite integration with marketing and provision of inputs, would tax to the utmost the capabilities of the cooperatives. There seems to be little a priori reason why they should be further encumbered with the administration of a sophisticated program of mobilization of voluntary saving from countryside. Yet such

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[91] F. H. King, op. cit., p. 22.

a program needs to be instituted if it is to bear significant results. It may perhaps be best left to specialized institutions, properly strengthened and reinforced. The main contribution of cooperative credit to rural saving should come through programs which will convince the farmer that increased effort and higher production lead to higher income and eventually higher consumption, in that sequential order.[92]

Government Departments and Rural Credit

It appears to be almost impossible to obtain a clear picture of the role of government departments in agricultural credit. Data relating to past operations are incomplete and inaccurate.[93] There is no coherent system of accounts, no demarcation of responsibility, and only occasional traces of audit. Inasmuch as lending activities of the several government departments have developed in response to varied pressures and stimuli, no single authority took it upon itself to trace these activities over time or to evaluate their effects.

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[92] The statement in the text is clearly a value judgement. But in the Thai setting, where well-trained personnel willing and able to operate in remote rural areas are a scarce resource, there seems to be little reason for tolerating duplication and wasteful competition between, say, cooperatives and a local branch of the Government Savings Bank.

[93] This section relies heavily on National Economic Development Board, Policy and Principles of National Agricultural Credit and Draft Act of the Bank of Agriculture and Cooperatives (Bangkok, 1965), informal translation, mimeo document in Thai.

Some exceptions do exist, however; and from fragmentary evidence gathered elsewhere, as well as from the few reliable sources in existence, it is possible to piece together a somewhat uneven pattern of activities of government agencies in the rural credit field.

In the Ministry of Agriculture various circulating funds were set up from time to time to make loans either to encourage a certain type of cultivation, to introduce a new crop, or to make possible the purchase of a specific kind of output. Thus some 16 million baht was advanced to farmers between 1952 and 1954 to propagate new varieties of rice. Some 4 million baht was advanced in the same period for the purchase of fertilizer and about 7 million baht to buy farm equipment. Somewhat earlier, a fund of some 15.4 million was lent for various inputs under a project which shows about a 60 per cent ratio of bad debts. Other circulating funds included slightly over 3 million lent to rubber cultivators and about 2 million to cotton growers. Some 10 million was lent to fishermen and another 20 million to livestock breeders in the late 1950s and early 1960s. Again, the repayment record was not good, and the entire financial record remains somewhat murky.

In the Ministry of the Interior loans falling roughly under the heading of agricultural credit were made by the Departments of Administration, Social Welfare, and Community Development. No details are available on the operations of the Department of Administration except

for the prevailing impression that a good deal of money was lost on various schemes to promote hog raising and livestock marketing. The Social Welfare Department disbursed some 16 million baht in loan funds to some 40,000 families in the 10-year period ending in 1963. Less than 4 million baht has been repaid to date. Of similar welfare nature were the 4 million baht disbursed by the Community Development Revolving Fund.

Unlike the operations of the Agriculture and Interior Ministries, the loan operations of the Ministry of National Development were made primarily to the cooperative institutions. In addition to the Ministry's interest in cooperative credit, touched on in the preceding pages, it has also made loans to paddy marketing cooperatives out of a revolving fund of some 38 million baht. The 110 paddy marketing societies incurred a loss of more than 8 million baht by the close of 1963. Other types of cooperatives borrowed some 36 million baht. A certain proportion of these loans was counted as a loss as a number of cooperatives, unable to repay, were liquidated.

Commercial Banks and Agricultural Credit

With the exception of some attempts of the Siam City Bank in the past and cautious explorations of the Bangkok Bank of Commerce at present, the only commercial bank in Thailand actively engaged in direct lending to farmers is the Bangkok Bank Ltd., the largest commercial bank of the Kingdom.

Bangkok Bank, Ltd., has entered the field of agricultural credit relatively recently, in January 1963, in part to establish its influence more firmly in the countryside. It had somewhat neglected the countryside in the past, concentrating on branches in the urban centers and abroad.

Two kinds of credit are extended. One, individual loans to the more established and prosperous farmers, is of the standard type. The prospective borrower makes an application and offers a collateral, usually in the form of a registered land mortgage. The application is reviewed by the branch manager, but the final approval must come from the head office. The rate of interest ranges from 12 per cent, for production loans, to 15 per cent for longer term loans for the purpose of settling debts. Intermediate rates are charged for loans ranging from one to five years for such purposes as purchase of heavy machinery and construction of warehouses. There is no set limit on the amount of the loan.

The other kind of loan is of special interest because it combines some of the most promising features of agricultural credit under the aegis of a profit-making organization. This is the group loan scheme of supervised credit for production purposes. The program of the Bangkok Bank, Ltd., group loans derives from the experience of the Farm Credit Administration in the U. S. A., from the successful experiments with supervised credit in a number of Latin American Countries and, finally, from the pioneering efforts of the production credit societies in Thailand

itself.[94]

Under the scheme, loans are made both for short term and long term to groups of farmers, of no less than 5 and no more than 20 members, residing in the same village or hamlet. Up to 3,000 baht can be borrowed by each of the group's members without collateral other than the security of the crop to be produced and the joint liability of the entire group, limited to the amount of the debt outstanding. The rates of interest are similar to those under the individual loan scheme.[95]

Unlike the individual loans, the authority to grant the amounts requested by the borrowers is vested in the manager, assisted by the agricultural credit officer of the branch. The latter plays a key role in the implementation of the entire program. It is he who will make the preliminary survey, who will advise the group on the best means of using

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[94] Information about the operation of the Bangkok Bank, Ltd., credit program in agriculture was obtained through direct contact with the Bank's officers and from field trips to the area of its most extensive operations. See also Bangkok Bank, Ltd., Agricultural Credit (November 1964). The United States Operation Mission to Thailand has long attempted to orient the granting of credit to farmers along the lines of supervised credit. See John L. Wann, John W. Sims and Fulton Want (eds.), A Report on Agricultural Credit: Cooperative Organization, Management and Administrative and Agricultural Marketing (Bangkok: Thai-American Audiovisual Service, November 1959); and W. J. Maddock, Agricultural Credit Thailand 1964 (August 1964), mimeo.

[95] In addition to the interest payable to the bank, the group members undertake to pay an additional 1 per cent per annum to cover administrative costs of the group, mainly the costs of travel of the group's selected representatives to the branch office of the bank for meetings, conferences, and so on.

the loan proceeds, and who will offer technical assistance throughout the life of the loan, which is paid out in installments. These agricultural credit officers are graduates of the Kasetsart Univeristy (Agricultural University) and are specially trained to carry out supervisory functions.

An interesting feature of the group loan program is its integration, whenever possible, with both marketing and the provision of inputs. Thus, in the areas where the crop pattern allows it, the bank will arrange for millers and processors to buy the crop from its borrowers at a price guaranteed not to be below the market. The loan account is then automatically credited by the amount of the sale. With respect to inputs, the bank will provide them directly whenever the purpose of the loan calls for such inputs as are handled by distributors who are also clients of the bank.[96]

Even though the program is still in its early stages, it bears

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[96] The bank claims that this arrangement enables the group to enjoy extra benefits in that a part of the dealer's commission is passed on to the farmer. For example, the usual dealer commission on a Fordson tractor is 7.5 per cent. Under an arrangement with the group wishing to borrow for a tractor, the dealer will get only 2.5 per cent commission but will still service the tractor. The group will benefit to the extent of getting a tractor, including servicing, for 5 per cent less than the retail price. Still, the borrower's choice of inputs is somewhat limited as a result of such an arrangement. It is interesting that some 73 per cent of all group loans have been allegedly used to secure labor inputs. This is a very high proportion, indeed, and a suspicious mind would seek some connection between this high percentage and the fact that labor inputs are not yet provided by the Bangkok Bank, Ltd.

the mark of success. Strangely enough, it is the group program which has proved the more rewarding to the Bangkok Bank, and there is a possibility that the program of individual loans will be discontinued.

Table III-31 summarizes the operations of the group loan program. Even though the scope of the program is confined to areas where there are branches of the Bangkok Bank and so far extends only into five provinces, the annual value of loans has increased nearly sevenfold in the space of only three years. Even so, the limiting factors have proved to be the shortage of qualified field personnel and the sheer inability of the overworked credit officers to visit those villages where there appears to be some interest in forming a loan group. As a matter of fact, the bank appears to do very little proselyting, and yet word of mouth spreads so effectively that in the Chiengmai province alone there are apparently some 100 tentative loan groups formed, which the branch officers had no time even to interview initially.

Equally encouraging is the excellent record of repayments shown by the groups. Some 96 per cent of all loans are paid on or around maturity and, so far, no group loan has remained unpaid for longer than four months. This testifies to the importance of proper technical advice combined with continuous supervision but also to the heavy drain on administrative and technical personnel required under a successful supervised group program.

Table III-31

Bangkok Bank
Summary of Operations of Group Loans

Year	1963	1964	1965
Number of Groups	57	224	776
Number of Members	851	3,091	8,122
Value of Loans*	2,338,482	4,746,096	15,554,300

Source: Bangkok Bank Ltd., (Courtesy of Chusak Himathongkom, Chief, Agricultural Credit Division).

*Amounts outstanding at end of year.

The officers of the Bangkok Bank, Ltd., estimate that the costs of running the group loan program amount to 4 or 5 per cent of the value of loans. This seems to be a very high percentage, but it would seem that a substantial proportion of these expenses may be invariant with respect to volume of loans. Be that as it may, the bank admits to making a modest profit on the operation.

The success of the Bangkok Bank, Ltd., in the field of supervised group credit should be viewed in the proper perspective. Having the field to itself, and disposing of great resources, the Bangkok Bank, Ltd., could, as it were, skim off the cream of the business. On the one hand, it could select its borrowers from those areas which present the best prospects and, on the other hand, it had first pick at the requisite personnel. Were the program to be expanded substantially, with participation of other commercial banks, with nationwide coverage, and with a vastly increased volume of loans, serious problems would arise both with respect to risks and with respect to the availability of personnel. All the same, the experience of the Bangkok Bank, Ltd., has demonstrated that it is possible for a commercial bank to operate successfully in the field of agricultural credit.[97]

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[97] This has, of course, been demonstrated in other countries. While the experience of Australia and New Zealand may be of little relevance for Thailand, that of the Philippines should be instructive. See Jose E. Desiderio, "Rural Banking in the Philippines," The Philippine Economic Bulletin (November-December, 1963).

Implications for Developmental Planning

The preceding survey of the organized market for agricultural credit shows that this market is dominated by cooperative institutions which only recently and haltingly have begun to develop techniques and methods which may reduce, sometime in the future, farmers' dependence on the facilities available in the unorganized market. Even with the promise implicit in the formation of the new Bank for Agriculture and Cooperatives with its emphasis on supervised credit and administrative efficiency, it is not likely that much of a dent will be made in the unorganized market. Yet, as argued before, that market cannot be relied on to nurture a dynamic kind of credit designed to lift the farmer's income to a higher level, to provide him with incentives toward greater effort and productivity, and to show him the connection between forbearance for the present and a higher standard of libing in the future.

It would seem that in order for the institutions under public control and scrutiny to encroach significantly on the extent that the unorganized markets dominate rural credit, recourse must be had to financial entities not yet, to any significant degree, involved in that market. In Thailand it is the commercial banks which could provide the type of finance which the moneylender is either unwilling or incapable of providing.

Tha Bangkok Bank, Ltd., which has successfully promoted the very kind of supervised group credit which is consonant with developmental

objectives, is anxious to expand its operations to other provinces where, as yet, it has not established its branches. The effort to supplement the activities of the cooperatives cannot and should not be confined to one commercial bank, however aggressive and progressive that bank might be. On the other hand, other commercial banks show little desire or interest to enter rural credit. With one or two exceptions, the commercial banks incorporated in Thailand (and foreign chartered banks are probably not likely to enter rural credit anyway) prefer to steer clear of direct lending to farmers, citing lack of branches, lack of trained personnel, or lack of capital as their reason. Underlying all these there is, of course, the fact that banking is generally profitable in Thailand and that there are many attractive opportunities outside rural credit, opportunities with which the commercial bankers are much more familiar by training and experience.[98]

The obstacles to the entry of commercial banks into the field of rural credit must be overcome, but they are not likely to be overcome by a process of suasion alone. To insure commercial banks active participation, the development planner could consider a system of rewards

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[98]The newly formed Krung Tai Bank is committed to enter the field of rural credit. This bank was formed from a merger of two government-sponsored banks, and its management and control remains in official hands. The new bank has a large number of branches in the provinces. See Chapter V.

and incentives more or less along the following lines:

The Bank of Thailand, one of the few central banking institutions in the developing countries not already actively engaged in agricultural credit, would announce a policy of support of commercial banking operations in rural areas. First, however, the Bank of Thailand may find it necessary to nudge the banks in that direction by increasing the required reserves against deposits from the present level of 6 per cent to, say, 10 per cent but will allow the extra 4 per cent to be kept in the form of agricultural paper. The Bank of Thailand would proclaim its readiness to discount such paper at 5 per cent, provided the commercial bank rate did not exceed 15 per cent.

With the current level of deposits at some 12 billion baht, a 4 per cent increase in reserve requirement would mean that the commercial banks would need to provide another 480 million. However, the banks as a whole have more than 300 million of excess reserves, not counting cash resources outside the Bank of Thailand. Given the generous spread which the Bank of Thailand would allow in its rediscounting of agricultural paper, the commercial banks should not suffer undue hardships and may even find the business of rural lending a profitable line of endeavor.[99]

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[99] It is quite true that while commercial banks as a group have large excess reserves, individual banks may be fully lent out or otherwise unable to conform to the new ruling. In any event, the percentages and figures given in the text can be modified in the light of circumtances.

A 10 per cent spread between the commercial bank rate and the Bank of Thailand rate should provide a sufficient margin for risk, for heavy initial administrative expenses, and for lack of experience. Equally important will be the Bank of Thailand determination that its new line of rediscounting does not get bogged down in red tape, administrative delays, and the sort of requirements which, while in principle are sound, in practice have the effect of grinding the entire scheme to a halt. Subject to general rules of eligibility, which should be few in number and clear in intent, the Bank of Thailand should rediscount paper presented to it without any further credit investigation, but subject to post-audit and severe penalties for willful misrepresentation.[100]

It is possible that even with the crisp carrot dangling from the stick, the commercial banks will find it difficult to recruit and train technically qualified and properly motivated personnel. The problem is indeed a major one. In order to supervise and administer a billion baht worth of loans per annum (see below), some 2,000 men will have to be found. Of course, not all of them will have to become available at once. It would be unrealistic to expect the volume of agricultural loans handled by commercial banks to reach the goal of one billion baht in a year or two. This will take several years. Assuming one trained supervisor's ability to handle between 15 or 20 groups of rural borrowers per year, the task

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[100] See Chapter VI for a discussion of the Bank of Thailand rediscounting operations.

of providing supervisors should not be an impossible one. Even so, the initial cost of recruitment and training may prove prohibitive to some of the smaller banks, and there may be real difficulty in locating suitable candidates. At the same time, there would be great merit in having the training conducted on fairly standard lines, if only to facilitate the task of passing on agricultural paper's eligibility. It would seem that the primary responsibility for such training should be assumed by the newly-formed Bank for Agriculture and Cooperatives. This institution has the status and the resources to coordinate a vast training program with the Universities and may well find that the outlay on the training program yields greater returns than its direct lending activities.

The entry of the commercial banks with their more than 400 branches into rural credit should substantially change the existing structure of the market for lendable funds in agriculture. An average yearly balance of agricultural paper of 400 million baht implies at least one billion baht of loans annually. Even though much of this accommodation will be additive, the respective shares of the market of the organized and unorganized lenders will shift in favor of the former.[101]

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[101] In 1967, as part of the Accelerated Rural Development (ARD) Program in the Northeast of Thailand a number of commercial banks in that region were induced to participate in a group loan program for farmers. It is too early to judge the results of this effort but it contains one feature which, prima facie, does not promise great efficiency. Under the ARD plan the participating banks are guaranteed against losses for either 50 per cent of the total loss or (under special circumstances) for 100 per cent of the loss. Unlike the guarantee program, the rediscount feature

The proposal, as outlined above, is designed to increase directly the share of organized markets in financing rural households. But, as the discussion of the unorganized markets has suggested, there appears to be scope for increasing the proportion of loans made by organized markets indirectly by absorbing certain of the activities of the unorganized markets in agriculture. One line of approach would be to draw certain moneylenders into the institutionalized orbit. One reason for the high rates of interest charged by moneylenders is their inability to replenish their working capital at certain times of the year plus the fact that their limited funds are employed only for a portion of the year. It might be worthwhile to develop some mechanism whereby moneylenders could discount with commercial banks or public institutions certain kinds of paper. Such an arrangement could be a prelude to gradual integration of at least a segment of the moneylending profession into the organized network.[102] To

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[101] (continued)
(discussed in the text) has a built-in efficiency incentive inasmuch as the banks operating on a fixed "spread" are interested in: a) making loans more cheaply; b) making them for productive purposes; c) underwriting non-repayment.

[102] An interesting proposal on similar lines has been made in connection with the Muda Project in Malaysia in 1967. Under the proposed "agricultural bills scheme" farmers IOU's would be endorsed by the lenders and discounted by commercial banks and rediscounted by the Central Bank.

some extent, such integration has taken, and is taking, place in most of the developing countries, certainly in Thailand. But the entry of the commercial banks into the field of agricultural credit on a large scale should provide many opportunities to speed up this juncture, the Thai commercial banking system, with its complex of branches, agencies and correspondents, appears singularly well adapted to this task.[103]

The measures so far discussed aim at channeling a greater proportion, as well as a greater absolute amount, of agricultural loans into productive uses. But it must be recognized that there will continue to exist a demand for loans for consumption purposes which cannot be dealt with along sound "banking" principles. No doubt, a certain proportion of such loans may be considered undesirable on social grounds, and some sort of campaign to eliminate the demand for them might well be instituted. But it would be naive to suppose that such a campaign will be entirely successful. The fact is that, while it is important to separate the demand for production loans from the demand for consumption loans, some device must be found to meet the latter demand if an even greater burden is not to be borne by those least able to bear it. Again, while no detailed proposals will be made here, there appear to be two promising avenues of approach to the problem. One of them would actually attempt to draw the poor, improvident farmer into the vortex of productive activity, in the belief that once

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[103]The system of branches, agencies, and correspondents of the Thai commercial banks will be discussed more fully in Chapter V.

exposed and immersed in such activity he will actually have less need, as well as less desire, to borrow for non-productive purposes. One possibility would be to set up a pilot system of communal credit run on the lines of a corporate undertaking for a specific project. Say a storage silo is considered to be a worthwhile project. A group of villagers might incorporate for the specific purpose of constructing, managing, and maintaining the silo and exploiting it for commercial uses. The group acquires an equity in the undertaking in proportion to the resources it contributes, with the important proviso, however, that the poorer farmers can contribute labor, if nothing else. The value of such labor would be expressed as an equity in the undertaking. The group obtains a loan from an institution in the organized market, covered by a joint guarantee of the group.

The other avenue of approach would be to set up institutions dealing explicitly and exclusively with consumption loans, loans for emergencies, and similar demands. It would seem that rural pawnshops could serve in this capacity,[104] and such pawnshops could be run either by the cooperatives or by licensed pawnbrokers.

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[104] For some evidence that rural pawnshops can, in fact, operate successfully, see United Nations, State Pawnshops in Indonesia, (E/CN. 11/I&T/WP. 1/13) and United Nations, Pawnshops in the Associated States of Indochina, (E/CN. 11/I&T/WP. 1/20)

It is not pretended here that these suggestions will be easy to put into operation. No panaceas and no easy and painless solutions exist to the manifold problems of rural finance.

Above all, it cannot be overemphasized that credit cannot operate in a vacuum. The best thought-out and the most soundly implemented credit system will do little for economic development if the farmer is left to the vagaries of the weather and of the market. He cannot be left to fend for himself if one or the other fails him in spite of his best efforts, for in that case he will cease to care or to respond to stimuli and incentives. It is incumbent on the development planner to insure, as much as possible, that this does not happen.

CHAPTER IV

COMMERCIAL BANKING

Commercial banks have a threefold function to perform in the intermediation process. First of all, they borrow surpluses of the household units in exchange for the indirect securities they issue, i.e., demand and time deposits. Second, they transmit the funds so borrowed to deficit spending units in exchange for direct securities of these units. Finally, commercial banks facilitate the adjustment of portfolios of spending units by enabling them to hold the desired proportion of direct and indirect securities.[1]

In Thailand, it would appear that the relative importance of commercial banking in the organized financial market structure is greater than in most countries at a similar stage of development. There are two reasons for this. First, Thai banks have experienced a remarkable record of growth, particularly in the last 10 years.

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[1]Direct securities are those issued by the spending units themselves, such as bonds, accounts payable, and bills. Indirect securities are those which represent claims against financial intermediaries, such as time and demand deposits, insurance claims, and unit trust certificates. See J. G. Gurley and E. S. Shaw, "Financial Aspects of Economic Development," American Economic Review (September, 1955), pp. 519-20.

Second, and perhaps more important, Thailand is singularly devoid of the many semi-official financial intermediaries which abound in several other countries. Thai authorities, perhaps wisely, have refrained from setting up and sponsoring a plethora of institutions whose contribution to economic growth is problematical, whose bewildering variety of instruments often confuse both savers and investors, and whose staffs constitute a real drain on the meager administrative and managerial resources of the developing countries. Moreover, for historical and ideological reasons, Thailand has been able to withstand the pressure for such measures as compulsory insurance and industrial pension funds, which elsewhere constitute a substantial proportion of total financial securities circulating within the economy.

The predominance of commercial banking in the financial structure of Thailand is not likely to diminish in the near future. In preparing financial estimates for the Second Five Year Plan, the National Economic Development Board assumes a total supply of investible funds from the private sector of nearly 70 billion baht over the period 1966-71. Of this total, the financial institutions as a whole are expected to supply 9.1 billion, the share of the commercial banks being 7.1 billion, or nearly two-thirds. Even this probably underestimates the relative importance of commercial banking inasmuch as the estimates for investible funds to be provided by such institutions as the IFCT and the newly formed

Bank for Agriculture and Cooperatives, appear to be overly generous.[2]

The Growth of Commercial Banking in Thailand

It is possible to distinguish three significant phases in the history of commercial banking in Thailand. The initial phase, from the establishment of the first bank in 1888 (a branch of the Hongkong and Shanghai Banking Corporation) up to World War II, was dominated by branches of large foreign banks engaged mainly in financing export and import bills in the European trade, which itself was largely controlled by British, Danish, French, and German firms operating out of Bangkok. During this phase most local banks were Chinese and their primary business was to transmit remittances to the mainland. In the second phase, these Chinese remittance banks were joined by banks established by native entrepreneurs, very frequently merchants, traders, and exporters who were enticed into the banking business by the large profits to be made in financing the

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[2]National Economic Development Board, "The Second Five Year Plan - Preliminary Draft," (Bangkok: Government of Thailand, 1966), Chapter 5 (mimeographed in Thai). At the same time, while the NEDB computations include financial institutions such as Commercial banks, life insurance companies, Small Industry Fund, IFCT, Bank for Agriculture, and the Stock Exchange, they leave out pawnshops and pension funds whose importance is comparable to that of, say, the Bangkok Stock Exchange. The quantitative situation is further confused by the fact, that in national income estimated (prepared by a different division within NEDB), value added in finance includes pawnshops and money changers but, as far as can be ascertained, excludes the Stock Exchange and the IFCT (Industrial Finance Corporation of Thailand). For further details see Chapter II.

booming postwar export trade. The entry of native entrepreneurs into commercial banking was facilitated by three developments: 1) the changing pattern of foreign trade, with its focus shifting away from Europe towards neighboring countries and Japan; 2) the shutdown during World War II of the Thai branches of the large European banks; and 3) the requirement that export proceeds be sold to the Bank of Thailand. It was this last requirement which has enabled the small and inexperienced bankers to grow and expand, inasmuch as they, by guaranteeing their customers conformance with the law, have been able to charge a handsome commission on the export proceeds.

The last phase in the development of Thai commercial banking, and the one that will receive most attention in the succeeding pages, may be termed the "modern" phase. During this phase, commercial banks incorporated in Thailand forged far ahead of the branches of foreign banks in volume of deposits, capital, and accommodation to business. They began to establish numerous branches in the country and to expand their activities beyond making remittances and financing foreign trade. Most important, they started to be integrated into the monetary system of the country, principally through a series of regulatory measures which culminated in the Commercial Banking Act of 1962. While it is difficult to date precisely the onset of the modern phase, it may be convenient to regard the year 1955 as a demarkation point inasmuch as the period of multiple exchange rates ended that year. It was, however, 1962, which really marked the beginning of

commercial banking in Thailand along lines comparable with modern banks elsewhere.[3]

Of the 29 commercial banks currently doing business in Thailand, 13 are incorporated abroad and 16 in Thailand. Two of those incorporated in Thailand, the Agricultural Bank and the Provincial Bank, have recently been merged under the name of Krung Thai Bank which opened for business in March of 1966. As seen in Table IV-1, only four of the 16 banks incorporated in Thailand received their charters prior to the Second World War. Of these four, one, the Wang Lee Chan Bank, is not a commercial bank in the full sense of the term but essentially a family concern not generally dealing with the public.[4]

The historical background of Thai commercial banking has left three residual strains which are of interest in the analysis of the current scene. The first of these is that the former great prestige and power of British

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[3]For a full account of the early history and development of Thai Banking, see Paul Sithi-Amnuai, Banking and Finance in Thailand: A Study of the Commercial System 1888-1963 (Bangkok: Thai Watana Panich, 1964), and the sources cited therein, particularly S. Y. Lee, "Currency, Banking and Foreign Exchange of Thailand," Far East Economic Review (October 1959); and Ravi Amatayakul and S. A. Pandit, "Financial Institutions in Thailand," IMF Staff Papers (December, 1961).

[4]C. Y. Lee, op. cit. Throughout the present paper, much of the information has been obtained from private and unpublished, rather than printed sources. Statistical information has been provided by the Bank of Thailand under a special arrangement whereby an official of the Bank collaborated with the author in developing data from confidential sources without exposing or compromising these sources. Even when the information and data cited in this paper were available to the public at large, they had frequently been modified for the purposes of this study. For that reason, unless otherwise indicated, statistical tables here included are to be taken as derived from information provided by the Bank of Thailand.

Table IV-1

THAI COMMERCIAL BANKS - DATES OF OPENING OF MAIN OFFICES AND BRANCHES

	Prior to 1955	1955	1956	1957	1958	1959	1960	1961	1962	1963	1964	1965
Siam Commercial Bank (1906)	6	2	1	1	2	1	-	-	5	-	-	18
Wang Lee Chan Bank (1933)	1	-	-	-	-	-	-	-	-	-	-	1
Thai Development Bank (1934)	1	-	-	-	-	-	29	15	2	-	-	47
Bank of Asia (1936)	7	-	-	-	-	-	-	2	-	-	-	9
The Siam City Bank (1941)	18	1	9	12	18	2	-	-	4	-	1	63
The Provincial Bank (1942)	7	1	2	4	7	-	-	-	-	-	1	22
Bangkok Bank of Commerce (1944)	1	1	1	10	21	12	11	12	-	6	1	76
Bangkok Bank (1944)	7	2	1	3	4	2	1	5	10	5	9	49
Bank of Ayudhaya (1945)	7	-	2	-	4	9	-	4	-	3	2	31
The Thai Farmers Bank (1945)	13	-	6	4	4	3	-	3	4	3	8	48
Laem Thong Bank (1948)	1	-	-	-	-	1	-	-	-	-	-	2
Union Bank of Bangkok (1949)	2	-	2	1	1	2	-	-	-	-	1	9
Thai Dhanu Bank (1949)	1	-	-	1	1	1	-	1	-	-	1	6
The Agricultural Bank (1950)	15	5	5	2	22	-	2	3	-	4	2	60
The Metropolitan Bank (1950)	1	-	-	-	4	1	-	1	-	1	3	11
The Thai Military Bank (1957)	-	-	-	1	-	-	-	-	-	1	-	2
Offices of Foreign Banks	12	3	1	1	-	-	1	-	1	-	1	20
Total	100	15	30	40	88	34	44	46	26	23	30	474

Note: First column indicates date of opening of the headquarters of each bank with rows indicating number of branches opened since.

Source: Unless otherwise indicated the data in this and other tables in this chapter are derived from information obtained from the Bank of Thailand, either privately or from published statistics.

banks still influence the attitudes and practices of Thai Bankers, particularly those in positions of official authority.[5] Second, and perhaps related to this, is that the compradore system, though now somewhat on the decline, still persists and seems to have taken on forms which are at variance with its original rationale. Initially, the managers of local branches of foreign banks had to rely on persons conversant with local conditions and the status of many of their clients when conducting their daily business. To that end, they appointed a special agent, the compradore, whose functions were analogous to that of a London acceptance house. The compradore, frequently operating on a commission, in effect assumed the risk of a loan made to a borrower whose credit rating was unknown to the bank manager and whose books, or what passed for them, were incomprehensible to him. It is somewhat surprising to note that while foreign banks tend to rely less and less on the traditional compradore, or else to replace him with a salaried "Chinese manager," many locally chartered banks still use the compradore, though not necessarily for the purposes for which he was originally intended.

A third residual strain, also stemming from the way in which commercial banking has developed in Thailand over the years, is the

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[5]Not only was the Hongkong & Shanghai the first Bank chartered in the country, but it and the Chartered Bank were two of the three banks which up to 1903 could issue notes. The Chartered Bank was the one where, for a time, both the Royal Family and the Royal Treasury had open accounts. Up to at least 1941, all the principal financial advisers to the Kingdom were British. Until very recently, the leading officials in the field of finance and banking tended to be trained in England.

predominance of foreign trade financing. To an extent perhaps greater than a scrutiny of official data would indicate, Thai banks are, with few exceptions, mainly interested in accommodating exporters and importers and/or those closely connected with them. In the past, of course, this was the commercial bank's raison d'etre. It is much less so at present, but habits and attitudes persist, and skills and experience nurtured in a particular tradition need time and careful tending before they can be fruitfully transferred elsewhere.[6]

Assets and Liabilities of Commercial Banks

Table IV-2 presents a summary account of the principal balance sheet items of all the commercial banks in Thailand for 11 calendar years, beginning with 1955 and ending with 1965. It should be borne in mind that the composition of the banks has changed slightly during the years, with new banks being chartered and old banks merging or changing their names. More significant is the fact that the accounting procedures and practices have been changed, mainly as a result of the passage of the Commercial Banking Act of 1962. In particular, the data on demand and time deposits prior to May 1962, are not strictly comparable to those following that date. The great increase shown in time deposits after 1962 must be attributed, in part, to the reclassification of accounts which has taken place in

[6]This point will be elaborated later.

Table IV-2

MAIN ASSETS AND LIABILITIES OF COMMERCIAL BANKS[1]
(Millions of Baht)

End of Period	Deposits[2]				Cash on Hand and Balance with Bank of Thailand		Liquid Assets[4]		Loans, Overdrafts and Discounts		Risk Assets[5]	Capital Account[6]	
Dec.	Demand	Time	Others[3]	Total	Amount	As % of D & T Deposits	Amount	As % of Total Deposits	Amount	As % of Total Deposits		Amount	As % of Risk Assets
1955	1,967.3	243.6	-	2,210.9	443.6	20.06	756.1	34.20	2,391.4	108.16	3,034.0	455.0	15.00
1956	2,180.7	371.0	315.3	2,867.0	502.0	19.67	883.0	30.80	2,839.3	99.03	3,210.1	458.7	14.29
1957	2,491.9	452.2	431.4	3,375.5	564.5	19.17	1,024.9	30.36	3,339.0	98.92	3,749.2	502.9	13.41
1958	2,886.7	649.1	423.8	3,959.6	538.7	15.24	947.8	23.94	3,977.7	100.46	4,631.2	518.3	11.19
1959	3,153.7	980.4	332.0	4,466.1	676.4	16.36	1,073.6	24.04	4,488.4	100.50	5,077.4	514.8	10.14
1960	3,840.5	1,223.6	385.4	5,449.5	743.5	14.68	1,333.9	24.48	5,397.3	99.04	6,374.8	561.0	8.80
1961	4,313.4	1,690.6	504.6	6,508.6	876.3	14.60	1,607.8	24.70	6,333.3	97.31	7,527.7	614.9	8.17
1962	4,233.8	3,347.0	226.3	7,807.1	1,004.4	13.25	2,174.6	27.85	7,459.3	95.55	8,681.6	813.3	9.37
1963	5,025.4	4,514.3	243.2	9,782.9	1,284.1	13.46	3,018.5	30.85	8,712.6	89.06	9,532.4	804.6	8.44
1964	5,615.5	5,614.3	232.3	11,462.1	1,295.6	11.54	3,187.6	27.81	10,546.3	92.01	11,274.3	1,085.8	9.63
1965	6,209.4	6,935.7	300.0	13,445.1	1,325.1	10.08	3,434.9	25.55	12,747.5	94.81	14,000.0	1,400.0	10.00

[1] Excluding those of Thai bank branches abroad, but data on risk assets and capital account as from May, 1962, were included.

[2] Excluding foreign currency deposits and inter-bank deposits.

[3] Comprising certified cheques, cashiers' cheques, marginal deposits, etc.

Source: See Table IV-1.

[4] Comprising cash on hand, balances at the Bank of Thailand, balances at banks abroad, gold and government securities other than those pledged or deposited as guarantee with the Bank of Thailand.

[5] From May 1962, as defined in the Commercial Banking Act, B.E. 2505.

[6] From May 1962, comprising paid-up capital, statutory reserve, other reserves, net profit after distribution and capital funds of foreign bank branches.

connection with the implementation of the Commercial Banking Act.[7] At the end of 1965, time deposits actually exceeded the demand deposits of commercial banks, a rather unusual situation when compared with the distribution of banking assets elsewhere.

It is interesting to note that at the end of 1965, the ratio of cash on hand and balances with the Bank of Thailand to total deposits was half as large as at the end of 1955. The ratio of liquid assets (which comprise, in addition, balances at foreign banks, and gold and government securities other than those pledged with the central bank) to deposits, however, had declined only slightly, and was actually higher at the end of 1965 than at the end of 1959, unlike the former ratio which showed a continuous decline during the period.[8]

While a fuller analysis of the behavior and significance of various balance sheet items of Thai commercial banks will be made in subsequent sections of this chapter, Table IV-2 attracts attention to two other ratios which merit immediate comment. The first of these is the ratio of loans,

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[7]The spectacular increase in time deposits since 1962 must, however, be ascribed to other causes as well. This matter will receive attention later. See pp. 23ff.

[8]It should be noted that the ratio of cash and balances to deposits at the central bank is not the legal reserve ratio familiar to students of the fractional reserve systems. In Thailand, the commercial banks can keep a part of their legal reserves in the form of government securities. Again, a fuller discussion of the commercial banks reserve position will be found on pp. 37ff.

overdrafts, and discounts to total deposits. The other is the ratio of capital account to "risk assets."

At the end of 1965, the former ratio stood at nearly 95 per cent and for most of the period surveyed has oscillated around 100 per cent, exceeding it in three out of the 11 years. Prima facie, this ratio appears abnormally high when compared to that of American banks, for example, which hold to a ratio of loans, etc., to deposits of some 70 per cent as a prudent maximum.[9] But such a direct comparison may be misleading. In the first place, Thai banks, unlike American banks, lend a good proportion of their total accommodations in the form of overdrafts. A customer will obtain a line of credit against which he will overdraft. The difference between the line of credit and the actual overdraft will not be shown as a deposit, as is the practice in the United States where "every loan creates a deposit".[10] This tends to understate the denominator of the ratio.

In the second place, Thai banks can apparently maintain what to an American banker would be a dangerously illiquid situation because they can

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[9] For example, at the end of 1963, the ratio of commercial bank loans to demand and time deposits combined, was slightly over 60 per cent. This ratio has varied but slightly since 1960. See, Federal Reserve Bulletin (October 1964), p. 1288.

[10] There is an interesting provision in the Commercial Banking Act of 1962 (section 11), which empowers the Bank of Thailand to instruct the commercial banks to add the unused balances of overdrafts to their deposits for the purpose of determining the required cash reserve. This power has never been invoked and, in fact, commercial banks do not report the amounts of unused overdraft balances.

easily obtain funds from foreign banks and the Bank of Thailand.[11] Finally, to the extent that a greater proportion of assets of Thai banks are in the form of self-liquidating paper to finance exports and imports, they can, at least in principle, afford a higher ratio of earnings assets to deposits. This certainly applies to banks operating in Thailand which are incorporated abroad and to those locally chartered and soundly managed banks whose main business is the financing of foreign trade.

The other ratio in the table which merits comment at this juncture is the one shown in the last column. Both the numerator and the denominator of the ratio require explanation. The Commercial Banking Act passed in 1962 was a generally successful attempt to bring the practices of Thai banks into one with those of other modern banking systems. It provided that two separate "reserves" be maintained, both in the interest of sound banking practice and so as to furnish the central bank with effective means of control over banking operations. The first of these reserve requirements obligated the banks to maintain a proportion of their deposits (both demand and time) in the form of legal reserves, comprising cash and prescribed government securities, within the range of from 5 to 50 per cent, the exact

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[11] See Charoen Chinalai, "Thailand: Mopping Up," Far Eastern Economic Review (April 14,1966). The ability of the Thai commercial banks to obtain additional resources is of significance which goes beyond the determination of an arbitrary ratio, however unorthodox the high ratio of loans, etc., to deposits may appear in the case of Thai banks. See a further discussion of this ability to obtain resources, p.IV-89, footnote 64.

percentage to be determined by the Bank of Thailand subject to approval by the Minister of Finance. It is 6 per cent at present, with government securities not to exceed 50 per cent of the required reserves. The second requirement specified that:

> A commercial bank shall maintain capital funds in proportion to: (1) total assets at a ratio not less than that prescribed by the Bank of Thailand and approved by the Minister; such ratio shall be not less than five percentum and not more than fifteen percentum; (2) each category of assets at a ratio not less than that prescribed by the Bank of Thailand and approved by the Minister (of Finance). Assets under paragraph (1) and (2) shall not include cash, deposits with the Bank of Thailand, Thai government securities and any other assets as the Minister may prescribe.[12]

The prescribed ratio of capital funds to these "risk assets" is currently 16 per cent but the concept of "risk assets" (or total assets less excluded items) is now difficult to define with precision. In general, they exclude preferred securities such as those of the Treasury, the Industrial Finance Corporation of Thailand, Buffer Stock Certificates (issued in connection with tin ore control), bank premises and equipment, and, more importantly, a large proportion of the paper used in the financing of export trade.[13]

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[12] Commercial Banking Act of B. E. 2502 (English Translation), Section 10. "Capital Funds" means the sum of paid-up capital, reserves, including other reserves appropriated from net profit, and undivided profit.

[13] There are now at least nine major regulations in force which amend, amplify, and clarify the provisions of the Act. On May 1, 1962, shortly after the passage of the Act, one such regulation provided for several exemptions from total assets under Section 10 (Government Gazette, Vol. 79, Part 40, Article 4). Additional discussion of these reserve requirements will be found in Chapter VI.

As seen in Table IV-2 the ratio of capital account to risk assets stood at 10 per cent at the end of 1965, compared with 15 per cent at the end of 1955. However, since the passage of Commercial Banking Act of 1962, the ratio has remained fairly steady, suggesting that the commercial banks, given a steady increase in their risk assets, have had to increase their capital resources rather substantially.[14]

At the time the Act of 1962 was being implemented, the provision pertaining to the ratio of capital to assets was the one that provided the most heated debates and caused the greatest consternation among bankers. In particular, several bankers were faced with the prospect of reducing their earning assets within one year unless they could raise additional capital.[15] As it turned out, there was little trouble raising additional capital, especially insofar as the monetary authorities were determined to restrict

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[14] This is also seen in Table IV-2, but the figures there include increases in risk assets and capital funds of both the existing banks and those newly formed. In fact, existing banks were compelled to increase their paid-up capital, and newly chartered banks commenced business with capital much higher than that averaged by the established banks.

[15] See P. Sithi-Amnuai, "An Appraisal of the Commercial Banking Act 1962," Bangkok Bank Monthly Review (June, 1962), pp. 31-33.

the entry of new banks.[16]

Detailed data on commercial banks assets and liabilities are presented according to sources and uses of funds in Tables IV-3 and IV-4. The percentage distribution and an index for sources and uses of banking funds, respectively, are given in Tables IV-5 and IV-6.[17]

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[16] It appears that due to a resolution passed by the Council of Ministers and advice tendered by the Financial Advisers in the 1950's, no more than one branch of a foreign bank per country diplomatically represented in Thailand will be authorized in the future. Exceptions have been made, as in the case of the Bank of Tokyo (with the Mitsui Bank established in Thailand since 1952) and Chase Manhattan (which, however, took over the charter acquired by the Nationale Handelsbank). Since 1957, the only really new local bank that has been established is The Asia Trust Bank.

[17] It may be useful to reconcile the definitions of Thai terms for certain items which may be at variance with the usage familiar to students of western banking.

First of all, the summary balance sheet for all the commercial banks in Thailand is not a truly consolidated account because it includes inter-bank balances. For a variety of technical reasons these are not eliminated but carried on both the sources and the uses sides. Cash on hand (which is not counted as part of the legal reserve against deposits) includes foreign currency purchased by commercial banks in their course of business. Other securities (other than Treasury bonds and bills, carried at book value) include debentures and equity securities of private and state corporations, some of which, such as those of the IFCT, the commercial banks were encouraged to acquire. Trust Receipts represent mainly import bills which have fallen due but the maturity of which has been extended by the importer who issues a trust receipt to the commercial bank to secure the extension.

On the sources of funds side,capital account is tantamount to the "capital fund," i.e., net worth. With respect to demand deposits, those of other banks include domestic as well as foreign banks. Those of the government are exclusively those of government departments. Deposits of municipalities and state enterprises are lumped together with those of business and individuals under the "private residents" label. Demand deposits of non-residents include those of foreign embassies and foreign government officials. The same classification applies to time deposits. Other demand liabilities include cashier's and certified checks issued by the banks and not yet collected, as well as marginal deposits of customers

Table IV-3

THAI COMMERCIAL BANKS - USES OF FUNDS
(Millions of Baht)

	1955	1956	1957	1958	1959	1960	1961	1962	1963	1964	1965
Cash on hand	135.6	174.9	205.4	211.8	234.8	262.9	287.1	309.1	369.8	369.2	360.4
Balance with banks:											
Bank of Thailand	309.6	328.0	359.4	328.5	446.7	480.6	593.9	701.7	919.7	940.0	942.2
Banks in Thailand	54.3	153.5	215.5	178.2	213.9	227.0	247.4	284.0	463.0	648.9	769.9
Banks abroad	170.9	264.2	265.0	253.2	248.7	283.8	283.0	372.7	508.8	540.6	679.0
Investment											
Treasury bills	53.5	94.1	79.8	43.7	16.1	23.5	80.0	195.1	304.3	267.7	197.0
Bonds	188.1	142.8	155.9	204.2	294.6	394.8	518.0	946.0	1,380.6	1,903.8	2,342.9
Others	22.7	23.2	21.8	29.9	27.9	40.8	-	56.2	128.8	156.2	201.1
Loans and overdrafts	1,620.4	2,040.9	2,426.7	2,894.4	3,268.4	3,809.3	4,361.5	5,392.8	6,188.2	7,401.8	8,930.7
Bills											
Domestic	250.1	284.5	289.9	360.8	317.9	497.5	681.0	605.0	751.0	905.2	995.7
Import	271.0	350.2	420.0	473.0	620.4	735.6	847.0	488.7	628.0	805.8	971.0
Export	249.9	163.7	202.4	249.5	281.7	354.9	443.4	446.7	572.7	719.9	929.5
Trust receipts	-	-	-	-	-	-	-	603.0	667.6	763.2	968.6
Fixed assets	161.9	170.3	213.1	256.4	322.2	458.1	514.4	626.5	779.9	880.7	897.7
Other assets	458.2	221.7	258.3	437.9	278.5	478.6	641.4	373.1	404.0	406.5	542.6
	3,946.2	4,412.0	5,113.2	5,921.5	6,571.8	8,047.4	9,498.1	11,400.6	14,066.4	16,709.5	19,728.1

Source: See Table IV-1.

Table IV-4

THAI COMMERCIAL BANKS - SOURCES OF FUNDS
(Millions of Baht)

	1955	1956	1957	1958	1959	1960	1961	1962	1963	1964	1965
Sources of funds											
Demand deposits											
Banks	42.3	141.2	191.6	164.0	114.9	170.1	149.4	206.6	243.6	358.1	617.4
Government	79.9	117.9	220.5	172.6	207.3	223.8	350.0	273.6	355.6	437.5	656.6
Private residents	1,885.7	2,042.6	2,343.9	2,753.2	2,939.9	3,619.1	3,963.5	3,980.0	4,627.0	5,127.6	5,709.1
Nonresidents	21.4	56.4	3.7	11.8	35.0	20.2	26.8	43.9	68.7	74.3	75.6
Time deposits											
Banks	-	55.3	32.2	66.3	82.5	141.9	111.8	112.3	136.0	176.7	194.7
Government	71.9	11.7	8.7	17.6	185.5	197.3	205.3	158.6	223.2	226.7	442.4
Private residents	168.0	349.4	438.5	621.7	766.7	1,025.7	1,485.3	3,148.6	4,255.0	5,368.3	6,406.8
Nonresidents	3.7	9.9	5.0	9.8	28.2	0.6	11.7	52.6	42.8	29.2	39.1
Other liabilities	-	131.6	180.7	121.1	88.3	160.7	279.9	157.6	167.3	159.6	188.4
Borrowings											
Bank of Thailand	3.0	-	-	8.7	41.9	98.5	106.3	103.6	98.0	164.7	244.3
Banks in Thailand	56.0	99.1	95.1	101.4	252.8	202.2	243.4	293.1	370.2	326.4	241.4
Banks abroad	338.2	438.6	543.8	559.9	738.4	804.9	1,065.5	1,506.7	1,896.2	2,318.1	2,760.5
Other liabilities	821.1	499.6	546.6	795.1	575.6	821.4	884.3	589.2	759.2	969.6	893.2
Capital accounts	455.0	458.7	502.9	518.3	514.8	561.0	614.9	774.2	823.6	972.7	1,258.7
	3,946.2	4,412.0	5,113.2	5,921.5	6,571.8	8,047.4	9,498.1	11,400.6	14,066.4	16,709.5	19,728.1

Source: See Table IV-1.

Table IV-5

THAI COMMERCIAL BANKS - USES OF FUNDS

	Percentage Distribution		Index 1955 =100
	1955	1965	
Cash on hand	3.44	1.84	265.78
Balances with banks:			
Bank of Thailand	7.85	4.81	304.33
Banks in Thailand	1.38	3.93	1,417.86
Banks Abroad	4.33	3.46	397.31
Investment			
Treasury bills	1.36	1.00	368.22
Bonds	4.77	11.95	1,245.56
Others	0.58	1.03	885.90
Loans and Overdrafts	41.06	45.56	551.14
Bills			
Domestic	6.34	5.08	398.12
Import	6.87	4.92	358.30
Export	6.33	4.71	371.95
Trust receipts	-	4.91	-
Fixed assets	4.10	4.55	554.48
Other assets	11.61	2.75	118.42

Source: See Table IV-1.

Table IV-6

THAI COMMERCIAL BANKS - SOURCE OF FUNDS

	Percentage Distribution		Index 1955 = 100
	1955	1965	
Demand deposits			
Banks	1.07	3.11	1,459.57
Government	2.02	3.31	821.78
Private residents	47.79	28.74	302.76
Nonresidents	0.54	0.38	353.27
Time deposits			
Banks	-	0.98	-
Government	1.82	2.23	615.30
Private residents	4.26	37.25	3,813.57
Nonresidents	0.09	0.20	1,056.76
Other	-	-	-
Liabilities	-	0.95	-
Borrowings			
Bank of Thailand	0.08	1.23	8,143.3
Banks in Thailand	1.42	1.22	431.07
Banks Abroad	8.57	13.99	816.23
Other liabilities	20.81	4.50	108.78
Capital accounts	11.53	6.34	276.64
	100	100	

Source: See Table IV-1.

Starting with sources of funds, the tables show that the greatest percentage increase occurred with respect to borrowings from the Bank of Thailand. This has risen eightyfold over the period. But the significance of this must be tempered by the realization that even in 1965, borrowings from the Bank of Thailand still accounted for only 1.23 per cent of all the sources of funds. Moreover, most of the increase occurred before 1962. Even though the Bank of Thailand has since then established several new lines of credit to the commercial banks, their rate of utilization has been somewhat disappointing. Indeed, as mentioned earlier, foreign banks have been a much more important source of funds. The proportion of borrowing from them rose from 8.6 per cent in 1955 to 14.6 in 1965, showing a ninefold increase over the period. At the end of 1965, commercial banks had borrowed only 244 million from the Bank of Thailand, and the total of rediscounts was slightly over 200 million, while loans from head offices and correspondent banks of Thai banks totalled over 2.5 billion baht.[18]

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[17] (continued)
prior to opening of letters of credit. Borrowings from other banks include loans from the Government Savings Bank. Other liabilities consist of provident funds, suspense accounts, and time bills under trust receipts. These are import bills that have been discounted by foreign banks and remitted to Thailand for collection after the importer has extended their maturity under the trust receipt procedure.

[18] See above, p. 13. It has been suggested to the writer by Mr. Somkiert Limsong that the official statistics overstate the volume of borrowings from foreign banks because of the practice of showing contingent liabilities (i.e., import bills not yet due for collection) as borrowing from abroad. However, most of the bankers do agree that they have little difficulty in borrowing against import bills and that they could do so if they would borrow income. On the other hand, end of period figures of

Of prime importance as a source of funds to the commercial banks of Thailand was the nearly fortyfold increase in time deposits of private residents. In fact, by the end of 1965, these time deposits had become the most important single source of funds when measured as a percentage of total liabilities. With time deposits now exceeding demand deposits, a variety of explanations has been adduced to explain this rather striking phenomenon. No doubt, the monetary and political stability, the growth of personal income and confidence, and the sound stewardship of commercial banks which the public came to expect from the Bank of Thailand after 1959, all have played a part.[19] To some extent, legislative enactments have also been instrumental. The reclassification of accounts has already been mentioned. Other observers attach considerable importance to the increase in the rate of return which allegedly occurred during the period,[20] though the influence of higher interest rates payable on time deposits is by no means a simple one. While it is true that the rates of interest payable on three and six month deposits increased from 3 to 5 per cent per annum after 1959, it should also be noted that the return on the longest term time deposits (12 months) was actually

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[18] (continued)
borrowing from the Bank of Thailand tend to understate the volume of borrowing from that source which, if quite heavy at certain times of the year, reflects the seasonal nature of much of commercial banking activity in Thailand.

[19] See Bank of Thailand, Annual Economic Report, 1964 (Bangkok: Bank of Thailand Publication, 1964), pp. 34-35.

[20] See for example, Antonin Basch, Financing Economic Development (New York: Macmillan, 1964), p. 159.

lowered in 1962 from 8 to 7 per cent. Also, and probably of at least equal importance to the changes in interest rates, was the legislation passed in 1962 exempting interest on deposits from income taxation.[21]

While the spectacular growth of time deposits cannot be gainsaid, there are those who remain somewhat skeptical about the extent to which these deposits fully measure the growth of voluntary savings. They view the rapid increase in time deposits largely as a shift from demand deposits which has resulted not merely because of the reclassification but also because of the ease with which time deposits can, allegedly, be treated as checking accounts.[22]

Turning to the uses of funds, the most striking development was the growth of investments in government bonds. Their twelvefold increase over time is also reflected in the percentage distribution. From less than 5 per cent of assets in 1955, government bonds rose to some 12 per cent in 1965.[23]

Loans and overdrafts represent the most significant use of funds from the standpoint of financial intermediation. Unlike commercial bills, loans and overdrafts presumably indicate the supply of funds used for purposes more related to development planning than is the financing of

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[21] Bank of Thailand, Annual Economic Report, 1962 (Bangkok: Bank of Thailand, 1962), p. 27.

[22] See, for example, A. Mousny, The Economy of Thailand: An Appraisal of an Exchange Policy (Bangkok: Social Science Association Press, 1964), pp. 192ff. However, this view, with variations, is held by a number of other observers.

[23] For further discussion of this development, see pp. 23-65.

exports and imports.[24] In fact, as Table IV-6 shows, these loans rose faster than did foreign trade bills. They also moved upward at a faster rate than did demand deposits, giving some credence to the theory alluded to earlier, namely, that an account in a time deposit does not necessarily forego all the advantages of a demand deposit.

Balances with other banks are an item that looms large on both sides of the commercial bank's balance sheet, even though, as suggested earlier, it represents largely a "wash" transaction. It does, however, indicate the importance of inter-bank transaction and reflects some bank's need for funds, both to meet demands for accommodation at short notice and for "window dressing" purposes.

Time Series-Analysis of the Composition of Commercial Bank's Balance Sheets

A scrutiny of the commercial bank's sources and uses of funds, while instructive, fails to relate the structure of the banking system to the trend of the economy as whole. The two economic variables which best put the changing composition of the commercial bank's balance sheets into perspective are the Gross National Product (GNP) and the money supply. Accordingly, simple regressions of selected balance sheet items on these two variables will be presented and briefly discussed in this section.

Tables IV-7 and IV-8 present some of the results of time series

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[24] Many of these loans and even more of the overdrafts were also used for purposes connected with trade.

Table IV-7

THAI COMMERCIAL BANKS, 1955 - 1965 TIME SERIES ANALYSIS

Dependent Variable (y)	Independent Variable (x)	
(Simple Correlation Coefficients)	GNP	Money Supply
Private Demand Deposits as % of Total Liabilities	-8.9489	-9.2177
Loans, Overdrafts & Discounts as % of Total Assets	-4.3369	-4.8057
Total Deposits as % of Total Liabilities	9.1952	9.3270
Loans, Overdrafts, Discounts & Investments as % of Total Assets	7.0260	6.8507
Time Deposits as % of Total Liabilities	9.6589	9.5005
Private Deposits as % of Total Liabilities	-8.9489	-9.2177
Private Time Deposits as % of Total Liabilities	9.6589	9.5005
Demand Deposits as % of Total Liabilities	-8.8804	-8.9457
Investments as % of Total Assets	7.7593	8.2443
(Slope of Regression)*		
Private Demand Deposits as % of Total Liabilities	-6.1018	-7.8336
Loans, Overdrafts & Discounts as % of Total Assets	-2.00784	-17.8503
Total Deposits as % of Total Liabilities	2.6034	3.2914
Loans, Overdrafts, Discounts & Investment as % of Total Assets	72.0616	56.3739
Time Deposits as % of Total Liabilities	23.4514	28.7502
Private Deposits as % of Total Liabilities	-6.1018	-7.8336
Private Time Deposits as % of Total Liabilities	23.4514	28.7502
Demand Deposits as % of Total Liabilities	-5.2580	-6.6017
Investments as % of Total Assets	5.0254	4.2840

*Note: Slope defined as percent change in y associated with 10 percent increase in x. Minus sign indicates an inverse correlation.

Source: See Table IV-1.

Table IV-8

THAI COMMERCIAL BANKS - 1955-1965 TIME SERIES ANALYSIS

Dependent Variable (y)	Independent Variable (x)	
(Simple Correlation Coefficients)	GNP	Money Supply
Borrowings of Local Banks as % of Liabilities	8.8056	8.6250
Borrowings of All Banks as % of Liabilities	8.8937	8.7361
Foreign Borrowing of Local Banks as % of Liabilities	8.9832	8.7445
(Slope of Regression)*		
Borrowings of Local Banks as % of Liabilities	14.975	18.2825
Borrowings of All Banks as % of Liabilities	5.6619	1.9320
Foreign Borrowing of Local Banks as % of Liabilities	21.9210	26.5963

*Note: Slope defined as percent change in y associated with a 10 percent increase in x.
Source: See Table IV-1.

analysis. The first conclusion which appears to emerge from the tables is that, for analytical purposes, it seems largely superfluous to use two independent variables inasmuch as GNP and money supply yield almost identical results, suggesting that these two variables are highly correlated with each other.[25] This conclusion may be a little too hasty. The slopes of regression on the two variables do differ from each other and thereby justify the inclusion of both in the analysis.[26]

With few exceptions, the selected balance sheet ratios in Table IV-7 and IV-8 show very high correlations both with GNP and the money supply, even though in four instances the correlation is an inverse one. Thus, the ratios of loans, etc. to total assets and that of demand deposits, both private and total, to all liabilities, are inversely correlated, indicating a steady decline in their relative importance over time. This is not surprising. On the liabilities side, time deposits have increased relative to the total much faster than demand deposits, and on the assets side, the share of loans, etc. to the total diminished steadily over time relative to that of investments. The lower value of correlation coefficients for

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[25] Correlating MS with GNP yields a coefficient of 0.98.

[26] In fact, the slopes of the regressions may be of greater significance throughout this analysis of time series where all relevant magnitudes show an upward trend throughout the period. An attempt to introduce an explicit time variable into the regression analysis did not yield meaningful results. The use of ratios (of a given balance sheet item of total assets and total liabilities) was resorted to in order to reduce somewhat the influence of time over the values of the regression coefficients.

the ratios of earning assets to total assets (negative for earning assets, less investments) suggests a more erratic behavior over time, with the numerator or the denominator changing direction, and, hence, the sign of the ratio in some years.

Slopes of regression, as defined here, are perhaps of greater interest for analytical purposes than simple correlation coefficients, which merely indicate the conformance of observations to a straight trend line. While the relationship mentioned above, of course, holds here as well, it is perhaps useful to note that as money supply and/or GNP increase, the relative share of time deposits among total banking assets increases at over twice their rate and that of investments at five times the rate of increase of the independent variables.

Thus, Tables IV-7 and IV-8 emphasize and underline the points made in the preceding section. In the period from 1955 through 1966, Thai commercial banks have grown with the national income and the money supply. But the composition of their portfolios and debts has changed significantly during these years. Time deposits and borrowings have become the most important sources of funds, and investment in government securities has been the most important use to which these funds were put. "Important" in this context means relative to other assets and liabilities. From the standpoint of development finance, one could question the importance of purchases of government securities over loans to business, agriculture, and industry. While these, too, have grown over time, as have indeed all items on the balance sheet, they have not grown as fast as investments relative

to national income or the money supply.[27]

In Table IV-8, the times series analysis was extended to cover bank borrowings from various sources, again expressed relative to other items in the balance sheet.

While the coefficients show the same monotonously high degree of correlations as in Table IV-7, an examination of the regressions' slopes discloses some interesting developments. In particular, it strongly suggests that it is the borrowing of local banks from foreign banks which has been the dynamic source of funds over the past 11 years. The relative share of this type of borrowing has increased at over twice the rate of either the GNP or the money supply and faster than borrowings of all banks, from all sources. This suggests, somewhat surprisingly, that the locally chartered banks had sought funds abroad more eagerly than branches of foreign banks.[28]

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[27] This is not to be taken as meaning that bank earning assets other than investments have not grown faster than either the national income or the money supply. See next section.

[28] One reason is that foreign banks when borrowing abroad have to contend, on occasion, with the authorities' interpretation that such borrowing is in reality an addition to capital, hence the cost of this borrowing is not deductible for tax purposes. See Chapter VI.

Time Series Analysis-Commercial Banks Expansion of Credit

The changing structure of sources and uses of commercial bank funds was related in the preceding section to the trend of national income and the money supply. Now an analysis of some of the factors which appear to have been significant in the expansion of credit by the banking system as a whole will be attempted. A fractional reserve banking system expands the means of payment in the hands of the public by creating debts against itself, primarily through the crediting of demand deposits. The usual difficulties of time series analysis are further compounded in this instance by the fact that expansion of bank credit affects the level and rate of growth of national income and, even more directly, of money supply. In the case of Thai banks, moreover, there are two additional considerations which cast further doubts over the validity of any findings derived from this method of analysis. In the first place, the distinction between time and demand deposits remains somewhat vague, at least in some years, secondly, the non-reporting of unused overdraft balances obscures somewhat the concept of demand deposits in the hands of the public. Accordingly, the observations made in this section must be regarded as very tentative.

The economic significance of the ability of the commercial banks to create credit lies, from the standpoint of the saving-investment process, in the fact that it enables them to issue their liabilities to deficit spending units in exchange for portfolio assets and to do so in excess of initial cash resources. This is the one reason why bank loans, overdrafts,

and discounts can increase faster than income and money supply. In the period from 1955 to 1965, a 10 per cent increase in GNP was associated with a 26.2 per cent increase in loans, overdrafts, and discounts, and this rate was even greater when related to a 10 per cent increase in money supply.[29]

As seen from Table IV-9, expansion of earning assets of commercial banks is very highly correlated with both cash and deposits. Here again, it is the slopes rather than the coefficients which appear to be of greater analytical interest. While an increase in cash at banks and in the hands of the public are both associated with a relatively greater increase in earning assets, it is the latter which is accompanied by the more significant increase of earning assets.[30] A 10 per cent increase in time deposits is associated with 20 per cent increase in all earning assets,

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[29] This was 37 per cent to be exact. It follows, from the fact that money supply increased at a slower rate than income in the period under consideration.

[30] This is somewhat surprising because the traditional banking theory would lead one to expect that it is the banks cash resources which are more directly associated with its ability to expand earning assets. The finding provides a somewhat flimsy basis for the speculation that the Thai banks' ability to expand credit is not necessarily highly correlated with their willingness to do so. This point will be discussed more fully later.

Table IV-9

THAI COMMERCIAL BANKS - 1955-1965 TIME SERIES ANALYSIS

Simple Correlation Coefficients	Time Deposits	Demand Deposits	Currency Banks	Currency Held by Public
Loans, Overdrafts, Discounts & Investment	9.9251	9.9062	9.7597	9.7597
Loans, Overdrafts & Discounts	9.9366	9.9303	9.7257	9.7257
Slope of Regression*				
Loans, Overdrafts, Discounts & Investment	20.0754	6.5319	24.167	24.167
Loans, Overdrafts & Discounts	20.8293	6.7858	24.959	24.959

*Slope defined as the percentage change in y associated with a 10 percent increase in x.
Source: See Table IV-1.

while the same increase in demand deposits is linked to an increase in earning assets of only 7 per cent. This is to be expected because even if many loans were given in the form of overdrafts, other loans would take the form of demand deposits. One possible implication here is that (to the extent that a regression equation may be said to have any predictive value) a continuing growth of time deposits ahead of demand deposits may be expected to result in a rate of growth of earning assets which will be slower than that experienced in the past.

Inasmuch as cash and deposits are those elements which presumably underlie the ability of the banks to expand credit to the private sector, Table IV-10, which relates the banks cash resources to their deposits is of interest here. The table shows that the correlation coefficients are uniformly high, as could have been expected. The values of the slopes indicates a greater elasticity of time deposits than of demand deposits. A 10 per cent increase in bank cash resources corresponds to a less than 10 per cent increase in demand deposits but represents a 28 per cent increase in time deposits.[31] This suggests that the expansion of time deposits adds more to cash resources than the expansion of demand deposits, hardly an unexpected finding, inasmuch as the latter constitute a liability more directly convertible into cash in the hands of the public than does the former.

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[31]The slopes as expressed here do, of course, give elasticities when the decimal points are adjusted. Thus, a slope of regression of all deposits on cash and deposits at the Bank of Thailand of 15.2 indicates an elasticity of 1.52 . (All correlations were calculated in log-log space).

Table IV-10

THAI COMMERCIAL BANKS - 1955-1965 TIME SERIES ANALYSIS

	Cash on hand, Foreign Currency & Balances with Bank of Thailand (x)	
	Simple Correlation Coefficient	Slope*
Demand Deposits	.96928	9.4354
Time Deposits	.98786	27.9778

*Slope defined as the percentage change in y associated with a 10 percent increase in x.
Source: See Table IV-1.

In Thailand, cash held by banks does not count as part of legally required reserve against deposits. Deposits held at the Bank of Thailand forms a part of the reserve, together with the commercial banks' holdings of government securities. Since mid-1966, the required reserves have been allowed to consist of deposits of cash at the Central bank and of government securities in the commercial banks' portfolios, in equal parts. As mentioned earlier, Thai commercial banks do have total legal reserves that are no less related to earning assets and deposits over time than are the cash resources themselves. In fact, as shown in Table IV-11, the association is striking. The rate of increase of total deposits is three times that of excess reserves. While it is true that reserves, hence excess reserves, contain government securities, so do earning assets. Table IV-11 hints that excess reserves have been used to expand holdings of government securities rather than that of loans, overdrafts, and discounts.

This proposition is worth exploring. Unfortunately, detailed information about the composition of the commercial banks' required and excess reserves has been available only since 1962. This information is presented in Table IV-12. What this table, in effect, strongly suggests is that excess reserves were invested in government securities rather than used to expand other earning assets. This point will be elaborated further below.

Table IV-11

THAI COMMERCIAL BANKS - 1955-1965 TIME SERIES ANALYSIS

Dependent Variable y	Excess Reserves (Independent Variable (x))	
	Simple Correlation Coefficient	Slope*
Loans, Overdrafts, Discounts & Investment	.85472	24.5660
Government Securities	.91262	39.2350
Deposits (Demand and Time)	.9326	30.1234

*Slope defined as percentage change in y associated with a 10 percent increase in x.
Source: See Table IV-1.

Table IV-12

THAI COMMERCIAL BANKS - LEGAL, REQUIRED, AND EXCESS RESERVES
(Millions of Baht)

Ending	Reserves		Reserve Requirement	Excess Reserves
	Thai Gov't Securities	Deposits		
	(1)	(2)	(3)	(4)
1962				
December	117.9	681.8	484.5	315.2
1963				
March	114.4	598.3	496.5	216.2
June	126.8	676.6	527.9	275.5
September	125.1	675.7	550.1	250.7
December	139.5	805.8	595.8	349.5
1964				
March	137.3	721.3	618.7	239.9
June	147.0	754.3	646.1	255.2
September	164.5	731.1	676.2	219.4
December	174.5	957.0	708.8	422.7
1965				
March	168.4	736.7	723.2	181.9
June	334.6	708.9	746.9	296.6
September	370.3	736.8	797.2	309.9
December	403.5	864.8	847.4	420.9
1966				
March	425.9	879.3	894.5	410.7

Source: See Table IV-1.

What are then the findings of this section? Subject to the qualification made above, it can be conjectured that during the 11 years of the "modern" phase the expansion of credit by commercial banks was made possible by the rapid expansion of time deposits of private residents. However, this expansion of credit did not realize its full potential, as evidenced by the maintenance of substantial excess reserves which were used primarily to purchase government securities far beyond the quantities required against total deposits.[32]

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[32] An attempt was made to arrive at a more rigorous expression of the relationship between excess reserves and various balance sheet items by multiple regression analysis. Unfortunately for this sort of analysis, however, all the pertinent variables are dominated by a strong upward trend. The resulting multi-collinearity makes it statistically difficult to distinguish the influence of one variable from another. A number of multiple regressions were run, but only one, given below, may be said to be statistically meaningful and even there the size of standard errors do not inspire great confidence.

If E -- excess reserves
X_1 -- commercial banks cash assets
X_2 -- loans and discounts
and X_3 -- Government securities

$$E = 195.10 + \underset{(.205)}{.1575X_1} - \underset{(.0188)}{.0195X_2} + \underset{(.0541)}{.0889X_3}$$

Cross Section Analysis, July 1962 and 1966, for Banks Operating in Thailand

Given the severe limitations of time series analysis, it may be useful to supplement that analysis with an examination of the balance sheets of the commercial banks at points of time. July 1962 has been chosen because it was the earliest month for which reasonably consistent and comparable data were available, even though only in raw form. For purposes of comparison, a similar set of data was prepared for July 1966, the last month for which raw data were available at the time of writing.[33] The data are presented separately for banks incorporated in Thailand and for those with head offices abroad.[34]

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[33] Data were also available for June 1962 and for June 1966. However, inasmuch as June statements (required by law) may contain an element of "window dressing," the decision was made to take July, the last month in 1966 for which comparable data could be developed.

[34] The data are not exactly comparable to those presented earlier for all banks, mainly because, for purpose of cross-section analysis, it was possible to net out private deposits and, in the case of banks locally chartered, to adjust for operations of foreign branches of banks with headquarters in Thailand. The difference between the totals given in this section and those given in the Bank of Thailand Monthly Bulletin (on which Table IV-2 was based) is of the order of 5 per cent. Below, the differences (in millions of baht) are given for each of the columns shown in Table IV-13 for July 1966 and July 1962, respectively.

	July 1966											
Total of all banks	2,043	17,311	2,625	1,684	2,973	3,934	283	10,050	4,835	1,058	531	23,663
From Monthly report	1,388	16,390	3,124	1,152	2,768	3,940	217	9,589	4,026		1,513	22,053
Difference	655	921	(499)	533	205	(6)	66	461	809		75	1,610
Column	1	2	3	4	5	6	7	8	9	10	11	12

Table IV-13

COMPARATIVE STATEMENT OF CONDITION
BANKS INCORPORATED IN THAILAND, JULY 1962
(Millions of Baht)

Banks Incorporated in Thailand	Capital Fund	Deposits	Borrowing	Other Liabilities	Cash	Gov't. Securities	Other Secur. and Invest.	Loans and Advances	Bills Receivable	Banks' Prem. and Eqpt.	Other Assets	Total Capital & Liabilities or Assets
	1	2	3	4	5	6	7	3	9	10	11	12
1. Siam Com. B.	113.9	477.8	-	13.4	177.7	17.0	13.1	285.5	58.4	32.3	20.2	605.1
2. Wang Lee Chan B.	3.0	6.4	-	0.3	2.3	0.3	0.1	5.6	-	0.1	0.3	9.5
3. Bank of Asia	48.3	268.5	1.1	9.2	48.8	35.6	3.2	139.6	19.2	46.1	34.6	327.1
4. Siam City B.	19.7	347.3	4.0	25.2	89.9	40.0	0.5	151.2	84.4	14.6	16.2	396.8
5. Provincial B.	41.8	759.9	90.6	47.1	76.7	13.6	1.7	671.7	98.1	65.6	12.2	939.5
6. Bangkok Bank	106.0	1,363.3	722.9	182.2	208.5	181.6	19.0	1,005.7	826.0	90.0	42.9	2,373.7
7. Bangkok Bank of Com.	27.1	445.3	-	52.5	118.8	52.8	0.7	235.3	58.4	28.2	30.3	524.6
8. B. of Ayudhya	27.0	415.9	81.1	43.2	43.7	16.0	8.2	325.7	105.8	30.8	37.1	567.3
9. Thai Farmers B.	35.1	384.2	17.3	36.0	80.1	57.1	1.0	145.9	141.9	36.3	10.0	472.5
10. Laem Thong B.	33.5	159.5	39.5	11.5	21.5	13.6	1.9	166.0	32.1	8.6	0.4	244.3
11. Union B. of Bangkok	17.1	217.2	34.5	44.5	42.3	33.0	1.1	104.0	97.0	17.4	18.4	313.2
12. Thai Danu B.	25.7	134.4	-	21.6	20.1	24.3	0.6	91.3	25.3	7.5	12.8	181.7
13. Agricultural B.	21.1	929.4	107.8	49.7	127.2	180.1	2.1	562.0	62.3	150.7	23.7	1,108.1
14. Bangkok Metropolitan B.	35.2	226.2	196.8	86.0	62.6	31.0	6.3	157.6	272.2	4.5	9.9	544.1
15. Thai Military B.	20.2	230.5	7.9	29.2	65.5	52.9	0.3	101.6	58.2	2.8	6.3	287.5
16. Thai Development B.	11.5	224.1	13.6	40.3	31.7	10.0	0.5	157.4	54.2	14.8	21.3	289.5
Total	586.2	6,589.9	1,317.1	691.9	1,217.4	758.9	60.3	4,303.1	1,993.5	550.3	296.6	9,184.5

Source: See Table IV-1.

Table IV-14 gives the principal items of the balance sheets of the sixteen incorporated banks operating in Thailand as of July 1962. The degree of disparity with respect to size is considerable. Capital funds range from 3 to over 110 million, deposits from 6 million to substantially more than 1 billion baht, and loans and overdrafts from less than 100 million to over 1 billion.[35]

Table IV-15 provides similar data for those banks which have head offices abroad but maintain branches in Thailand.[36] Here the differences with respect to size are no less pronounced.[37]

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[34] (continued)

Total of all banks	656	7,750	1,882	992	1,438	935	62	5,455	2,480	588	321	11,279
From Monthly Report	663	7,577	1,585	812	1,385	920	51	5,107	2,249		924	10,636
Difference	(7)	173	297	180	54	15	11	348	231		(16)	643
Column (See Table IV-14)	1	2	3	4	5	6	7	8	9	10	11	12

[35] As mentioned previously, Wang Lee Chan Bank, whose capital, deposits, and loans are by far the smallest, is more properly regarded as a family bank rather than a commercial bank.

[36] Actually, the "foreign" banks operate in Thailand out of branches located in Bangkok with the single exception of the Chartered Bank which operates a branch in Phuket.

[37] Data for capital fund could not be obtained on a consistent basis for 1962. The Act of 1962 changed rather drastically the provisions with respect to capital assets to be maintained in Thailand by foreign banks as well as the method of accounting for them.

Table IV-14

COMPARATIVE STATEMENT OF CONDITION
BANKS INCORPORATED ABROAD, JULY 1962
(Millions of Baht)

Banks Incorporated Abroad	Capital & Liabilities				Assets							
	Capital Fund	Deposits	Borrowing	Other Liabilities	Cash	Gov't. Securities	Other Sec. and Invest.	Loans and Advances	Bills Receivable	Banks' Prem. & Eqpt.	Other Assets	Total Capital & Liabilities or Assets
	1	2	3	4	5	6	7	8	9	10	11	12
1. The Hongkong and Shanghai B.	24.0	200.8	24.7	44.7	17.1	4.8	0.2	149.4	103.4	19.6	0.2	294.7
2. The Chartered B.	17.7	223.6	57.0	136.2	18.9	13.0	0.2	254.8	138.1	2.5	6.8	434.4
3. Banque de L' Indochine	0.9	67.8	43.4	18.6	26.5	5.2	0.4	72.0	23.1	0.3	3.1	130.6
4. Sze Hai Tong B.	16.9	17.0	29.8	3.8	16.9	7.5	0.2	15.2	27.3	0.1	0.4	67.5
5. The B. of Canton	1.0	32.7	23.0	3.2	12.9	5.0	-	22.0	19.8	0.2	0.1	60.0
6. Mercantile B.	-	66.3	61.5	10.7	7.7	7.2	0.2	90.5	26.7	6.2	0.1	138.5
7. The B. of China	3.8	38.3	89.9	10.7	32.3	14.5	-	45.0	45.5	2.4	2.9	142.6
8. The Indian Overseas B.	-	41.1	29.9	1.8	8.9	5.6	0.2	27.8	29.3	0.6	0.3	72.7
9. The Chase Manhattan B.	5.6	136.9	28.9	7.9	12.5	7.5	-	113.2	39.3	-	6.7	179.2
10. The B. of America	-	270.5	35.0	19.2	54.4	69.5	-	169.5	26.9	2.5	1.8	324.7
11. The Mitsui B.	-	58.2	111.0	42.5	11.8	14.0	0.2	176.8	6.9	1.3	0.8	211.7
12. The B. of Tokyo	-	6.4	30.4	0.6	1.1	21.9	-	10.6	0.4	2.1	1.2	37.4
13. The United MAlayan B.	-	-	-	-	-	-	-	-	-	-	-	-
Total	69.9	1,159.6	564.5	299.9	221.0	175.7	1.6	1,146.8	486.7	37.8	24.4	2,094.0

Source: See Table IV-1.

In Table IV-15 and IV-16, comparable data were provided for July 1966 and then expressed in the form of an index (with July 1962 as a base) in Tables IV-17 and IV-18.

Table IV-17 suggests that while the growth of domestic banking operations was relatively uniform with respect to deposits, capital fund, and, indeed, total assets and liabilities, it varied considerably from the mean in a few banks with respect to investments and borrowings. It would seem that where domestic commercial banks diverge the most in their individual policies is, as regards investments, in their use of funds, and with respect to borrowings, in their sources of funds. The picture is much more confusing when foreign banks are considered. Table IV-18 shows drastic deviations from the mean for several foreign banks, in part because some of them had barely begun operations in 1962 and were thus starting from a very small base. Looking at total assets and liabilities, and abstracting from the Bank of Tokyo which was but a fledgling in 1962, one gets a more consistent pattern of growth.

It may perhaps be useful to restate the figures given in the preceding tables in terms of the rank order of the individual banks for each of the items given in Table IV-13 through IV-18. This has been done in Tables IV-19 and IV-20 for domestic banks and in Tables IV-21 and IV-22 for foreign banks. The ranking is given on an ascending scale, with the bank ranked first given the highest number, and the bank ranked last given the number of one. Tables IV-23 and IV-24 rank domestic and foreign banks in terms of the growth of their balance sheet items form 1962 to 1966.

Table IV-15

COMPARATIVE STATEMENT OF CONDITION
BANKS INCORPORATED IN THAILAND, JULY 1966
(Millions of Baht)

Banks Incorporated in Thailand	Capital Fund	Deposits	Borrowing	Other Liabilities	Cash	Gov't. Securities	Other Secur. and Invest.	Loans and Advances	Bills Receivable	Banks' Prem. and Eqpt.	Other Assets	Total Capital & Liabilities or Assets
	1	2	3	4	5	6	7	8	9	10	11	12
1. Siam Com. B.	142.2	1,283.4	-	26.7	243.3	562.3	50.5	505.5	22.3	47.1	21.3	1,452.3
2. Wang Lee Chan B.	3.5	5.9	-	0.6	1.5	0.9	0.1	6.4	-	0.1	1.0	10.0
3. Bank of Asia	90.1	307.9	1.1	45.2	51.8	20.2	3.8	237.6	89.8	38.1	3.0	444.3
4. Siam City B.	53.9	826.2	19.6	61.3	160.4	101.9	2.3	416.4	172.5	38.2	69.3	961.0
5. Krung Thai B.	146.7	3,258.3	162.8	163.5	339.9	1,198.6	24.4	1,641.4	193.8	308.5	24.7	3,731.3
6. Bangkok B.	291.9	3,570.9	1,004.5	392.1	639.4	448.6	100.0	1,970.5	1,803.3	214.5	82.7	5,259.4
7. Bangkok B. of Com.	63.0	1,035.6	1.8	86.4	197.7	175.3	8.7	548.8	135.2	63.6	57.5	1,186.8
8. B. of Ayudhya	145.1	1,066.7	375.3	55.8	193.4	250.0	16.6	703.2	318.4	84.5	76.8	1,642.9
9. Thai Farmers B.	78.0	888.0	4.3	382.1	104.2	210.0	20.1	391.9	542.2	17.3	16.7	1,352.4
10. Laem Thong B.	41.5	239.6	17.1	26.0	28.5	29.4	6.8	226.0	10.8	19.8	2.8	324.2
11. Union B. of Bangkok	48.2	386.3	34.2	20.2	79.6	90.0	4.4	168.8	98.7	20.9	26.5	488.9
12. Thai Danu B.	57.8	340.0	3.7	46.6	44.8	115.3	7.3	206.9	32.9	7.1	33.8	448.1
13. Bangkok Metropolitan B.	60.6	647.7	382.4	30.1	124.9	160.5	10.2	405.7	385.8	19.1	14.6	1,120.8
14. Thai Military B.	79.5	489.5	37.6	87.2	153.1	122.0	7.2	314.7	85.2	3.9	7.7	693.8
15. Thai Development B.	39.5	630.5	13.2	32.4	76.3	33.0	4.1	458.1	78.7	44.0	21.4	715.6
16. Asia Trust B.	44.4	126.9	183.3	4.5	58.3	15.6	2.0	62.5	202.4	15.6	2.7	359.1
Total	1,385.9	15,103.4	2,240.9	1,460.7	2,497.1	3,533.6	268.9	8,264.4	4,172.0	942.3	462.5	20,190.9

Source: See Table IV-1.

Table IV-16

COMPARATIVE STATEMENT OF CONDITION
BANKS INCORPORATED ABROAD, JULY 1966
(Millions of Baht)

Banks Incorporated Abroad	Capital and Liabilities				Assets							
	Capital Fund	Deposits	Borrowing	Other Liabilities	Cash	Gov't Securities	Other Secur. and Invest.	Loans and Advances	Bills Receivable	Banks' Prem. and Eqpt.	Other Assets	Total Capital & Liabilities or Assets
	1	2	3	4	5	6	7	8	9	10	11	12
1. The Hongkong & Shanghai B.	46.5	220.4	-	12.7	28.7	33.0	1.1	131.3	52.1	32.4	0.5	279.6
2. The Chartered B.	49.5	300.8	0.7	49.6	35.6	43.5	1.1	226.7	86.4	5.2	2.1	400.6
3. Banque de L' Indochine	33.0	77.8	27.1	10.4	7.4	15.2	1.0	80.4	34.3	6.9	3.1	148.3
4. Sze Hai Tong B.	26.6	30.0	22.8	6.7	21.4	11.5	0.6	15.0	36.9	0.1	0.6	86.1
5. The B. of Canton	9.1	70.0	7.7	2.6	39.2	5.0	-	18.1	26.3	0.1	0.7	89.4
6. Mercantile B.	26.2	69.9	5.8	11.5	21.1	10.0	0.2	48.9	26.9	6.1	0.2	113.4
7. The B. of China	46.4	66.9	82.4	22.5	72.3	14.0	-	66.3	60.8	1.9	2.9	218.2
8. The Indian Overseas B.	11.6	43.7	5.4	4.3	20.0	8.3	0.3	14.0	21.5	0.5	0.4	65.0
9. The Chase Manhattan B.	99.4	173.7	4.7	14.2	31.7	43.0	7.0	133.7	67.8	1.6	7.4	292.0
10. The B. of America	104.1	399.6	-	18.9	118.1	66.5	-	195.1	95.5	2.8	44.6	522.6
11. The Mitsui B.	90.2	241.0	70.7	26.5	34.8	65.0	1.1	317.3	6.8	2.0	1.4	428.4
12. The B. of Tokyo	60.3	283.2	56.2	18.3	17.4	56.9	1.1	301.5	37.6	1.5	2.0	418.0
13. The United Malayan B.	54.0	230.4	100.6	25.4	27.8	28.0	0.4	236.6	110.5	4.3	2.8	410.4
Total	656.9	2,207.4	384.1	223.6	475.5	399.9	13.9	1,785.4	663.4	65.4	68.7	3,472.0

Source: See Table IV-1.

Table IV-17

BANKS INCORPORATED IN THAILAND
INDEX OF ASSETS AND LIABILITIES JULY 1966
JULY 1962 = 100

Bank Incorporated in Thailand	Capital Fund	Deposits	Borrow-ing	Other Liabili-ties	Cash	Govt Securi-ties	Other Secur. and Invest.	Loans and Advances	Bills Receiv-able	Banks' Prem. and Eqpt.	Other Assets	Total Capita Liabil or Ass
	1	2	3	4	5	6	7	8	9	10	11	12
1. Siam Com. B.	125	269	-	199	137	3,308	385	176	38	146	105	240
2. Wang Lee Chan B.	117	92	-	200	65	300	100	97	-	100	333	105
3. Bank of Asia	187	115	100	491	106	57	119	170	468	83	8	136
4. Siam City B.	273	238	490	243	178	255	460	275	204	262	428	242
5. Krung Thai B.	233	193	82	169	167	619	642	133	121	143	69	182
6. Bangkok B.	275	262	139	215	307	247	528	196	218	238	193	222
7. Bangkok B. of Com.	232	233	-	165	166	332	1,243	233	231	226	190	226
8. B. of Ayudhya	537	256	463	129	443	1,563	202	216	301	274	207	290
9. Thai Farmers B.	222	231	25	1,062	130	368	2,010	269	382	48	167	286
10. Laem Thong B.	124	150	43	226	133	216	359	136	34	230	700	133
11. Union B. of Bangkok	282	178	99	45	188	273	400	162	102	120	144	156
12. Thai Danu B.	225	253	-	216	223	474	1,217	227	130	95	264	247
13. Bangkok Metropolitan B.	172	286	194	35	199	518	162	257	142	424	147	206
14. Thai Military B.	394	212	476	299	234	231	2,400	310	146	139	122	241
15. Thai Development B.	344	281	97	80	241	330	820	291	145	297	100	247
16. Asia Trust B.	-	-	-	-	-	-	-	-	-	-	-	-
Total	236	229	170	211	205	466	446	192	209	171	156	220

Source: See Table IV-1.

Table IV-18

BANKS INCORPORATED ABROAD
INDEX OF ASSETS AND LIABILITIES JULY 1966
JULY 1962 = 100

Banks Incorporated Abroad	Capital & Liabilities				Assets							
	Capital Fund	Deposits	Borrowing	Other Liabilities	Cash	Gov't. Securities	Other Sec. and Invest.	Loans and Advances	Bills Receivable	Bank's Prem. and Eqpt.	Other Assets	Total Capital & Liabilities or Assets
	1	2	3	4	5	6	7	8	9	10	11	12
1. The Hongkong & Shanghai B.	194	110	-	28	168	688	550	88	50	165	250	95
2. The Chartered B.	280	135	1	36	188	335	550	89	63	208	31	92
3. Banque de L'Indochine	3,667	115	62	56	28	292	250	112	148	2,300	100	114
4. Sze Hai Tong B.	157	176	77	176	127	153	300	99	135	100	150	128
5. The B. of Canton	910	214	33	81	304	100	-	82	133	50	700	149
6. Mercantile Bank	-	105	9	107	274	139	100	54	101	98	200	82
7. The B. of China	1,221	175	92	210	224	97	-	147	134	79	100	153
8. The Indian Overseas B.	-	106	18	239	225	148	150	50	73	83	133	89
9. The Chase Manhattan B.	1,775	127	16	180	254	573	-	118	173	-	110	163
10. The B. of America	-	148	-	98	217	96	-	115	355	112	2,478	161
11. The Mitsui B.	-	414	64	62	295	464	550	179	99	154	175	202
12. The B. of Tokyo	-	4,425	185	3,050	1,582	260	-	2,844	9,400	71	167	1,118
13. The United Malayan B.	-	-	-	-	-	-	-	-	-	-	-	-

Source: See Table IV-1.

Table IV-19

BANK INCORPORATED IN THAILAND
ASSETS AND LIABILITIES BY RANK ORDER JULY 1962

	Capital Fund	Deposits	Borrowing	Other Liabilities	Cash	Gov't Securities	Other Sec. and Invest.	Loans and Adv.	Bills Rec.	Banks' Prem. and Eqpt.	Other Assets	Total Capital & Liabilities or Assets
1. Siam Com. B.	16	13	-	4	15	6	15	12	10	11	10	13
2. Wang Lee Chan B.	1	1	-	1	1	1	1	1	-	1	1	1
3. Bank of Asia	14	8	1	2	7	10	12	5	12	13	14	7
4. Siam City B.	4	9	2	6	12	11	3	7	5	6	8	8
5. Provincial B.	13	14	9	12	10	3	9	15	13	14	6	14
6. Bangkok B.	15	16	12	16	16	16	16	16	14	15	16	16
7. Bangkok B. of Com.	9	12	-	14	13	12	6	11	8	9	13	10
8. B. of Ayudhya	8	11	8	10	6	5	14	13	9	10	15	12
9. Thai Farmers B.	11	10	5	8	11	14	7	6	11	12	5	9
10. Laem Thong B.	10	3	7	3	3	4	10	10	4	5	2	3
11. Union B. of Bangkok	3	4	6	11	5	9	8	4	7	8	9	6
12. Thai Danu B.	7	2	-	5	2	7	5	2	3	4	7	2
13. Agricultural B.	6	15	10	13	14	15	11	14	15	16	12	15
14. Bangkok Metropolitan B.	12	6	11	15	8	8	13	9	2	3	4	11
15. Thai Military B.	5	7	3	7	9	13	2	3	1	2	3	4
16. Thai Development B.	2	5	4	9	4	2	3	8	6	7	11	5

Source: See Table IV-1.

Table IV-20

BANKS INCORPORATED IN THAILAND
ASSETS AND LIABILITIES BY RANK ORDER JULY 1966

Bank Incorporated in Thailand	Capital Fund	Deposits	Borrow-ing	Other Liabili-ties	Cash	Gov't. Securi-ties	Other Sec. and Invest.	Loans and Advances	Bills Receiv-able	Banks' Prem. and Eqpt.	Other Assets	Total Capital and Liabilities or Assets
1. Siam Com. B.	13	14	-	5	14	15	15	12	3	12	8	13
2. Wang Lee Chan B.	1	1	-	1	1	1	1	1	1	1	1	1
3. Bank of Asia	12	4	1	8	4	3	4	6	7	9	4	4
4. Siam City B.	6	10	7	11	11	7	3	10	10	10	14	9
5. Krung Thai B.	15	15	10	14	15	16	14	15	11	16	10	15
6. Bangkok B.	16	16	14	16	16	14	16	16	16	15	16	16
7. Bnagkok B. of Com.	9	12	2	12	13	11	10	13	9	13	13	11
8. B. of Ayudhya	14	13	12	10	12	13	12	14	13	14	15	14
9. Thai Farmers B.	10	11	4	15	8	12	13	8	15	5	7	12
10. Laem Thong B.	3	3	6	4	2	4	7	5	2	7	3	2
11. Union B. of Bangkok	5	6	8	3	7	6	6	3	8	8	11	6
12. Thai Danu B.	7	5	3	9	3	8	9	4	4	3	12	5
13. Bangkok Metropolitan B.	8	9	13	6	9	10	11	9	14	6	6	10
14. Thai Military B.	11	7	9	13	10	9	8	7	6	2	5	7
15. Thai Development B.	2	8	5	7	6	5	5	11	5	11	9	8
16. Asia Trust B.	4	2	11	2	5	2	2	2	12	4	2	3

Source: See Table IV-1.

Table IV-21

BANKS INCORPORATED ABROAD
ASSETS AND LIABILITIES BY RANK ORDER JULY 1962

Banks Incorporated Abroad	Capital & Liabilities				Assets							
	Capital Fund	Deposits	Borrow-ing	Other Liabili-ties	Cash	Gov't. Securi-ties	Other Sec. and Invest.	Loans and Advances	Bills Receiv-able	Banks' Prem. and Eqpt.	Other Assets	Total Capital and Liabilities or Assets
1. The Hongkong & Shanghai B.	6	10	2	10	8	1	1	9	11	11	3	10
2. The Chartered B.	5	11	9	12	9	8	1	12	12	8	12	12
3. Banque de L' Indochine	1	8	8	8	10	3	7	6	4	3	10	5
4. Sze Hai Tong B.	7	2	4	4	7	6	1	2	7	1	5	3
5. The B. of Canton	2	3	1	3	6	2	-	3	3	2	1	2
6. Mercantile B.	-	7	10	6	2	5	1	7	5	10	1	6
7. The B. of China	3	4	11	6	11	10	-	5	10	7	9	7
8. The Indian Overseas B.	-	5	5	2	3	4	1	4	8	4	4	4
9. The Chase Manhattan B.	4	9	3	5	5	6	-	8	9	-	11	8
10. The B. of America	-	12	7	9	12	12	-	10	6	8	8	11
11. The Mitsui B.	-	6	12	11	4	9	1	11	2	5	6	9
12. The B. of Tokyo	-	1	6	1	1	11	-	1	1	6	7	1
13. The United Malayan B.	-	-	-	-	-	-	-	-	-	-	-	-

Source: See Table IV-1.

Table IV-22

BANKS INCORPORATED ABROAD
ASSETS AND LIABILITIES BY RANK ORDER JULY 1966

Banks Incorporated Abroad	Capital & Liabilities				Assets							
	Capital Fund	Deposits	Borrowing	Other Liabilities	Cash	Gov't. Securities	Other Secur. and Invest.	Loans and Advances	Bills Receivable	Banks' Prem. and Eqpt.	Other Assets	Total Capital and Liabilities or Assets
	1	2	3	4	5	6	7	8	9	10	11	12
1. The Hongkong & Shanghai B.	7	8	-	6	7	8	7	7	8	13	3	7
2. The Chartered B.	8	12	1	13	10	10	7	10	11	11	8	9
3. Banque de L'Indochine	5	6	7	4	1	6	6	6	5	12	11	5
4. Sze Hai Tong B.	4	1	6	3	5	4	4	2	6	1	4	2
5. The B. of Canton	1	5	5	1	11	1	-	3	3	1	5	3
6. Mercantile B.	3	4	4	5	4	3	1	4	4	10	1	4
7. The B. of China	6	3	10	10	12	5	-	5	9	6	10	6
8. The Indian Overseas B.	2	2	3	2	3	2	2	1	2	3	2	1
9. The Chase Manhattan B.	12	7	2	7	8	9	5	8	10	5	12	8
10. The B. of America	3	13	-	9	13	13	-	9	12	8	13	13
11. The Mitsui B.	11	10	9	12	9	12	7	13	1	7	6	12
12. The B. of Tokyo	10	11	8	8	2	11	7	12	7	4	7	11
13. The United Malayan B.	9	9	11	11	6	7	3	11	13	9	9	10

Source: See Table IV-1.

Table IV-23

BANKS INCORPORATED IN THAILAND
INDEX OF ASSETS AND LIABILITIES BY RANK ORDER JULY 1966
(July 1962 = 100)

Banks Incorporated in Thailand	Capital Fund	Deposits	Borrow-ing	Other Liabili-ties	Cash	Gov't. Securi-ties	Other Secur. and Invest.	Loans and Advances	Bills Receiv-able	Banks' Prem. and Eqpt.	Other Assets	Total Capital and Liabilities or Assets
1. Siam Com. B.	3	13	-	7	5	15	6	6	2	8	4	9
2. Wang Lee Chan B.	1	1	-	8	1	7	1	1	-	4	13	1
3. Bank of Asia	5	2	6	14	2	1	2	5	14	2	1	3
4. Siam City B.	10	9	11	12	8	5	8	13	9	12	14	11
5. Krung Thai B.	9	5	3	6	7	13	10	2	4	7	2	5
6. Bangkok B.	11	12	7	9	14	4	9	7	10	11	10	7
7. Bangkok B. of Com.	8	8	-	5	6	9	13	10	11	9	9	8
8. B. of Ayudhya	15	11	9	4	15	14	4	8	12	13	11	15
9. Thai Farmers B.	6	7	1	15	3	10	14	12	13	1	8	14
10. Laem Thong B.	2	3	2	11	4	2	5	3	1	10	15	2
11. Union B. of Bangkok	12	4	5	2	9	6	7	4	3	5	6	4
12. Thai Danu B.	7	10	-	10	11	11	12	9	5	3	12	12
13. Bangkok Metropolitan B.	4	15	8	1	10	12	3	11	6	15	7	6
14. Thai Military B.	14	6	10	13	12	3	15	15	8	6	5	10
15. Thai Development B.	13	14	4	3	13	8	11	14	7	14	3	12
16. Asia Trust B.	-	-	-	-	-	-	-	-	-	-	-	-

Source: See Table IV-1.

Table IV-24

BANKS INCORPORATED ABROAD
INDEX OF ASSETS AND LIABILITIES BY RANK ORDER, JULY 1966
(JULY 1962 = 100)

Banks Incorporated Abroad	Capital & Liabilities				Assets							
	Capital Fund	Deposits	Borrowing	Other Liabilities	Cash	Gov't. Securities	Other Secur. and Invest.	Loans and Advances	Bills Receivable	Banks' Prem. and Eqpt.	Other Assets	Total Capital Liab. Assets
1. The Hongkong & Shanghai B.	2	3	-	1	3	12	5	4	1	9	10	4
2. The Chartered B.	3	6	1	2	4	9	5	5	2	10	1	3
3. Banque de L' Indochine	7	4	6	3	1	8	3	7	9	11	2	5
4. Sze Hai Tong B.	1	9	8	8	2	6	4	6	8	6	6	6
5. The Bank of Canton	4	10	5	5	11	3	-	3	6	1	11	7
6. Mercantile B.	-	1	2	7	9	4	1	2	5	5	9	1
7. The Bank of China	5	8	9	10	6	2	-	10	7	3	2	8
8. The Indian Overseas B.	-	2	4	11	7	5	2	1	3	4	5	2
9. The Chase Manhattan	6	5	3	9	8	11	-	9	10	-	4	10
10. The Bank of America	-	7	-	6	5	1	-	8	11	7	12	9
11. The Mitsui Bank	-	11	7	4	10	10	5	11	4	8	8	11
12. The Bank of Tokyo	-	12	10	12	12	7	-	12	12	2	7	12
13. The United Malayan B.	-	-	-	-	-	-	-	-	-	-	-	-

Source: See Table IV-1.

While a detailed examination of the series of tables presented in this section would, no doubt, be rewarding to a student of banking practice, the question of chief interest here is whether the growth of individual banks, in terms of total assets, earning assets, or deposits, is in any way related to the bank size, its capital resources, or its cash position.

Insofar as available data permit a firm conclusion, the answer appears to be that there is no perceptible connection between, say, cash and deposits, or capital and loans, as explanatory variables of growth of individual banks. In other words, the bank whose cash resources increased most from 1962 to 1966 is not necessarily the one whose either deposits or loans have grown most.[38] In Tables IV-25 and IV-26 are given the Kendall rank correlation coefficients which have been computed for relevant variables on the basis of the rankings given in the two preceding tables.[39]

Even though the results of rank correlation analysis yield such meager numerical values, they are not without considerable relevance to an inquiry into the role of Thai commercial banking in the financial intermediation process. The results are consistent with the proposition already hinted at in the course of time series analysis, namely, that as an industry,

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[38] This should be distinguished from a simple time series correlation between the same variables. As stated below, the regression over time of such variables as cash on deposits is, in fact, suspiciously high.

[39] The choice of Kendall rather than Spearman rank correlation was dictated by the number of observations.

Table IV-25

BANKS INCORPORATED IN THAILAND - JULY 1966
RANK ORDER OF INDEX OF ASSETS AND LIABILITIES (1962 = 100)
MATRIX OF KENDALL COEFFICIENT

	Deposits	Cash	Capital Fund	Government Securities	Loans & Advances	Bills Receivable	Other Secur. & Investments
Deposits	1.0	0.4857	0.2190	0.3905	0.3143	0.0440	
Cash		1.0		0.1048		0.0989	0.2000
Capital Fund			1.0	-0.0476	0.3619	0.1868	
Government Securities				1.0			
Loans & Advances					1.0		
Bills Receivable						1.0	
Other Securities & Investment							1.0

Source: See text.

Table IV-26

BANKS INCORPORATED ABROAD - JULY 1966
RANK ORDER OF INDEX OF ASSETS & LIABILITIES (1962 = 100)
MATRIX OF KENDALL COEFFICIENTS

	Capital Fund	Deposits	Cash	Government Securities	Loans and Advances	Bills Receivable
Capital Fund	1.0	-0.2857		-0.1515	0.2424	0.3030
Deposits		1.0	0.2727	-0.0303	0.5455	0.2424
Cash			1.0	-0.0909	0.1818	0.1212
Government Securities				1.0		
Loans & Advances					1.0	
Bills Receivable						1.0

Source: See text.

banking in Thailand operates below capacity. That is, it is suggested that the ability of an individual bank to expand loans has not been hampered by its inability to obtain additional cash or capital and, conversely, that an individual bank's superior performance in expanding its assets has not been dependent on its performing equally well with respect to raising additional capital or retaining sufficient cash resources. Admittedly, the empirical evidence is too thin to sustain fully such a far flung proposition, but such evidence as that provided in Tables IV-25 and IV-26 is at least compatible with it.

For the purposes of present discussion, capacity of the Thai banking industry may be taken to mean its ability to attract additional deposits, on the one hand, and its ability to expand earning assets, on the other. To the extent that attracting deposits is only in part amenable to the decision-making of the individual commercial banks and insofar as, in Thailand, the economically significant earning assets would exclude the purchases of government securities, the index of capacity would be the ratio of loans, overdrafts, and discounts actually made, to that amount which could potentially be made.[40]

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[40] This clearly overstates the case. Banks do have some ability to attract deposits through variations in the rates of interest they pay, the quantity and quality of service they provide, and so on. Conversely, the ability to expand loans is limited by the willingness of the public to borrow. As will be argued later, however, the Thai banks do seem to compete for deposits, but their competition for loans, etc., seems to be rather more subdued in the face of what is alleged to have been sustained and continuing high demand for accommodation on the part of the public.

Thai banks are restricted in their ability to make loans by both legal and economic constraints. Among the latter are the willingness of their customers to borrow, the quality and quantity of would-be borrowers, and the need to maintain liquidity and a balanced portfolio. The legal constraints are much easier to quantify. These are the ratio of cash and government securities to total deposits and the ratio of capital funds to risk assets.[41] It may be worthwhile to consider some of these relevant ratios, both for domestic and foreign banks, as they are presented for 1962 and 1966 in Tables IV-27 and IV-28.

Taking domestic banks first, it is interesting to note that, at least in the case of the bigger banks, the ratio of loans, etc., to deposits has actually declined from 1962 to 1966, even though the ratio of cash to deposits declined but slightly and that of capital to earning assets has actually increased. The slight drain on total cash resources is explained both by the high purchases of government securities and the fact that these securities could be used as part of legal reserves in increasing quantities.

Foreign banks, even more than the domestic ones, appear to have steered shy of their full potential. Despite the increase in both cash resources and capital fund relative to deposits and risk assets, respectively, their ratio of loans, etc., to deposits has decreased rather

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[41] See pp. 14-16. Other constraints are available in the Act of 1962 but have not yet been invoked. A fuller discussion of these constraints is given in Chapter VI.

Table IV-27

THAI COMMERCIAL BANKS INCORPORATED IN THAILAND
KEY BALANCE SHEET RATIOS, 1962 and 1966

		A		B		C		D		E	
		1962	1966	1962	1966	1962	1966	1962	1966	1962	1966
1.	Siam Commercial Bank	0.72	0.41	0.78	0.89	0.37	0.19	0.33	0.27	0.30	0.12
2.	Wang Lee Chan Bank	1.03	1.08	1.09	1.25	0.36	0.25	0.45	0.55	0.43	0.47
3.	Bank of Asia	0.59	1.06	0.74	1.14	0.18	0.17	0.30	0.28	0.24	0.26
4.	Siam City Bank	0.68	0.71	0.79	0.84	0.26	0.19	0.08	0.09	0.07	0.08
5.	Krung Thai Bank	0.83	0.56	0.94	0.94	0.12	0.10	0.05	0.08	0.04	0.05
6.	Bangkok Bank	1.34	1.05	1.49	1.21	0.15	0.18	0.06	0.08	0.05	0.07
7.	Bangkok Bank of Com.	0.66	0.66	0.78	0.84	0.27	0.19	0.09	0.09	0.08	0.07
8.	Bank of Ayudhya	1.04	0.96	1.09	1.21	0.11	0.18	0.06	0.14	0.06	0.11
9.	Thai Farmers Bank	0.75	1.05	0.90	1.31	0.21	0.12	0.12	0.08	0.10	0.07
10.	Laem Thong Bank	1.24	0.99	1.34	1.14	0.13	0.12	0.17	0.18	0.16	0.15
11.	Union Bank of Bangkok	0.93	0.69	1.08	0.94	0.19	0.21	0.09	0.18	0.07	0.13
12.	Thai Danu Bank	0.87	0.71	1.05	1.07	0.15	0.13	0.22	0.24	0.18	0.16
13.	Bangkok Metropolitan Bank	1.90	1.22	2.06	1.49	0.28	0.19	0.08	0.08	0.08	0.06
14.	Thai Military Bank	0.69	0.82	0.92	1.08	0.28	0.31	0.13	0.20	0.09	0.15
15.	Thai Development Bank	0.94	0.85	0.99	0.91	0.14	0.12	0.05	0.07	0.05	0.07
16.	Asia Trust Bank	-	2.09	-	2.23	-	0.46	-	0.17	-	0.16
	Total	0.96	0.82	1.08	1.08	0.18	0.17	0.09	0.11	0.08	0.09

A - Ratio of Loans, Overdrafts, and Discounts to Deposits.
B - Ratio of Loans, Overdrafts, Discounts, and Investments to Deposits.
C - Ratio of Cash to Deposits.
D - Ratio of Capital Fund to Loans, Overdrafts, and Discounts.
E - Ratio of Capital Fund to Loans, Overdrafts, Discounts and Investments.

Source: See Table IV-1.

Table IV-28

THAI COMMERCIAL BANKS INCORPORATED ABROAD
KEY BALANCE SHEET RATIOS, 1962 and 1966

	A		B		C		D		E	
	1962	1966	1962	1966	1962	1966	1962	1966	1962	1966
1. The Hongkong and Shanghai Bank	1.26	0.83	1.28	0.99	0.09	0.13	0.09	0.25	0.09	0.21
2. The Chartered Bank	1.76	1.04	1.35	1.19	0.08	0.12	0.05	0.16	0.04	0.14
3. Banque de L'Indochine	1.40	1.47	1.49	1.68	0.39	0.10	0.01	0.29	0.01	0.25
4. Sze Hai Tong Bank	2.50	1.73	2.95	2.13	0.99	0.71	0.40	0.52	0.34	0.42
5. The Bank of Canton	1.28	0.63	1.43	0.71	0.39	0.56	0.02	0.20	0.02	0.18
6. Mercantile Bank	1.77	1.08	1.88	1.23	0.12	0.30	-	0.35	-	0.30
7. The Bank of China	2.36	1.90	2.74	2.11	0.84	1.08	0.04	0.37	0.04	0.33
8. The Indian Overseas Bank	1.39	0.81	1.53	1.01	0.22	0.46	-	0.33	-	0.26
9. The Chase Manhattan Bank	1.11	1.16	1.17	1.45	0.09	0.18	0.04	0.49	0.04	0.40
10. The Bank of America	0.73	0.73	0.98	0.89	0.20	0.30	-	0.36	-	0.29
11. The Mitsui Bank	3.16	1.34	3.40	1.62	0.20	0.14	-	0.28	-	0.23
12. The Bank of Tokyo	1.72	1.20	5.14	1.40	0.17	0.06	-	0.18	-	0.15
13. The United Malayan Banking Company	-	1.51	-	1.63	-	0.12	-	0.16	-	0.14
Total Foreign Banks	1.41	1.11	1.56	1.30	0.19	0.22	0.04	0.27	0.04	0.23
Total Domestic Banks	0.96	0.82	1.08	1.08	0.18	0.17	0.09	0.11	0.08	0.09
Total	0.60	0.86	0.68	1.10	0.11	0.17	0.08	0.14	0.07	0.11

Source: See Table IV-1.

For definitions of the ratios, see Table IV-27.

significantly over the last five years. This is the more striking because the foreign banks have shown a rate of growth of deposits much below that of the domestic banks. (See Chart V)[42].

In addition to cash on hand and deposits with the Bank of Thailand, cash resources of commercial banks also include balances with banks abroad and gold. Thus, the concept of "liquid assets" as defined in Table IV-2 cannot be applied to them because Thai government securities are excluded. Between 1962 and 1966, most domestic banks show a decline in relation to deposits; however, three, including the largest domestic bank, actually managed to increase the ratio of cash to deposits (see Table IV-28). Almost all foreign banks, on the other hand, did increase their ratio of cash to deposits, and one of those that did not actually showed cash resources in excess of its total deposits (see Table IV-28).

As mentioned before, since mid-1966, cash deposited with the Bank of Thailand has not needed to exceed 3 per cent of total deposits. It is clear that every one of the Thai commercial banks could multiply its total deposits without running up against any cash constraints. This point if further emphasized in Tables IV-29 and IV-30 where the two legally required ratios as they apply to the individual banks in 1962 and 1966, along with

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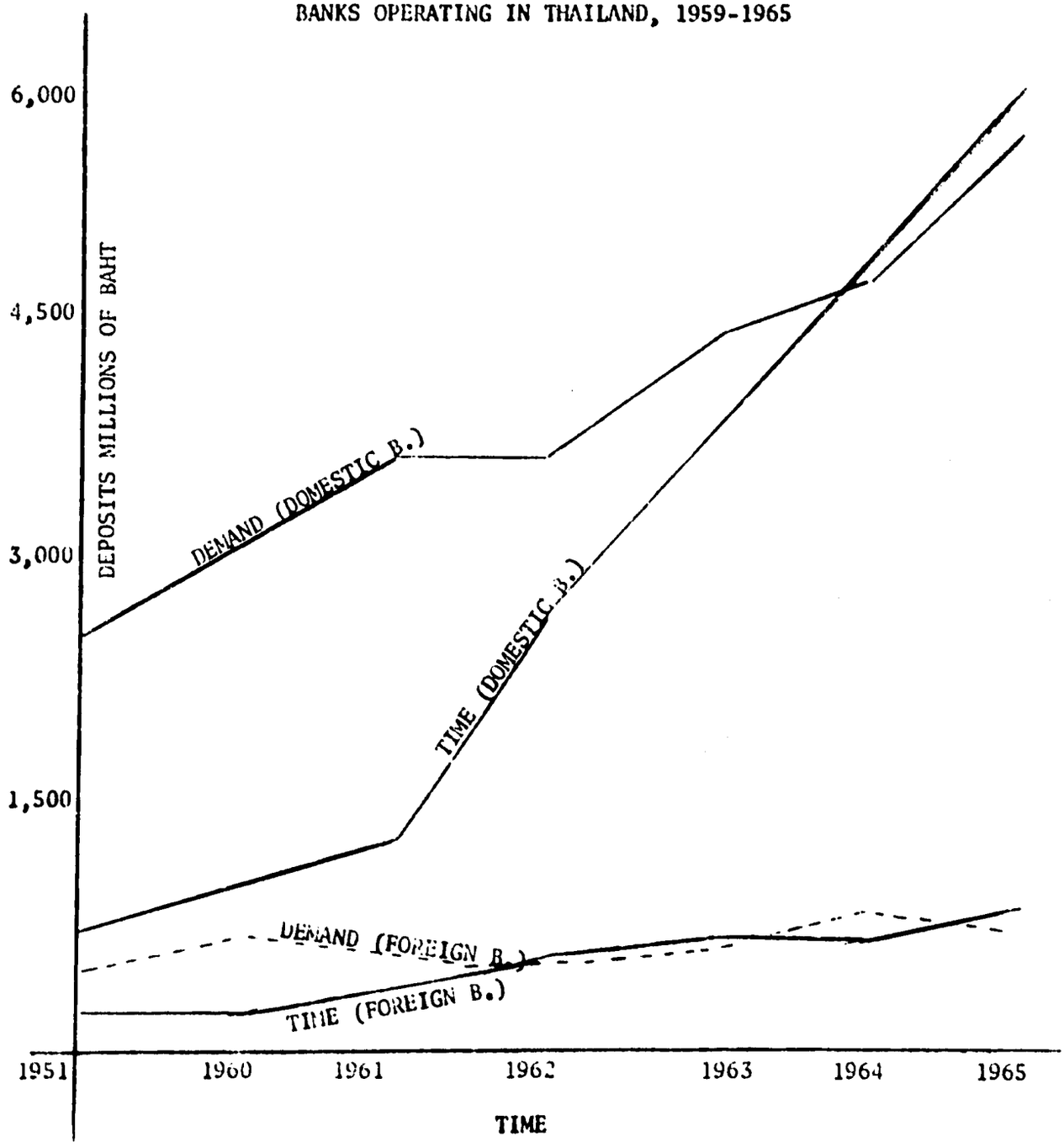
[42] In particular, they did not share fully in the spectacular growth of time deposits. One reason for this is that foreign banks are not allowed to open branches in the provinces. See Chapter V.

CHART V

TIME AND DEMAND DEPOSITS OF DOMESTIC AND FOREIGN BANKS OPERATING IN THAILAND, 1959-1965



the rank orders of the banks in both years based on these ratios. These rankings have not changed significantly for domestic banks, but the changes were more pronounced for foreign banks, again, presumably, because some of the foreign banks were relative newcomers to the scene in 1962 and did not have time to fully deploy their activities and resources. The significant thing about Table IV-29, however, is that the ratio of liquid resources to deposits has generally increased since 1962. The point is worth making because, even though the domestic banks as a whole may have had the capacity to expand credit, the ability of individual banks to expand debts through extension of credit could have varied significantly. Table IV-30 shows that a similar situation has prevailed with respect to foreign banks.

While it seems that the existing liquid resources would make it possible for every single commercial bank operating in Thailand to expand credit considerably,[43] there is the possibility that undue expansion of credit would be limited by the other legal reserve ratio, that of capital fund as a per cent of "risk assets."

Inasmuch as it was impossible to obtain the amount of risk assets for each individual bank, an attempt was made in Tables IV-29 and IV-30 to

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[43] It will be recalled that, under provisions currently in force, the ratio of reserves (deposits at the Bank of Thailand and government securities to total deposit liabilities) cannot be less than 3 per cent and a similar proportion applies with respect to the minimum ratio of capital funds to risk assets.

Table IV-29

BANKS INCORPORATED IN THAILAND, SELECTED RATIOS (%)

BANKS	1962				1966			
	Ratio of Capital Fund to Loans & Advances and Bills Receivable		Ratio of Cash, Government Securities to Deposits		Ratio of Capital Fund to Loans & Advances and Bills Receivable		Ratio of Cash, Government Securities to Deposits	
	Ratio	Rank Order	Ratio	Rank Order	Ratio	Rank Order	Ratio	Rank Order
1. Siam Com. Bank	33.0	14	40.7	13	26.9	14	62.8	16
2. Wang Lee Chan Bank	45.5	15	40.6	12	54.7	16	40.7	8
3. Bank of Asia	30.4	13	31.4	6	27.5	15	23.4	2
4. Siam City Bank	8.4	6	37.4	10	9.2	6	31.7	5
5. Krung Thai Bank	4.5	1	23.5	4	8.0	4	47.2	13
6. Bangkok Bank	5.8	3	28.6	5	7.7	2	30.5	4
7. Bangkok Bank of Com.	9.2	8	38.5	11	9.2	6	36.0	7
8. Bank of Ayudhya	6.3	4	14.4	1	14.2	8	41.6	9
9. Thai Farmers Bank	12.2	9	35.7	9	8.4	5	35.4	6
10. Laem Thong Bank	16.9	11	22.0	3	17.5	10	24.2	3
11. Union Bank of Bangkok	8.5	7	34.7	8	18.0	11	43.9	10
12. Thai Danu Bank	22.0	12	33.0	7	24.1	13	47.1	12
13. Bangkok Metropolitan Bank	8.2	5	41.4	14	7.7	2	44.1	11
14. Thai Military Bank	12.6	10	51.4	15	19.9	12	56.2	14
15. Thai Development Bank	5.4	2	18.6	2	7.4	1	17.3	1
16. Asia Trust Bank	-	-	-	-	16.8	9	58.2	15

Source: See Table IV-1.

Table IV-30

BANKS INCORPORATED ABROAD, SELECTED RATIOS (%)

	1962				1966			
	Ratio of Capital Fund to Loans & Advances and Bills Receivable		Ratio of Cash, Government Securities to Deposits		Ratio of Capital Fund to Loans & Advances and Bills Receivable		Ratio of Cash, Government Securities to Deposits	
	Ratio	Rank Order	Ratio	Rank Order	Ratio	Rank Order	Ratio	Rank Order
1. The Hongkong and Shanghai Bank	9.5	6	10.9	1	25.3	5	28.0	4
2. The Chartered Bank	4.5	5	14.3	2	15.8	2	26.3	3
3. Banque de L' Indochine	0.9	1	46.8	8	28.8	7	29.0	5
4. Sze Hai Tong Bank	39.8	7	143.5	11	51.3	13	109.7	12
5. The Bank of Canton	2.4	2	54.7	9	20.5	4	63.1	10
6. Mercantile Bank	-	-	22.4	4	34.6	9	44.5	8
7. The Bank of China	4.2	4	122.2	10	36.5	11	129.0	13
8. The Indian Overseas Bank	-	-	35.3	5	32.7	8	64.7	11
9. The Chase Manhattan Bank	3.7	3	14.6	3	49.3	12	43.0	7
10. The Bank of America	-	-	45.8	7	35.8	10	46.2	9
11. The Mitsui Bank	-	-	44.3	6	27.8	6	41.4	6
12. The Bank of Tokyo	-	-	359.4	12	17.8	3	26.2	2
13. The United Malayan Bank	-	-	-	-	15.6	1	24.2	1

Source: See Table IV-1.

approximate the amount sought by using, as the denominator of the ratio, the sum of loans, overdrafts, and discounts (or what is in reality the same thing as loans, advances, and bills receivable). In 1966, the reserve position of foreign banks was stronger than five years before because since 1962 they have had to substantially increase their capital resources held within Thailand. For domestic banks, surprisingly enough, the overall ratio has also increased, albeit slightly. There are, however, considerable variations among individual banks, with some of the banks edging fairly close to the legal minimum in 1966 and others far exceeding it.

With respect to legal limitations, it would thus appear that capital is much more important than liquid assets in determining the limits of expansion of commercial bank credit in Thailand. But, it could be argued that the capital limitation, even for the few banks that operate close to the legal minimum, is more apparent than real, given the ease with which additional capital can be obtained by Thai banks in a period when the banking business is profitable and there are stringent limitations on entry.[44]

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[44] It will be noted that the ratio of capital to risk assets obtained in Table IV-23 is fairly close to that given in Table IV-2 (allowing for difference in dates), even though the concepts used in the two tables are not identical. Risk assets in Table IV-2 include some securities but exclude quite a few of the other earning assets. On the other hand, the numerator of the ratio is higher in Table IV-23 than in Table IV-3 (see footnote 32, p. IV-37.

Commercial Banks and Unused Capacity

In order to quantify the concept of unused capacity introduced in the preceding section, Tables IV-31 and IV-32 give the results of an instructive, if admittedly not very rigorous, exercise. Unused capacity may be defined as the difference between the level of deposits maintained in fact and the level which could, in theory, be maintained, given the banks' reserves and the continuation of the present reserve requirements. In Tables IV-31 and IV-32, potential expansion of credit is calculated first on the basis of banks' liquid assets and then on the basis of capital fund. Both calculations are approximate. Not all liquid funds could possibly be converted into legal reserves against deposits[45] and, further, the legal definition of risk assets (or capital funds, for that matter) does not coincide with that employed in the tables. More important, the calculations given in the tables do not pretend to provide a normative guide to Thai commercial banks. Clearly, no one would seriously suggest that an expansion of credit on the scale indicated either could have or should have been provided (if only from standpoint of monetary stability). The tables are merely intended to

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[45] Excess of liquid funds over reserve requirements is of course, much greater than "excess reserves" as defined, say, in Table IV-12. There, only amounts actually deposited at the Bank of Thailand count as reserves. As seen in Table IV-3, liquid assets are nearly three times the size of the legal reserves.

Table IV-31

BANKS INCORPORATED IN THAILAND JULY, 1966
POTENTIAL EXPANSION OF CREDIT

		Excess Reserves (Liquidity)	Potential Expansion	Excess Reserves (Capital Fund)	Potential Expansion (Capital Fund)
1.	Siam Commercial Bank	728.60	12,143.33	36.73	612.17
2.	Wang Lee Chan Bank	2.04	34.00	0.72	12.00
3.	Bank of Asia	53.52	892.00	21.46	357.67
4.	Siam City Bank	212.72	3,545.34	72.17	1,202.83
5.	Krung Thai Bank	1,343.00	22,383.33	223.09	3,718.17
6.	Bangkok Bank	873.74	14,562.34	70.77	1,179.50
7.	Bangkok Bank of Com.	310.86	5,181.00	80.06	1,334.33
8.	Bank of Ayudhya	379.40	6,323.33	100.00	1,666.67
9.	Thai Farmers Bank	260.92	4,348.67	22.05	367.50
10.	Laem Thong Bank	43.52	725.34	8.39	139.83
11.	Union Bank of Bangkok	146.41	2,440.35	31.35	522.50
12.	Thai Danu Bank	139.70	2,328.34	26.51	441.83
13.	Bangkok Metropolitan Bank	246.54	4,109.00	13.79	229.83
14.	Thai Military Bank	245.72	4,095.33	12.39	206.50
15.	Thai Development Bank	71.46	1,191.00	33.19	553.17
16.	Asia Trust Bank	66.28	1,104.67	2.41	40.17
		5,124.43	85,407.35	755.08	12,584.67

Source: See Table IV-2.

Table IV-32

BANKS INCORPORATED ABROAD JULY,1966
POTENTIAL EXPANSION OF CREDIT

	Excess Reserves (Liquidity)	Potential Expansion	Excess Reserves (Capital Fund)	Potential Expansion (Capital Fund)
1. The Hongkong and Shanghai Bank	48.48	808.00	21.07	351.17
2. The Chartered Bank	61.04	1,017.33	11.49	191.50
3. Banque de L'Indochine	15.20	253.33	3.12	52.00
4. Sze Hai Tong Bank	31.10	518.34	2.41	40.17
5. The Bank of Canton	40.00	666.66	1.86	31.00
6. Mercantile Bank	26.90	448.34	1.75	29.17
7. The Bank of China	82.28	1,371.33	2.83	47.17
8. The Indian Overseas Bank	25.68	428.00	1.23	20.50
9. The Chase Manhattan Bank	64.28	1,071.33	3.09	51.50
10. The Bank of America	160.62	2,677.00	29.96	499.33
11. The Mitsui Bank	85.34	1,422.33	16.05	267.50
12. The Bank of Tokyo	57.30	955.00	16.85	280.83
13. The United Malayan Bank	41.98	699.67	13.73	228.83
	740.20	12,336.66	125.44	2,090.67

Source: See Table IV-1.

dramatize the proposition that commercial banks could have substantially increased the size of their lending operations had they so wished.[46]

Why should not the commercial banks desire, if indeed they do not, to expand their lending operations? Certainly, very few bankers would be willing to acknowledge that they are less than anxious to expand their earning assets. It is equally certain that most of them would, when queried as to why their earning assets are below full potential, reply that it is due to the lack of credit-worthy borrowers, or adequate collateral, or applicants, or any of a dozen other plausible factors which might prevent them from making additional loans. Nevertheless, after all these explanations are accounted for and given due weight, there still exists a prima facie case for the contention that Thai bankers, whether deliberately or subconsciously, are less interested in expanding earning assets than objective circumstances would seem to warrant.

For example, the existence of unused capacity does not appear to arise from an inadequate demand for the product. Judging from the high level of interest rates and even more, their persistence over time, the demand continues strong relative to supply (see Table IV-33).[47] It is also doubtful that the excess capacity results from the existence of too many

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[46] The banks can only expand credit by lending or investing their resources. While loan operations lead to expansion of deposits, in Thailand the relationship is not a simple one, due to the widespread custom of lending against a line of overdraft credit. It so happens, however, that most banks show a ratio of earning assets to deposits of around unity. Hence, the text talks interchangeably of expansion of assets and liabilities of the banks.

[47] The issue of the structure of interest rates is discussed later.

Table IV-33

THAI COMMERCIAL BANKS' RATES CHANGED ON ACCOMMODATION
(in per cent per annum)

Type of Accommodation	Year				
	1962	1963	1964	1965	1966
Call Money	6 - 12	6 - 12	6 - 12	6 - 12	6 - 12
Commercial Bills	15	15	15	15	14
Import Bills	10 - 15	6 - 10	6 - 10	6 - 10	6 - 10
Export Bills	8 - 12	8 - 10	8 - 10	8 - 10	8 - 9
Rice Warrants	7	7	7	7	7
Bills on Industrial Raw Materials	-	7	7	7	7
Bills or Industrial Credit Bills	-	7	7	7	7
Loans & Overdrafts	9 - 15	9 - 15	10 - 15	10 - 15	9 - 14

Source: See Table IV-1.

banks. Even in the mid-fifties the Thai government imposed strong restrictions on new country, and it seems unlikely that the number of banks operating at present in the country is too great with relation to the needs of the economy, although it is possible that the facilities for financing foreign trade could be provided with fewer banks. One bit of evidence which indicates that there is little fear of overcapacity, at least from the viewpoint of outsiders to the industry, is the long waiting line of applicants for banking charters.[48]

Moreover, the industry is a highly profitable one, even on the basis of official and declared income data. As shown in Table IV-34, the average return on net worth (i.e., capital fund) for the last decade was over 10 per cent.[49] It is somewhat surprising that the rate of return of foreign banks is much higher than that of domestic banks, even though the former are relatively more prominent in the financing of foreign trade, which is less risky and accordingly commands lower average accommodation rates.[50] These very high rates of return on capital shown by foreign banks may be accounted for, in part, by the vagueness of the capital and concept

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[48] It is said, for instance, that the (hypothetical) value of a new charter is in excess of 20 million baht at present. Add to it the at least 30 million currently required as capital, and it is seen that entry into banking is highly prized, indeed.

[49] The rate seems to have declined rather sharply in 1965. The figures for that year are preliminary, however.

[50] Domestic banking may actually be more profitable in the aggregate. In addition to the admittedly lower rates of interest, bankers charge fees for opening of letters of credit, exchange transactions fees, and so on, which make the total return on this type of business compare favorably with that obtained on more risky loans.

Table IV-34

THAI COMMERCIAL BANKS - PROFIT RATES, 1956-1965

	Net Profit (1)			Net Worth (2)			(1) as percentage of (2)		
	Banks Incorporated in Thailand	Banks Incorporated Abroad	Total	Banks Incorporated in Thailand	Banks Incorporated Abroad	Total	Banks Incorporated in Thailand	Banks Incorporated Abroad	Total
	(Thousands of Baht)								
1956	33,841	26,380	60,221	409,200	49,500	458,700	8.27	53.29	13.13
1957	30,974	35,663	66,637	450,400	52,500	502,900	6.87	67.92	13.25
1958	31,592	32,324	63,916	462,600	55,700	518,300	6.82	58.03	12.33
1959	34,063	23,091	57,154	474,000	40,800	514,800	7.18	56.59	11.10
1960	43,755	19,890	63,645	508,000	53,000	561,000	8.61	37.52	11.34
1961	51,148	31,470	82,618	554,800	60,100	614,900	9.22	52.36	13.44
1962	61,730	37,755	99,485	695,500	78,700	774,200	8.87	47.97	12.85
1963	70,182	34,718	104,900	742,900	80,700	823,600	9.45	43.02	12.74
1964	101,683	56,098	157,781	887,900	84,800	972,700	11.45	66.15	16.22
1965	62,198	29,264	91,462	1,152,100	106,600	1,258,700	5.39	27.45	7.26

Source: See Table IV-1.

regarding banks with headquarters abroad and in part by the greater tradition of compliance with corporate income reporting that, perhaps, can be expected from foreign banks.[51]

If, then, the usual economic explanations for excess capacity--too many producers, inadequate demand for the product, lack of alternative opportunities, etc.--do not seem to apply to Thai banking,[52] the reasons for the Thai bankers' alleged lack of enthusiasm to expand their earning assets further must be sought elsewhere.

At this point, one is tempted to develop a hypothesis which, albeit difficult to prove, does fit with some of the observations brought to light in the course of the preceding discussion. The hypothesis runs as follows:

Thai bankers do not maximize the long-run profits of the banks they control because, consciously or not, they do not fully identify their personal interests with those of the banks. Most of them are traders and manufacturers as well as bankers, and their economic position, social

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[51] The ambiguity of the concept of capital funds for banks with foreign operations was mentioned earlier (see footnote 12, P.IV-13). In particular, it is difficult to distinguish clearly between capital and borrowings from banks abroad.

[52] This last point (opportunity cost near zero) was not discussed explicitly, but high profits within the industry, coupled with stringent limitations on entry, make it unlikely that bankers would be anxious to leave that business. In fact, as stated earlier, the very opposite is the case. Moreover, most bankers do operate in other industries and thus have options which they do not appear anxious to exercise to the detriment of banking activities.

status, personal prestige, and the like may not always weigh most heavily on the banking side of their activities. (see Table IV-35). A banker who is at the same time the manufacturer of one product and the importer of yet another could, for instance, feel that a vigorous expansion of his earning assets, while possibly indicated from a banking standpoint, would run counter to his manufacturing or trading interests. Even if a loan or an advance were not made to a direct competitor, it might be made to one who would eventually compete wihh some of the non-banking activities of the lender or, in any case, add to the existing competitive pressures surrounding such resources as office space or skilled help. Moreover, the Thai banker may have an erroneous conception of the demand elasticity for bank credit. He may prefer to make fewer loans at high average rates than try to compete for a larger volume of loans at lower rates of interest.[53] His rational evaluation of demand elasticities may, further, be influenced considerably by less tangible, yet potent, considerations which stem from a situation where money is scarce and costly, where the loan granting ability confers subtle advantages, and where, finally, it is possible to reap individually a pecuniary harvest that need not necessarily be shared with the bank.

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[53] It is doubtful whether many bankers will long maintain this conception, provided they take their business of banking seriously. There are very few industries with a greater range of increasing returns to scale.

Table IV-35

INTER-OWNERSHIP OF MAJOR SHAREHOLDERS OF BANKS
AND THEIR RESPECTIVE OUTSIDE INTERESTS

Bank	Position of Major Shareholders of Bank	Outside Interests	Respective Position
A	Vice Chairman	1. Trading Co.	Director
		2. Hotel	Managing Director
		3. Trading Co.	Director
		4. Finance Co.	Director
		5. Weaver	Chairman
B	Managing Director	1. Distillery	Managing Director
		2. Chemical	Director
		3. Distillery	Director
		4. Trading	Chairman
		5. Distillery	Managing Director
		6. Exporter-Importer	Managing Director
		7. Trading	Chairman
		8. Warehouse Co.	Director
C	Managing Director	1. Trading	Director
		2. Building Contractor	Director
		3. Trading	Director
	Asst. Managing Director	1. Chemical	Director
		2. Insurance Co.	Director
D	Managing Director	1. Investment Co.	Director
		2. Weaver	Chairman
		3. Sugar Industry	Managing Director
		4. Match Manufacture	Managing Director
	Asst. Managing Director	1. Rubber Co.	Manager
		2. Restaurant	Chairman
E	Managing Director	1. Insurance Co.	Manager
		2. Rice Mill	Director
F	Managing Director	1. Rubber Manufacture	Director
		2. Paper Mill	Director

Table IV-35
(continued)

INTER-OWNERSHIP OF MAJOR SHAREHOLDERS OF BANKS
AND THEIR RESPECTIVE OUTSIDE INTERESTS

Bank	Position of Major Shareholders of Bank	Outside Interests	Respective Position
G	Managing Director	1. Warehouse Co.	Chairman
		2. Rubber Co.	Managing Director
		3. Trading	Director
H	Vice Chairman	1. Importer	Chairman
		2. Warehouse Co.	Director
		3. Cinema	Director
		4. Trading	Chairman
I	Managing Director	1. Building Contractor	Director
		2. Saw Mill	Director
		3. Liquor Agent	Director
		4. Provision Food	Director
		5. Forestry	Managing Director
		6. Saw Mill	Director
		7. Trading	Chairman
		8. Transportation Co.	Director
		9. Insurance Co.	Director
		10. Motor Spare Parts	Director
		11. Building Contractor	Director
		12. Sugar Refinery	Director
		13. Warehouse Co.	Director
		14. Mining Co.	Director
J	Chairman	1. Liquor Agent	Director
		2. Trading	Director
		3. Agricultural Trade	Chairman
		4. Insurance	Director

Table IV-35
(continued)

INTER-OWNERSHIP OF MAJOR SHAREHOLDERS OF BANKS
AND THEIR RESPECTIVE OUTSIDE INTERESTS

Bank	Position of Major Shareholders of Bank	Outside Interests	Respective Position
	Managing Director	1. Trading	Director
		2. Finance Co.	Managing Director
		3. Finance Co.	Managing Director
		4. Shipping	Director
		5. Motor Trade	Chairman
		6. Motor Trade	Chairman
		7. Warehouse Co.	Director

Source: See text.

The Thai bankers have been able to maintain this dichotomy of interests and behavior for a number of reasons. In the first place, banking is profitable and, for persons making money elsewhere, there is little pressure to maximize profits in banking per se. Secondly, banking assets and liabilities have shown a consistent upward trend, though, as argued earlier, the main expansion took place with respect to assets which have been used little to finance the needs of the small manufacturer, farmer, or mining operator. This apparent growth in banking accommodation has tended to obscure the degree of under-utilization of capacity. Thirdly, a number of factors have served to provide bankers with a convenient rationalization for their alleged lackadaisical attitude toward the expansion of loans and advances. Thus, existing traditions, practices, and standards of Thai banks have enabled bankers to maintain that the limitations of demand are responsible for restricting the expansion of loans.[54] To the extent that many bankers may consider banking operations tantamount to financing foreign trade, neither their skills nor their attitudes prepare them to consider

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[54] This, if true (and there is no hard information on the number of applicants turned down), operates on both sides of the schedule for lendable funds. Prospective borrowers do not go to a bank if, say, they lack the proper collateral, and the bank, consequently, does not see them.

It has been suggested that an additional reason for potential borrowers avoiding commercial banks is the "halo effect." Many smaller manufacturers and traders simply know too little about the resources and practices of commercial banks and therefore do not believe that they qualify as borrowers even though their business status and asset position may be quite sound.

extending their operations beyond accommodations to exporters, importers, and wholesale traders.[55]

Finally, under-utilization of capacity has been possible to maintain because the existing banking structure, together with policies of monetary management, has not provided strong incentives for expanding loans and advances to the sectors other than foreign trade. For a variety of reasons, the central bank has had to rely mainly on moral suasion when dealing with commercial banks. Its well-intended measures to develop a money market have run counter to its avowed desire to reduce the cost of bank credit. Likewise, its commitment to monetary stability has militated against an unduly large expansion of bank credit.[56]

The Operational Policies of Thai Commercial Banking

As has been suggested, the hypothesis of deliberate maintenance of excess capacity is a tempting one, but whether its validity can be established with a high degree of confidence is doubtful. Yet, the hypoth-

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[55] No doubt, most Thai bankers do realize that banking functions extend beyond foreign trade and many actually go outside it. Nevertheless, it is both easier and less risky, as well as profitable, to finance foreign trade than to venture into untested and unknown territory. It should be added, in all fairness, that even those less tradition-bound that would be interested in venturing forth into new territory have to contend with scarcity of qualified personnel. For example, it is said that when commercial banks first began to establish provincial branches, they were compelled in some cases to appoint, as branch managers, persons with little, if any, experience in banking, i.e., the wives of provincial governors.

[56] For a fuller discussion of the relationship of Thai commercial banks with the central bank see Chapter VI.

esis does at least provide a convenient focus for viewing the operations of commercial banks without becoming bogged down in a maze of detail or concerned unduly with developments of secondary importance to economic analysis. In this section, some of the points touched on in the closing paragraphs of the preceding one will be discussed more or less in the order in which they were made.

First, there is the matter of the profitability of commercial banks. A relatively high rate of return on invested capital in commercial banking may be simply a function of its efficiency and may not be out of line with the rate of return in other sectors of a prosperous and buoyant economy.[57] However, the profitability of Thai banks appears to stem principally from the spread between the average rate of interest paid on deposits and the average rate charged for accommodations. While precise information is not available, qualified observers think that the spread is of the order of 5 to 8 per cent (of earning assets).[58] Table IV-36 gives the rates of interest payable by Thai banks on deposits.

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[57] There are no firm data regarding rate of return on invested capital in Thailand.

[58] Through the courtesy of a leading commercial bank, it was possible to obtain, but not publish, the results of the bank's calculations of average costs and payments of interest for 1962, 1963, and 1964. Taking the average for the three years, total interest income was 8 per cent of loans and advances, while interest payments average slightly over 3 per cent of deposits.

Table IV-36

THAI COMMERCIAL BANKS RATES OF INTEREST
PAYABLE ON DEPOSITS
(percent per annum)

Type of Deposit	1962	1963	1964	1965	1966
Demand Deposits	0.5	0.5	0.5	0.5	0-0.01
*Limited Demand Deposits	4-5	4-5	3	3	Cancelled
Savings Deposits	4-5	4-5	4-5	4-5	3-5
Time Deposits under 3 months	5	0.5	0.5	0.5	0.01
3-6 months	6	5	5	5	5
6-12 months	8	6	6	6	6
over 12 months	8	7	7	7	7

*Subject to maximum drawing of four checks per month.
Source: See Table IV-1.

Now a spread of five or six basic points is not usually associated with very efficient banking operations.[59] It could be contended that, even when not a reward for superior efficiency, a high rate of return is necessary to compensate for risks. While risks are, of course, taken daily, the record of Thai banks does not seem to indicate that the business has been subject to unduly large losses in the past. As seen in Table IV-37, bad debts as a proportion of loans averaged less than one half of one per cent in the past decade.[60]

The fact that a considerable spread exists between interest paid by banks and that payable to them by borrowers may indicate that so long as the relatively high level of the latter can be maintained, there is little stimulus for the banks to improve operational efficiency. It also suggests

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[59] In the United States, commercial banks show a rate of return on capital of about 9 per cent out of a spread which is less than half that of Thai banks. For example, in the period 1951-60, the average difference between the rate of return on earning assets of member banks (members of the Federal Reserve System) and the effective rate paid on time deposits (no interest is payable on demand deposits) was two percentage points. In 1951, for instance, the rate of return on earning assets was 2.71 per cent and that paid on time deposits was 1.0. In 1959, the former rate stood at 4.33 per cent and the latter at 2.36 per cent. See H. Peter Gray, "The Effects of Monetary Policy on Rising Costs in Commercial Banks," Journal of Finance (March 1963), p. 231.

[60] It appears that some caution is necessary in interpreting Table IV-37. The table may understate the proportion of bad debts to the extent that some banks will carry loans made for other than economic reasons for years without writing them off, even though the chances of repayment are very poor indeed. Still, the proportion of bad debts is not likely to exceed 1 per cent. The risk on investments, which are primarily in the form of government securities, is, of course, even less.

Table IV-37

THAI COMMERCIAL BANKS - BAD DEBTS AS PROPORTION OF LOANS

	Bad Debts (1)			Loans, Overdrafts & Discounts (2)			(1) as percentage of (2)		
	Banks Incorporated in Thailand	Abroad	Total	Banks Incorporated in Thailand	Abroad	Total	Banks Incorporated in Thailand	Abroad	Total
1956	10,808	2,889	13,697	2,015,200	824,100	2,839,300	.54	.35	.48
1957	10,901	3,337	14,238	2,351,500	987,500	3,339,000	.46	.34	.43
1958	10,964	3,793	14,757	2,899,600	1,078,100	3,977,700	.30	.35	.37
1959	18,368	8,908	27,276	3,344,300	1,144,100	4,488,400	.55	.78	.61
1960	28,313	6,957	35,270	4,067,600	1,329,700	5,397,300	.70	.53	.65
1961	34,503	5,075	39,578	4,769,100	1,564,200	6,333,300	.72	.33	.62
1962	30,292	4,563	34,855	5,883,800	1,652,500	7,536,300	.51	.28	.46
1963	31,689	6,436	38,125	6,941,400	1,866,100	8,807,500	.46	.34	.43
1964	32,552	539	33,091	8,443,100	2,152,900	10,596,000	.39	.03	.31

Source: See Table IV-1.

that to the extent that excess capacity in the industry is consistent with other motivations of the bankers, there will be little competitive pressure to reduce the rate of interest payable by borrowers.

Tables IV-38 and IV-39 provide a breakdown of commercial bank loans by purpose. While there has been some improvement in the relative share of loans going to manufacturing, the shares of agriculture and mining have actually declined. In any event, there is a strong feeling among students of Thai banking practice that such breakdowns are not very meaningful inasmuch as the bankers themselves are often ignorant of the real purpose to which their funds are directed though fully cognizant of the Bank of Thailand's desire to increase the proportion of loans going into manufacturing.[61]

One reason why commercial bankers may not always know the real purpose of the loan is that many have been nurtured in a tradition which attaches much more importance to the person of the borrower than the reason for his application. No doubt, the two aspects of the transaction are not unrelated. But very few, if any, banks will spend much time analyzing the project, its future flow of cash, or other conditions which might indicate the project's chances for success. Instead, they will concern themselves primarily with the asset position of the borrower, his past credit rating, and, above all, the type of collateral he can offer.

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[61] The efforts of the Bank of Thailand to induce the commercial banks to direct more of their resources into the financing of manufacturing activities are discussed in Chapter VI.

Table IV-38

THAI COMMERCIAL BANKS-LOANS AND OVERDRAFTS CLASSIFIED BY PURPOSE
(Millions of Baht)

	1958 Dec.	1959 Dec.	1960 Dec.	1961 Dec.	1962 Dec.	1963 Dec.	1964 Dec.	1965 Dec.
1. Agriculture	99.0	91.8	115.9	124.6	201.6	239.6	292.8	324.8
2. Mining and Quarrying	45.1	33.5	36.6	23.3	117.1	55.4	66.7	157.4
3. Manufacturing	292.8	351.5	402.6	538.3	603.2	954.0	1,099.9	1,428.2
4. Contract Construction	210.3	246.6	296.1	585.0	425.9	485.8	549.4	585.2
5. Real Estate					262.4	331.8	407.2	440.0
6. Import	1,069.9	1,233.1	1,529.0	1,808.5	1,168.0	1,368.9	1,466.8	1,707.4
7. Export					739.5	744.7	945.0	1,279.1
8. Wholesale & Retail Trade	486.6	508.7	531.3	558.3	776.8	857.2	1,036.4	1,198.7
9. Public Utilities	43.2	39.0	29.3	34.5	150.5	156.7	199.2	145.7
10. Banks and Other Financial Institutions					23.5	48.6	58.1	141.6
11. Service	647.5	764.2	868.5	689.0	136.1	312.1	321.8	427.1
12. Personal Consumption					464.8	541.5	782.2	874.4
13. Others					123.4	91.9	176.3	221.6
Total	2,894.4	3,268.4	3,809.3	4,361.5	5,192.8	6,188.2	7,401.8	8,931.2

Source: See Table IV-1.

Table IV-39

LOANS AND ADVANCES OF COMMERCIAL BANKS
CLASSIFIED BY PURPOSE - PERCENT DISTRIBUTION*

	1958 Dec.	1959 Dec.	1960 Dec.	1961 Dec.	1962 Dec.	1963 Dec.	1964 Dec.	1965 June
1. Agriculture	3.42	2.81	3.04	2.85	3.88	3.87	3.96	3.64
2. Mining and Quarrying	1.56	1.02	0.96	0.53	2.25	0.90	0.90	1.76
3. Manufacturing	10.12	10.75	10.57	12.34	11.62	15.42	14.86	15.99
4. Construction					8.20	7.85	7.42	6.55
5. Real Estate	7.27	7.54	7.78	13.41	5.05	5.36	5.50	4.93
6. Import					22.49	22.12	19.82	19.12
7. Export	36.96	37.73	40.14	41.47	14.24	12.03	12.77	14.32
8. Wholesale and Retail Trade	16.81	15.56	13.95	12.80	14.96	13.85	14.00	13.42
9. Public Utilities	1.49	1.19	0.77	0.79	2.90	2.53	2.69	1.63
10. Banks and Other Financial Institutions					0.45	0.79	0.78	1.59
11. Services	22.37	23.38	22.80	15.80	2.62	5.04	4.35	4.78
12. Personal Consumption					8.95	8.75	10.57	9.79
13. Others					2.38	1.49	2.38	2.48
	100.00	99.98	100.01	99.99	100.00	100.00	100.00	100.00

Source: See Table IV-1.
*Details may not add up to total because of rounding.

For really top-notch names among the business community, no collateral, other than a signature or two, may be required. But in most cases, certainly in over half of the loans by value, a tangible security is required by the banks, more often than not in the form of a land mortgage. This is shown in Table IV-40. Land's preponderance as a source of lendable funds has several consequences. As mentioned before, it tends to orient the bankers toward the nature of the collateral rather than the purpose of the loan. It makes it more difficult to obtain funds for those who, for one reason or another, cannot own land. It makes investment contingent on the availability of unencumbered real estate and thereby directs the attention of a would-be investor to land and real estate development and away from more productive investment.[62]

The reasons for the limited success of the central bank in reducing the cost of borrowing and in directing more commercial bank resources into developmental channels are discussed in Chapter VI. Of special significance for the "unused capacity" hypothesis, however, is the Bank of Thailand's policy with respect to government securities. As shown previously, the amount of these securities held by the banks comes closer and closer to the volume of their excess reserves. These securities yield 7 or 8 per cent per annum, are tax free, and can be used as legal reserves against deposits for up to 50 per cent of the total reserves required. These attractive

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[62] Banks usually lend only about 30 per cent of the value of the collateral. In a period of rising land values, commercial banks do not mind repossessing the land even though the legal procedures are lengthy and cumbersome. This is another factor which militates against putting emphasis on the productive purpose of the loan.

Table IV-40

THAI COMMERCIAL BANKS:
BREAKDOWN OF COLLATERAL BY TYPE, 1965

Type of Collateral	Amount (Millions of Baht)		Per cent of total	
	May, 1965	Oct. 1965	May 1965	Oct 1965
Land only	1,130.8	1,307.4	29.47	29.33
Land plus Inventory	309.6	404.5	8.07	9.07
Land plus Buildings	446.9	574.2	11.65	12.88
Land plus Notes Receivables	205.9	125.6	5.37	2.82
Land plus Personal Guarantee	339.4	331.3	8.84	7.43
Personal Guarantee	1,020.1	1,202.5	26.58	26.97
Business Guarantee	308.4	433.6	8.04	9.73
Inventory plus Personal Guarantee	1.7	3.9	0.04	0.09
Land plus Stock	31.1	25.2	0.81	0.57
Time Deposit Certificate	14.6	15.6	0.38	0.35
Stock plus Inventory	8.5	5.9	0.22	0.13
Bonds and Gold	20.7	17.7	0.54	0.40
Time Deposit Certificate plus Stock	-	9.8	-	0.22
Time Deposit plus Bonds	-	0.1	-	0.002
	3,837.6	4,457.3	100	100
Total, Foreign Banks	982.4	1,187.2		
Grand Total	4,820.1	5,642.5		
Total outstanding as shown in Monthly Bulletin	8,225.1	8,820.9		

Difference due to fact that the table refers only to loans and advances in excess of 500,000 baht and further excludes loans to very large borrowers made without any collateral.

Source: See Table IV-1.

holdings, thus, make it less painful for commercial banks to tolerate large excess reserves and, to that extent, remove any strong pressures on them to compete for additional business with the resultant downward impact on interest rates changed for banking accommodation.[63]

This brief examination of the salient operational characteristics of Thai commercial banks does reveal a number of elements which seem to be consistent with the "unused capacity" hypothesis. Thai bankers seem to direct their activities toward trade (and real estate development) and are less interested in sectors where those financed by them may be competing for scarce resources. They can maintain high interest rates rather than vie for additional banking business because they find attractive outlets for their excess reserves either in the form of government securities or employment outside banking.[64] Finally, partly because of their contacts and

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[63] These and other aspects of this problem will be discussed in Chapter VI.

[64] The existence of large excess reserves in the face of high demand for funds and the relatively high cost of lendable funds is, in fact, the main prop of the unused capacity hypothesis. Indeed, large excess reserves are only a fraction of the resources available to Thai commercial banks in the event that they decided (and the central banks and would-be borrowers cooperated) to expand loans and advances. In that case they could count on borrowing from foreign banks and on credit from the central banks whose facilities have been used only to a limited extent in the past. A rough and ready estimate of the extent to which commercial banks have availed themselves of the various credit lines offered by the Bank of Thailand over the past three years is about 20 per cent of actual utilization. (See Chapter VI).

activities outside commercial banking, Thai bankers can resist such pressures as may be exerted by the central bank to reorient their activities and reduce the cost of borrowing.[65]

While the preceding discussion and argument was about Thai commercial banks, in general, a distinction should perhaps be made between the foreign and the domestic banks. As a rule, the inability or unwillingness of the foreign banks to expand their loans and overdrafts to the fullest extent possible stems from rather different considerations from those emphasized in the preceding paragraphs. By tradition and design, foreign banks specialize in foreign trade or in trade of businesses run by the nationals of the countries they represent. They are also somewhat less well equipped to go much beyond their traditional lines of activity. Finally, being guests in Thailand, many of them seem to feel that any aggressive drive for additional banking business would be out of place.[66]

Commercial Banking in the Saving-Investment Process

It should be stated at the outset that the findings and conclusions of this section are tentative. Additional research is needed before the

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[65] This is not to say that moral suasion by the Bank of Thailand is always ineffective. Following a number of pleas on the part of the Governor, the commercial banks did, in fact, reduce their lending rates in mid-1966 (see Table IV-34).

[66] It should be emphasized that the alleged "unwillingness" of Thai bankers to expand their earning assets is closely related to the real and imaginary difficulties in following an aggresive lending policy. The scarcity of personnel was already mentioned. This scarcity is acute in those professions, i.e., auditors, loan appraisers, etc., which are the key ones.

development planner can, with confidence, attempt to modify the structure and the operations of commercial banks. In particular, more information is required about the breakdown of deposits by origin, size, and possible motivation. Similarly, more needs to be known about the primary securities of the business sector and the way business finances its requirements of both fixed and working capital. Subject to these and other qualifications, however, it does appear that the performance of Thai commercial banks as financial intermediaries could be substantially improved.[67]

On the face of it, the banks have done quite well in getting the households to accept claims against banks, particularly time deposits. Even so, it is doubtful whether the increase in commercial banks deposits over the past 10 years represents an increase in real saving or merely a shift in the composition of financial assets, particularly cash into deposits and demand deposits into time deposits. The latter kind of asset shift would, in itself, be significant, because it would enable the banks to lengthen their portfolios, provided one could be confident that time deposits did actually represent the banks' longer-term liabilities.

But it is in financing deficit spending units, particularly with regard to investments of a developmental character, that the banks have

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[67] Many of the assertions about the behavior of banks and bankers in Thailand appear to be confirmed by the findings of an Urban Credit Survey which the Bank of Thailand completed in 1967. The present writer collaborated on the survey design and drafted the questionnaire. See Chapter VII.

fallen short of their potential.[68] If the hypothesis of excess capacity has any validity, it strongly implies that Thai commercial banks could have provided more funds to industry, mining, and agriculture, even at the expense of trade, real estate development, or sheer speculation.

Here the problem is one of quality as well as quantity of financing. Not only could commercial banks have increased the volume of their loans to sectors other than trade and real estate but they could have worked harder to develop the types of claims which would be attractive to the deficit units and still satisfy the banks' needs for liquidity and safety. It would be difficult to finance the fixed capital requirements of industry, for instance, when, as suggested earlier, the claims on the banks themselves are of a short-term nature. Step one would hope to see the development of term-lending or revolving credit within the Thai banking system as a partial answer to the dilemma of "lending long and borrowing short."[69]

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[68] This is especially so with respect to financing of small and medium manufacturers producing primarily for an export market. See Chapter I and also Chapter VII for some evidence on this point.

[69] It is not generally appreciated that term lending is really quite consistent with liquidity because term lending may typically contain amortization features. For a fuller discussion of term lending in American practice see: Federal Reserve Bank of New York, "Term Lending by New York City Banks" Monthly Review (February 1961); and Federal Reserve of Chicago, "Term Loans--Big Business for Big Banks" Business Conditions, (May 1968).

Insofar as increasing the volume of credit is concerned, there remains the problem of its impact on the money supply and, hence, on monetary stability. The bankers in Thailand, including central bankers, have good reasons for favoring a conservative monetary policy which emphasized the self-liquidating paper doctrine of banking. It should be noted, however, that the inflationary impact of bank financing can, in principle, be minimized by a variety of measures including offsetting fiscal, monetary, and debt management policies; shifting bank portfolios by selective and other controls; and channelling bank loans into more "productive" outlets.

It was shown in Chapter II that only 17 per cent of the private sector's investment outlays were financed by bank credit in 1965. While this proportion has increased substantially since 1957, it is still only a small fraction of the requirements.[70]

The allegation implicit in the "unused capacity" hypothesis is that the commercial banks in Thailand simply did not expand their output sufficiently and, by failing to compete vigorously for business, helped to maintain a structure of high interest rates. If this is true, it has important implications for developmental planning.[71]

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[70] Much of this increase is due to increased participation of commercial banks in the real estate boom, particularly in the Bangkok-Thonburi area. The degree of this participation is, allegedly, only imperfectly shown in the data giving the breakdown of bank loans by purpose. See Tables IV-38 and IV-39.

[71] Prima facie, the type of market behavior in which several firms in an industry maintain a high price for their product by failing to expand output sufficiently, is characteristic of oligopoly. But the analysis of imperfect competition does not appear very promising from the standpoint of the developmental saving-investment process. See, however, the discussion of "efficiency" in Chapter I.

High interest cost to the would-be investor means that the payoff cannot be a distant one. The capital has to be recouped in a very short period when the annual cost of capital ranges 4 per cent.[72] An industrial undertaking with a fairly long gestation period will appear less attractive to the entrepreneur than a short-term enterprise, frequently of a speculative character. For many productive undertakings with good prospects of substantial profits in the future, there will be the problem of the initial period of construction, development of markets, etc., during which there are no revenues but a heavy debt burden to service. In this way, high cost of borrowing tends to distort the pattern of allocation of resources, at least from the social, developmental vantage point.

The fact that there is no substantial spread between the return to the saver and the cost to borrower in Thailand means that a "liquidity gap" exists, indicating that the financial markets do not efficiently perform their function of intermediation.[73] Increasing the level of interest rates given to the depositors would, in the absence of higher rates charged to the borrowers, impinge on the profits of the banks, and raising the costs to the investors would further aggravate the problems touched upon in the preceding paragraph. In order to simultaneously reduce costs to borrowers

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[72] While the cost of bank credit to sectors other than foreign trade was until recently only 15 per cent per annum, many investors without access to bank credit had to pay more. Even in the case of bank credit, there were in some cases additional costs beyond the legal maximum rate. See Chapter VII.

[73] See Chapter I.

and increase returns to savers, the banks would have to increase their operational efficiency and/or greatly reduce their profits.[74]

As a matter of fact, while the Thai commercial banks do not show any great drive to expand their loans and overdrafts to sectors other than trade, they do seem anxious to attract more deposits, particularly longer-term deposits. One of the banking community proposals, repeatedly submitted to Thai authorities, asks the government to allow banks to pay a higher rate on deposits held for periods longer than one year.[75] Moreover, while there is little competition for loans and advances, there seems to be vigorous for time deposits.[76]

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[74] The statement in the text implies that savings and investment is interest-elastic. See, Tibor Scitovsky, Welfare and Competition: The Economics of a Fully Employed Economy (Chicago: Richard D. Irwin, 1951) and J. A. Buttrick and H. K. Williamson, (eds.), Economic Development: Principles and Patterns (New York: Prentice-Hall, 1954).

[75] See, for example, "Draft Submission of the Thai Bankers Association to the Subcommittee on Financial Institutions of the NEDB" (November 1965), mimeo (in Thai). This particular suggestion was incorporated in the official Second Five-Year Plan. See also Chapter VI.

[76] Another area where Thai commercial banks show a high degree of competition is in their drive to establish provincial branches. Some of the largest banks, in particular, are anxious to expand in the provinces, but, in order to do so, have to satisfy a number of criteria set down by the Bank of Thailand. The provincial branches are of interest on several counts and are discussed at length in the next chapter.

This competition for deposits is difficult to reconcile with the alleged disinterest in expanding loans and advances. It is one thing to argue that Thai commercial banks do not maximize profits and quite another to suggest that they deliberately incur costs of additional deposits without intending to utilize the proceeds fully. This, indeed, is a challenge to the "unused capacity" hypothesis. It may mean that the hypothesis is invalid, or valid only in part (the banks do lend out a proportion of the funds at their disposal). Alternatively, it may mean that the bankers are not fully rational or not very sincere in their clamor for additional deposits. Finally, it is possible that they somehow manage to put the additional funds to use without such flows being fully reflected in the bank statements.[77]

It is this uncertainty about the validity of the "unused capacity" hypothesis, plus the lack of information mentioned at the beginning of this section, which make one cautious of suggesting far reaching reforms for commercial banking in Thailand. There is little question that commercial banking could and should participate more fully in the financing of other sectors of the economy, particularly manufacturing, mining and agriculture.

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[77] This last possibility would not only vitiate the hypothesis but also offer additional support for it. Yet the point is a very delicate one and as strongly suggested by some as it is denied by others. The question is not so much one of misappropriating bank funds for private purposes (although an incident of this sort did come to light a few years ago) but rather of dividing the banking transaction into two parts: one of which is effected through the bank itself and the other through a separate, if bogus, entity such as compradore.

Some suggestions as to how this participation could be brought about will be given in Chapter V and VI. In the main, the suggestions call for strengthening of the moral suasion exerted by the central bank by other measures.[78] It is also clear that institutions other than the commercial banks would be needed to provide non-contractual, long term finance to manufacturing.[79]

Within their present structure and functions, however, there is still room for further improvements and modifications which could make the banks more efficient. The need to institutionalize term-lending has already been mentioned. Another possibility worth exploring is that of a self-insurance scheme among the Thai banks which would increase the confidence of the public, on the one hand, and help to introduce more uniform and, hopefully sounds practices among the Thai commercial banks, on the other.

Certain changes in existing laws and regulations could also help commercial banks serve the public better and could, in principle, be offered as a quid pro quo against the costs of say, a FDIC-type self-insurance scheme. For example, simplification of the registration of mortgage deeds,

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[78] The proposal made in Chapter III to bring commercial banks into the agricultural credit field is perhaps the most promising of these suggestions.

[79] See Chapters VIII and IX.

facilitating the pledge against second mortgage, subdividividing one land title into smaller parcel, etc., would fall into that category. Legislation of chattel mortgage is now being implemented and should help to remove some of the attachments to land collateral.[80]

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[80] This could lead eventually to a type of banking operation which analyzes the project rather than the borrower on a basis for making loans. The full tuition of project-oriented banking will take some time in Thailand not only because of ingrained attitudes but also because of the shortage of qualified loan appraisers. Yet there is some evidence that traditionally-oriented bankers can sometimes change their attitudes and practices rather quickly and, once having changed them, perceive their merits and attractions. See David C. McClelland, "Achievement Motivation can be Developed," Harvard Business Review (November-December,1965), and example cited therein.

Chapter V

BRANCH BANKING

Branch operations of Thai commercial banks, especially in the provinces, have a number of characteristics of special interest to the developmental planner. The existence of these characteristics prompted a separate discussion of branch banking even though these branches form an integral part of the commercial banking system.

In the first place, relative to its geographic size and its gross national product, Thailand appears to be quite well endowed with respect to branch banking.[1] Compared with its neighbors, the spread of commercial banking throughout the countryside is a significant feature of the Thai financial system. At least 500 private banking offices dot the Thai landscape. Although these offices are concentrated in urban centers, they do provide banking facilities to most of the country's rural population. In the Philippines and elsewhere, semi-official, specialized provincial financial institutions may be more numerous, but no country in the area can boast a better network of private institutions providing general banking facilities outside the capital.

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[1]According to available information the number of branches and/or bank offices in selected countries of Southeast Asia at the end of 1967 was approximately as follows: Singapore 117, Vietnam 36, Malaysia 277, Philippines 215 (in 1962), Indonesia 277.

When an extensive network of institutions is financed by sources other than budgetary appropriations and has a reservoir of talent in its employ that is not affiliated with the civil service, it constitutes an important national resource which can and should be brought into the service of developmental planning. One way in which this could be done was spelled out in Chapter III where a scheme for involving provincial branches of Thai banks in providing productive, supervised group credit to the farmer has been suggested. Such credit is regarded as one means of weaning the farmers away from their current overwhelming dependence on the village moneylender.

But the possibilities for using provincial branches as instruments for reducing the scope of unorganized markets, thus bringing financial flows within the purview of official scrutiny and control, extend beyond agricultural credit. In fact, a study of the development of branch banking in Thailand is of special interest because the evolution of this form of financial activity provides insights into the ways in which the activities of the unorganized markets can be brought within the framework of organized financial intermediaries and directed into developmental priorities.

Moreover, inasmuch as branch banks reflect the transition from the less to the more organized forms of financial intermediation, a study of their operations throws some badly needed light on the mechanism

of resource transfer from agriculture to the rest of the economy.[2]

Finally, the right to license new branches is perhaps one of the most effective instruments of control, potentially if not actually, at the disposal of central monetary authorities.[3] These special aspects of branch banking in Thailand merit a chapter of their own.

The Extent of Branch Banking in Thailand[4]

The spread of commercial bank branches in Thailand is a comparatively recent phenomenon. At the end of 1953, there were less than 100 branches. Their number quadrupled within the next 12 years and, as of this writing, numbers in excess of 500 (See Tables V-1 and V-2).

The first branch set up by a commercial bank in Thailand was

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[2]See Chapter II.

[3]A fuller discussion of control of commercial banks will be found in Chapter VI.

[4]Little published data is available regarding commercial bank branches in Thailand. In particular, information regarding individual banks is not generally available to the public (except their location and number) and the author's sources at the Bank of Thailand were constrained with respect to the detail they could release. Thus, infomation given in this chapter had to be culled from interviews with bankers and from data gathered during field trips, as well as from data made available by the Bank of Thailand. Consequently, the figures are not always strictly comparable, do not always pertain to the same time period, and, on occasion, are not reliable. In general, however the statistics given in the text do provide a picture of branch operations which would not be modified drastically had accurate figures been available throughout.

The only published account of commercial bank branches in Thailand known to the author is contained in Paul Sithi-Amnuai, Finance and Banking in Thailand: A Study of the Commercial System 1888-1963 (Bangkok: Thai Watana Panich, 1964), Chapter VI. Some aggregate statistical information is published periodically in the Bank of Thailand Annual and Monthly Reports and in similar publications of the Bangkok Bank, Ltd. (See particularly Commercial Banks in Thailand, 1964 [Bangkok, 1965] Part I).

Table V-1

Thai Commercial Banks - The Distribution of Bank Branches at the End of December, 1965.

Changwad (Province)	Population (Census 1960) 000	No. of Bank Offices	Changwad (Province)	Population (Census 1960) 000	No. of Bank Offices
Bangkok	1,577	142	Ubol Rajadhani	1,131	6
Songkla (Haadyai Included)	500	20	Udorndhani	744	6
Dhonburi	559	19	Kanchaaburi	233	6
Trang	240	13	Puket	76	6
Chiengmai	798	13	Pichit	389	5
Rajburi	411	12	Sukothai	316	5
Cholburi	392	12	Pattani	282	5
Nakorn Sawan	648	11	Ayudhaya	479	4
Khon Kaen	844	10	Lopburi	335	4
Yala	149	10	Saraburi	304	4
Nakorn Srithamaraj	730	10	Samud Prakarn	235	4
Lampang	472	9	Prae	299	4
Nakorn Rajasima	1,095	9	Pitsanulok	352	4
Naradhiwat	266	9	Nakorn Pathom	370	4
Surajdhani	325	8	Petchaburi	238	4
Chiengrai	812	7	Samud Songkram	162	4
Chumporn	175	7	Supanburi	491	4
Chanburi	158	6	Nondaburi	196	3

Table V-1 (continued)

Thai Commercial Banks - The Distribution of Bank Branches at the End of December, 1965.

Changwad (Province)	Population (Census 1960) 000	No. of Bank Offices	Changwad (Province)	Population (Census 1960) 000	No. of Bank Offices
Chazerngsao	323	3	Samud Sakorn	166	2
Rayong	148	3	Patalung	234	2
Chayapoom	486	3	Chainat	245	1
Nongkai	257	3	Patoomthani	190	1
Lampoon	250	3	Singburi	154	1
Uttaradit	260	3	Angtong	198	1
Tak	168	3	Trat	66	1
Petchaboon	320	3	Nakorn Nayok	154	1
Prajuab Kirikhan	152	3	Prachinburi	335	1
Pang-Nga	93	3	Sri Saket	601	1
Ranong	38	3	Kalasin	427	1
Buriram	584	2	Mahasarakam	499	1
Surin	582	2	Loey	211	1
Nakorn Panom	436	2	Kampaeng Petch	173	1
Roi-et	668	2	Krabee	94	1
Skol Nakorn	427	2	Stul	70	1
Nan	240	2	Sub: Total	26,178	474
Uthaidhani	146	2	Mae Hong Sorn	81	-
			Total	26,259	474

Source: Based on information provided by the Bank of Thailand.

Table V-2

Branches of Thai Commercial Banks
at the End of 1966

Name of Commercial Bank	Number of Branches		Total
	In Bangkok and Dhonburi	In Provinces	
1. Siam Commercial Bank Ltd.	7	11	18
2. Wang Lee Chan Bank Ltd.	1	-	1
3. Thai Development Bank Ltd.	13	35	48
4. Bank of Asia Ltd.	4	6	10
5. Siam City Bank Ltd.	10	54	64
6. Bangkok Bank of Commerce Ltd.	5	72	77
7. Bangkok Bank Ltd.	27	28	55
8. Bank of Ayudhya Ltd.	16	16	32
9. Thai Farmers Bank Ltd.	25	28	53
10. Leam Thong Bank Ltd.	2	-	2
11. Union Bank of Bangkok Ltd.	10	1	11
12. Thai Danu Bank Ltd.	5	1	6
13. Bangkok Metropolitan Bank Ltd.	13	-	13
14. Thai Military Bank Ltd.	2	-	2
15. Asia Trust Bank Ltd.	1	-	1
16. Krung Thai Bank Ltd.	10	72	82
17. Hong Kong and Shanghai Banking Corp.	2	-	2
18. Chartered Bank	2	1	3
19. Banque de L'Indochine	2	-	2
20. Four Seas Communication Bank Ltd.	1	-	1
21. Bank of Canton Ltd.	1	-	1
22. Mercantile Bank	2	-	2
23. Bank of China	1	-	1
24. Indian Overseas Bank Ltd.	1	-	1
25. Chase Manhattan Bank, N.A.	1	-	1
26. Bank of America NT. & SA.	1	-	1
27. Mitsui Bank Ltd.	2	-	2
28. Bank of Tokyo Ltd.	1	-	1
29. United Malayan Banking Corporation Ltd.	1	-	1
Total	169	325	494

Source: See Table V-1.

actually that opened by the Chartered Bank (itself a branch of a bank with headquarters abroad) in 1910 in Phuket.[5] The first branch established by a locally chartered bank was that opened by the Siam Commercial Bank in Chiengmai in 1926. At the time, this was a daring move and hotly argued. However, events proved its soundness, and in 1930 the Siam Commercial Bank set up another branch in Lampang.

Very few branches were established during the Second World War, but with the advent of the Korean War branch banking really got into stride. On the average, 35 branch establishments have been set up annually since 1955.

As seen in Table V-1 commercial banks in Thailand operate branches in every province of the Kingdom except Hac Hong Sorn, a remote northwestern area bordering on Burma. Apart from the Bangkok-Thonburi area, there is little correlation between the number of persons inhabiting a province and the number of branches, even though these branches do tend to be located in the more populous towns within a province. Thus, the Songkla province, which includes the important mining and plantation center of Haadyai, has at least 20 banking establishments while Ubol with

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[5] If one considers a foreign-chartered bank to be itself a branch, then the honor of being the first in Thailand goes to the Hongkong and Shanghai Bank, set up in Bangkok in 1888. See Sithi-Amnuai, op. cit., pp. 120ff, for a detailed account of the development of branch banking in Thailand.

more than twice its population, had only six branches at the end of 1965. A point of some importance, which is not apparent from Table V-1, is that there has been a pronounced tendency in recent years to establish branches outside the capital, with the ratio running currently 3:1 in favor of the provinces.[6]

As shown in Table V-2, even though the marginal ratio of provincial to capital branches is now 3:1, the average ratio is only 2:1. Commercial banks with headquarters abroad are precluded from setting up branches in the provinces, and several locally chartered banks do business only in the Bangkok area. Moreover, as a comparison of the totals in Tables V-1 and V-2 suggests, only 20 new branches were founded in 1966 as contrasted with an annual average of 35 in the preceding decade.[7] This decline does not appear to stem from any lack of desire on the part of commercial banks to continue expanding their facilities in the provinces but, rather, from a deliberate policy of the central monetary authorities to control the

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[6]Sithi-Amnuai, op. cit., p. 127.

[7]Between 1954 and 1965 more than 370 branches were established. Note that, while 45 permits were granted in 1966, only 20 branches were actually established (p. V-34). However, the 45 permits were the lowest recorded proportion of requests made.

indiscriminate spread of branches.[8]

Of the 16 locally chartered banks authorized to open branches in the provinces, one, the Wang Lee Chan Bank, is more properly regarded as a family, rather than a commercial, bank. Four other banks have branches only in the capital area, and two additional banks operate only one provincial branch each. Thus, only nine or 10 Thai banks can be said to be actively engaged in the business of branch banking in the provinces.

Operational Characteristics of Branch Banks

Branches of Thai commercial banks fall into two major categories. On the one hand, the head office has subsidiary establishments which it fully controls and supervises, owns and operates, and directs by placing one of its own paid officials in charge. These are branches as that term is understood in the United States. On the other hand, there are a number of subsidiary establishments which have no exact counterpart in Western banking. In these establishments, the mother institution lends its name, its credit status, and other facilities to a local entrepreneur who, while operating under the formal aegis of the headquarters, is in fact a partner in the local operation. This is the agency arrangement that, although decreasing in importance, is still an important part of the branch banking scene in Thailand. Generally, the manager of an agency has greater latitude and more operational discretion than his branch counterpart. He can engage

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[8]This point will receive attention later. See pp. V-20-23.

in a greater range of banking functions. He can make more and more substantial loans than a branch manager and he shares in the profits of the local branch, usually on a 50-50 basis with the headquarters. At the same time, he is usually required to post a substantial personal bond with the mother institution and is, more likely than not, required to contribute to the cost of operation, if not to the initial capital, of the local branch.

While the branch manager may or may not be a local man, the agency manager is almost invariably a local person, most frequently a prominent merchant who continues to ply his trade in addition to his banking activities.

Although the latitude of the agency manager typically exceeds that of the branch manager, both are subject to various operational constraints. These pertain to the types of accommodation, to the maximum size of loan which can be made without prior consent of the headquarters, and to the overall ratio of earning assets to deposits.

With respect to types of accommodation, seldom are these clear or explicit. In one or two cases, the subsidiary establishments are interdicted from making "straight" or fixed term loans and are confined to bills and discounts. In those instances when loans are allowed there is a distinct preference for overdrafts over "straight" loans. Even though the limitations are not imposed explicitly, there seems to be a definite preference for granting business accommodation which is in the nature of self-liquidating

paper for the carrying of trade. On the other hand, headquarters seems to impose few restrictions or regulations with respect to the type and size of the collateral. It would appear, however, that, with the exception of certain kinds of shipping bills, the collateral actually required by managers is predominantly real estate mortgage instruments, with only an occasional personal or business guarantee accepted in lieu of, or in conjunction with, a mortgage deed. In any event, the matter of collateral is handled sooner or later at the headquarters, either when granting prior approval to a loan application or when confirming smaller loans made at the discretion of the branch manager.

The amount of an individual loan which the branch manager can make on his own authority varies considerably from bank to bank, from one branch of the same bank to another branch, and from prescribed rules to actual practice. With one exception, mother institutions set a baht limit on the amount of a single loan, with 150,000 being indicated as the highest amount allowable among Thai banks. The one exception puts the limit on an individual loan at 95 percent of the borrower's deposit at the branch where the loan is to be made.[9]

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[9] There may be a number of reasons why a person would prefer to borrow even though his assets at the bank exceed the amount of the loan. His deposit may be for a fixed period of time, with loss of interest revenue in the event the deposit is reduced prior to the expiry of that time period. Interest payable on deposit is tax-exempt while that due on bank accommodation is deductible for tax purposes.

More significant from the standpoint of developmental finance, are the restrictions placed on the subsidiaries -- both branches and agencies with respect to the overall ratio of accommodation to deposits. The earning assets of branches seldom contain much else beyond over-drafts, bills, and discounts. There is only a modicum of straight loans, and there are hardly any investments. Maximum ratios of these assets to deposits liabilities range from a low of 10 percent to a high of 70 percent. In actuality, however, there is much greater flexibility than these ratios suggest. Even when they are set out explicitly, a considerable deviation is allowed individual branches at different times. The ratios are set mainly as guidelines, and appear to apply to the entire complex of branches of a given bank rather than to each separate branch in particular. Nevertheless, rigid or not, these prescribed ratios do have the effect of inhibiting the growth of bank accommodation relative to deposits. The implications of this state of affairs will be discussed later.

Tables V-3a and V-3b summarize the available information regarding the chief characteristics of Thai branch banks. Much of the contents of the tables have been touched upon in the preceding discussion but one aspect of Thai branch operations emerging from Table 3a merits a separate discussion. This aspect has to do with employment of compradores by provincial banks.

There are at present over 120 compradores attached to commercial banks, and most of them operate in the provinces. Both agencies and

Table V-3a

Frequency of Agencies and Compradores Among Thai Branch Banks

Group	Total Number of Branches	Number of Branches Operating as Agencies or Employing Compradores
Group A - Banks with Agencies		
A_1	76	58
A_2	63	50
A_3	31	3
Group B - Banks employing Compradores		
B_1	81	49
B_2	54	17
B_3	47	33
B_4	10	4
B_5	9	5
Group C - Directly controlled by Head Office		
C_1	52	
C_2	17	
C_3	12	

Source: Compiled from data obtained from field interviews and other sources.

Table V-3b

Selected Operational Characteristics of Thai Branch Banks

Bank	Individual Loan Limit	Total Loan Limit	Restriction on Loan Type
A	10,000	10% of branch deposits	only overdrafts
B	20,000	30% of branch deposits	apparently no fixed term loans
C	25,000	25% of branch deposits	none
D	50,000	30% of branch deposits	no term loans
E	50,000	50% of branch deposits	none
F	50,000	50-60% of branch deposits	none
G	100,000	not clear	none
H	150,000	50-60% of branch deposits	none
I	150,000	70% of branch deposits	none
J	95% of borrowers' deposits	40% of branch deposits	not clear
K	not clear	none	some but not clear

Source: Compiled on the basis of information obtained from Thai commercial banks.

branches appear to avail themselves of the services of the compradore, but the latter employ the bulk of them.

The ambiguous position of the compradore in Thai commercial banking was briefly discussed elsewhere.[10] He is apparently employed by commercial banks both to bring in additional business and to guarantee the repayment of advances by customers whose credit status is unknown to the bank manager. Presumably, the second function is the more important one, inasmuch as most branches are not particularly aggressive in seeking out local borrowers. But even in his capacity of an acceptor or a guarantor, the exact role played by the compradore is by no means clear, partly because loans (used in the broad sense to include all kinds of bank accommodation) are sooner or later reviewed by the headquarters. Doubtlessly, the compradore's acceptance is of importance in determining the headquarters' position with respect to the loan application. But, insofar as much of the branch lending is secured either by commercial paper or by mortgage instrument, the function performed by the compradore can only occasionally be a truly crucial one.

Even less clear is the profit nexus in which the compradore himself operates. In principle, the compradore is supposed to receive 3 percent on the volume of loans made either under his sponsorship or under his

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[10] See Chapter IV, p. 8.

guarantee.[11] Inasmuch as the volume of such business is limited by the amount of the security bond that the compradore himself is required to deposit with the headquarters, it is difficult to see, at first glance, why anyone would want to engage in the compradore business. After all a return of 3 percent on assets cannot appear too attractive to someone well versed in the business affairs of a town. It is true that the bond which has to be deposited with the mother bank can be concurrently engaged elsewhere. This means, for example, that the headquarters may accept a lien on the total operating assets of a well known local trader as bond which permits this trader to continue to obtain the usual rate of return from his business while earning the compradore's commission from these very same assets on a contingent basis, as it were. Sometimes the compradore's volume of business at the branch may exceed the amount of his bond, and he, in his capacity as trader or merchant, may then derive some ancilliary benefits from his compradore activities. Nevertheless, the apparent modesty of the commission paid to the compradore is one reason why rumors abound that he supplements that commission by "kick-backs" from the branch customers.

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[11] In cases where the borrower brought in by the compradore has a gilt-edged collateral, the compradore's guarantee is presumably superfluous.

Those who are prone to take a sinister view of the compradore and his function as an intermediary in branch banking operations point to the incidence of postdated checks among branch banks' assets.[12] This assertion is very difficult to document for a variety of reasons. Official data on the subject of postdated checks are not available or, if available, not likely to be released. Those branch managers who are queried on the subject show a very marked reluctance to provide any precise answers. Postdated checks are not apt to be held prominently among branch assets, particularly at a time of official audit. To the extent that they are issued to the compradore personally, there is no reason why they should appear in the branch portfolio at all.

The significant fact about postdated checks is that their misuse has been liable to criminal penalties since 1954, while with respect to other types of collateral only civil remedies are available to creditors. That is, a branch holding a mortgage deed of a delinquent borrower will have to secure a court order for eviction, repossession, sale, and so on. On the other hand, a delinquent borrower, who writes a postdated check and whose deposit is inadequate at the time his check falls due, may find

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[12]Postdated checks are written with a date sometime in the future, presumably when the loan becomes due. The presumption is that the drawer will, at the date written on the check, deposit sufficient funds to his account at the branch on which the check was drawn.

himself in prison.[13]

At the very worst, an unscrupulous compradore (or, for that matter, a branch manager or agent) may accept a postdated check from a hard-pressed borrower, knowing full well that the borrower is unlikely to make the check good by the date due. The possibility of criminal action is then held over the unfortunate borrower who is thus blackmailed into paying the lender or the guarantor an extortionate interest.[14] More often, the postdated check serves as a convenient device to evade income tax liability or cover up the use of bank funds for purposes other than those for which they were intended.[15]

The use of postdated checks, while certainly quite widespread in Thailand, appears to be concentrated in the unorganized, rather than the organized, financial markets. Branch managers in the provinces usually deny strongly that they ever accept them or, at most, admit that they accept them only occasionally. The anatomy and pathology of postdated checks' usage would certainly throw much needed light on the transition from one

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[13] See Sithi-Amnuai, op. cit., pp. 131-32.

[14] See T. H. Silcock, "Thai Money: Review Article, "Malayan Economic Review (April, 1966), p.109.

[15] Interest income on loans is, of course, taxable. A postdated check can include the interest cost in its face value, thus escaping income tax liability. The possibility that some bank funds could, conceivably, be turned to uses other than those of the bank itself has been touched upon in Chapter IV, p.96.

type of market to another. It is the compradore who plays a key role in this process of transition though, as suggested above, the use of post-dated checks cannot be laid at the feet of the compradore alone.

Be that as it may, the decline in the relative importance of the compradore on the Thai banking scene has been aided and abetted by the monetary authorities who, whether speaking off-the-record or officially, do not conceal their dislike of this intermediary. It is interesting to note that foreign banks, the originators of the compradore system, are using it less and if they have not given it up altogether, they merely have a Chinese manager to help read Chinese signatures or supply credit information. On the other hand, it is the Thai local banks who have recently adopted the compradore system, some of them including a government bank on quite a substantial scale.[16]

Both branches and agencies are subject to periodic internal audit. There is a growing informal clearing arrangement among branches of various banks in the same locality and among branches of the same bank in various localities, but the bulk of interbank clearing continues to be sent via

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[16]The decline of the compradore was also caused by the foreign banks' gradual abandonment of this intermediary as they developed their own credit services.

Bangkok. As a result, a check drawn on a branch will take from one to three weeks to clear.[17]

Thai Branch Banking in the Development Process

As mentioned above, there is no close correlation between the number of people living in a province and the number of branches operated by Thai commercial banks there. Similarly, there exists no apparent relationship between the overall size of a bank and the number of branches it operates. Thus, the Thai Development Bank, whose total assets are about half those of the Siam Commercial Bank, has three times its number of branches. In Table V-4, the relationship between the banks' overall main assets and liabilities, and the same assets and liabilities attributed to branches, can be seen. The figures in this table are at best tentative. They were obtained from sources that could not be expected to give data on a comparable basis for identical periods or on the basis of similar accounting procedures. Nevertheless, the figures are believed to reflect the situation

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[17]The delay in clearing is attributable, in part, to the lack of any formal clearing mechanism in the provinces and, in part, to inadequate postal facilities. It is also possible to argue that some of that delay is deliberate, and designed to prolong control over funds. (See Sithi-Amnuai, op. cit., p.134 where it is suggested that postdated checks are commonly issued by buyers of commodities, the receipt of which is delayed in the expectation, presumably, that by the time the check is presented for payment at the Bangkok Clearing House, the goods will be sold and the proceeds deposited to the buyer's account. Silcock, on the other hand, hints that the delay may well be to the advantage of the branch manager or compradore.)

Table V-4

Thai Commercial Banks - Branch Operations, Fall, 1966

(Million of Baht)

Name of Bank	Time Deposits			Demand Deposits			Loan & Overdrafts		
	Total	Branches	%	Total	Branches	%	Total	Branches	%
Bank of Asia	144	44	30.56	193	41	21.24	269	39	14.50
Siam City Bank	570	525	92.11	347	265	76.37	476	324	68.07
Krung Thai Bank	2,129	1,311	61.58	1,464	1,068	72.95	953	466	48.90
Bangkok Bank	1,566	983	62.77	660	386	58.48	1,404	393	27.99
Bangkok Bank of Com.	621	567	91.30	507	452	89.15	562	401	71.35
Bank of Ayudhya	491	365	74.34	686	378	55.10	750	234	31.20
Thai Farmers Bank	453	357	78.81	513	361	70.37	342	137	40.06
Laem Thong Bank	170	7	4.12	63	3	4.76	235	7	2.98
Union Bank of Bangkok	96	29	30.21	317	79	24.92	278	4	1.44
Bangkok Metropolitan Bank	422	154	36.49	322	81	25.16	460	23	5.00
Thai Military Bank	300	10	3.33	250	5	2.00	300	10	3.33
Thai Development Bank	268	241	89.93	348	247	70.98	416	150	36.06
Total	7,230	4,593	63.5	5,670	3,366	59.4	6,445	2,188	33.9

Source: Compiled from data obtained from Thai Commercial Banks.

as it generally existed in the fall of 1966, and as it exists at the time of writing.[18]

The relative importance of branch banking varies greatly among Thai banks. For demand deposits, the proportion held by branches ranges from a low of 2 percent to a high of 89 percent. Similar range obtains with respect to time deposits, from 3 percent for the Thai Military Bank (which has only one or two Bangkok branches), to over 90 percent for the Bangkok Bank of Commerce.

For all commercial banks (for which data were available), the ratio of all branch deposits to total deposits hovers around 60 percent. On the asset side, however, the importance of branch banking diminishes sharply and amounts to less than 40 percent for all the banks surveyed. This points out the key issue of branch banking in Thailand relative to developmental planning. Commercial banks appear to be less interested in providing accommodation to local business than in collecting deposits from areas outside the capital. This point emerges with much greater force when the

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[18] A particularly cumbersome circumstance is that it was not possible, either in Table V-4 or in the succeeding tables, to obtain the relevant information for the same group of banks. However, the omissions and juxtapositions pertain only to one or two smaller banks and, again, the main picture would not be changed had consistent data been available throughout.

chief assets and liabilities of commercial banks are considered with respect only to those branches which are provincial, i.e., outside the Bangkok-Thonburi area. As seen in Table V-5, the proportion of provincial branch deposits to total deposits is about twice that of loans and overdrafts.

A closer examination of the behavior of individual banks suggests that while those banks with greater commitment to provincial branch banking (as measured by the number of branches and the relative size of branch deposits) generally shows a greater proportion of local earning assets relative to total assets, the correlation is far from perfect. In Table V-6, the pertinent ratios for individual banks were ranked in ascending order. Thus, in Column (a) of Table V-6, the numeral "10" indicates that the Bangkok Bank of Commerce ranks highest with respect to the ratio of its provincial time deposits to its total time deposits. The same bank is next to the highest both with respect to demand deposits, shown in Column (b), and with respect to the relative importance of its provincial earning assets, shown in Column (c).[19] Such sporadic evidence as is available

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[19] Kendall coefficients are as follows:

a and b : = 0.82222
a and c : = 0.57777
b and c : = 0.51111

Spearman coefficients are:

a and b : r_r = 0.9394
a and c : r_r = 0.78182
b and c : r_r = 0.7091

Table V-5

Thai Commercial Banks - Activities of Country Branches, Fall, 1966

(Million of Baht)

Name of Bank	Time Deposits			Demand Deposits			Loans & Overdrafts		
	Total	Branches	%	Total	Branches	%	Total	Branches	%
Siam Com. Bank	863	-	-	386	-	-	524	-	-
Bank of Asia	124	21	16.94	184	28	15.22	327	51	15.60
Siam City Bank	466	338	72.53	359	211	58.77	589	380	64.52
Krung Thai Bank	1119	830	74.17	691	444	64.25	1835	286	15.59
Bangkok Bank	1414	216	15.28	1087	247	22.72	1840	174	9.46
Bangkok Bank of Commerce	554	422	76.17	464	294	63.36	684	408	59.65
Bank of Ayudhya	377	127	33.69	369	79	21.41	1032	103	9.98
Thai Farmers Bank	424	158	37.26	464	148	31.90	934	69	7.39
Laem Thong Bank	167	-	-	72	-	-	237	-	-
Union Bank of Bangkok	94	7	7.45	293	9	3.07	267	-	-
Thai Danu Bank	195	8	4.10	112	2	1.79	240	6	2.50
Bangkok Metropolitan Bank	416	-	-	230	-	-	431	-	-
Thai Military Bank	72	-	-	67	-	-	400	-	-
Thai Development Bank	281	159	56.58	349	164	46.99	537	104	19.37
	6566	2286	34.82	5127	1626	31.71	9877	1581	16.01

*In the provinces only. Exclude branches in Bangkok-Thonburi area.
Source: See Table V-4.

Table V-6

Thai Commercial Banks - Activities of Country Branches, Fall, 1966

Name of Banks	Time Deposits	Demand Deposits	Loans & Overdrafts
	Rank* (a)	Rank* (b)	Rank* (c)
Bank of Asia	4	3	7
Siam City Bank	8	8	10
Krung Thai Bank	9	10	6
Bangkok Bank	3	5	4
Bangkok Bank of Com.	10	9	9
Bank of Ayudhya	5	4	5
Thai Farmers Bank	6	6	3
Union Bank of Bangkok	2	2	1
Thai Danu Bank	1	1	2
Thai Development Bank	7	7	8

*Rank, in ascending order, of: (a) ratio of provincial time deposits to total time deposits, (b) provincial demand deposits to total demand deposits, and (c) provincial loans and overdrafts to total loans & overdrafts.

Source: See Table V-4.

strongly suggests that the ratio of provincial earning assets to a banks total assets tends to be greater for agencies than for branches. Both the Siam City Bank and the Bangkok Bank of Commerce operate a number of agencies the former in particular. The middle position of the Bank of Ayudhya, another institution with a significant number of agencies, may be explained by its modest total of branches, resulting in moderate rankings with respect to both the deposits and the earning assets ratios.

The tendency for agencies to be somewhat more involved than branches in the provision of local credit is not particularly surprising. As seen in Table V-3, an agency manager is given greater latitude with respect to both individual and overall loan limits and, like the local businessmen, tends to be more interested in developing local trade, especially as he has a direct stake in the profits of the branch he manages.[20]

Insofar as the earning assets are substantially below deposits, in most subsidiaries operated by commercial banks in the provinces, interest payable by the branch exceeds substantially the interest received on loans, discounts, and overdrafts. Hence, provincial operations per se as money

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[20]The entire question of the incentives of branch managers is extremely difficult to pin down. In numerous field interviews, the managers of branches, as distinct from agencies, could not relate their performance to their rewards in any precise fashion. This applies to such factors as salaries, promotion, or the locale of posting. Their salaries were quite modest, though many of them enjoyed other emoluments in kind.

losing propositions.[21] At the same time, Thai commercial banks continue to clamor for the right to establish more and more branches. The inescapable conclusion is that provincial subsidiaries are viewed primarily as a means of collecting resources from the countryside and transferring them to Bangkok, although the banks, even at the headquarters level, do not make full use of their available resources.[22]

This state of affairs is of concern to the development planner for several reasons. The emphasis on channelling local funds to the capital inhibits the development of new lines of banking activity in the provinces and deprives local businessmen of needed accommodation. The concentration of funds in Bangkok tends to deflect these funds to purposes other than those which would be dictated by development priorities. By helping to drain the countryside of investible funds, the branch operations thereby accentuate further the somewhat lopsided economic growth of the country and aggravate the kurtosis of the distribution of both regional and personal incomes.

Even though, as indicated in Table V-3, headquarters seldom formally interdicts any particular kind of accommodation, earning assets of branches

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[21] The accounting device employed in this connection is that of a "headquarters account." A provincial branch will, typically, list among its assets such an account which contains the excess of deposits collected over the loans disbursed. The headquarters account is supposed to bring interest revenue to the branch, to the tune of 5 to 6 percent per annum. The interest is not listed as revenue but is added to the principal.

[22] See, Chapter IV, pp. 66 ff.

usually consist predominantly of discounts, financing of shipping bills, and overdrafts. In very few cases will the branch make a loan to a manufacturing enterprise, or take advantage of the special rediscounting facilities offered by the Bank of Thailand, or finance a nascent enterprise merely on the basis of good prospects for success rather than land collateral. Only one or two banks show any interest in expanding their activities in new directions, such as, for example, the financing of supervised group credit to farmers. There is little awareness that one of the key functions of a commercial bank is to develop economically the area in which that bank operates.[23]

When the bank funds are concentrated in Bangkok, they certainly serve to raise the overall ratio of commercial bank earning assets to deposits. But this, as argued in Chapter IV does not preclude the Thai commercial banks from underutilizing their capacity, nor from concentrating their activities on speculation and the financing of real estate construction.[24]

Information on the ownership of deposits in provincial branches is not readily available. But, it would appear that at least 50 percent of fixed deposits, particularly those lodged with the branch for 12 months or

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[23] Most of the branch managers interviewed in the field were keenly aware of the role they have been assigned to play that of transmitters of funds to Bangkok. Many were chafing at the constraints, formal and informal, which inhibited them from opening new lines of business. Several indicated that they thought that even relatively risky and complex operations, such as those of agricultural credit, could and should be undertaken.

[24] It is interesting to note that in those areas of the Thai countryside which are booming under the impact of defense--connected construction, the financing does not come from the local branch but rather from the headquarters, if indeed it comes from the parent bank at all.

or longer, can be attributed to persons who are not resident in the urban center in which the branch is typically located. A substantial proportion of these depositors appears to be net savers. That is, they seldom, if ever, borrow and are content to let their savings accumulate while earning 7 percent per annum. To the extent that more precise data on the distribution of deposits by type and origin could be developed, the crucial process of transferring resources from agriculture to the rest of the economy could be better understood and gauged. But there is little doubt that large resources, with potentially high net marginal product for regional development are diverted to socially less productive ends. If it were possible to induce the owners of these funds to invest their resources locally, there is good reason to believe that the return on their investment would exceed that payable by the branches. Such an inducement, both in terms of available opportunities and available instruments, is not currently being offered by any Thai financial institution, let along by the branches of the commercial banks operating in the provinces.

Implications for Development Planning

There is serious question about whether branch banks in a developing country such as Thailand should act mainly as depositories and transmitters of provincial funds to the headquarters or, instead, be prodded into participating more actively in the developmental process.[25] This prodding

[25] Of course, branches do perform functions other than merely collecting and transmitting deposits. They provide for safe custody of funds, pass requests for productive loans on to the headquarters, supervise the existing loans made by the headquarters, etc. Nevertheless, the collection and transmission of funds appear to be their chief functions, and all others are distinctly secondary.

may well adopt a dual approach. On the one hand, Thai commercial banks should be encouraged and given incentives to participate more actively in developmental financing on the provincial level. On the other hand, the monetary authorities should consider the use of control instruments to insure that the provincial subsidiaries of Thai banks behave as true credit and financing institutions rather than as mere branches of a saving bank or provincial treasury.

Providing incentives and inducements to branch banks so that they will lend to local enterprise more frequently and utilize local resources more productively is a complicated task because, by tradition and training, even the parent institutions are ill-equipped to provide the kind of finance which is most desirable for developmental purposes. Under existing circumstances, it is difficult to conceive of the provincial branches doing much balance sheet, term-lending to manufacturing or other new enterprises. Moreover, developmental finance often connotes acquisition of relatively illiquid paper which the branches should not be persuaded to hold in large proportion to their total assets. Even after taking into account all qualifications, there seems to be ample opportunity for commercial bank branches to pursue more aggressively business such as agricultural lending, financing the operating capital requirements of local manufactures, and others.

Perhaps the most promising avenue of this kind is that which would link provincial branch operations with those of a specialized developmental institution. For example, a branch could develop its agricultural credit

activities in cooperation with the Bank for Agriculture and Cooperatives. The Bank would concentrate on training the necessary supervisory personnel, providing the longer-term credit, and handling the other activities which the commercial banks cannot be expected to do profitably.[26]

Another interesting possibility is that which would tie in the provincial activities of the Industrial Finance Corporation of Thailand (IFCT) with those of the branch banks.[27] Project evaluation, grace period of loan, and, perhaps, contingent liability would be assumed by the IFCT, while the local branch would contribute to the loan and supervise it on the spot.[28]

The second approach that of having Thai monetary authorities employ control instruments, could be implemented more promptly. As mentioned previously, Thai commercial banks are anxious to expand their network of branches for a variety of reasons--not all of them economic. The Minister of Finance grants the permit to open a new branch; however, he usually abides by the recommendation of the Bank of Thailand. The set of regulations which govern the system of granting permits make it remarkable both in terms of comprehensiveness and vagueness. Whether or not a permit is granted

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[26] See Chapter III, p. III-109.

[27] The Industrial Finance Corporation of Thailand is discussed in Chapter VIII.

[28] This possibility was suggested to the author by Somkiert Limsong of the National Economic Development Board (NEDB).

appears to depend upon a host of considerations, including the applicant's former record, his competitive position in the past and present, the economic situation, prospects of the locality, and so on.[29] But there are no clear-cut rules or criteria which would define these considerations. Perhaps this is as it should be. The power to grant permits for new branches

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[29] According to Section 7 of the Commercial Banking Act B. E. 2505, a commercial bank authorized to undertake the business of commercial banking may establish a branch only with the prior approval of the Minister of Finance. And an application for such permit shall contain details, as stated in Article 3 of the Ministry of Finance Notification issued under the said Act, as follows:

1.1 Expected deposits and sources of such deposits
1.2 Main businesses to be undertaken by the branch
1.3 Scope of operation
1.4 Power granted to the executive officers
1.5 Names, working records, and qualifications of the executive officers
1.6 Period during which the branch expects to earn enough income to cover preliminary expenses

2. Aside from the requirements mentioned above, in granting the permit the Minister shall be satisfied that:
   2.1 The economic development of the locality justifies the opening of an additional branch of the commercial bank, and the opening of a new branch shall not endanger deposits or the continuance of their operations in raising income of the existing banks or branches
   2.2 The bank applying for a permit to open a branch shall be in a position strong enough to warrant the opening of a new branch, and the increased investment in fixed assets shall not endanger the stability and the cash position of that bank
   2.3 The cooperation that the bank has given with regards to regulations and directions, the control that the bank has carried over the operations of its branches and the contribution of the bank branches have added to the economic development of the districts wherein they have operated
3. Each year, applications for permits to open commercial bank branches are considered in four lots according to the periods in which they are submitted namely:
   3.1 Applications submitted in designated period around February 15
   3.2 Applications submitted in period around May 15
   3.3 Applications submitted in period around August 15
   3.4 Applications submitted in period around November 15

All applications submitted within the periods mentioned above are given equal treatment. Applications submitted for consideration which fall within any other period shall not, under any circumstance, be registered. If the commercial bank so concerned, nonetheless, wished to open a branch in the same locality for which it was formerly refused a permit, the commercial bank can submit a new application in another period if it wishes.

is a valuable one and, hence, one which should be used with discretion. That it had been so used is apparent from Table V-7.

There is, then, a prima facie case for the monetary authorities to intimate to the banks that aggressive development of local business will, henceforth, become a prime factor in their examination of applications to open branches. Inasmuch as the future conduct of a branch cannot be determined at the time an application is submitted, it would seem to make sense to grant permits for a limited number of years, the continuance of the permit being subject to review at the end of the stated period. After all, there is nothing in the law or custom which would compel the monetary authorities to grant a business privilege in perpetuity. Many such concessions and privileges are now being granted, both in Thailand and elsewhere, for a limited time only. There are ample precedents in such fields as taxation, customs, patents, and copyrights.

It could be argued that it is difficult, if not impossible, for a commercial bank to make a heavy investment in a branch operation without knowing whether or not such an operation will be allowed to continue beyond say five years. This is a cogent argument, but the same sort of problem arises in the case of the tire factory which obtains a special import concession for a limited period of years. Moreover, as indicated earlier, most branches lose money in their provincial operations and are profitable only in the sense that they manage to obtain relatively cheap funds for use by the headquarters.

Nonetheless, the granting of permits for a limited time only would

Table V-7

Thai Commercial Banks - Applications for Permits and Permits Granted to Open Branches, 1962-1966.

Year	Number of Applications	Number of Permits Granted	As % of Applications
1962 (May-Dec.)	38	12	32
1963	36	20	56
1964	36	14	39
1965	64	29	45
1966	156	45	29

Source: Bank of Thailand.

have to be handled gingerly. It would probably be inappropriate to lay down specific rules of good behavior, such as requiring the branch to have at least 60 percent of its deposits lent locally by the end of a five-year period. Rather, the monetary authorities would reserve the right to review the entire picture five years hence and, in the event that external indices suggested that the branch fell woefully short of desirable performance, they would invite the branch and the headquarters representatives to state their positions. Refusal to renew a permit would be resorted to very rarely and only in cases of blatant non-adherence to the guidelines set down by the monetary authorities. After all, even when such an extreme measure is employed, it can hardly mean the collapse of the entire bank.

The importance of the suggested control instrument would thus lie not in rigid rules and ruthless elimination of branches at the expiry of their probationary period, but in suasion, guidance, and example backed, however, by the possibility of a real sanction in extreme cases.

The commercial banks will be given notice that provincial branches must serve the developmental interest of the province rather than the interests of headquarters exclusively. The putting-on-notice should in itself be instrumental in improving the operational performance of many branch banks.[30]

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[30] It appears that the actual performance of branch bankers is at least partially conditioned by the behavior of their competitors, even though the inclinations of some may lie elsewhere. Thus, it is conceivable that were all banks put on notice that provincial developmental financing is

Neither the tie-in with developmental institutions nor the probationary granting of branch permits can be expected to effect drastic changes in the operations of provincial banks in the near future. Most of the people who run these banks are hard working, competent people who have the long-term interests of the country very much at heart and who honestly believe that they are doing the best they can. In a sense, they are, indeed. Thai commercial banking has developed to the point it is today by force of circumstances, rather than by any sinister plot to impede developmental financing. To veer now toward developmental planning, much effort and patience must be expended by both the banks

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30 (continued)

to be taken seriously, a certain number of bankers will sigh with relief and act vigorously upon the beliefs which were held in check by the imagined reaction of their competitors. This, perhaps nebulous point, is of some importance in other contexts as well. See, for example, J. G. Gurley, "Financial Structures in Developing Economies", in David Kruine, ed., Rehovoth Conference on Fiscal and Monetary Problems in Developing States (New York: F. A. Praeger, 1967) p. 9.

In the case of Thailand, the case for granting permits to open branches for a stated period of years, subject to subsequent review, can be further strengthened by the mention of yet another general point. The monetary authorities of the Kingdom do not dispose of too many effective control instruments in their dealings with financial institutions. Of these instruments, the branch permits are among the most potent ones. It makes sense to retain their potency as long as possible.

and the monetary authorities.[31] More can be lost than gained by drastic measures and sudden attempts at "fundamental" reform. The suggestions made here are modest ones and are designed to insure that the real contribution of Thai banking to the economic life of the country is enhanced, rather than tampered with.

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[31] One thing which the monetary authorities ought to reconsider is their decision of a few years ago not to grant permits for new subsidiaries to agencies, but only to branches. While there have been occasional abuses and instances of slack agency management in the past, such abuses and sloth were not confined to agencies. In fact, in some parts of the country and for some banks, the agency record is far superior in almost every respect to that of competing branches. Moreover, as argued in the text, agency managers have, prima facie, greater incentives to develop local business and greater interest to engage a higher proportion of local deposits in earning assets. What is needed is the removal of the rigid interdiction against agencies and a consideration of each application on its merits.

It should be noted that the probationary granting of permits suggested in the text is not meant to apply to branches already established, but only to those which might be set up after the suggested measure was put into operation. This arrangement could, however, be combined with one where, after a period of years, a branch could revert to the status of an agency.