2-3. Taxation and Tariff

2-3-1. Taxation

(1) Tax System

The main taxes are divided into domestic taxes, corporate income taxes, personal income taxes, business taxes, various excise taxes, and revenue stamp taxes, and duties are divided into export duties and import duties.

Taxes are administered exclusively by the central government under the authority of the Ministry of Finance. Administrative work for taxation is handled by the Revenue Department, Excise Department, and Customs Department, but amendments to the tax system and other fundamental matters regarding tax policies are handled by the Fiscal Policy Office.

The tax structure features a low percentage of direct taxes and a high percentage of indirect ones such as business taxes and excise taxes. In fiscal 1986, 22.5% of revenues came from direct taxes and 77.5% from indirect taxes.

The percentage of personal income taxes in total tax revenues was 12.5% in fiscal 1986, while that of corporate income taxes was just 10%. Thailand is unable to depend on income taxes, corporate taxes, and other direct taxes for most of its fiscal revenues as is done in the advanced countries. The reason for this is that about 70% of its total population are engaged in primary industries such as agriculture and fisheries and thus have low income levels in general. Further, self-employed persons and companies are not very conscious of their obligation to pay taxes and lack sufficient accounting know-how. Due to these and other reasons, it is difficult to secure direct taxes.

The private sector claims that, in addition to the lack of accounting know-how on the part taxpayers and companies and the low awareness of the obligation to pay taxes, there are unclear matters and unfair points in the progressive and high tax rates and the methods of tax collection. In particular, there is much contention on the business tax, which is assessed on each state of transaction. The tax authorities also have been studying tax reforms for a few years now, based on a fundamental review of the business taxes.

Here, we will touch upon the structure of the business taxes and problems therein.

(2) Structure of Business Taxes

The business tax was introduced back in 1932. It taxed all commodities except unprocessed food in all stages of transactions up to retailing, taking as a sales tax 1% of the total sales or total revenue, except for unprocessed foods. A wide tax rate of 0.25 to 15% was established for the service sector. In 1961, major tax reforms were implemented which were removed transactions at the retail stage from the coverage of the business tax and changed tax rates to a range from 1.5% for primary vendors of printed matter and publications to 40% for automobile vendors, thus establishing different rates for each industry and transaction. The average tax rate at the time was 7%.

In 1976, the government instituted structural reforms to simplify the taxes by dividing them into ones for raw materials, intermediate goods, and final goods. The business taxes thus came to be assessed by class according to the following three schedules:

Schedule 1: Primarily final products, 7%, same rate as in the past (current tax rate of 9%)

Schedule 2: Mainly machinery in the stage of final or intermediate goods, 3% (current 5%)

Schedule 3: Some final products, building materials, tools, and other intermediate goods, and products used in the fisheries industry, 1.5% (current 1%) (Note.)

(Note) From November 1983, it has become possible to have the 1.5% minimum tax rate applied to almost all materials and parts, but the application procedures are complicated and few companies are making use of the system. It often has been pointed out that the distinction between semifinished products and finished products is also not clear.

Products not falling under the above three schedules were exempted from business tax, but now are subject to a current flat 1% business tax on their value.

The business tax is also assessed on imports and exports of some products. The tax schedule is based on the "CIF price + import duties + standard profit".

Individuals and companies obligated to pay business taxes must register their businesses for each business establishment within 30 days from the start of business record and keep books on their total revenue. Taxes must be filed and paid for each month by the 15th of the following month.

(3) Problems in Business Taxes

The Thai government is currently studying introduction of a VAT (valued added tax) and major reforms of the tax system. Industry welcomes the introduction of a VAT in principle, but has various conflicting opinions from various different standpoints at the detailed level. Further, it is expected that the introduction of a VAT will become a major political issue as the plans for the same become clearer in view of the fact that the scope of persons covered by the tax will be much larger than the scope of persons currently taxed. Right now, the details on the implementation of a VAT and the timing of the same are not clear, but the introduction of a VAT should eliminate some of the problems in the business taxes. These problems in current business taxes are explained below.

The biggest defect in the system of assessment of business taxes is that assessment is made at each stage of transaction against the total revenue or total sales, with no deductions for expenses allowed. Therefore, the current system is remarkably unfair with respect to competition among manufacturers. Since business taxes are assessed at each stage of transaction from the primary subcontracting to final assembly, businesses involving numerous stages of transactions bear a heavier tax burden. The fewer the stages of transaction, the lighter the tax burden, so the practice has spread of vertical in-house production or switching from procurement of domestic goods, with their heavy business tax burdens, to imports with lighter tariffs.

Looking at one of Thailand's leading industries, textiles, manufacturers are engaged in comprehensive, vertical operations from the raw materials to spinning, weaving, and dyeing. In general, joint spinning and weaving and vertical production systems are considered low in economic efficiency as production systems, but despite this, vertical production has become the prevalent form of operations in Thailand. One of the reasons for this is the undeveloped state of subcontractors, but the business tax system is also a major factor.

Under the current tax system, in general, it is more expensive to build up affiliated subcontractors than to use imported parts, which are reliable in quality and delivery, taxed a single time, and lower in taxes than with business taxes, or than to produce parts in-house and form a vertical production system. This situation has become a major obstacle to the formation of supporting industries and affiliated subcontractors.

2-3-2. Tariff System

Thailand's tariff system is based on the Tariff Act and the Tariff Schedule Act. The classification of goods is based on the CCCN, but the Harmonized System was introduced and implemented from January 1988. A import tariff of 25 to 60% is applied to the majority of commodities. Recently, reflecting the increase in investment, Thailand has been making frequent reviews of the system of taxation of imports and tariffs as a means of protecting new industries and suppressing imports.

Export duties are assessed on seven items: rice, scrap iron, leather, rubber, lumber, rice flour, and fish powder.

There are two tariff systems: one by value and one by volume. The ad valorem system is used for almost all commodities. When a commodity is labeled by both value and volume, the system giving the most revenue is adopted. The ad valorem tax is in principle based on the wholesale cash price (price by which importer wholesales the commodity on domestic market after adding fixed margin). In actuality, the invoice used in reports to the customs authorities is used as evidence. At this time, the importer reports all expenses and costs incurred until unloading the imported cargo from the ships. The actual standard for assessment, with the exception of automobiles etc., is the CIF price.

There are two types of taxes on imports: [1] those assessed on imported products of the same type as products and produce made by domestic parties encouraged by the BOI under the Investment Promotion Act (including similar products and alternative products in a tax range up to 50% of the CIF price or the producer's cost, enforced for up to one year from the date of publication in the official gazette) and [2] tariffs and various other taxes established by the Ministry of Finance.

Note that when importing goods in Thailand, one is assessed not only tariffs, but also business taxes, and there is a further municipal tax over and above the business taxes (10%).

The methods of calculation of the import duties and business taxes are as follows:

[1] CIF price x ad valorem tax rate or import quantity x specific tariff rate = import dury

[2] (CIF price + import duty) x standard profit margin = standard profit

[3] (CIF price + import duty + standard profit margin) x business tax rate = business tax

[4] Business tax x additional municipal tax rate (10%) = municipal tax

[5] Total amount of taxes to be paid upon customs clearance = import duty + business tax + municipal tax

There has been criticism regarding the method of assessment of taxes upon imports asserting that the anticipated profit based on the standard profit margin is too large.

Table I-2-12. Taxation in Thailand

	1980	1981	1982	1983	1984	1985	1986
Taxation:	88,473	100,906	105,076	129,062	136,246	144,947	154,202
Income taxes:	16,880	22,484	24,790	27,870	31,810	35,231	34,767
Personal	7,268	9,036	12,011	14,672	17,194	19,841	19,218
Corporation	9,612	13,448	12,779	13,198	14,616	15,390	15,549
Indirect taxes:	71,593	78,422	80,286	101,192	104,436	109,716	119,435
Import duties:	19,463	21,896	20,183	28,014	29,692	30,742	31,106
of which:							
Mineral fuel and lubricants	2,806	2,167	1,130	1,041	1,956	673	n.a.
Chemicals	3,781	4,744	3,953	3,898	5,397	6,246	n.a.
Machinery	6,430	7,887	6,636	9,893	12,123	12,510	n.a.
Manufactured goods	4,107	4,531	3,350	3,705	4,530	4,832	n.a.
Export duties:	3,379	2,811	1,794	2,619	1,862	1,079	806
Rubber duties	2,424	1,459	677	1,404	1,161	571	n.a.
Other export duties	955	1,352	1,117	1,215	701	508	n.a.
Business taxes	18,363	21,521	22,487	25,698	30,191	29,515	28,150
Selective sales taxes	21,308	24,767	28,253	31,851	34,209	37,642	46,332
Fiscal monopolies	2,888	1,984	1,863	2,631	2,603	2,765	3,040
Royalties	4,169	3,312	2,763	2,270	2,554	3,726	2,098
Licences and fees	805	807	1,397	6,028	778	1,784	5,426
Other taxes	1,218	1,324	1,546	2,081	2,547	2,463	2,477
Sales and charges	1,353	1,475	2,133	2,129	2,131	2,545	2,906
Contribution from government enterprises and dividends	2,319	3,495	3,309	3,524	3,509	6,251	5,836
Miscellaneous revenue and income	3,412	5,967	5,462	8,721	6,356	6,909	6,981
Total revenue	95,557	111,843	115,980	143,436	148,242	160,652	169,925

Source: Bank of Thailand

2-4. Financing

2-4-1. General

Companies raise funds for their activities through loans from financial institutions such as the commercial banks and finance companies and through loans from individuals. The public institutions providing financing for manufacturers are the Industrial Finance Corporation of Thailand (IFCT) and the Small Industry Finance Office (SIFO) under the Ministry of Industry. In addition, the Bank of Thailand has established a loan based on refinancing of industrial bills through the commercial banks and the IFCT, and IFCT has schems for export industry and credit guarantee.

Here, a summary will be given of institutional financing, the most powerful tool in industrial promotion, in particular the system of financing for small and medium sized enterprises, which account for the majority of companies in the industrial structure of Thailand, rather than the financing of large corporations, which have various fund raising means available to them.

A look at the state of financing in Thailand by financial institutions shows, as seen below, the commercial banks accounting for 75% of the financing, followed by the finance companies with 14%. On the other hand, the IFCT and the SIFO together account for just 1% or so, i.e., are very small in scale of activities.

Below, a look will be taken at the IFCT, SIFO, the industrial bill refinance system of the Bank of Thailand, and the Small Industry Credit Guarantee Fund (SICGF), established to compensate for the lack of collateral of small enterprises.

2-4-2. IFCT

As a financial institution for industrialization, there is Industrial Finance Corporation of Thailand (IFCT, established in 1959). The IFCT is a private financial institution organized as a joint share company and was established under the IFCT Law. It was set up under the recommendation of the World Bank and in the beginning received technical and capital assistance from the International Finance Corporation (IFC) and U.S. Agency for International Development. The IFCT provides financing to private industry and is the only industrial development financing institution in Thailand which provides medium- and long-term funding.

The IFCT Law provides as follows regarding the objects of the IFCT:

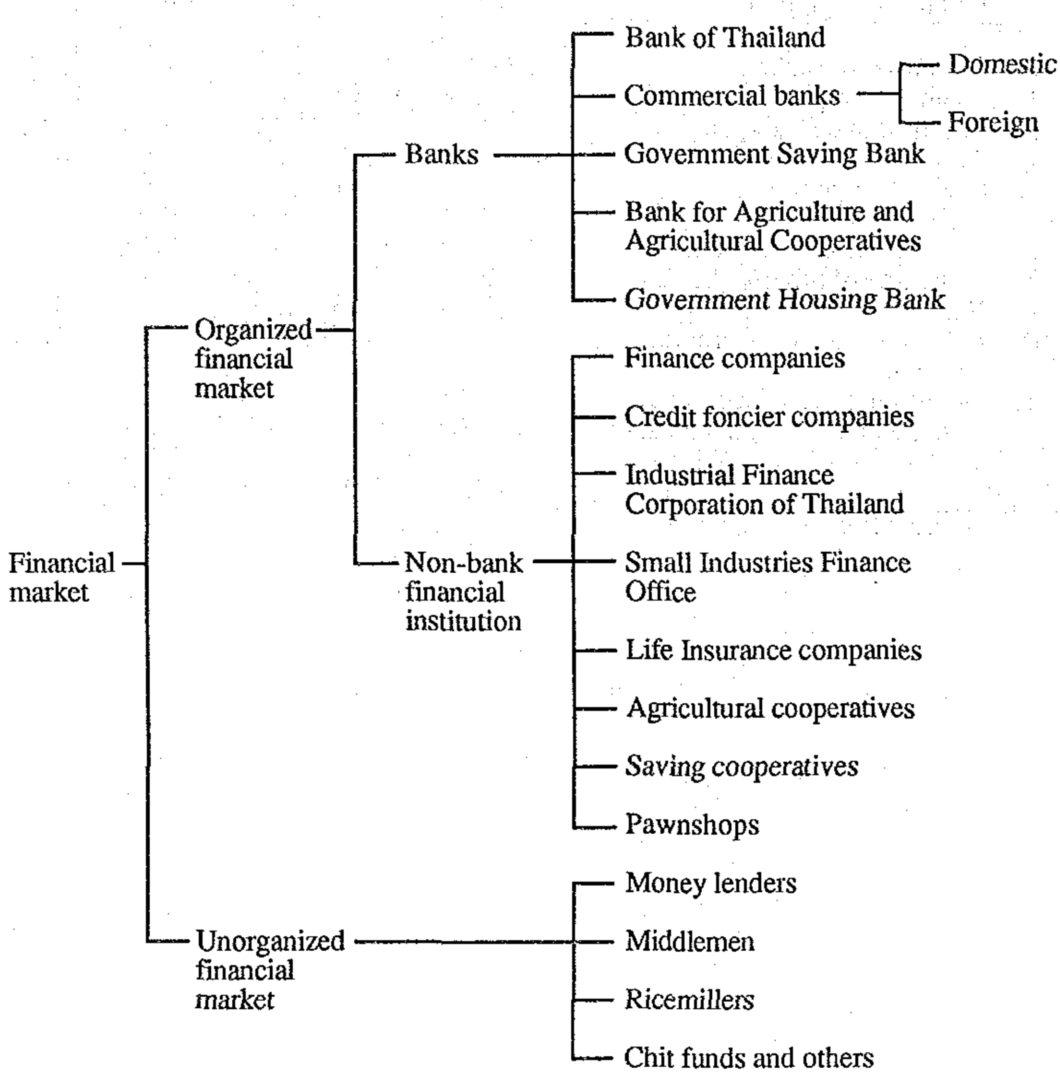
[1] To assist the growth and modernization of private enterprise

Credit by Financial Institutions (Ratio, %)

	Financial institution	1981	1982	1983	1984	1985
1.	Commercial Banks	69.02	69.19	72.70	74.69	74.99
2.	Finance Companies	17.74	18.35	16.42	14.94	14.08
3.	Life Insurance Companies	0.91	0.94	0.92	0.98	1.04
4.	Agricultural Cooperatives	1.13	1.05	0.87	0.81	0.84
5.	Saving Cooperatives	1.41	1.54	1.56	1.73	1.95
6.	Rawnshops	0.85	0.73	0.59	0.55	0.66
7.	Credit Foncier Companies	0.79	0.82	0.66	0.47	0.40
8.	Government Savings Bank	0.57	0.47	0.60	0.19	0.20
9.	BAAC	3.84	3.63	3.10	3.08	3.11
10.	Industrial Finance Corporation of Thailand	1.17	1.08	0.89	0.96	1.13
11.	Government Housing Bank	2.55	2.19	1.68	1.59	1.61
12.	Small Industries Finance Office	0.02	0.01	0.01	0.01	0.01
TOTAL		100.0	100.0	100.0	100.0	100.0

Source: Bank of Thailand

Chart I-2-3. Structure of the Financial System in Thailand



Source: Central Bank

[2] To promote the mobilization of private capital domestically and overseas so as to increase industrial capital and to build up a capital market.

(1) Capital and Shareholder Composition

Capital: 1.3 billion bahts (all paid in) (as of end of December 1986)

Shareholder composition by type as of end of 1986

Commercial banks:	42.5%
Finance companies:	12.6%
Ministry of Finance:	15.1%
Insurance companies:	2.3%
Private enterprises:	19.2%
Private individuals:	8.3%
(Domestic/Foreign ownership)	
Thai domestic:	60.0%
Foreign:	40.0%

(Source) IFCT, "Introduction to EIMP - Thai Export Industry Modernization Program" (May 1987)

(2) Total assets: 17.9 billion bahts (as of end of December 1986)

(3) Range of activities

a. Loans: The loans of the IFCT are limited to private enterprises. Most of the loans are medium and long term ones, primarily for capital investment. Loans for operating funds are also available. (However, the loans of the EIMP system are only for capital investments.)

b. L/C opening: The IFCT can open L/Cs when a private company receives credit from a domestic or foreign financial institution or machinery supplier etc. The guarantee fee is 1%.

c. Credit guarantees for banks (by special fund account): This is aimed at the promotion of small sized industries and covers loans of 5 million bahts or less. Portions of loans from banks which cannot be covered by collateral are covered by this guarantee. The guarantee fee is 1.5%.

d. Liquidity participation: The IFCT can invest in a private company in accordance with that company's request. However, the equity of the IFCT may not exceed 10% of the total capital of the company and the total value of the equity may not exceed the capital of the IFCT.

e. Other activities: The IFCT, in addition to the above business, provides advice on management, technology, and marketing to private companies, surveys project financing, arranges group financing for large sized projects, etc.

(4) Features

The IFCT was established relatively long ago, but it belongs to institutions of small scale funding among the industrial financial institutions of Asia. Further, although it has increasingly been raising funds domestically, it still relies on overseas funding for over 40% of its funds - a high degree of dependence.

The IFCT, seen from its shareholder composition, is primarily operated on a private sector basis. But since it receives government financing and government guarantees, it is organizationally and personnel-wise strongly guided and restricted by the government. Its basic loan policies fundamentally follow the development policies of the government. Recently, the IFCT has been operating on the following main policies: [1] promotion of agro-industries, [2] loans to promote regional dispersion of industry, and [3] expanded loans to small sized projects - all of which reflect the basic government policies of the economic and social development plan. This is different from the inherent profit-oriented operations of private banks.

On the other hand, the IFCT participates to a considerable extent in the drafting of development policies. The chairman of the IFCT is a member of the board of the Board of Investment (BOI) and the president of the IFCT is the chairman of the Thai Securities Commission and a member of the BOI's Investment and Economic Planning Subcommittee. In addition, staff of the IFCT participate in the formulation of development plans of the National Economic and Social Development Bureau (NESDB).

While the IFCT is basically a private sector operation, it has the somewhat unique function of supplying industrial funding along with government development policies. The government thus has provided the following preferential treatment to the IFCT of support its activities:

- [1] Government guarantee on IFCT's borrowings of overseas funds
- [2] Covering of exchange losses resulting from overseas loans
- [3] Interest-free or low interest funding (direct or through Bank of Thailand)
- [4] Guarantee on bonds issued by IFCT
- [5] Designation of IFCT bonds as suitable collateral when commercial banks borrow from the Bank of Thailand
- [6] Exemption of IFCT from corporate taxes

(5) Loan Activities

The IFCT invests in and provides loans to private enterprises engaged in industrial production using its fund resources. The loans are mostly medium and long term funding for capital investment and are at interests considerably flexible than those of loans of commercial banks. As of 1988, the usual interest rate on loans of the IFCT to the industrial sector was 9 to 13%. As opposed to this, the interest rates on loans of commercial banks are 11.5 to 14%.

<Basic Guidelines> (Source: IFCT: IFCT's Twentieth Anniversary Issue, p. 44)

[1] The basic principle in investments and loans is "solidity"

[2] The upper limit on total debts is six times the total capital (paid in shares + reserves + retained profits)

[3] Concentration of investments and loans in any specific field is prevented and the fields of investment and loan are diversified.

- a. Loans to any specific one company are limited to 25% of the total capital.
- b. Investments in any specific one company are limited to 10% of the total capital.
- c. Total investment in shares may not exceed the value of the total capital.
- d. The lower limit on loans per case is normally 1 million bahts.

[4] Loans to the local regions are to be encouraged.

[5] The agriculturally based industries are to be promoted.

[6] Loans to small sized projects are to be expanded.

(6) Fiscal Resources

The fiscal resources for the loans of the IFCT may be roughly divided into two categories: [1] funds on hand such as profits arising from investment and loan activities, increased issuance of shares, etc. and [2] loans from domestic and overseas sources.

Due to the difficulty in raising low cost funds domestically, the IFCT has been raising funds through issuance of bonds (5-year bonds). Loans from overseas are very risky due to the fluctuating exchange rates, so the IFCT tends to restrict itself to superlow interest official assistance from the U.S., Japan's OECF, etc. It is also increasing its fund raising activities domestically through bond flotation. Its bonds are received by local commercial banks, foreign banks, insurance companies, and finance companies. Due to the high operating costs in medium and long term financing, the overall procurement cost is higher than the procurement costs of commercial banks.

Under the IFCT Law, the IFCT is supposed to provide financing to private enterprises for any promising project which contributes to the national economy, regardless of the size of the enterprise. However, a look at the past loans shows that most have been for large sized projects. Due in part to the lackluster performance of the SIFO,

Table I-2-13. Main Fund Resources of IFCT

(Unit: Million Baht)

	1981	1982	1983	1984	1985
Capital Resources					
Capital account	774.45	1,135.24	1,237.73	1,781.51	2,312.5
Domestic borrowings					
Commercial banks	--	--	--	--	--
Bank of Thailand	139.85	193.37	156.87	119.08	81.5
Government	170.27	169.27	164.51	159.75	155.0
AID	9.00	8.00	7.00	266.00	265.0
Bonds and debentures	36.00	100.00	100.00	300.00	528.5
RABO Bank	--	--	--	572.25	572.3
Total	1,129.57	1,605.88	1,666.11	3,198.59	3,914.8
Foreign borrowings					
Mitsui FIN	--	--	--	--	347.1
Citi Bank	--	--	--	--	621.0
KfW	284.41	332.02	351.65	357.12	531.1
International Bank of Reconstruction and Development (IBRD)	894.23	1,054.62	1,037.60	1,004.87	907.6
Asia Development Bank	801.02	821.69	982.18	1,633.69	2,029.4
Government of Denmark(1)	15.76	75.80	63.13	64.41	77.8
Japan Export Import Bank	828.35	867.25	899.99	849.07	756.6
Yen syndicate loans and Japan Long-Term Credit Bank	681.93	677.75	1,033.09	1,824.04	2,152.8
Singapore syndicate loans	285.11	285.11	241.25	197.39	153.5
Others	245.34	256.78	389.04	382.63	412.8
Other debts	366.33	613.00	764.12	1,591.36	3,236.1
Total	4,402.48	4,984.02	5,762.05	7,904.58	11,225.8

Note: (1) including loans from Belgium government
Source: IFCT

Table I-2-14. Applications of Funds of IFCT

(Unit: Million Baht)

	1981	1982	1983	1984	1985
Cash on hand and bank account-deposits	13.35	6.96	16.96	46.28	55.6
Time deposits and short-term bills	736.22	1,110.00	1,522.65	3,262.61	4,090.5
Government bonds	1.60	1.60	15.87	21.50	57.8
Loans to private sector	4,300.91	4,700.50	4,919.45	6,094.79	7,847.9
Investments	123.88	205.96	209.57	220.70	244.8
Fixed investments	52.24	49.44	53.11	56.06	96.4
Other assets	303.85	514.44	690.55	1,401.23	2,567.6
TOTAL	5,532.05	6,588.90	7,428.16	11,103.17	14,960.6

Source: IFCT

which was established in 1963 to provide institutional financing to the small and medium sized enterprises, the IFCT established the Small Scale Industry Finance Facility in 1984 to help promote such small industries.

Summary of SSI Finance Facility

(1) Loan coverage

Companies with fixed capitals of not more than 10 million bahts which fall under any one of the following:

- Manufacturing industry
- Service industry
- Agricultural or livestock raising related industry
- Industry recognized as suitable by IFCT

The manufacturers must be registered at the Industrial Works Registration Department of the Ministry of Industry.

(2) Loan Terms

Usage

Acquisition or purchase of fixed assets

Operating funds (Up to 50% of total financing, financing of operating funds alone not possible)

Loan amount	
New projects	500,000 to 5 million bahts
Expanded projects	200,000 to 5 million bahts
Repayment period	4 to 7 years
Grace period	1 to 2 years
Interest rates	13.0%/year (February 1988) (Fixed interest rate)

Security (collateral)

Land, buildings, machinery, guarantees by leading companies, guarantees of Small Industry Credit Guarantee Fund, bank guarantees

(3) Fund Raising Method and Cost of SSI Finance Facility

The Facility raises funds through issuance of bonds by the IFCT (5-year bonds), private-sector long-term overseas loans, long term loans from the Bank of Thailand, and official loans such as from the FMO of the Netherlands. With the exception of the loans from the FMO, funds are not raised especially for the Facility, but rather as part of the overall fund raising activities of the IFCT. The fund raising costs in 1987 was believed to have been about 10% a year. Adding on to this the operating costs and the costs of the bad debt allocation, the SSF Finance Facility, which operates on an interest rate on loans of 13% a year, may be estimated to operate on a very small profit margin.

(4) State of Utilization

The SSI Finance Facility is being used to a greater extent in both the number of approved loans and the approved value than envisioned in the initial plans, as seen below:

Year	Loan plan	Approved loans
1984 (Apr.-Dec.)	36 cases	57 cases
	100 million bahts	153 million bahts
1985	55 cases	72 cases
	150 million bahts	178 million bahts
1986	73 cases	75 cases
	200 million bahts	203 million bahts

(5) Approved Loan Cases as Seen by Industry

The industries with the most loans approved, in order, are food processing, woodworking and furniture, agro-industries, and mineral products, such as ceramics, not including metal resources. All of these are resource utilizing industries and regionally situated. About half of the loans are for new projects and half for expansion of facilities.

Approved Loan Cases as Seen by Loan Size, Size of Companies Provided with Loans, and Location

The SSI Finance Facility offers loans from 200,000 bahts to 5 million bahts, but a look at the size of loans divided into five ranks shows the most loans being in the range of 2 million to 3 million bahts (56 cases). The average size of the loans is 2.5 million bahts.

A look by corporate size shows the most loans going to borrowers having from 21 to 40 workers. There were only 14 medium sized firms with over 100 employees.

A look by the regional distribution shows regionally located firms accounting for three-quarters of the loans, despite companies situated in the Bangkok metropolitan area

Table I-2-15. Approved loans by types of industries (1984 Apr.-1986 Sept.)

(Unit: Million Baht)

Types of industries	No. of projects	Amount	%
Agro-industries	20	43.50	10.0
Mining and Quarrying	8	20.70	4.7
Food processing	50	132.21	30.3
Textiles	10	32.30	7.4
Wood products and Furniture	22	48.43	11.1
Paper products and Printing	3	6.65	1.5
Chemical, Rubber and plastic prod.	13	47.90	11.0
Non-metalic mineral products	16	29.00	6.7
Metal products	13	30.55	7.0
Industrial gas	2	5.00	1.1
Storage	2	5.30	1.2
Services	8	14.20	3.3
Other industries	8	20.55	4.7
TOTAL	175	436.29	100.0

Source : IFCT
The Development Strategies for the Small and Medium Industries in Thailand by JICA Expert Kuroda, Kasaji.

Table I-2-16. Approved Loans by Types of Projects (1984 Apr.-1986 Sept.)

Types of projects	No. of projects	%
New projects	82	46.9
Expansion projects	93	53.1
TOTAL	175	100.0

Source : IFCT, The Development Strategies for the Small and Medium industries in Thailand by JICA Expert Kuroda, Kasaji.

Table I-2-17. Approved Loans by Size of Loans and Geographical Region (1984 Apr.-1986 Sept.)

(Unit : Million Baht)

	No. of projects	Amount	%	Average amount
Size of loans				
0.2 - 1.0 million	30	20.84	4.8	0.69
1.1 - 2.0	42	65.65	15.0	1.56
2.1 - 3.0	56	149.80	34.3	2.68
3.1 - 4.0	21	74.85	17.2	3.56
4.1 - 5.0	26	125.15	28.7	4.81
Total	175	436.29	100.0	2.49
Geographical region				
Urban (Bangkok and nearby 5 provinces)	46	142.30	32.6	3.09
Rural	129	293.99	67.4	2.28
(Central & East)	(26)	(73.70)	(16.9)	(2.83)
(North)	(32)	(56.95)	(13.1)	(1.78)
(Northeast)	(41)	(94.95)	(21.6)	(2.30)
(South)	(30)	(69.03)	(15.8)	(2.30)
Total	175	436.29	100.0	2.49

Source : IFCT, The Development Strategies for the Small and Medium industries in Thailand by JICA Expert Kuroda, Kasaji.

Table I-2-18. Approved Loans by Employment Size and Loan Period (1984 Apr.-1986 Sept.)

	No. of projects	%
Employment size		
- 20 persons	70	40.0
21 - 40	51	29.1
41 - 60	14	8.0
61 - 80	17	9.7
81 - 100	9	5.1
more than 100	14	8.0
Total	175	100.0
Loan period		
4 - 5 years	18	10.3
5 - 6	54	30.9
6 - 7	103	58.9
Total	175	100.0

Source : IFCT, The Development Strategies for the Small and Medium industries in Thailand by JICA Expert Kuroda Kasaji.

accounting for one-quarter of all companies, as previously made clear by the breakdown by industry.

Loan Scheme for Small and Medium Enterprises:

The IFCT has been implementing a "Loan Scheme under the Export Industry Modernization Program (EIMP) for Small and Medium Industry of Thailand" since 1986.

<Summary of EIMP Scheme>

(1) Objectives of the Scheme:

The EIMP financing scheme is to loan long-term funds at a low interest rate to export-oriented small and medium enterprises and offers a package of consulting services on finding and planning of projects, design of equipment, market research and technical and business management. It has as its objective the development of export companies and thus the acquisition of foreign currency and promotion of employment as well.

(2) Industries covered by the Scheme:

The scheme is applied to the following eight types of industries:

1) Food processing
2) Apparel (excluding knitwear)
3) Rubber processing
4) Electrical and electronic products
5) Wooden products and furniture
6) Metal processing
7) Footwear (excluding leather products)
8) Toys

(3) Companies and projects covered:

Companies shown under the following 1) and projects meeting the requirements of the following 2) are eligible for the financing under this scheme.

1) Companies covered:

Companies (private businesses and corporations including foreign owned companies and joint ventures with foreign companies) which had Net Fixed Assets (Fixed Assets after depreciation) if 50 million Bahts or less at the time of application.

The investors (parent companies) in joint ventures which are applying for financing under this scheme are not questioned as to qualifications. There are no limitations for parent companies on type of industry or net fixed assets for parent companies. (Local affiliates of Japanese and other foreign companies are also eligible for this facility if their production is oriented toward exports.)

2) Projects covered:

Companies or projects meeting one of the following requirements may receive financing.

a. Companies deriving 30% of their annual sales from exports (including indirect exports).

b. Projects which are expected to produce exports (including indirect exports) corresponding to 30% of annual sales within three years from startup.

(4) Uses of Fund:

1) Expansion or modernization of existing factory facilities

2) Investment in new facilities

3) Joint production or processing facilities required for joint export of products by a number of companies, either existing or new.

* In principle, funds for purchases of land are not covered by this scheme. Operating funds are also no covered, but such funds are available separately from the other IFCT facility. The loan conditions, however, are not necessarily the same as those of this scheme.

(5) Value of Loans:

Two loan rages are set according to the size of the Net Fixed Assets (Value after Depreciation) at the time of application.

1) For companies with Net Fixed Assets of less than 10 million Bahts at the time of application, from 0.2 to 5 million Bahts.

2) For companies with Net Fixed Assets of from 10 to 50 million Bahts at the time of application, from 0.2to 20 million Bahts

(6) Loan Periods:

Within eight (8) years including one to two years' grace period.

(7) Interest on Loans:

Fixed interest of 11.25% a year.

(8) Collateral:

1) Land, Buildings, Machinery and equipment

2) In the case of guarantees from commercial banks (including foreign banks with branches in Thailand), Physical collateral need not be provided. (No such exemption shall be provided in the case of guarantees by finance companies and other such financial institutions.)

   Further, There are cases where physical collateral is waived when there is a guarantee from a leading company, for example, a Japanese parent company. (Judged case by case)

(9) Documents to be attached to Loan Application:

The following supporting documents must be submitted to the Preliminary Screening Section of the Business Development Department.

1) A copy of Certificate of Corporate Registration issued by Industrial Work Department.
2) A copy of rights of company directors or joint investors
3) The recent Balance Sheet and Profit and Loss Statement
4) Features of Investment Plan
5) Names and resumes of key related personnel
6) A copy of document on Land Rights
7) A copy of Factory Permit issued by Industrial work Department
8) Costs, Specifications and Blueprints of the buildings constructed
9) Details on machinery and equipment to be installed and relevant documents
10) A Copy of industrial promotion certificate of BOI

(10) Resources:

70% of the funds used for this financing scheme comes from loans from the Japanese OECF.

(11) Consulting Services:

Consulting services are offered to companies applying for financing under the scheme by one to three Japanese experts stationed in Thailand and 10 or so support personnel in Japan.

A look at the state of use of the scheme in 1986 shows that there were 20 cases of use in the food processing industry, 11 in lumber and furniture, six in textiles, and four

Table I-2-19. EIMP: Approved Projects by Loan sizes and Types of Industries

Sizes of loans (Million Baht)	No. of projects by types of industries								
	Food	Garment	Rubber	Electric	Wood & furniture	Metal	Foot-wear	Toys	TOTAL (%)
Small scale enterprises	9	2	2	1	7	2	0	1	24 (47.1)
0.2-1.0	0	0	0	0	2	0	0	0	2 (3.9)
1.1-3.0	5	2	0	0	1	2	0	1	11 (21.6)
3.1-5.0	4	0	2	1	4	0	0	0	11 (21.6)
Medium scale enterprises	11	4	0	3	4	1	1	3	27 (52.9)
5.1-10.0	4	1	0	2	2	1	0	2	12 (23.5)
10.1-15.0	4	2	0	1	1	0	1	1	10 (19.6)
15.1-20.0	3	1	0	0	1	0	0	0	5 (9.8)
TOTAL	20	6	2	4	11	3	1	4	51 (100.0)

Source: IFCT

each in electrical and electronic equipment and toys, for a total of 51. This shows that use of the scheme is growing in industries which are now experiencing export growth.

This scheme is being funded by the OECF for a scheduled three years, starting 1986, but it got off to a very good start in its first fiscal year, so the IFCT is seeking extension of a new soft loan from Japan to further finance it.

The scheme is available to use by companies including superior credit medium level firms, so is in a sense competing with commercial banks. To promote future use, greater management effort will be sought to streamline loan procedures etc.

Problems in IFCT

(1) Problems in General

The biggest problem facing the IFCT overall is the lack of stable sources of supply of low cost funds. The IFCT has been asked, in view of its nature as a public institution, to offer lower interest rates on loans compared with commercial banks. However, it must set interest rates by the cost plus method, so the rates often end up higher than those of the commercial banks.

The medium (three to five year) and long term (five to 20 year) interest rates of the IFCT are currently 9 to 13%, but the rates have to be adjusted every year from June. On the other hand, the interest rate on loans of commercial banks has recently been from 11.5 to 14% - not much different from the rates of the IFCT.

(2) Problems in SSI Finance Facility

The SSI Finance Facility faces the problem of a thin profit margin due to the difficulties of procurement of low cost funds. As already mentioned the fund raising costs of the IFCT as a whole are higher than those of commercial banks and, further, the interest rates of the Facility are set to be lower than those of the maximum rate offered to small and medium sized enterprises by the commercial banks. Therefore, in view of its management as a joint stock company, the IFCT may find it difficult to expand the operations of the SSI Finance Facility ignoring the costs incurred.

If the number and size of loans are restricted due to the difficulties in raising funds, only naturally the selection process will become severer. On the other hand, even the private commercial banks are now beginning to become interested in superior small and medium sized projects, so competition with the private sector is becoming intenser. On top of the lack of a distinctively large difference in interest rates, the application procedures are considered complicated by the private sector, requiring preparation of medium and long term sales and profit projections and plans just as the same with a large loan project, so the better the project, the more likely the company is to go to a private commercial bank.

It would be desirable if there were greater extension of soft loans from the government and other means for raising low interest funds and greater streamlining of loan procedures.

2-4-3. Small Industry Finance Office (SIFO)

The Small Industry Finance Office (SIFO), an organization in the Department of Industrial Promotion of the Ministry of Industry, provides special financing for small sized enterprises.

The system is summarized below:

Summary of SIFO

(Objectives and Basic Policies)

(1) Promotion of Small Sized Enterprises

The SIFO has as its object to supply funds at interest rates lower than commercial banks so as to assist existing and new small sized enterprises and promote their expansion and modernization and new investment.

(2) Interest Rate Policy

The maximum interest rate is supposed to be 2% less than the interest rates of general commercial banks and is not to exceed the interest rate for similar financing by the IFCT. (Decision of SIFO Loan Board dated March 10, 1986)

(Loan Regulations)

(1) Definition of "Small Sized Enterprises"

Companies in the industrial field with fixed capitals of not more than 10 million bahts.

(2) Companies Covered by Loans

1) Companies with fixed capitals of not more than 10 million bahts which are

2) Companies which engage in any one of the following:

[1] Manufacture of machinery and parts, rubber and plastic products, building materials, processed foods, etc.

[2] Casting, machining, auto repair and painting, and other metalworking industries

[3] Jewel polishing, lacquerware production, wood carving, and production of other handicrafts

[4] Production of ceramicware, knives, handwoven fabrics, handwoven mats, and other cottage industries

(3) Persons Eligible for Applications for Loans

(1) Individual Person who received a license of business establishment and operation
(2) Juristic person who received a license of business establishment and operation (Ordinary partnership, Limited partnership, Limited Company)

(4) Loan Coverage (Applications)
(1) Acquisition of land, adjustments, and improvements
(2) Construction of factories and buildings
(3) Purchase of machinery and equipment
(4) Purchase of transportation equipment and vehicles
(5) Operating funds

(5) Loan Conditions and Repayment Terms

<Type 1> Direct loans

Loan ceiling	500,000 baht
Interest rate	10% a year
Usage	Fixed assets, operating funds (however, only 2/3)
Repayment term	3 to 7 years (principal and interest, monthly payments)
Grace period	About one year

<Type 2> Joint financing with Krun Thai Bank

Loan ceiling	500,000 baht to 3,000,000 baht
Interest rate	11% a year
Usage	Fixed assets, operating funds (however, only 1/3)
Repayment term	3 to 7 years (principal and interest, monthly payments)
Grace period	About one year

<Type 3> Loans of operating funds

Loan ceiling	1,000,000 baht
Interest rate	10% a year for up to 200,000 baht 11% a year for 200,000 baht up
Usage	
Repayment term	3 years (principal and interest, monthly payments)
Grace period	Three months

(6) Security (collateral)
(1) Land
(2) Buildings
(3) Registered machinery

(4) Bank guarantees

(7) Fees

(1) Project analysis: 1% of loan value (payment upon loan contract)

(2) Fees for setting security: 1% of collateral evaluation (payment upon setting of security)

State of SIFO

(1) Outlook of SIFO Office

Location of office: Part of a private three story building (three floors) is rented. At the beginning, only one floor was rented, but along with the increase in the staff, three floors were rented. To reduce the image of the SIFO as being a government organization, it is situated far from the Ministry of Industry.

Number of staff: 51. In rank, all are quasi-civil servants of up to managerial level, not government employees.

Office equipment: At the present time, the only official vehicle the SIFO has is a microbus. It has had this for the past 10 years. It would like a further three to four cars, but in addition to the cost of purchase, there would be the expense of hiring drivers etc. and so an increase in the number of vehicles would be difficult budget-wise. The SIFO does not have any personal computers yet, but is scheduled to install two through assistance from the JICA. It has only one copier and six typewriters.

(2) Funds

The SIFO currently has 153 million bahts in total funds, with investment having ben increased by 100 million bahts in 1987. This entire amount constitutes allocations from the general account. However, the SIFO has yet to receive any actual payments from the Ministry of Finance, so is operating on just the initial 53 million bahts. Out of this 53 million bahts, 25 million is on deposit at the Krun Thai Bank receiving 5% interest and the remaining 27 million bahts is on deposit at the Government Savings Bank and the Krun Thai Bank branches receiving 7.5% interest.

In March 1988, an agreement was signed with Canada for 100 million bahts in free assistance, so the total fund will rise all at once to 250 million bahts. However, it is still not determined when the money will be paid in the fund.

Table I-2-20. Types of Industries Not Eligible for the SIFO Loan

I	Food, Tobacco, Beverage	IV	Paper and printing
1	Rice mill	14	Printing & writing paper by machine
2	Sugar mill except red sugar	15	Printing shops
3	Ice factory	V	Chemicals and clay products
4	Slaughtering of animals	16	Match factories
5	Tapioca products (only new factory establishment)	17	Soap
		18	Monosodium glutamate monohydrate
6	Tobacco	19	Drugs
7	Whisky, beer and other alcoholic beverage	20	Cement
		VI	Metal & machinery products
8	Carbonated drinks	21	Car assembling
II	Textiles	22	Dry cell and battery
9	Yarn spinning	23	Cool storage
10	Gunny bag	24	Painting factories except car repair shops
11	Jute pressing		
III	Wood & wood carving	25	Movie production
12	Saw mill	26	Factories receiving IFCT's financial assistance
13	Plywood and saving board		

Source: SIFO

Table I-2-21. Main Fund Resources and Operation of Funds of SIFO

(Unit: 1,000 bahts)

	1981	1982	1983	1984	1985
Fund Resouces					
Capital account	53,650	53,650	53,650	53,650	53,650
Liquid debts	69	47	69	28	180
Profit and loss account	1,500	1,255	1,721	2,214	2,632
Total	55,219	54,952	55,440	55,892	56,462
Operation of funds					
Cash on hand	6	2	2	1	1
Cash on deposit at Ministry of Finance	1,222	469	642	810	710
Bank account deposits					
Bank of Thailand	11	14	16	21	20
Krun Thai Bank	50,500	50,500	50,500	50,500	50,500
Government Saving Bank	862	1,211	1,496	1,629	890
Increasing assets	1,171	1,767	2,118	2,412	2,939
Fixed assets	218	182	141	126	96
Other assets	1,229	807	525	393	1,305
Total	55,219	54,952	55,440	55,892	56,461

Source: SIFO

(3) State of SIFO Schemes

Relaxation of Loan Conditions: To promote usage, the SIFO increased the ceiling on its loans and lowered interest rates in 1987, resulting in the current loan conditions.

Number of loans: Up until 1986, there were an average annual 37 loans made, but in 1987 this soared to 128 loans. In 1988, about 200 loans are expected to be made.

(4) Character of SIFO

The SIFO is an organization under the Department of Industrial Promotion of the Ministry of Industry and is thus not an independent loan financing institution with any legal basis. It is supervised by the Loan Board, comprised of representatives of various government agencies, and the DIP and MOF (Ministry of Finance). However, the following problems have arisen due to the lack of a legal basis: [1] since its legal basis is vague, it is not recognized as a financial institution under the regulations of the Bank of Thailand. As a result, as will be mentioned later, it cannot utilize the SICGF scheme for direct loans. The refusal of the MOF etc. to allow use of soft loans by the SIFO is also considered to be due to this. [2] The Loan Board examines and decides on loans, but there are not that many opportunities for the Loan Board to convene - this has become one reason for the long time required before extension of loans. Further, the members of the board do not necessarily have sufficient ability to analyze finances, specialized knowhow in judging loans, etc., so they do not necessarily make the right decisions in approvals. [3] The Loan Board and the DIP cannot be said to be sufficiently supervising the operation of the SIFO, so where the responsibility in management lies is unclear and the management and the operations in the organization tend to be allowed to run unchecked.

While the ceiling on financing in joint loans with the Krun Thai Bank is 3 million bahts, the limit on direct loans is just 500,000 bahts, not enough for the loans required by small and medium sized enterprises. There is further a tremendous difference compared with the 2 million bahts offered under the bill refinance scheme of the Bank of Thailand and the 5 million bahts offered by the IFCT. With the emphasis currently shifting to direct loans, this loan ceiling will have to be raised.

Since there is a temporary no-collateral state from the date of financing to the setting of security, the land and machinery etc. purchased by the loans cannot be used as collateral. This represents a considerable difference from Japan, where the purchased articles can serve as collateral, but in Thailand there are many problems with the borrowers and under the present conditions it would be difficult to make any sudden reforms.

(5) Use of Credit Supplementation System (Small Industry Credit Guarantee Fund (SICGF))

User of the SICGF must be a member of the Fund. The Krun Thai Bank is a member of the fund, so this system could be used for cofinancing of the SIFO with the Krun Thai Bank, but could not be used for direct loans of the SIFO.

The surge in the number of applications and approvals since 1986 has been largely due to the increase in direct loans. Of the 213 applications made in 1986, 131 were for direct loans and the remaining 82 for joint loans with the Krun Thai Bank. As opposed to this, in 1985, there were 29 applications for direct loans and 55 for joint loans with the Krun Thai Bank. In terms of the loans extended in 1985, there were 16 direct loans and 24 joint loans with the Krun Thai Bank, with Krun Thai Bank joint loans being more numerous up until 1985. However, there has not been much activity in cofinancing with the Krun Thai Bank in the past, so starting from 1986 the SIFO has been taking measures to promote direct loans.

1. Periodic dispatch of staff for visits to three regional offices of DIP to develop clients
2. Requests for cooperation in handling applications at DIP regional offices
3. Preparation of SIFO pamphlets and posters and streamlining of application forms
4. Shortening of examination time by bolstering staff for handling loans
5. Increase of ceiling on direct loans from 300,000 bahts to 500,000 bahts

As of the end of 1986, there were 72 bad loans out of the total 159 loans made. Of the loans made by cofinancing with the Krun Thai Bank, 65 of the 96 or 67.7% were bad and of the direct loans seven of the 63 or 11.1% were bad. A look at the total value of the bad loans shows 26 million bahts of the 43 million bahts in joint loans with the Krun Thai Bank, or 61.9%, being bad, while only 600,000 bahts of the 10 million bahts in direct loans or 5.7% were bad. Many of the direct loans have been recent, however, and it will be necessary to wait to see whether the percent of bad loans will rise. So far as the joint loans with the Krun Thai Bank show, however, the deposits of the SIFO at the Krun Thai Bank are being gradually reduced and reached 25.5 million bahts in 1986, corresponding to the amount of the bad loans, so there may be said to be almost no benefit for the Krun Thai Bank in using this scheme.

Problems in SIFO

Restrictions on Expansion of Business due to Insufficient Budget

At the present time, the SIFO has barely enough office space and staff for its operations. It must cover operating expenses by interest on its fund operations and interest on its loans, so holds its yearly operating budget down to about 4 million bahts. To increase its business, it has to quickly open up branches, but under the present conditions it cannot hope to do this.

It is also necessary to provide further training to the staff on project evaluation and assessment of collateral, but such training is not sufficient at present. Right now a project is underway with the assistance of the Netherlands, but this cannot be said to be enough. In addition, the restricted budget for promotional activities limits the SIFO to one official vehicle and hampers PR campaigns and seminars.

Due to the restricted operational budget, there is strain on normal activities too and in principle long distance phone calls to customers or the regional offices of the DIP are prohibited, with communications limited to the mail. This is one reason for the slow processing. Further, the repayment plans of the customers are prepared using common calculators, which is inefficient.

In 1986, the SIFO increased its loan examination staff from seven to 12, but was not able to shorten the loan examination time as much as it wanted so it still takes from three to four months from application to extension of the loans. In 1986, there were 73 loan applications approved, which works out to six approvals a year per staff, a very poor rate. In joint loans with the Krun Thai Bank, there are also procedures to be followed between the Krun Thai Bank and SIFO, so the examination time becomes further longer.

The amount of documentation for loan applications is tremendous and places a large burden on the borrower, but the SIFO is working to streamline it right now.

2-4-4. Industrial Bill Refinance System of Bank of Thailand

Starting in 1986, the Bank of Thailand adopted a refinance system for industrial bills so as to make available institutional financing to the private industrial sector through the commercial banks and IFCT. Bills for purchase of materials issued by manufacturers had been discountable by the Bank of Thailand at lower rates than the commercial interest rates, but the loan conditions were strict etc., so the system was not used much at all for the eight years of its existence and was replaced by the current system in 1986.

In the current bill refinance system, the commercial banks handle the bill examination, collateral arrangements, bill purchases and payments, reports on fund usage, and the rest of the procedures and bear the risks. The Bank of Thailand repurchases the bills.

Under the present system, further, there is a general scheme and a scheme for small and medium sized enterprises. The general industrial bill refinance scheme and the small and medium enterprise scheme are summarized in the attached tables. The biggest differences between the two schemes are that the loan conditions of the small and medium enterprise scheme stipulates the company have fixed assets of less than 10 million bahts, extremely easy conditions, and the minimum loans are 30,000 bahts for the general scheme and 10,000 bahts for the small enterprise scheme. Note that the interest rate on loans from the Bank of Thailand to the commercial banks is 5% under the general scheme and 4% under the small enterprise scheme, with encouragement thus given to financing of small enterprises.

Problems in Bill Financing System of Bank of Thailand

(1) Little Hope for Positive Activities of Private Financial Institutions

Loans to small and medium sized enterprises are accompanied by greater risks than loans to large corporations and further offer smaller profit margins. When commercial banks engage in financing using their own funds, they can currently secure a profit margin of 6 to 8%. To promote use of the present system by the private commercial banks, it would be necessary to bring the profit margins under the current schemes closer to those of private based loans.

(2) Complicated Procedures, Strict Regulations, and Insufficient Publicitization of System

Troublesome procedures are involved in using the schemes, so both entrepreneurs and banks express dissatisfaction with the operation of the system. Behind this dissatisfaction may be considered to be the following: [1] the company side does not engage in strict accounting and do not wish to lay open their finances, so it is difficult for the banks to prepare and submit the financial documents required in the loan procedures,

[2] there are only a few branches of the Bank of Thailand, so procedures have to be handled through the regional channels of the handling bank and the head office of the Bank of Thailand, [3] the branches of the commercial banks do not have sufficient staff capable of examining projects of the small and medium sized enterprises and do not have sufficient branch networks in the regional areas, and [4] PR of the schemes is insufficient, so the bank staff is unfamiliar with them.

To encourage use of the schemes, it will be necessary to train the staff of the commercial banks to eliminate their over reliance on collateral and to raise their ability to examine projects. Further, since the risk of dishonored bills is borne completely by the commercial banks under the current schemes, consideration should be given to combination loans under the schemes and the SICGF scheme so as to lighten the load. (Please refer to 2-4-5: Small Industry Credit Guarantee Fund.)

Table I-2-22. The Bank of Thailand's Industrial Credit Refinancing Scheme

Objectives :	1. To help finance parts of input cost while encourage the use of domestic inputs and labour. 2. To help promote industries which export their products.
Loan Channel :	Funds are provided via commercial banks and IFCT.
Conditions :	Allocated to each project according to the following criteria. 1. Industries using inputs from domestic agricultural sector of at least 20 per cent of total inputs. 2. Industries exporting at least 20 percent of total sales value. 3. Industries employing domestic inputs of at least 50 percent of total inputs. 4. Industries employing labour as a major part of total inputs. 5. Industries contributing to rural developments. 6. Industries where the values of domestic inputs together with other domestic expenditures exceed 50 percent of total production costs. or / Industries undertaking manufacturings for export or / Assembling undertakings employing domestic input as a proportion not less than 50 percent of total input cost.
Amount of Refinance :	The refinancing amount will be between 60-90 percent of neccessary production cost with special consideration given to medium size industries having fixed asset of not more than B200 million.
Maturity :	120 days, the facility will not be extended beyond 5 years.
Interest rates :	BOT charges commercial banks 5 percent (P.A.) Commercial banks charge not more than 7 percent (P.A.)
Penalty for breach of regulation :	1. 11 percent (P.A.), with additional 5 percent for repeated breaches within 1 year. 2. If commercial banks or IFCT commit repeated breaches within 1 year, they will be charged additional 2 percent (P.A.).
Minimum amount for each note submitted :	B30,000
Note :	1. Industries, where greater than 50 percent of capital is either foreign capital or equities held by non-residents and having asset values greather than B30 million while capital values as proportions of total assets fall below 50 percent, will have amount refinanceable reduced as the BOT deems appropriate. 2. The modification of refinancing procedure from discount to purchase basis, since January 15, 1986, impiles the interest rate reduction of 0.53 percent (P.A.)

Source: Bank of Thailand

Table I-2-23.
The Bank of Thailand's Industry Credit Refinancing Scheme for SSIs

Objectives :	1. To provide low cost funds for small industries. 2. Conditions involve in obtaining funds are less stringent than in the case of Industrial Credit Refinancing scheme.
Loan Channel :	Funds are provided via commercial banks and IFCT.
Condition :	The definition of a small industry is one which either the value of capital or net fixed asset does not exceed B10 million.
Amount of Refinance :	Allocated to each projects according to the amount needed to finance necessary cost with maximum amount set at B2 million.(the revolving credit line)
Maturity :	120 days, the facility will not be extended beyond 5 years.
Interest rates :	BOT charges commercial banks 4 percent (P.A.) Commercial banks charge not more than 7 percent (P.A.)
Penalty for breach of regulation :	1. 11 percent (P.A.), with additional 5 percent for repeated breaches within 1 year by the industry concerned. 2. If breaches were committed by commercial banks or IFCT, they will be charged an additional 2 percent.
Minimum amount for each note submitted	$10,000

Note: 1. For industries located in Bangkok Metropolitan area or 4 other specified well developed provinces, additional condition imposed for obtaining refinance is that they use labour as a major input.
2. There are 7 categories, 55 items, of undertakings listed which are permitted to apply for the facility.

Source: Bank of Thailand

Table I-2-24. Comparison between the New Scheme and the Old Scheme of Industrial Credit Refinancing Facvility for SSIs

	New scheme	Old scheme
Naming	P/N refinancing facility for SSI	P/N Rediscount facility for SSI
Interest payment	Payable on due date	Payable on rediscount data
Loan amount	Up to 2 million baht Each SSI can issue P/N for rediscount three times per year within the outstanding limit of 2 million baht (Revolving fund system)	Up to 1 million baht Each SSI can issue P/N several times, but total book value of the P/N issued in a year must not exceed 1 million baht (Fixed credit line system)
Interest rate	Interest rate for purchasing P/N from SSI ... 7% p.a. Interest rate for repurchasing P/N from participating bank ... 4% p.a. (Effective from march 1986)	Discount rate for SSI ... 8% p.a. Rediscount rate for the participating bank ... 5% p.a.

Source: Bank of Thailand

2-4-5 Small Industry Credit Guarantee Fund (SICGF)

The need for the establishment of the SICGF for the promotion of loans to small and medium sized enterprises was taken up by the Joint Public-Private Consultative Commitee in 1983. It was formally launched in the IFCT in 1985 by joint public and private investment. It is treated as one fund in the IFCT, but is under the control of the Fund Management Committee, which draws its members from the Ministry of Finance and financial institutions, and is operated by a separate account from the investment in the IFCT. The investors and investment amounts are the Ministry of Finance with 10 million bahts, the IFCT with 20 million bahts, the Krun Thai Bank with 20 million bahts, and 15 other commercial banks with 60 million bahts, for a total of 200 million bahts.

The fund has as its aims [1] the increase of loans from financial institutions to small and medium sized enterprises, [2] the promotion of loans to small and medium sized enterprises in the regional areas by financial institutions through use of the fund, and [3] promotion of industrial development in accordance with the targets of the national economic development plan.

Details of Scheme

1. Borrowers Eligible for Guarantees

Small and medium sized enterprises with fixed assets of not more than 10 million bahts borrowing from 200,000 to 5 million bahts. Both companies and individuals may be covered. The industries covered by the guarantees are based on the industries covered by loans of the IFCT.

2. Loans Covered by Guarantees

Medium and Long-Term Loans

Overdrafts, letters of guarantee, packing credit, bills, check discounting, and other short-term loans.

3. Collateral

The SICGF does not demand collateral from its borrowers, but instead makes the banks agree to use their fixed assets as collateral. However, the banks may demand collateral from the borrowers for the portion of the loans which cannot be covered by the SICGF guarantees.

4. Guarantee Coverage

The SICGF provides guarantees for the amount of loans which cannot be covered by collateral. The SICGF will in principle cover up to 80% of the amount which cannot be covered by collateral.

However, it will allow 100% guarantees of the amount not covered by collateral for priority projects along with promotional programs of the government.

The amount not covered by collateral is not determined by the SICGF, but by the bank providing the loan. The SICGF just examines the guarantees based on the assessed value given by the banks in their applications.

5. Guarantee Fee

The SICGF requires 1.5% of the guaranteed value as its fees. The yearly rate is constant, but the real fees paid are reduced each year along with the repayment.

6. Obligation for Independent Fund Procurement by Borrowers

Persons using the SICGF are required to raise 20% of the required funds on their own.

Current State

According to a survey by JICA experts sent to the Ministry of Industry, the larger the size of the commercial bank and the interest in financing small and medium sized enterprises, the more this scheme is used. The reason for this is that utilization of this scheme enables good small and medium sized enterprises which have trouble raising funds due to lack of collateral to raise funds and enables banks to lend money to small and medium sized enterprises without worrying about the lack of collateral. On the other hand, criticism was expressed that the application and approval procedures are complicated, it takes too much time until finalization, and the processing of the guarantees when loans are dishonored is slow.

There were 43 credit guarantees made in the first half of 1987, worth 27.5 million bahts, of which 35 cases worth 20.1 million bahts were for loans to companies in regional areas and eight worth 7.4 million bahts were for loans to companies in the metropolitan area. There have been 59 guarantees provided, worth 35.9 million bahts, since the start of operations in November 1985. As of the end of February 1988, the number of guarantees had soared to 156 cases.

Note that the SICGF is scheduled to start loans and guarantees to regional enterprises through the assistance of USAID. This project is summarized below:

Qualifications for use	Only regionally located projects, not including six provinces nearby Bangkok
Loans covered	Operating funds etc. Guarantees also provided. Up to loan ceiling of long-term loans and limit of assets of borrowers. Loan ceiling is 2.5 million bahts and limit of fixed assets of borrowers is 5 million bahts.

Repayment term	Repayment of year or more after half year grace period
Industries covered by loans	No restrictions

This scheme will last until September 30, 1996.

The scheme has US$8 million in funding and is scheduled to receive US$40,000 a year in subsidies for expenses.

Other Matters

The SICGF has a staff of 19. It has just one personal computer, one copier, and several typewriters, so is not very well equipped.

The ceiling on guarantees is presently the 200 million bahts of the total fund. Consideration is being given to raising the ceiling on the guarantees to two to three times the fund, but an increase in the fund itself is desired to ensure the stability of operations. The SICGF is presently just one fund in the IFCT, but consideration may be given to establishment of a corporation by a special law after five years of experience.

Problems

1. The operating costs have to be covered by the guarantee fees and the interest on the fund, so the operating funds are limited. Therefore, there is strict selection of applications and projects which seemingly might end in default are eliminated. The road to application of the system to small sized enterprises, which really require the guarantees, is therefore shut. To promote application of the system to small, weak enterprises, it will be necessary to consider increases in earnings through expansion of business and supplementation of business deficits by the Ministry of Finances.

2. The guarantees are provided through the commercial banks, but the staff of the commercial banks themselves often lack the ability to examine projects. For the time being, it will be necessary to shorten the time required for the processing and to increase business earnings through development of new customers by examinations by the fund's own staff and by the establishment of regional branches.

3. The current guarantees are limited in principle to 80% of the amount loans not covered by collateral, but it would be desirable to raise the guarantee coverage to 100% to promote more positive use of the scheme by the commercial banks.

4. This scheme does not cover the direct loans of the SIFO, a similar organization aimed at providing financing for small and medium sized enterprises, so the effectiveness of the two systems is reduced. It is necessary to consider some means for strengthening the ties between the two systems.

Table I-2-25. Summary of SICGF's Credit Guarantee Approval (As of February 1988) (1)

	Financial Institutes	Number of Approvals			
		Metropolitan Area	Rural Area	Total	Guaranteed Amount (1,000 bahts)
1.	Bank of Ayudhaya Ltd.	0	1	1	400
2.	The bangkok Bank of Commercial Ltd.	0	0	0	0
3.	Bangkok Bank Ltd.	6	21	27	17,910
4.	Bangkok Metropolitan Bank Ltd.	1	0	1	400
5.	The Bank of Asia Ltd.	0	3	3	1,360
6.	First Bangkok City Bank Ltd.	0	1	1	800
7.	The Industrial Finance Corporation of Thailand	7	40	47	26,579
8.	Krung Thai Bank Ltd.	2	14	16	9,198
9.	The Laem Thong Bank Ltd.	0	0	0	0
10.	Nakornthon Bank Ltd.	0	1	1	1,200
11.	The Siam Commercial Bank Ltd.	9	21	30	24,563
12.	The Siam City Bank Ltd.	0	1	1	279
13.	The Thai Danu Bank Ltd.	0	0	0	0
14.	Thai Farmers Bank Ltd.	1	12	13	6,712
15.	The Thai Military Bank Ltd.	2	11	13	10,663
16.	The Union Bank of Bangkok Ltd.	0	2	2	2,060
	Total	28	128	156	102,124
	Amount Guaranteed	21,841	80,283	102,124	

Metropolitan Area: Bangkok, Samut Prakan, Nonthaburi, Pathum Thani, Samut Sakhon and Nakhon Pathom

Table I-2-25. Summary of SICGF's Credit Guarantee Approval (As of February 1988) (2)

Region	Number of Approvals Project	Guaranteed Amount (1,000 bahts)
North	51	28,398
North East	19	9,183
South	33	23,039
Central	25	19,663
	128	80,283
Metropolitan Area	28	21,841
Total	156	102,124
Average	655	(Bt'000)/Projet

2-5. Industrial Promotion in the Other Countries

2-5-1. South Korea's Industrial Policy

The main distinguishing feature of South Korea's industry promotion policies has been the strengthening of export-oriented indsutrialization under the supervision of the government. During the 1950s after the end of the Korean War, like other developing countries, South Korea started to implement import substitution industrialization polcies. However, faced with the constraints of a small domestic market, its policies changed direction in the early 1960s so that they were now export-oriented industrialization policies aimed at export markets. Exports were used as the "engine for growth", and in the sense that they have brought about today's economic growth Korea's industrialization has had a considerable impact on the development policies of other developing countries.

An outline of the course taken by South Korea's industrialization policies and industry promotion polcies will be examined below in the context of the six Economic Development Five-year Plans (hereafter referred to as Five-year Plans).[1]

1. Industrialization Policies of the 1950s

As a consequence of the Korean War which started in 1950 and continued for three years South Korea's industrial base, which was fudamental for industrialization, was destroyed. Also, prior to the war industry had been concentrated in the northern part of the peninsula so that with the partition between north and south South Korea was left little industry and only an agricultural sector existed. The scale of the damage caused by the war was such that it was equivalent to two years' worth of GDP for South Korea at that time, and as such dealt a crushing blow. Consequently, South Korea's industrialization began with what little remained in the way of agriculture and light industry.

Aid from the United States formed the basis of the country's move towards industrialization during the 1950s.[2] The U.S.-South Korea Mutual Security Agreement was formed as a bridgehead for the allies in the Far East and large supplies of aid (wheat, unrefined sugar, raw cotton) entered Korea from the United States through PL 480. On

[1] The following sources were used as reference materials in regard to South Korea's industrialization policies: "South Korea's Plan for Industrial Development", Institute of Developing Economies; "Asian Nations' Policies, Chapter Seven", Institute of Developing Economies; "Venture Capitalism in South Korea", Toshio Watanabe.

[2] U.S. aid given to South Korea during this period was worth in excess of $3.0 billion up to 1961.

the basis of this aid, the flour milling, sugar, and textile industries, also known as the "three white industries", began to flourish during this period. However, the industrialization which occurred mainly in relation to these "three white industries" did not continue long. In less than no time the small domestic market was saturated, and in the late 1950s investment in surplus plant and equipment occurred.

Then, once into the 1960s the aid from the U.S. which had been gratis was changed so that it was now given in the form of loans, thus making it necessary for Korea to break away from its dependence on U.S. aid.

Through its consistent government leadership the Park administration, which came to power as a result of a military coup on 16 May, 1961, adopted industrialization policies until Park's assassination in 1979. A "policy of export-oriented industrialization" was the direction which the Park administration took for achieving economic development.

This policy involved promoting industrialization through the sale of labor-intensive goods on export markets by making use of South Korea's abundant resources of low-paid labor. The factors which were behind this policy were: (1) South Korea mainly existed of agricultural regions where there was a surplus in population and in order to industrialize capital goods had to be imported from advanced countries. Although in order to import, foreign exchange had to be earned through exports, the only goods which could be exported were labor-intensive light industrial goods; (2) The 1960s was a period of "simultaneous growth" for the world economy, and the climate for export was good. In advanced countries a rapid change was taking place in their industrial structure whereby labor-intensive industries were declining, thus making it possible for Korea to take over these areas.

Under such conditions the Five-year Plans began under the Park administration.

2. First Five-Year Plan (1962-66)

The basic objectives of the First Five-year Plan were to correct the vicious social and economic circle and to achieve an independent economy. With this basic structure the main objectives were to secure energy resources, expand indirect social capital, construct key industries, and improve the country's international balance of payments through increasing exports.

However, domestic savings were little and although positive attempts were made for the induction of foreign investment these resulted in failure. On top of this came the confusion which accompanied the currency reform in 1962, with the result that during the second year the plan came to a halt and from the third year on the objectives were adjusted downwards. As a consequence of this downwards adjustment the trend towards exports became much stronger through such moves as the strengthening of the export-import linkage system, a decrease in export finance interest rates, and the establishment of KOTRA (Korean Overseas Trade Association).

For example, it was considered that an export industry mainly in the private sector ought to be established and so a number of measures were taken. These included export income tax reductions and exemptions, a preferential tax system with special rebates, exemption of import duties, and special government finance.

During this period exports increased 500% so that whereas they had been worth $55 million in 1962 they amounted to $254 million in 1966. Goods exported consisted mainly of light industrial goods such as textiles and sundry goods.

The following helped resolve the foreign exchange shortage during the period of the First Five-year Plan: 1) the induction of right of claim funds from Japan (supply of gratis and considered funds,[1] which became possible through the normalization of relations between Japan and South Korea in 1965; and 2) its success in obtaining loans worth $150 million as a result of sending Korean armed forces to the Vietnam War and special procurements for Vietnam.

The export-oriented development strategy which was made clear in the First Five-year plan was an extremely high political risk. One reason for this was the necessity for foreign capital because of the reliance on foreign capital for investment funds. In 1962 83% of total investments was derived from foreign capital. Also, there were no plans whatsoever to pay back from export income the overseas loans which had accumulated from the 1950s up to 1965. It was quite natural that President Park himself, since December 1962, had taken the position of chairman of the Committee for Growth for Export Promotion which comprised of high government officials and leaders from the financial world, and took the lead in the promotion of exports.

3. Second Five-year Plan (1967-71)

The Second Five-Year Plan aimed to increase employment and improve the balance of international payments through the promotion of the industrialization of the heavy and chemical industries, increased exports and import substitution which were directed at modernising the industrial structure.

During this period the government selected priority industries which were to be fostered and it also enacted specific measures for their promotion and development. These comprised of the folowing six pieces of legislation: 1) Petrochemical Development Act

[1] For the 10-year period from 1966 this amounted to $200 million in considered and $200 million in gratis funds.

(1966); 2) Shipbuilding Industry Promotion Act (1967); Machine Industry Promotion Act (1967); 4) Electronics Industry Promotion Act (1969); 5) Steel Industry Promotion Act (1970); and Non-ferrous Metal Refinery Act (1971). These industries were selected because: 1) they could be developed into industries which had a high acquisition rate of foreign currency: 2) the effect they would have on related industries and on creating employment; and 3) their key importance as industries.

As for the specific measures which were taken, the government put participating companies under a licensing system, and took special preferential measures in the areas of taxation and finance (a promotion fund was established).

Then as part of putting the infrastructure in place it started creating industrial complexes and enacted the Export Industry Industrial Complex Development Act (1964), the Export/Free Zone Establishment Act (1970), and the Industry Base Development Promotion Act (1973). Although this policy was an effective means for an industrializing country, because it centered on large-scale industrial complexes in ten or so places the result was that they were concentrated in the coastal zone in the southeast of the country which meant considerable costs in relation to the provision of housing for the relocated workers.

In 1969 the Masan Free Zone was established based on Taiwan's Kaoshun Export Processing Zone.

During the period of the Second Five-Year Plan work on a network of expressways (Seoul-Pusan Expressway, Seoul-Inchon Expressway) was started and plans were devised for a iron manufacturing plant. The plans for the plant included the formation of KISA which was formed in December 1966 comprising of iron manufacturing companies from the U.S, West Germany, Great Britain and Italy. However, claiming that the project was not very economically viable the U.S. and West Germany pulled out, thus causing a temporary stalemate. But with the cooperation of Japan as well, work on the project finally started in April 1970 and it became responsible for the heavy and chemical industrialization of the 1970s.

4. Third Five-year Plan (1972-76)

The Third Five-year Plan aimed at an highly advanced industrial structure which would lead to full-scale heavy and chemical industrialization. A number of important pieces of legislation were enacted to make this possible. For example, in 1973 the Foreign Investment Induction Act which had been enacted in August 1966 was revised and the induction of foreign capital became one of the cornerstones of industrialization.

Also, various financial organizations were established in order to effect heavy industrialization. The People's Investment Fund was established in 1976, the South Korea Land Bank in 1975, and the Import-Export Bank of South Korea was established in 1976. Preferential interest rates for loans were implemented and greater provision was made for incentives for the heavy and chemical industries.

Instead of labor-intensive industries such as the textile and footwear industries, capital goods import substitution industries such as the petrochemical, shipbuilding and steel industries, were designated as priority industries.

Although in 1973 in the second year of the plan's implementation the first oil shock occurred bringing about a shortage of foreign currency, South Korea was able to overcome this through its construction projects in the Middle East and the skilfull selection of export markets. However, the oil crisis did bring about a change to the development strategies which were the result of an excess of government aid for export promotion at that time. A change was made over to encouraging heavy and chemical industrialization through import substitution for capital goods and intermediate goods, and to direct export incentives involving the tax system and preferential interest rates. Also, particular emphasis was placed on indirect incentives such as export promotion rates, export processing zones and attracting foreign export companies.

During the period of the plan progress was achieved in heavy and chemical industrialization, as symbolized by the completion of the Pohan Iron Manufacturing Plant, the start of production of the "Pony" by the Hyundai Motor Company and the construction of a 260,000 ton tanker by Hyundai Shipbuilding.

5. Fourth Five-year Plan (1977-81)

The priority objectives of the Fourth Five-year Plan were to make a high-level industrial structure and to carry out technical reform. With these objectives higher domestic production ratios were set for the machine industry and a change was sought over to increasing the quality of consumer goods rather than the volume. Also, the industrialization rate for heavy and chemical industries was raised.

While in November 1972 President Park had stated that it was the government's objective to reach exports of $10 billion by the year 1980, this goal had been attained in 1977. When he addressed a gathering at a celebratory party held in Seoul on 22 December 1977 President Park said, " West Germany needed 11 years before its exports increased from $1 billion to $10 billion, Japan needed 16 years, but South Korea achieved this in the space of seven years".

However, the Fourth Five-year Plan saw the first time ever since the long-term plans were first implemented that the targets were not met by considerable margins (refer Table 1). A number of factors were behind this, including the second oil crisis, the low growth of advanced countries, the rise in protectionism and the assassination of President Park who had until then provided strong leadership. In addition to this, the strains which had been caused by Korea's past rapid industrialization began to appear at this time. Because the industrialization of the heavy and chemical industries which the government had been strongly promoting had occurred mainly among the *zaibatsu* the development of medium and small-scale manufacturers lagged behind. As a consequence, trade deficits became a matter of course because of the increase in imports of consumer goods and intermediate goods. Also, labor-intensive goods lost their comparative merit because of the inflation which drove up wages, and other developing countries had started to catch up.

The start of the reorganization of the heavy and chemical sector which began in 1980 and included the reorganization of the *zaibatsu* companies and the abolition and amalgamation of heavy and chemical industry companies brought some confusion to the economic world and caused a decline in economic activities.

6. Fifth Five-year Plan (1982-86)

With the target of correcting the strains in the Korean economy which became exposed during the period of the Fourth Five-year Plan and the qualitative expansion of the economy rather than quantiative expansion, the basic objectives of the plan were 1) stability; 2) efficiency; and 3) equilibrium. It is true that in the short term the strategy of quantative expansion was effective in bringing about high growth. However, it also brought about an increase in the supply of foreign currency and a decrease in the savings ratio and also lowered international competitiveness and put the balance of international payments into the red. Furthermore, it widened the gap between the various income groups and created an imbalance between the regions.

The Fifth Five-year Plan started with the intention of overcoming these problems, but starting in 1982 inflation started to decline and the rate against the US dollar steadily began to decline as a result of the floating exchange system (1980) under the basket system for foreign currencies.

Development strategies since 1981 have featured 1) price stability; 2) market opening; and 3) a balanced economic growth. Price stability was sought through a tight monetary policy, retrenchment in finance, and controls on wages. Market opening policies have been put in practice since the establishment of the Fair Trade Commission within the Economic Planning Agency and the enactment of legislation concerned with monopoly regulations and fair trading. The percentages for the 80 liberalized import items were rapidly increased with 1979's 68.2% rising to 74.7% by 1982 and 91.5% by 1986. The number of industries for which foreign investment was possible also increased by the year. As for balanced economic growth, steps were taken for the dispersal of industries among the regions and the fair distribution of income. However, these did not necessarily bring about satisfactory results.

In the latter half of the plan's duration, since autumn 1985, the appearance of the "three low merits" has proven very beneficial for South Korea's economic growth and for its exports. The most significant developments during the period of the plan were the stability in prices brought about by the decrease in the cost of petroleum and primary products and the improvement of the current account balance, especially the 1986 current account surplus of $4.6 billion and the decrease in the overseas debt balance (from $46.8 billion at the end of 1985 to $44.5 billion by the end of 1986).

7. The Sixth Five-year Plan (1987-91)

During the first four Five-year Plans the entire emphasis was placed on expanding the economic pie, and afterwards various strains which accompanied that began to appear. While the main objective of the Fifth Five-year Plan was to correct these strains, the Sixth Five-year Plan was centered on "the construction of an independent growth base" for "a firm trend of surplus for the balance of international payments".

The following are the six major policies contained within the Sixth Five-year Plan:

1) The continuation of appropriate growth for the expansion of employment opportunities:
2) A settled trend of surpluses for the balance of international payments and an easing in the foreign currency burden;
3) The promotion of a harmonious industrial structure and turning the country into a technological country;
4) Developing equilibrium between the regions and revitalizing the regional economies;
5) Increasing welfare for the people and promoting equity;
6) Revitalizing the market economy system and re-establishing the function of the government.

In addition to putting the Sixth Five-year Plan into effect, South Korea faces some difficulties due to the international situation today. These include the move towards protectionism in the U.S. and the pressure which has been applied to South Korea to open up its markets, pressure to revalue its currency, and the rapid rate at which other developing nations are catching up. It would seem that some time is needed until the reliance on exports which has continued up until now is corrected.

Furthermore, the improvement in the balance of international payments depends on the outside factors of the "three lows", and there is no guarantee how long this situation will continue. It is necessary for South Korea to work on strengthening the economic base through fostering the medium and small-scale enterprises which supply intermediate goods and parts.

In order to succeed in research and development, raising the level of export goods, and competition with the later developing countries, it is necessary that the transfer of the latest in technology take place and the capacity for research and development be strengthened. In order to achieve this the Sixth Five-year Plan makes provision for the investment ratio for science and technology as represented by GNP to increase from the 1985 level of 1.7% to reach 2.5% by the year 1991 (refer Table 2).

The business management of the *zaibatsu*, which have up until now sustained South Korea's economic development, has also reached a turning point. First of all the *zaibatsu* are now faced with the changeover to the next generation in their top positions. Secondly, there is mounting criticism about the monopolistic situation and the way in which they carry too much weight in the South Korean economy. Then thirdly there is the call for a shift over to the "large variety small lot production" system from the "few goods mass production" system as the industrial structure is being improved, and there is the question of how effective their management systems will be in respect to their vertical management structure, etc.

Although the realization of the Sixth Five-year Plan will be influenced considerably by outside factors such as the situation surrounding international economies and politics, South Korea's independent economic base is firm and it now remains to be seen whether Korea will be able to join ranks with the economies of the advanced nations.

8. Features of South Korea's Industrial Policies

As we have seen above, the first characteristic of South Korea's industrial policies and industrialization policies is that they have been carried out under government guidance. Secondly, economic development is sought with exports forming the base accompanied by a number of welcome preferential measures being given to exporting companies. The third point of significance is that the capital needed for industrialization has depended on loans from abroad and direct foreign investment. Then fourthly there is the way in which Japan has been kept in mind as a model for economic development, with copies having been made of various Japanese systems. Also, a number of similar policies have been introduced in Korea. One example of this is the establishment of KOTRA, which resembles JETRO, as an organization for the promotion of trade.

It could be said that the finance system has proved to be very effective as a measure of promoting industry in South Korea. Since the First Five-year Plan each of the plans has been advanced by way of the government's induction of funds for limited allocation. The various financial organizations associated with the South Korean government have been in charge of the allocation of funds for the important polcies and their implementation (refer Table 11).

In regard to export financing, a number of preferential measures have been taken, among which are interest rates which are considerably lower than normal rates.[1] Since the Second Five-year Plan in particular, preferential development measures were taken for each separate priority industry in regard to the importation of capital goods and raw materials and the tax system. In the case of the priority industries, promotion measures have been taken for each individual industry in regard to funding. The establishment of the "Machine Industry Development Fund" on the basis of the 1967 Machine Industry Promotion Act is just one such example. In addition, the financing system was expanded to include funds, such as the Industrial Complex Creation Fund and the Petrochemical Industry Construction Fund, for the industrialization of the heavy and chemical industries.

During the period of the Third Five-year Plan the "People's Investment Fund" was created for increasing the supply of long-term capital for exports and the heavy and chemical industries.

A particular feature of Korea's finance is the existence of "private bonds" as a form of unsystematic finance. The private bonds are not the surplus funds of individuals or companies which are directed at banks or other systematic financial organizations. Rather, they are used for direct loans made to companies or for the purchase of bills and are a type of finance which aims to support real interest rates which are high. The interest rates for the private bonds range between 4-6% per month, and it is common for only small and medium-sized companies and companies affiliated to the *zaibatsu* which do not receive the advantages of guidance policy finance to depend on the bonds.

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[1] The role which low interest finance has played has been considerable. For instance, in 1965 when interest rates for commercial loans were 26% exporting companies were able to borrow up to 78% of necessary capital at the low rate of 6.5%.

Also, in South Korea there is a custom of mutual aid finance called *"Kei"*. Funds which are gathered from this system earn high interest rates on the private bond market through finance brokers. A survey undertaken in 1981 revealed that 64% of savings derived from the nation's household budgets are put into private finance markets such as the private bonds or *kei*.

Because the people's "angler" finance market is large, in 1984 the domestic savings ratio for South korea was 26.5%, lower than Taiwan's ratio of 30.5% and Japan's 31.6%.

Behind the overseas loans which sustained South Korea's economic development in respect of capital lie unsystematic factors within the country. A decisive factor in establishing an independent finance system which would not depend on loans from abroad will be whether it is possible to concentrate the nation's savings in financial organizations to a greater extent than at present.

In addition to the policies concerning heavy and chemical industrialization which were promoted in the Third Five-year plan the provision of incentives in the tax system also brought results. For example, companies which invested in priority industries such as the petrochemical and shipbuilding industries were exempt from paying corporation tax and income tax for a period of three years, and for the following two years after that were exempted from paying 50%. Also, companies which invested were given either 8% investment credit (10% for domestic machinery and equipment), or permitted 100% special depreciation (1974).

These kinds of financial and tax incentives stimulated the private activities of South Korea's *zaibatsu* and it could be said that they brought about the favorable circulation of private investment and economic development. Furthermore, the Korean people are very concerned about the education of their children, and so being able to make use of an abundant high quality work force was an important fundamental condition for carrying out industry promotion policies within Korea.

It is perceived that South Korea's future industry policies will entail the fostering and strengthening of technology related to advanced technology and engineering, and that it will move towards securing international competitiveness (refer Illustration 1). As pressure from the U.S. to open up markets is increased and the later developing countries catch up, South Korea's industry policies will promote liberalization and will include the task of joining the ranks of the world's advanced nations.

2-5-2. Taiwan's Industrial Policy

Industrial Policy Transitions

(1) Points of Departure

Tainwan's industrialization began at the end of World War II, when the Japanese monopoly capital and industrial facilities and infrastructure built up by small enterprise during the pre-war occupation were nationalized to create a national capital monopoly. Since it began with the reconstruction of industry and enterprise, the transition from the refurbishing of old facilities to an expansion of production was accomplished rather easily. By 1952, in fact, production of primary industrial goods had exceeded the highest levels of the pre-war period.

The vital foundations of Taiwan's industrial policy and industrialization strategy can be traced to three events: first, the currency reform of 1949; second, the agricultural reforms carried out during the years 1949-1953; and third, the influx of capital from the mainland during these same years.

At the time of Taiwan's establishment the new nation faced many difficulties, including the employment problems brought about by a dramatic population increase (with two million refugees from the mainland joining the six million native Taiwanese), the economic stagnation that resulted when Japan cut off economic relations, and severe inflation. The government responded with two major policies: the currency reforms, which aimed at a policy of monetary equilibrium independent of both fiscal and financial policy; and the agricultural reforms, which were carried out by the Kuomintang administration in order to dissolve the native land-owning population and consolidate their political power base on the island.

The currency reforms brought a neutral budgetary and financial policy foundation to the Taiwanese economy and eventually led to relatively stable prices and the development of a healthy savings-investment mechanism. Furthermore, small- and medium-sized businesses in the agriculture, forestry, and mining fields that were difficult for the bureaucracy to manage were sold off to private investors, as were large cement and paper manufacturers (the latter in the form of making up for insufficient compensation). In this way, landowner capital was transformed into commercial and industrial capital. The inflow of enterprise and capital from the mainland (primarily in the spinning industry) also made a significant contribution to later development of private capital. The inflow of people and money, in addition to breaking up a huge national capital monopoly and promoting the growth of private capital, ultimately played a major role in the growth of the Taiwanese economy as a whole.

(2) The Development Process and Transitions in Policy Emphasis

With the mitigation of inflation brought about by the currency reforms, the success of the epochal land reforms, and the effective utilization of U.S. aid, postwar reconstruction progressed steadily; by 1953, in fact, both agricultural and industrial production had returned to pre-war levels. In 1953 the first of the nation's economic development plans was unveiled. Altogether, there have been seven: the First Economic Construction Four-Year Plan (1953-56); the second plan (1957-60), which emphasized import-replacing industrialization; the third (1961-64), fourth (1965-68), and fifth (1969-72) plans, which stressed export-oriented industrialization; and the sixth plan (1976-81), which stressed heavy industrialization, with the 1980s being touted as the decade for advanced industrialization.

1. Industrial Policy During the 1950s (1953-60)
-- First steps toward import-replacing industrialization --

In accordance with the slogan of the day, "Cultivate agriculture through industry and develop industry through agriculture," the government's industrial policy centered around agriculture. Since Taiwan's economy had yet to fully recover, the primary objectives of the first four-year plan were to develop industries (mainly in the durable consumer goods sector) capable of producing substitutes for imported goods, eliminate shortages in daily necessities for the people, stabilize prices, and improve the nation's international balance of payments. In order to realize these goals, the following concrete steps were taken:

a. Emphasis was placed on the distribution of capital to the electric power industry, as a foundation for industry, and the fertilizer industry, as a foundation for agriculture (the latter specifically in order to increase production and exports of rice and sugar and reduce the nation's dependence on fertilizer imports).

b. Funding for these efforts was provided through national savings and export income, with the remaining portion being made up for with economic aid from the United States.

c. In order to efficiently utilize the limited foreign currency reserves, a comprehensive import plan for necessary goods was established that provided clear distinctions between products to be procured with foreign currency (i.e., U.S. aid) and those to be purchased with on-hand Taiwanese reserves.

d. High tariff barriers were erected to protect local industries, then in the process of recovery. Low tariff rates would be levied on an exceptional basis for those imports deemed necessary.

e. In order to achieve the above goals, strict import regulations such as the Import Permit Items List (?) and an import licensing system were enacted. Included in this administrative system were import prohibitions and restrictions covering product, origin, and intended use.

f. Adoption of currency management using compound exchange rates.

The use of compound exchange rates made it possible for the government to keep down the prices of necessities while at the same time making unnecessary, nonurgent items prohibitively expensive. This resulted in a de facto "sorting" of all imports.

During 1953-61, the econommy was host to several phenomena unique to the import-substitution period such as overvaluation of the currency, a relatively high rate of inflation, and an increase in the national budget were present, but annual economic growth of more than 7% was recorded under the first two economic plans.

From the 1950s through the early 1960s, the financial sector and government-managed enterprises in all fields of industry played a major role in place of private enterprise, which had not yet grown sufficiently. During this time, however, accumulated private capital, consisting of capital from the mainland as well as new local funds, grew steadily, and by the time that the export drive of the 1960s was about to begin a foundation for the development of labor-saving processed goods had already been established.

2. Industrial Policy in the 1960s

-- The transition to export-oriented industrialization --

By the end of the 1950s, the development of import-replacing industry had been accompanied by drastic increases in the production of textiles, agricultural goods, and other industrial products. By 1958 the domestic market had reached its saturation point, and so private enterprise began looking to overseas markets. It became increasingly recognized in government circles that, in order to allow continued industrial development and economic growth, foreign markets would have to be utilized.

The Taiwanese economic environment during the period from the late 1950s to the early 1960s was characterized by the following conditions:

1) The economy was plagued by a continuous international balance of payments deficit exceeding $100 million.

2) The urgent need for a change in policies to a self-powered type of government became apparent as U.S. economic aid was switched from grants to loans and signs could be seen of reductions and even cutoff.

3) Facility investment and raw materials had become responsible for over 90% of all imports. Since these imports were imperative to further economic growth it was difficult to impose import restrictions, and in order to improve the international balance of payments it became necessary to promote exports.

4) The government-managed key industries had been consolidated, and private enterprise had grown. Furthermore, Increased agricultural productivity had resulted in the emergence of surplus agricultural labor, thus preparing the soil for development of industrial sectors. In addition, work on the development of a transportation network encompassing domestic and international ports was proceeding, and the conditions required for exports had all been met.

The third, fourth, and fifth four-year economic construction plans of the 1960s were thus situated at a time when the foundations had been laid for export-oriented industrial development. Domestically, budgetary policies were enacted to stop the increase in defense expenditures, and trade reforms were enacted to liberalize imports, eliminate the compound exchange rate system that had hindered exports in the past, and correct the overvaluation of the currency. Interest rates were also brought in line with effective market rates. Externally, aggressive programs to attract foreign capital were introduced.

Superior compatibility and mobility were required of the concrete policies directed toward export-oriented industrialization, including import tariffs, import administration, and exchange rates. These were to contribute to the promotion of the various domestic policies.

First of all, the high across-the-board tariffs were reconsidered, and the government began a gradual roll-back of all import duties, allowing rapid progress in the liberalization of imports. Among laws established for the promotion of exports were the Investment Promotion Act, the Foreigner Investment Act, and the Technology Cooperation Act, and preferential tax treatment for production and investment was utilized. In 1965, with the creation of the Kaohsiung export processing district, foreign capital was aggressively sought out. Bonded factory and warehouse systems were also established.

Foreign-owned multinational corporations were the leading exporters, but local small- and medium-sized export enterprises began exports through the use of foreign and overseas Chinese trading company networks and began to increase their share of total exports. Mergers between smaller trading firms and joint ventures with foreign-owned firms were also tried, but the organization of such comprehensive trading firms proved to be difficult.

3. Industrial Policy during the 1970s
-- The road to flexible heavy chemical industrialization --

Under the third, fourth, and fifth economic construction plans, export and processing type industries developed with the introduction of foreign capital, exports grew rapidly, and the Taiwanese economy achieved amazing growth. The export-oriented industrialization, however, also had several weak points, including an overabundance of light industrial products and a continuing reliance on imports for intermediate raw materials and mechanical facilities. In order to improve this situation, heavy chemical industrialization policies, which might better be described as a policy of "second import-replacing industrialization", were enacted. In the sixth plan beginning in 1973, most of the emphasis was therefore placed on the promotion of heavy chemical industry.

As a comlementary policy to the sixth economic construction plan, the "10 Major Construction Projects"(?) plan (1974-79) was begun as a counter-inflationary measure. The economic plan itself was brought to a standstill only three years into its implementation because of the worldwide recession that followed the first oil crisis, but the "10 Major Construction Projects" plan continued, clearing the way for expanded production at nationally-managed enterprises and a consolidation of industry infrastructure. This plan attempted to nurture the steel, shipbuilding, and petrochemical sectors by mandating the creation of three large state-managed enterprises -- China Steel, China Shipbuilding, and China Petroleum. The remaining seven projects, however, were aimed at the social infrastructure -- highways, railroads, airports, maritime ports, etc. -- and investment in the petrochemical industry fields represented only 20% of the total for the plan.

In order to overcome the structural weak points that had become evident during the oil crisis and achieve modernization of the economy, the medium-term economic construction six-year plan (1976-81) was selected to replace the unsuccessful sixth plan. Emphasized in this plan were the preparation of social capital (mainly the above-mentioned ten construction projects) and the promotion of agriculture.

After the "10 Major Construction Projects" plan was concluded in 1979, the "12 Major Construction Projects"(?) plan (1979-83) was initiated, but again, six of the twelve items were directed towards roads and railways. The only industry-related item, in fact, was an increase in annual crude steel production at China Steel, with most of the plan's provisions directed toward the rebuilding of a foundation for agriculture, new city development planning, and other agricultural promotion and social welfare measures.

In any case, heavy petrochemical industry projects were few and far between, and the majority of capital was supplied domestically -- this in response to the lessons taught by two oil crises. In effect, government officials chose a course emphasizing stable growth over the rapid but risky route of heavy chemical industrialization. At the same time, current energy policies were reinforced with a further commitment to nuclear energy, and the need for a transition from highly labor-intensive and energy-consuming sectors to technology-intensive and labor-saving fields became fully recognized.

As private capital developed, the role of state-managed enterprise became one of supporting private enterprise from the sidelines. During the heavy chemical industrialization in the second half of the 1970s, in particular, a structure developed in which the huge state-managed enterprises oversaw key industry sectors requiring large capital investment, while private enterprise was entrusted with the downstream sectors.

4. Industrial policy in the 1980s
-- The road to industrial advancement --

Labor-intensive processing industries have been the centerpieces to Taiwan's industrialization. As the result of wage hikes and changes in the labor supply and demand structure, however, the prominence of labor-intensive industry as a means to national development has rapidly dwindled since the late 1970s across the globe. Since heavy industrialization has not produced significant results outside the petrochemical sector, emphasis has now been shifted to the new high-tech industries.

A ten-year construction plan has been laid out for 1980-89. Its most important objectives are "advanced technological industry, the securing of manpower for the chemical and technological fields, and the promotion of research and development in industrial technology." The plan puts forth a transition to energy-saving and technology-intensive industries in the country's attempt to make the great leap from the ranks of semi-developed countries to the circle of advanced nations.

Industries singled out in the current plan include electronics, automobiles, and machinery. These have been designated as strategic industries and as such are accorded certain incentives such as increased retention of corporate earnings, exemption from investment taxes, and long-term, low-interest financing. Components and materials with high-variety, low-volume and special production are emphasized: semiconductor materials, sensors, and computer peripheral devices (e.g., printers) in the electronics industry; automobile components in the automotive industry; and vending machines, sewing machines, and assembly machines in the machinery industry.

Taiwan's industrial advancement is proceeding at a relatively relaxed pace. Among the factors responsible is the current industrial organization, in which huge state-owned enterprises supervise the upstream sectors while private enterprise is limited mainly to downstream areas and small-scale light industrial goods production in particular. Given this situation, it is difficult to expect the small- and medium-sized private enterprises to put out the money required for research and development expenses or even to have the desire to move into new fields. Although private enterprise is supposed to bear part of the responsibility for industrial advancement, there are efficiency problems, and for the time being at least the tempo of advancement can be expected to be leisurely.

In order to break through the current economic quagmire, the Taiwanese government is proceeding in its liberalization of exchange rate and trade administration and is relaxing protectionist barriers. In addition, it appears to be moving toward an opening of the country as a processing and production base and toward the formation of an international trade and financial center.

Other Characteristics of the Taiwanese Economy

1) A double (Public-private) Capital Structure

In the Taiwanese economy, the state has control over key industries and financial institutions, administering industry and finance and promoting industrialization under government leadership.

Despite this, however, it is private enterprise that has borne the burden of increasing exports and pushing ahead with growth. Small enterprise has played a particularly important role in this. In the latter half of the 1960s, when foreign capital and export-led industrialization grew rapidly, private production surpassed production at state-owned enterprises, and by the mid-1970s private enterprise was responsible for more than 80% of all production in Taiwan.

2) Export-bearing Small Enterprise

During the period of high growth from the second half of the 1960s through the first half of the 1970s, the number of privately-owned small- and medium-sized corporations with fewer than 500 employees grew significantly, with production at these firms accounting for 50% of total Taiwanese production. Moreover, the ratio of exports to total sales at these firms was roughly 2:3.

3) An Emphasis on Public Welfare

Taiwan's economic development has come to recognize the importance of public welfare. In past economic plans, preparation of the social infrastructure (including farming villages) was emphasized, with considerable attention being paid to education, medical insurance, welfare, and the environment. Even during the peak of heavy chemical industrialization efforts, a complete balance was sought between industrialization and public welfare.

Workmen's insurance (comprising workmen's compensation, health insurance, and a pension plan) was introduced in 1950, and by 1955 it was made mandatory at businesses over a certain size.

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2-5-3. Japan's Industrial Policy

1. History of Japan's Industrial Policy

The issue facing the Industrial Policy from the late 1940s to the 1950s was reconstruction of the Japanese economy. To rebuild the devasted economy, emphasis was laid on reconstruction of such basic industries as electric power, coal, and steelmaking. The government adopted the policy of distributing the limited raw materials, funds, and foreign currency to these sectors on a priority basis. Materials were allocated, financing provided, and prices controlled.

To clarify the emphasis on promotion of small and medium sized enterprises, the government established the Small and Medium Enterprise Agency at around this time and created the prototype of its current small business policy, which includes promotion of modernization of small businesses, promotion of greater sophistication through financing and organization, and diagnosis of management operations.

Industrial Rationalization and Promotion Period (1950s)

Japan completed the reconstruction of its economy around the middle of the 1950s and then shifted emphasis in its industrial policy to greater self-sufficiency of the economy through promotion of exports and rationalization of industry.

The Ministry of International Trade and Industry, which was reorganized and launched anew from the old Ministry of Commerce and Industry in 1949, took a stance of priority to trade, giving predominance to its trade-related departments and giving then a clear role as sections in charge of production as well as export, thus combining production and trade. Further, in view of the export promotion it was thought to be essential not only to strengthen production but also to reduce cost of production and improve quality by industrial rationalization. The MITI established a section for comprehensively drafting and executing industrial rationalization policies for trade promotion and set forth a clear policy of promoting expots through improvement of facilities, enhancing of the level of technology, and other forms of rationalization of industry. In 1950, a single exchange rate of US$1=360 yen was set.

At the same time, the government decided on a basic policy for rationalization of industry by which it set for itself the goal of bringing the prices of domestic goods close to international prices. The government established policies for guidance of individual industries based on projections of the future industrial strucutre and guided and promoted business rationalization based on the same. Further, it established the Industrial

Modernization Council, comprised of 31 subcommittees, as an advisory organization for examining necessary matters pertaining to industrial rationalization.

In response to a proposal by the Council stressing the need for capital accumulation, the government strove to increase corporate capital in the early 1950s by reappraisal of assets, creation of reserves for uncollected credits etc., special tax privileges such as special exemptions on export income, special tax measures such as a special depreciation system, and the like.

While the government prompted companies to increase their capital accumulation internally through the preferential tax system, it expanded fiscal investments and loans through the Japan Development Bank etc. so as to provide support for capital accumulation externally.

After the enactment of the foreign investment law in 1950, there was an influx of foreign funds and technology, which played a large role in the rationalization and technical development of Japanese business. The system of exemptions of import duties on important machinery also contributed much to the promotion of technical transfers.

High Growth Period (1960s)

The 1960s saw Japan move to an open economy, through liberalization of trade and capital, as a member of the international community. In this process of this, Japan was experiencing high economic growth. The aims of the industrial policy during this period were to overcome the restrictions on economic growth arising due to the international balance of payments and to strengthen international competitiveness for the heavy machinery and chemical industries.

The government refrained from direct intervention in industry as a whole, prefering to set down general directions and guide business according to the same in a cooperative public-private manner. On the other hand, for key sectors such as machinery and electronics, it created special legislation and devised protective and promotive policies for modernization of the industrial structure.

In the "Law on Temporary Measures for the Promotion of the Machinery Industry", the government designated specific machines for promotion, including molds and dies, under rationalization schems and through financing.

Moderate Growth Period (1970s on)

By the 1970s, Japan was enjoying sustained high economic growth and had reached the income level of mid-rank European nations. At the same time, however, strains began to appear due to the rapid growth and industrialization. These changes in social conditions, the severing of the U.S. dollar from the gold standard under new U.S.

policies, the introduction of import duties, the subsequent rise of the yen value, and the oil crises all led to a great shift in the management of the Japanese economy in the 1970s.

Instead of the previous stress on export competitiveness, the government began to emphasize achievement of a balance in its foreign trade and moved to liberalize imports and capital. The oil crises triggered a decline in the growth rate which in turn led the government to seek various changes in the industrial structure such as rationalization, enhanced added value.

Under these conditions, the industrial policy served to summarize the government's conception of the direction of change in industrial structure and international relation and greater importance was taken on by means for guiding corporate activity in that direction. The basic idea followed in the 1970s was the achievement of "knowledge intensity" to cope with the changing needs of the people, i.e., a conversion to knowledge intensive industries such as research and development, advanced assembly, fashion, and information.

In the 1980s, Japan began to play a greater role in the global economy. Its industrial structure also has been shifting more and more away from an export dependent one to one characterized by a horizontal international division of labor. It was understood that domestic technology reached western levels and it became impossible to ensure future growth through just importation of foreign technology. In view of this judgment, the government took its industry policy a step beyond the stress on knowledge intensification of the 1970s to a stress on guidance for technology intensity and intellectual labor based on independent technical development. At the same time, Japan moved to supply the production technology and knowhow it had accumulated over the years to other countries along with capital so as to put them to use in the stimulation and development of the world economy.

2. Features of Japan's Industrial Policy

(1) Organization

Playing an important role in the decision-making process of Japan's industrial policy are, on the administrative side, [1] the bureaus in charge of the individual industries, started around 1930, and [2] the bureaus in charge of coordination within the ministries and agencies and, on the private side, the various industrial organizations. For important policy matters, further, opinions are sought from councils comprised of members from industry and government, with policies decided upon based upon their recommendations.

The industrial bureaus are in charge of drafting policies related to the industries under their jurisdictions. The government avoids direct intervention in industry as a whole and rather takes the policy of setting certain targets and guiding industry in accordance with the same, but for important policywise sectors adopts strong protective policies under specific individual laws. Laws relating to the promotion and control of specific industries are primarily drafted and executed by the industrial bureaus. Based on these laws, production plans are established, controls are enforced, industrial standards are prepared for products, and the production processes of businesses are rationalized.

The policy tools include abatement of taxes (special tax measures), providing subsidies, and extension of capital funds through government affiliated financial institutions. The proposals for the same are also put together primarily by the industrial bureaus. The original drafts for the policy of liberalization of imports, changes in tariff schedules, and policy of liberalization of capital related to various industries are also prepared by the industrial bureaus.

The coordinating bureaus both coordinate matters between various industrial bureaus and tackle a broad range of industrial readjustment policies relating to trade friction, energy, and development of high technology. The importance of industrial readjustment policies has been rising along with the reduction in the number of industries being specially promoted.

The industrial organizations and the councils may be said to function as a cooperative public-private system. In particular, in the execution of government policy, the industrial organizations cooperate with the government, rather than being subjected to mandatory measures under the law. They play important roles in promoting voluntary compliance by industry with the general policy directions indicated by the administrative side

(2) Policy Tools

In the industrial rationalization period and the high growth period from the 1950s to the 1960s, the following main policy tools were used:

[1] Priority fiscal expenditures for industrial infrastructure

[2] Preferential tax treatment in steelmaking, automobiles, shipbuilding, and other key industrial sectors through a special depreciation system

[3] Low interest financing and fiscal investment by government affiliated financial institutions using postal savings, the annuity account, etc., as main resources.

Starting in the middle of 1965, the government began providing financial assistance to large scale technical development projects relating to industrial technology, computers, etc. Since 1970, the government's industrial policy, based on Japan's "vision" of the future, has become of increasing importance as a blueprint for industrial activity.

(3) Small and Medium Enterprise Policy

The small and medium enterprise policy was started as far back as around 1930 and was reinforced with the establishment of the Small and Medium Enterprise Agency (1948) and the establishment of the Small and Medium Enterprise Basic Law (1963). Diverse policy tools have been used for this, including financing, taxes, subsidies, supply of information, preferential purchases of products by government offices, etc.

Table I-2-26. Industrial Promotion in 5 Asian Countries & Areas

JAPAN	KOREA	TAIWAN	THAILAND	MALAYSIA
Postwar Reconstruction Period (1946-48) "Priority Production System" Material Quota/Reconversion Finance Bank Loans/Price Control				
Industrial Rationalization Period (the first half of 1950's) Preferential Treatment for equipment investment (special depreciations)/Loans from the Japan Development Bank/Tax Exemptions	**After The Disturbance in Korea** (1950's) Import Substitutional Industrial Development Promotion Aids Quota System/Double Exchange Rate/Tax Exemption for Raw Materials & Machinery	**Import Substitutional Industrialization Period** (the first half of 1950's) Adjustment of Public Key Industries—Sugar, Cement, Fertilizer, ... etc./Textile Industry Promotion with Bave Import Quota	**Import Substitutional Industrialization Initial Stage** (1950's) Act on Promotion of Industries (1954) Import Substitutional Industrialization Focusing on National Enterprises & Light Industry	**Import Substitutional Industrialization Initial Stage** Pionir Status Ordinance (1958) Tax Exemptions & Deductions for Pionir Enterprises/Import Substitutional Industrialization (Food Processing & Textile)
Industrial Development Promotion Period (the latter half of 50's) Synthetic Fiber, Petrochemical, Electronics, Machinery Tariff Protection/Selective Fiscal • Financial Policy (Loans from the Japan Development Bank, Depreciations, Tax Exemptions & Reductions)/Approval of Technology Introduction		**Transitional Period to Export Oriented Industry** (the latter half of 50's) Adjustment of Public Key Industry/Textile • Agricultural Product Processing Industry Development.		

JAPAN	KOREA	TAIWAN	THAILAND	MALAYSIA
High-Growth Period (1960's) Building an Open Economy. Industry-Government Cooperation System (Investment Adjustment/Co-ordination of Production Field/Industry-by-Industry Development Programs (Law on Extraordinary Measures for Machinery Industries/Law on Extraordinary Measures for Electronic Industries.)	**Transition to Export Oriented Industrialization** (1960's) Stressing Economic Growth. Introduction of Foreign Capital (Mainly Loans)/Export Light Industry Promotion/ Tax Exemptions/Key Industry Promotion With The Government Initiative & Intervention	**Export Oriented Industrialization in Full-Swing** (1960's) Introduction of Foreign Capital (Loans & Direct Investment)/Focusing on Private Sector/Export Processing Zone/Tax Exemptions & Deductions/ Trading Company Promotion	**Import Substitutional Industrialization Progressive Stage** (1960's) Promotion of Industrial Investment Act/Stressing Public Enterprises & Introduction of Foreign Capital/ Remittance Foreign Capital Liberalization/Tax Exemptions of Raw Materials & Machinery Imports/Foundation of IFCT, SIFO	**Import Substitutional Industrialization Progressive Stage** (the latter half of 1960's) The First Malaysia Plan (66-) Import Substitutional Industrialization by Introduction of Foreign Capital.
Stable Growth Period (1970-) Drawing up "Vision". Utilizing Market Mechanism. Knowledge-Intensive Industry. High Technology Development.	**Export Oriented • Heavy & Chemical Industrialization** (1970's) "Heavy & Chemical Industries-Strategic Industrial Development Plan" Government Controlled Financing Organization. Export Industry • Heavy & Chemical Industries Promotion With Low-Interest Loan. Expansion of Equipments in Private Enterprises.	**Heavy & Chemical Industrialization** (1970's) 10 Major Development Plan Foundation of Public Enterprises of Iron & Steel, Oil and Shipping/Social Capital Adjustment	**Parallel Commitment With Export Oriented Industrialization** (1970's) Expanding Introduction of Foreign Capital/Strengthening BOI/Expanding privilege on Tax	**Parallel Period of Import Substitutional Industrialization & Export Industry Promotion** (1970's) New Economic Policy (NEP) Export Industry Promotion (Parallel with Import Substitutional Industrialization) Industrial Coordination Act. Guide Line of Foreign Capital Introduction Export Processing Zone. Heavy & Chemical Industrial Promotion.

JAPAN	KOREA	TAIWAN	THAILAND	MALAYSIA
	Liberalization • Heavy Chemical Industries Co-ordination (1980's) Economic Liberalization. Leaving Public Cooperation to Private. Foreign Capital Liberalization. Finance Liberalization. Heavy & Chemical Industries Co-ordination Small- and Medium-size Enterprises Promotion	**High Technology Promotion** (1980's) Specifying Strategic Industry. Tax Exemptions for Electronics & Machinery/Low-Interest Loans/Preferential Internal Revenue Fund/Automobile Industry Promotion.	**Export Oriented Industrialization in Full Swing** (1980's) Massive-neutralizing Foreign Capital Constraints/Strengthening Foreign Capital Introduction/Approval of Majority Foreign Capital/ Tax Exemptions & Deductions for Export Oriented Investment	**Export Oriented Industrialization** (the latter half of 1980's) The Fourth Malaysia Plan. Review of Foreign Capital Constraint. Specifying 12 Prior Type of Industry According to Industrial Master Plan.

3. Export Promotion Policies

3-1. Transition of Export Promotion Policies

Thailand began promoting exports with the 1960 Export Promotion Act. At the time, however, 13 traditional export products (rice, rubber, tin, maize, tapioca, jute, shrimp, tobacco, sugar, etc.) accounted for over 80% of the exports. Thailand had to wait until it industrialized through the influx of direct foreign investment before it could promote exports of so-called industrial manufactures.

Thailand began industrialization with the Act on the Promotion of Industries 1954. Before that, it lacked sufficient capital formation in the private sector and entrepreneurial ability, so the government adopted a policy of promotion and strengthening of state owned enterprises. In 1959, the BOI (Board of Investment) was established and in 1962 the Industrial Investment Promotion Act, which laid down a clear policy of turning over the leading role in industrialization to direct foreign investment, was enacted. Limitations on land holdings by foreign capital were eliminated, permission given for remittance of the principle and profit on investments to the home country, and other measures taken, thus creating the framework for Thailand's foreign investment policy.

On the other hand, the first economic development plan began from 1961. It was followed by a second plan. During those 10 years, Thailand industrialized at a fast pace. However, these plans were founded on import substitution industrialization and while there was progress in conversion to domestic production of final consumer goods, the increased demand for these consumer goods led to an increase in imports of intermediate goods and capital goods and thus resulted in a deterioration of the international trade balance. As a result, from 1971, in the third 5-year plan on, while the government continued to promote import substitution industrialization in its industrialization policies, *it also stressed the promotion of exports of industrial manufactures. In 1971, it* established tax refund systems for import duties and business taxes applied to the production of products for export. In 1972, it set up tax incentives such as rebates on import duties and business taxes applied to export goods. Further, the 1972 New Investment Promotion Act and the 1977 Investment Promotion Act established various privileges for promoted projects and export oriented projects. Exports were thus promoted as part of the foreign investment policies of the BOI.

The instrument used for export promotion throughout the 1970s may be said to have been basically the tax incentives, just as in the 1960s Thailand promoted import substitution industrialization.

In the 1980s, however, criticism arose that (1) the incentives to the promoted projects were conversely increasing imports of machinery, (2) the incentives to the large privileged enterprises were in a way obstructing the exports of local small- and medium-sized enterprises, and (3) there was a lack of incentives for human resource development, technical transfers, and research and development.

Therefore, in the fifth and sixth plans, the export promotion projects of the Ministry of Commerce were expanded, tax incentives improved and made more efficient, export financing increased, interest rates made more flexible, and measures taken to improve the quality of products, thus laying stress on improvement of the execution of the export promotion system, rather than creation of a new system as it were. Further, while the government maintained measures to strengthen the direct price competitiveness of export products, it also took measures to promote the development of non-price reduction areas such as marketing and improvement of quality.

On the other hand, the standards for extension of incentives are being reevaluated in accordance with the objectives of other policies, such as the decentralization of factories, the promotion of processing of agricultural and fishery products, etc. BOI's policy became more selective in application.

3-2. Outline of Export Promotion Measures

Thailand's export promotion measures can be roughly divided into (1) tax incentives such as exemption and reduction of import duties and business taxes, income deductions on export income, and refunds on import duties, and rebates on indirect taxes such as import duties and business taxes, (2) the export credit refinancing system of the Bank of Thailand, (3) the establishment of bonded manufacturing warehouses and export processing zones, and (4) the activities of the Department of Export Promotion (DEP) of the Ministry of Commerce.

3-2-1. Tax Privileges

These include privileges extended to projects promoted by the Board of Investment (BOI) and the refund and rebate systems for import duties and indirect taxes handled by the Custom Department (CD) of the Ministry of Finance and the Fiscal Policy Office (FPO).

(1) Privileges of BOI

Under the Investment Promotion Act 1977, the BOI may designate certain projects as approved for promotion of investment, which status is accompanied by special rights, and give tax privileges to investment promotion projects.

1) For export oriented enterprises

The Investment Promotion Act provides the following privileges to export oriented companies:

[1] Exemption on import duties and business taxes for raw materials used in the manufacture of export oriented products. Exemption on business taxes imposed on purchases of domestic raw materials.

[2] Exemption on import duties and business taxes for re-exported items

[3] Exemption on export duties and business taxes

[4] Deductions from taxable corporate income equivalent to a 5% increase of exports over the previous year, excluding cost of transportation and insurance.

Of these, [1], [2], and [3] are aimed at giving export products price competitiveness through lessening of the tax burden on imported raw materials and machinery, like the tax refund and tax rebate systems, while [4] is aimed at providing financial assistance to export promoted enterprises.

The export promotion measures of the BOI form the core of Thailand's export promotion policies. In recent years, export promoted companies have come to account for the majority of the enterprises promoted by the BOI. The qualifications for recognition as an export promoted enterprise differ depending on the product, but recognition is given to labor intensive goods for which Thailand has relative superiority. Some of the conditions for recognition are the export ratio of production and the date of start of the exports.

2) For enterprises exporting over 80% of production

In addition to the incentives given to export promoted enterprises, the BOI allows companies with export ratios of over 80% or those producing for export in principle a 50% or 100% exemption on the import duties for imported machinery, depending on the region in which the factory is situated, and 3 to 8 years' exemption on corporate taxes. However, in May 1988, the BOI changed some of the conditions on indirect export for exemption of corporate taxes. Now, when there are competing enterprises not receiving the tax privileges of the BOI in Thailand, a distinction is made between direct exports and indirect exports, which were previously viewed the same, and exemptions are allowed only when the direct export ratio is over 60%. Therefore, BOI's conditions on privileges to indirect export companies become more strict. On the other hand, even non-BOI approved local companies may now be promoted to enter the parts and intermediate goods markets.

The standards for application of privileges for promotion of investment were enforced as of September 1987.

<Problems and Issues Facing BOI>

The investment privileges of the BOI have played a large role in the expansion of exports of industrial manufactures, but there are the following problems.

First, it is necessary to clarify the guidelines for application of investment privileges for indirect export companies. Most of the increase in exports of industrial manufactures starting in the 1970s was based on industrial goods through processing deals. The group of products features a high dependence on imports of parts and intermediate goods. Therefore, the exemption and reduction of tariffs and indirect taxes on imports of input goods contributed to strengthening the international competitiveness of the export products, but on the other hand resulted in a delayed growth of the domestic parts and intermediate goods industries. As is same case to Asian NIEs. If Thailand is to proceed and shift its exports of industrial manufactures from one based on processing deals to one where it supplies its own parts and intermediate goods, then it will have to quickly promote investment in these fields. However, in extending its privileges, the BOI relies much on negotiations with the investing companies. This is one factor which causes companies interested in investment to hesitate. If the BOI were to make the guidelines for application of privileges in these fields clearer, it might help to promote investment.

Second, there is the strengthening of privileges for technical transfers. The BOI scheme is effective for strengthening international competitiveness by reducing costs, but does not sufficiently promote transfer of technology in industries where direct cost reductions are less urgent than improvement of technology, such as the mold and die industry. Future topics which should be considered are the improvement of the quality of export products and the improvement of the level of technology for the same.

3) For international trading companies (ITC)

ITCs, whose establishment was encouraged under the 1977 Investment Promotion Act, enjoy (1) the privileges for export oriented companies of the BOI mentioned above, (2) the privileges of exemption from income of overseas advertising expenses and various overseas costs, (3) the extension of special export credit of the BOT, and (4) special permission to hold up a certain amount of foreign currency.

The BOI has helped launch these international trading companies with the aim of promoting exports of new products through development of export markets and to shift trade transactions from foreign trading companies to Thai trading companies. However, while the BOI approved 21 companies at the start, most trading companies could not toe the mark and thus had their status as investment promoted companies cancelled. At the present time, only a handful of companies are active. In 1985, these accounted for only 4.7% of all exports (Table I-3-1)

Table I-3-1. Exports of International Trading Companies 1979 to 1985

(Unit: Million Bahts)

Year	Exports of International Trading Companies				Total Exports of Thailand	Share of International Trading Companies
	Account 1	Account 2	Account 3	TOTAL		
1979	43	621	217	880	103,179	0.81%
1980	370	1247	703	2319	133,197	1.74%
1981	979	2120	1102	4200	153,001	2.75%
1982	2,144	1,946	1,340	5,430	159,728	3.40%
1983	4,072	2,429	1,537	8,088	146,472	5.52%
1984	5,675	4,048	2,091	11,815	175,237	6.74%
1985	4,234	3,254	1,520	9,008	193,337	4.66%
TOTAL	17,517	15,664	8,559	41,741		

Source: BOI

Note: Account 1 covers traditional export items (including rice, maize, tin, rubber, and sugar, etc.)
Account 2 covers export items showing considerable export performance (canned goods, tobacco, textiles, apparel, wood products, plastic products, etc.)
Account 3 covers new export items.

For international trading companies to receive the privileges of the BOI, they must meet yearly targets for total exports and for exports of new products not exported much up until then. These conditions can in practice only be met by companies belonging to large corporate groups.

In addition, the international trading companies are facing problems in being forced to handle transactions with small profit margins, due to the stress on exports, and insufficient experience in trade practices, resulting in a low level of orders, lack of thoroughgoing quality control, delays in deliveries, and other hindrances to trade. The Ministry of Commerce is currently studying how to best foster international trading companies.

(2) Tax Refund

In addition to the incentives of the BOI, the Customs Department offers tax refund. This system allows for the repayment of import duties assessed on imported raw materials and parts and imported semifinished goods included in export products.

There are the following three main conditions to use this system:

[1] The amount of the imported goods used for the production, assembly, or packing of export goods is calculated by the customs authorities based on a predetermined formula.

[2] The exports must be made within one year after the import of the goods covered by the refund.

[3] The demand for the refund must be made within six months of the export of the export goods in principle.

When using this system, producers of export goods pay for the various import related taxes in cash upon the import or else give a bank guarantee (yearly rate of 1.5%).

The aim of this system is to strengthen the export competitiveness of products by eliminating the taxes included in export products and, simultaneously, to promote exports through reducing the export price to one lower than the price for the domestic market. For example, the textile industry is reported to rely on imports for one-third of its raw materials so this system has great merits for it.

There was criticism about the refund system, e.g., the long time taken until actual repayment and the heavy interest cost, but in recent years the Customs Department has been working on this and has shortened the period until repayment to an average three to four months. However, for some products, trouble still frequently occurs between the applicants and customs authorities on the percentage of imported raw materials and parts and semifinished goods included in the export product. The agency in charge of this system, the Fiscal Policy Office, ranks applicant companies and speeds repayments to top ranked companies.

The system is often used together with the tax rebate system, mentioned next, but the amount of refund under the system is higher than the tax rebate system (Table I-3-2).

(3) Tax Rebate System

The Fiscal Policy Office makes available a tax rebate system. This system is administered by the Customs Department. Under the system, part of the import duties, business taxes, etc. (not including income taxes, royalty taxes, regional taxes, and taxes exempted by above tax refund) assessed on materials, equipment, and parts included in export products. The rebates are paid out in tax coupons which are valid for three years. The rebate rates are calculated by a different system from the tax refund system, i.e., are indicated by ratios of FOB prices for each product according to the customs classification. The rebate rates come in two types: A and B, the A-rate schedule applying to imported and domestic raw materials etc. and the B-rate schedule applying to just domestic raw materials etc.

The A-rate schedule offers high rebate rates (0.45 to 8.42%). Companies producing export goods, after comparing the refund under the above tax refund system, either apply for the tax rebates with the A-rate schedule for domestic goods and imported goods or apply for the tax refund system for imported goods and the tax rebates with the B-rate schedule for domestic goods.

The rebate rates of each item are calculated using input coefficients of Thailand's streamlined IO table.

The repayment term of this system is short, usually from one to two months. However, it seems that the Fiscal Policy Office will be delayed in the transition to the H.S. method of classification of goods, a project it is now engaged in.

Table I-3-2. Total Value of Exempted and Reduced Tax

	1983		1984		1985		1986		1987	
	Million baht	%	Million baht	%	Million baht	%	Millin baht	%	Million baht	%
1. Total Imports	236.609	100.00	245.155	100.00	251.168	100.00	241.358	100.00	332.913	100.00
2. Imports under BOI Investment Promoted Privileges	11.960	5.05	15.113	6.16	20.326	8.09	20.756	8.60	35.524	10.67
Imports of Machinery	5.284	2.23	4.618	1.88	8.116	3.23	5.747	2.38	9.748	2.93
Imports of Materials	6.676	2.82	10.495	4.28	12.210	4.86	15.009	6.22	25.776	7.74
Exemption and Reduction of Import Duties and Business Taxes for Imports	3.301	1.40	3.20	1.60	4.713	1.88	6.207	2.57	10.748	3.23
3. Tax Refund under Customs Act	1.372	0.58	1.840	0.75	2.993	1.19	3.069	1.27	3.916	1.18
4. Tax Rebates for Export of Domestic Products	593.3	0.25	1.486	0.61	1.417	0.56	2.112	0.88	3.417	1.03

Source: FPO

3-2-2. Export Finance

As financial incentives for export, there is the export credit refinance offered by the Bank of Thailand through the commercial banks. Under this system, the BOT provides low interest to commercial banks for financing export related bills issued by export companies. The aim of this is to strengthen the price competitiveness by reducing interest costs and improving the profit margins of export companies.

Thailand began export finance in 1959 in the form of rediscounting of export bills for rice exports. Since the 1960s, it offered the same to other primary products and industrial manufactures as well. Further, in 1986, it improved the export credit refinance system so as to promote its use.

The main improvements over the rediscounting system were as follows:

[1] Under the old system, the interest was deducted from the principle on the date of discounting, so the real interest rate and nominal interest rate of the finance differed. Under the new system, they are the same.

[2] The complexity of the calculation of settlements before the time of bill settlement was eliminated.

The BOT decides on the overall framework of the finance for each year and allocates finance to the individual commercial banks in consideration of the previous performance. The overall financing framework is decided in consideration of the effects on inflation and interest trends.

This finance is applied to all items except re-export items and to all regions. It is also made available to commissioned processing production of export goods, contract labor, and other services.

3-2-2-1.

The schemes of the system are as follows:

(1) Basic Scheme

Interest rates (yearly)

Commercial banks to export companies: 7%

BOT to commercial banks: 5% maximum

(However, interest rate to commercial banks for production of new/ nontraditional products is 4%)

Amount of refinancing per note

BIll of exchange:	90%
L/C:	80%
Contract or purchase order:	70%
Warehouse receipt:	60%

(However, above rates are reduced by 10 percentage points each when exports are of specific new/nontraditional products by export trading companies encouraged by the BOI or when shipped by a Thai vessel.)

Maturity

Maximum 180 days from repurchase by BOT

Financing ceiling

Limited for each commercial bank in form of credit line

Measures in case of violation of financing obligation

Fine of 8% of financing to export company (year) or 2% to commercial banks (year). (However, additional 5% and 2% in the case of reoccurrence within one year.)

(2) To Small Scale Export Enterprises

The BOT sets small scale exporters, defined as exporters having a revolving credit outstanding of less than 5 million bahts, apart from the basic scheme mentioned above and designates an interest rate to the small scale export companies of 7% and one to the commercial banks of 4%. The interest spread of the commercial banks is 3%, advantageous financing terms for the commercial banks.

Note that in addition to the above (1) and (2), there is a scheme for approved international trading companies, which the BOI has encouraged the establishment of, under the 1977 Investment Promotion Act, and a scheme for exports of yarns and cloth to the U.S. under the textile agreement with the U.S.

<Problems and Issues>

The export credit refinance system of the BOT has grown steadily and in recent years has covered from 40% to 50% of the total value of exports. The items covered by the system used to be largely so-called traditional export goods such as rice, tapioca, sugar, and maize, but recently there has been an increase in financing for industrial manufactures, such as canned foods (see Table I-3-3). This may be considered to reflect the effects of the reduction of the interest rates on new, nontraditional export goods, the privileges extended to small scale export companies in financing, etc.

Table I-3-3. Export Bill Refinanced by the Bank of Thailand Classified by Nature of Products

(Unit: million baht)

Products	1980	1981	1982	1983	1984	1985	1986	1987	Percentage share (%) 1966-71	1972-79	1980-85	1986-87
1. Agricultural	13,801	14,386	21,981	25,266	29,529	26,519	25,859	19,867	77.1	31.7	33.4	27.0
Rice	6,341	5,677	11,843	12,780	14,640	11,224	11,330	13,087	39.0	13.0	15.9	14.4
Maize	1,803	2,150	3,344	5,057	6,436	6,123	5,604	1,767	27.4	6.5	6.3	4.4
Rubber	1,855	2,108	1,356	1,575	2,125	2,099	1,916	1,497	2.0	4.0	2.8	2.0
Seafood	2,051	2,848	3,710	3,866	4,074	4,768	4,359	1962	n.a.	n.a.	5.4	3.7
Beans	458	447	509	414	673	831	719	604	0.4	2.0	0.9	0.8
Others	1,293	1,147	1,219	1,574	1,581	1,474	1,931	950	8.3	6.2	2.1	1.7
2. Industrial	26,160	35,691	35,497	41,257	45,291	43,868	46,738	50,146	18.9	63.1	57.9	57.2
Sugar	3,329	9,927	5,620	5,721	4,517	5,049	5,851	5,181	4.1	24.8	8.7	6.5
Tapioca Products	10,046	9,570	11,255	14,401	14,409	11,836	12,276	13,590	9.3	18.3	18.2	15.3
Textiles	3,437	4,979	5,571	6,285	8,634	6,909	7,016	8,078	–	6.7	9.1	8.9
Canned Food	2,839	4,008	5,403	6,217	7,462	7,916	9,149	8,557	2.6	3.8	8.6	10.4
Tobacco	902	1,289	1,811	1,467	1,046	1,390	955	830	2.0	2.7	2.0	1.1
Others	5,616	5,918	5,837	7,166	9,223	10,768	11,491	13,910	0.9	6.8	11.3	15.0
3. Others	2,882	3,643	4,536	4,802	6,931	11,454	13,218	13,561	4.0	5.2	8.7	15.8
Mineral	666	1,147	785	509	665	795	380	365	n.a.	n.a.	1.2	0.4
Miscellaneous	2,216	2,496	3,751	4,293	6,266	10,659	12,838	13,196	n.a.	n.a.	7.5	15.4
4. TOTAL	42,852	53,720	62,014	71,325	81,751	81,841	85,815	83,574	100.0	100.0	100.0	100.0

Source: BOT

However, problems still remain. First of all, from interviews with different companies, it was reported that while the procedures, including preparation of variosu documents, are being streamlined, they are still fairly compicated. That is, companies have to submit financial statements, tax payment documents, and various other materials along with their applications. Usually, small and medium sized enterprises only rarely have all these documents on hand. Under the present conditions, therefore, these procedural problems are one of the main obstcles to get finance, it has been pointed out often. Supposedly, even the commercial banks are forced to engage in complicated administrative processing work due to the need to check on the credit of the companies for the BOT. On top of this are the severe restrictions of the BOT. This makes new borrowers reluctant to apply for the finance

Second, the financing is biased in large measure to large corporations and exporters of traditional export items. Financing of small and medium sized enterprises, with their low credit ratings, is inherently something to be avoided by the commercial banks in view of risk management. (For example, it was reported that there were less than 20 cases of financing of industrial bills of small and medium sized enterprises in the eight years from 1978.) Therefore, commercial banks demand securities as a condition for loans, thus limiting the increase in financing of small and medium sized companies, which account for an overwhelmingly large percentage of the exports of industrial manufactures.

A 1984 survey showed that the average export credit of the 482 small sized export companies out of a total 863 export companies studied was less than 2 million bahts and that these firms accounted for just 4% of the total financing. As opposed to this, the average finance to the top 30 companies was 300 million bahts, accounting for one-half of the total financing. For this reason, the fifth plan propounded the establishment of an Export Credit Guarantee Institute.

Third, the system should preferably be expanded more and be given more flexibility in execution. The coverage by export refinance of all exports in 1987 fell to 27% from the 47% of 1985 and the 42% of 1986. This reason may be in the smaller difference in its interest rates from commercial interest rates, but promotion of exports of industrial manufactures in the future will probably require raising the financing ceiling and giving more flexibility in interest rates.

3-2-3. Export Processing Zones and Bonded Factories

The export processing zones are established inside industrial estates for the effective promotion of export companies. To qualify for entry into an export processing zone, a company must export all of its production. The incentives to resident companies include the incentives given to the industrial estates plus the following:

[1] Exemption of import duties and business taxes on imported machinery and materials

[2] Rebates of import duties and business taxes on materials purchased from domestic businesses

[3] Exemption of export duties and business taxes on exported products

An export processing zone was established in the Lat Krabang Industrial Estate and others are being constructed at the Northern Industrial Estate and Laem Chabang Industrial Estate

Further, there are now over 70 bonded factories. These enjoy the same privileges as companies in the export processing zones.

<Problem and Issues>

[1] The IEAT is supposed to handle applications for entry into industrial estates and the construction and management of industrial estates, but companies scheduled to enter the export processing zones are supposed to apply to the BOI when receiving exemptions on corporate taxes. In recent years, the export processing zones have been also been dispersed to regional areas. It is therefore desirable that a single agency handle everything.

[2] More and more export processing zones have been established in recent years, notably in the regional areas. This is part of the government's policy of dispersing factories to the regional areas, but there is a problem with the infrastructure in such areas. Even various privileges (such as on water supply, power, and transportation) would not be enough to eliminate corporate unease over such locations, it has been said. The government should strive harder to establish the necessary infrastructure.

[3] Comparing the privileges of the bonded factories with those of companies in the export processing zones and those of the BOI, due to the condition imposed that goods imported under bond be reexported within one year, there is in practice no exemption of import duties or business taxes on imports of machinery. From the viewpoint of promoting rural industry, it would be desirable a broader range of incentives were extended.

3-3. Activities of Ministry of Commerce

3-3-1. Department of Export Promotion (DEP)

The Department of Export Promotion is an agency under the Ministry of Commerce and is in charge of marketing in overseas markets and collection of information for the purpose of export promotion.

<Staff>

The DEP has a formal staff of about 300 (including 60 Temporary staffs).

<Budget>

The DEP has three fund sources: [1] about 100 million bahts in budgetary allocations from the general account (fiscal 1987/88), [2] 90 million bahts from the Export Promotion Fund (EPF), funded in part by import duties, and [3] about 70 million bahts in foreign aid from international associations such as the ITC, UNCTAD, and EC.

<Organization and Business>

The DEP engages in the following activities handled by eight divisions and one office:

[1] Collection of information overseas and information service in Thailand

[2] Sponsoring of and participation in exhibitions in Thailand and overseas

[3] Dispatch and receipt of various missions

[4] Holding of lectures and seminars.

The DEP has trade centers in 13 locations overseas and commercial offices in 32 embassies. In Thailand, it has regional branches, i.e., Export Service Center, in Khon Kaen, Songkhla, and Chieng Mai.

The overseas trade centers collect information, participate in exhibitions, attend to missions, handle inquiries, and run credit checks on buyers. They make overall reports on their work once a year and frequently send other reports. The representative staff returns to Thailand once a year for exchanges of information with the local authorities and to participate in formulation of the plans for projects of the DEP of the following fiscal year and are thus very active.

The commercial offices engage in the same work as the trade centers, but their staff returns home only once every four years, so they may be unfamiliar with current conditions at home and cannot get their opinions sufficiently across to the headquarters.

The three local ESCs make available information on overseas markets, distribute DEP materials, and hold lectures and seminars.

The DEP takes up 75 key export goods each year from the three categories of agricultural produce, mining products, and industrial manufactures, designates 19 of these as target products and sets export targets for the same for each year, and engages in the above activities (Table I-3-4). Further, it designated [1] textiles and garments, [2] processed food, and [3] jewelry as key items out of the above 19 products for fiscal 1988/89.

As an information service to domestic businessmen, it publishes the Daily Trade News, with a paid circulation of 15,000, the biweekly Exporter's Review, and a yearly directory Thailand Exporters Selected List.

Table I-3-4. DEP's Target Products

Garment & Textiles	Household Textile
Processed Food	Fresh Horticulture
Gems & Jewelry	Gift Items
Artificial Flowers	Toys
Footwear	Leather Products
Furniture & Parts	Construction Materials
Wall & Floor Tiles	Household Utensils
Electrical Appliances	Plastic Products
Rubber Products	Printing Industry
Auto Parts & Accessories	

<Problems and Issues>

The various activities of the DEP and other organizations contribute to the improvement of the export environment - an area in which the government should play the leading role, but there are many problems in expansion of activities and improvement of efficiency.

First, a factor inhibiting the expansion of activities is the limited budget. The World Bank ran a survey in 1985 on the export promotion organizations of the world. Compared by country, Thailand spends about half that of Hong Kong, Sri Lanka, and Taiwan in public funds for export promotion activities (not including export related financing). Apart from that, it has insufficient information on competing countries. At the present, it would be desirable that Thailand establish trade centers, now in 13 locations, in the competing export countries as well to improve its ability to gather information.

Second, there is the problem of improvement of efficiency of activities. The DEP is promoting the establishment of export associations through its various activities.

To further promote these services, it is necessary to more positively reflect the wishes of the exporting companies in the formulation of projects and foster closer ties between the DEP and private companies. Toward this end, greater activity by the regional branches and a brisker exchange of opinions between the DEP and private companies would be desirable.

Third, there is the problem of coordination with other agencies in the export promotion activities and consolidation of projects. Promotion of exports requires projects spanning administrative boundaries of the various government agencies. In Thailand, the semipublic Export Development Committee (EDC), chaired by the Minister of Commerce, is in charge of such coordination and elimination of obstructions to exports. However, there is a complicated tangle of authority among the various ministries and committees and the EDC has been unable to perform as envisioned, it has been pointed out. One conceivable method to deal with this would be to set up an independent agency for execution of export promotion projects.

3-3-2. Export Inspection System

Thailand established its export inspection system with the 1960 Export Standard Act. In 1979, it further established the current Export Commodities Standards Act. Under this system, exporters of items designated as requiring inspection register with the Commodities Standards Division of the Foreign Trade Department of the Ministry of Commerce, under inspections by the inspection offices or designated inspection organizations, and receive quality certificates.

At the present time, inspections are compulsory for 12 agricultural and mineral products (Table 1-3-5).

Table I-3-5. List of Designated Commodities

Bleached jute
Caster seed
Fishmeal
Kapok cotton
Maize
Mung beans
Salt
Silver
Sorghum
Tapioca products
Teak conversion
Thai silk

Further, commodity standards for the following seven items are expected to be established shortly:

[1] gold products, [2] legumes, [3] vegetables, [4] seafood, [5] fruits, [6] raw rubber, and [7] tapioca powder.

The commodity standards rank products in terms of quality, i.e., first grade, second grade, third grade, etc. are are applied flexibly in accordance with the commodity's application and destination. Further, provisions are made on the sampling methods for the tests, specific methods for testing and analysis, and durability and performance considering packaging and shipping conditions.

Note that the surge in direct investment in export oriented industries in recent years has resulted in continued growth in exports of industrial manufactures to Japan. Therefore, there is strong interest in the JIS designated factory system and the Electrical

Appliance and Material Control Law and rising need for an inspection system with sufficient inspection facilities and staff.

<Problems and Issues>

At the present time, the actual export inspections are performed by public testing organizations and the SGS and other private firms and there are not particular problems. However, in the future, it will be necessary to extent the coverage of the compulsory inspections to industrial manufactures and light industrial goods. Toward this end, it is desirable to obtain more inspection facilities and measurement apparatus and further improve the industrial standards.

As a second point, the advanced nations are currently all establishing sanitation regulation standard systems for toys and electrical appliances. The requirements on sanitary Thai standards from the markets of the advanced countries are currently being handled by the exporters themselves through the inspection organizations, but to secure confidence from these markets, it would be necessary to establish strict, independent sanitary regulations which prohibit the sale of toys or other items containing toxic or hermful substances.

3-4. Export Promotion Policies in the Other Countries

3-4-1. South Korea's Export Promotion Policy

South Korea's export-oriented economic polcies started with the First Five-year Plan which was implemented in 1962. After the Korean War the domestic economic resource which the country could make use of was a "cheap, but considerably high-level" labor force. Since the First Five-year Plan the government has almost consistently implemented economic policies guided by foreign investment and which involve the addition of foreign investment to this labor resource. These policies have been implemented under close government guidance with the government mobilizing all possible means to foster the targetted industries and to promote exports.

The economic development strategy which was first implemented in 1962 involved import substitution of labor-intensive consumer goods, for which Korea was in a relatively good position, and also the promotion of exports. But since then the former has changed to import substitution of intermediate goods and the fostering and development of capital goods industries as a result of the development of the heavy and chemical industries. The objective of export promotion policies is to build an economic base for higher level industrialization and for independent growth, and as such the policies make up the foundation of the country's economic policies.

3-4-2. History of Export Promotion Policies

Although it is only natural that South Korea's export promotion policies have changed with the stages which have been reached in the country's economic development, they can be broadly divided into the export promotion policies of the 1960s which centered mainly on consumer goods, and the policies of the 1970s.

(1) Promotion Policies of the 1960s

During this period the change was made over to exports from the import substitution of consumer goods, and the latter part of the 60s was a period when the import substitution of intermediate goods was advanced. The policies for the establishment of the economic and related organizations for the various policies and systems aimed at export promotion at that time formed the basis of later export promotion policies.

1) Export Subsidies

In 1961 temporary legislation was enacted for the payment of export subsidies. Export goods were divided into four classifications and the amount paid in subsidies varied according to the classification. The export subsidies were abolished in 1965.

2) Export Finance

This was based on export letters of credit and loans were made for a 90-135 day period. The interest rate in 1960 was 13.87% which was a considerably better rate than the general 17.5% rate for loans at one time. The proportion of this export related finance was high and during the 1960s and 1970s export related preferential loans continually accounted for between 40-60% of total loans made by the Bank of South Korea. Also, the proportion of private sector domestic credit outostanding increased to 21% by 1975.

This export finance was the most preferred guidance policy finance. As it was possible to receive loans at low preferential interest rates from the Bank of Korea which were funds supplied by private financial organizations (rates decreased further by the Bank of Korea), the margins for the financial organizations were high and the loans became most profitable.

3) Tax Reductions and Exemptions

From 1959 import duties on raw materials imported for use in exports were exempted. Then in 1961 commodity taxes and government enterprise taxes for export goods were also exempted. In addition, the income tax rates for income derived from exports (income obtained from foreign currency) were cut by 50%. This was later abolished in 1973.

4) Approval for the decrement exemption system in Imported Raw Materials for Export Use

This was an indirect subsidy for export industries where a decrease for a fixed amount of imported raw materials for use in export was permitted.

5) Discounts in transportation fees and electricity charges for export industries

(2) Export Policies of the 1970s

1) Preferential Taxation Measures

Although the system for reductions and exemptions in taxes on income derived from foreign currency was abolished in 1973, new measures were put in its place. They were:

(a) system for inclusion of money lost on reserve goods for developing overseas markets

(b) system for inclusion of losses from export reserve funds

(c) system for inclusion of losses from lost reserve funds for overseas investment

(d) special accelerated depreciation ratio for export companies

2)Tax Rebates

The system was established in 1975. The system for reductions and exemptions in the payment of import duties for imported raw materials for use in exports was changed to a system of tax rebates.

3) General Trading Company System

A system for general trading companies based on Japanese general trading companies was introduced to provide an effective overseas marketing system. While in 1975 the amount of exports handled by general trading companies accounted for only 14.5% of exports, this amount had risen to 55.5% in 1984.

4) Export Industry Base Expansion Funds

This involved a change from the promotion of the heavy and chemical industries and from the short-term financial assistance given to mainly trading companies to increasing the amount of funds provided to production companies for expanding plant and equipment, and production, and medium and long-term finance.

5) Establishment of Export Associations

6) Export Manufacturing Complexes

(3) Export Promotion Policies of the 1980s and Future Tasks

Although the export promotion policies of the 1960s and the 1970s contributed to the increase in exports, mainly involving light industries, once into the 1980s this type of economic policy guided by exports has caused more than a few problems. As regards export promotion, firstly, although the assistance given under government direction contributed to the formation of company groups, this caused stagnation amongst the small and medium-sized companies which form the base of technologically advanced industries. Secondly, the inflationary financial assistance had the end result of causing the accumulation of foreign debts.

3-4-2. Taiwan's Export Promotion Policy

Taiwan's domestic market, just as South Korea's, is very limited, and as a result industrialization has from the very beginning inevitably aimed at export (import?) substitution. By the early 1960s, in fact, the first export (import?) substitution period had already begun. The cutoff of U.S. economic aid in 1965 also served to intensify this trend. Major Taiwanese export promotion policies are described below.

1) Export Refund Tax Policy (1955)

A system by which tariffs paid on raw materials for products to be exported are refunded. In June 1983, it was decided to eliminate this system five years hence. The tariffs themselves, however, are gradually being rolled back across the board.

2) Exchange Rate Policy (1958)

Until 1958 a compound rate system ($1 = 10 yuan or 15 yuan) had been utilized. These rates were overvalued, however, and in 1958 the rate was established at 40 yuan to the dollar to conform with realistic world conditions (this rate remained effective until 1973).

3) Relaxation of Import Restrictions (since 1958)

Imported products are currently divided into three categories: prohibited, restricted, and free. The number of free items is gradually increasing.

4) Establishment of Export Processing Zones (1965)

In the arena of foreign capital induction policies, 1954 saw enactment of the "Foreigner Investment Act," while the "Overseas Chinese Investment Act" was passed into law the following year. At the time, however, the Taiwanese political situation was far from stable, and foreign investment was minimal.

With the advent of the 1960s Taiwan began to take aggressive measures to attract foreign capital. The "Investment Promotion Act" was enacted in 1960 to allow identical legal treatment for domestic and foreign capital, provide tax reductions and exemptions for investment in specified fields, and relax restrictions on profit remittances. Concerning the introduction of technology, the "Technology Collaboration Act" was established in 1962, providing a tentative system for the protection of know-how and patent rights. Furthermore, the "Processing Exit Zone Facility Management Act" was passed in 1965 as a foreign capital introduction policy with the objective of promoting exports, providing the foundations for the first export free zone to be constructed at Kaohsiung.

Although it is estimated that exports of products produced at the export processing zones totaled only 7% - 8% of Taiwan's total exports and the hiring effect was roughly the same, these zones can be said to have fulfilled their "pump-priming" role as show windows for the nation's foreign capital induction policies. The bonded factory system was also set up in 1965, and outside the export processing zones was applied to export industries.

The foreign capital induction policies, which provided in most cases for obligatory exports, coupled with domestic market factors, allowed Taiwan to achieve rapid export growth starting in the mid-1960s. This was to be the beginning of the nation's road to membership in the ranks of the NIES.

In the 1970s export promotion policies were pursued further, and the second import-replacing (heavy chemical) industrialization was embarked upon. The effect of these policies, however, was far less than the authorities had hoped for.

In 1973 the ten national construction projects were begun, starting the nation down the road to heavy chemical industrialization, but with the sole exception of the petrochemical industry heavy industrialization such as occurred in neighboring South Korea was not to be seen. In contrast to the latter nation, where heavy chemical industrialization proceeded as almost a national project and *zaibatsu* were formed, in the case of Taiwan small- and medium-sized enterprise developed and free competition was encouraged.

References: Yamazawa, I., and Hirata, A. "Industrializaion in LDC and Export Promotion Policy" (Institute of Development Economy)

3-4-3. Directions of Export Promotion Policies of South Korea and Taiwan

The most effective incentive offered in the export promotion policies of South Korea is said to be its low interest export financing. The interest rate on export loans substantially remained below the 10% mark throughout the 1960s and 1970s, offering a difference from the loan interest rate of commercial banks of as high as 20%. During this time, export financing accounted for about 50% of the overall loans of the Bank of Korea.

On the other hand, South Korea abolished the commodity tax on export goods and the business tax on export industries in 1961. Further, in 1977, with the introduction of the ad valorum tax, it was returning almost all taxes paid on export goods in the process of manufacture and sales.

As opposed to this, Taiwan placed stress on tax privileges for investments under its initial Foreigner Direct Investment Act. Later, it shifted to a stress on construction of export processing zones.

However, these two regions have been changing their export promotion policies in recent years. Both regions have lowered their tariff rates. South Korea is reviewing the privileges provided to export industries, for example, reducing the difference in its interest rates on export financing from commercial rates since the end of the 1970s. In the two regions, the export promotion policies have worked for labor intensive goods and light industrial goods, but the authorities have realized that they cannot work to promote industrialization in the high tech fields requiring advanced skills or in creation of an export industry for the same.To reinforce their international competitiveness, they are shifting their emphasis from cost reductions and conventional input such as labor and capital to improvement of technology and technological transfers.

Export industry promotion policies and export promotion policies of Asean countries are show Table I-3-6.

Table I-3-6. Export Industrial Promotion & Export Promotion in 5 Asian Countries & Areas

JAPAN	KOREA	TAIWAN	THAILAND	MALAYSIA
Industrial Rationalization Period (the first half of 1950's) Financial Preferential Measures. Export Preferential Finance (Low Interest Rate Reduction of the Bank of Japan)/Foundation of the Export Bank of Japan in 1950. Tax Preferential Measures. Export Income Deduction Special Deduction for Export Export Insurance. Foundation of JETRO.	**After the Disturbance in Korea** (1950's) Export Promotion in Import Substitutional Industrialization Export Promotion Fund/ Export Credit Finance/ Foreign Capital Deposit/ Export Subsidiaries (but Export was depressed)	**Import Substitutional Industrialization Period** (the first half of 1950's) Public Key Industry Adjustment/Bave of USA Aids Import Quota/Multiple Exchange Rate/Double Price System		
Industrial Development Promotion Period (the latter half of 1950's) Shipment Export (Loans from Export-Import Bank of Japan) Special Deduction of Incomes related to overseas transactions		**Transition Period to Export Oriented Industrialization** (the latter half of 1950's) Starting Rice, Sugar, Agricultural Processing Products Export (Public Sector)/Export • Import Exchange Link System		**Import Substitutional Industrialization Period** (1958-) Prior Status Ordinance (1958) Import Substitutional Industrialization with Introduction of Foreign Capital
High-Growth Period (1960's) Economic Liberalization • Strengthening International Competitiveness. Plant Export (Loans from Export-Import Bank of Japan) Special Deduction for Exports Overseas Market Development Reverse System Expansion of JETRO	**Transition to Export Oriented Industrialization** (1960's) Private Enterprises Promotion in Export Industry/ Direct Subsidiaries/Low Interest Loans/Accelerated Depreciation/Tax Exemptions & Deductions (Cost Reduction) Export Light Industry (Textile • Wig) Promotion	**Export Oriented Industrialization in Full Swing** (1960's) Exceptional Loans/Export Loans/Export Processing Zone/Trade Company Promotion/Tax Preferential Treatment by Investment Act./Introduction of Foreign Capital	**Import Substitutional Industrialization Period** (1960's) Promotion of Industrial Investment Act Establishment/Export Promotion According to Economic Plan/Raising Tariff due to Trade Deficit Expansion	

JAPAN	KOREA	TAIWAN	THAILAND	MALAYSIA
	Export Industry Rapid Growth Period (1970's) Expansion of Low Interest Loan/Export Processing Zone/Won Devaluation/ Sōgō-Shōsha System/ Export-Import Bank of Korea/Introduction of Value Added Tax	**Export Industry Advanced Period** (1970's) Strengthening Public Enterprises/Export Insurance/ Export Import Bank's Medium- & Long-Term Export Loan System/Foreign Trade Development Association (Far East Trade Service)	**Parallel Commitment with Export Oriented Industrialization** (1970's) Export Industry Promotion Project by Investment Promotion Act. Investment Preferency on Domestic Raw Materials, Labour-Incentive, and Localization/Tariff & Transaction Tax Exemptions & Deductions/Preferential Treatment on Reduction by Bank of Thailand. Strengthening Export Industry Promotion Project Streng-thening Tax Preferential Treatment/ Sōgō-Shōsha Promotion	**Parallel Commitment with Import Substitutional & Export Industry Promotion** (1970's) Export Industry Promotion Guide Line of Introduction of Foreign Capital/FTZ Act (1971) Electronics Processing with Introduction of Foreign Capital Export Financial System (1977) BUMIPUTRA by NEP
	Coping With Trade Conflict (1980's) Export Self-Constraint/Enterprise Advances to U.S.A. Promoting Open Market		**Export Oriented Industrialization in Full Swing** (1980's) Strengthening Policy Adjustment Function/Strengthening Export Development Promotion Organization/Establishment of Trade Training Center/Strengthening Investment Preferential Treatment & Introduction of Foreign Capital/Various Export Tax Rebate/Consideration on VAT Introduction	**Export Oriented Industrialization** (1980's) Strengthening Export Development Promotion System in 1983 Income Deduction/Accelerated Depreciation/Investment Deduction/Sōgō-Shōsha/ Neutralizing Foreign Capital Constraint Industrial Master Plan (1986-) Specifying 12 Prior Type of Industry. Resource • Non-resource