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The Effects of the Thai Economic Crisis and of Thai Labor Market Policies on Labor Market Outcomes: Executive Summary*

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Thailand was the first of the Asian developing economies to experience the financial crisis of the 1990s. For most Thais the most important manifestations of the financial crisis have been through the labor market because their most important earning assets—particularly for the poorer members of society—are their labor. The unemployment rate for the third quarter was fairly stable or declining during 1995-7, but then more than tripled in 1998 and further increased in 1999 to include 1.75 million people.

The objective of this report is to contribute to better understanding of the effects of the economic crisis on Thai labor markets and what role public policies have played or might have played in mitigating the adverse effects of this economic downturn on labor earnings and employment. The results in this report in some ways complement that in the previous literature, but also in some important ways go beyond or differ from the previous literature. They go beyond the previous literature, for example, by discussing in some detail the nature of relevant labor market policies and presenting new multivariate estimates of what geographical location, firm and worker characteristics are associated with such policy related measures as receiving wages below the minimum wages, being covered by severance pay, being covered by social security and being union members. This study also differs from most of the previous literature by demonstrating that real wage rates as estimated from the Labor Force Surveys (LFSs) did NOT decline in the immediate post-crisis period relative to the immediate pre-crisis period, despite many previous claims that suggest that they did fall. This casts a considerably different light from most of the previous literature on the extent to which the negative shock on the labor market caused quantity adjustments in

employment and hours worked versus adjustments in wage rates, which may have important implications not only for understanding the recent past but also for anticipating future developments. This study further differs from the previous literature in showing that, while overall the labor market impact probably was regressive in terms of income distribution, there were a number of important exceptions.

OVERALL LABOR MARKET EFFECTS

Analysis of the post-crisis period in comparison with the pre-crisis period and the time paths of labor market outcomes relative to the underlying secular trends, all using the LFS, indicate:

(i) A number of possible labor market quantity, price and earnings outcomes need to be considered. Examination of just employment on the quantity side, for example, may miss important quantitative adjustments in hours worked and in shifts between wage and nonwage employment. The pre-/post-crisis comparison suggests that there were important downward quantity adjustments in employment, but also in hours worked and in shifts from wage to nonwage employment.

(ii) The same pre-/post-crisis comparison suggests that there was *not* a downward adjustment in the real wage rate on the average, though there was some downward adjustment across rounds within the post-crisis period. In fact, post-crisis average real wage rates *exceeded* pre-crisis average real wage rates apparently due to a combination of reduced hours worked for workers paid monthly and weekly and selective movements from wage to nonwage employment and to unemployment by previously lower wage workers.

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(iii) The time patterns of adjustments differed importantly among the major labor market outcomes. Initially, for the third quarter of 1997, employment was on the longer-run secular trend and the number of unemployed workers was below the secular trend, so that the quantity adjustment basically was in hours worked (including some increased underemployment). This, together with apparent wage rigidities, contributed to increased measured real wage rates. Subsequently, adjustments became larger in employment and in wages.

(iv) Thai workers fared better (in terms of their real earnings being protected) than workers in most other countries affected by the Asian financial crisis. Wage labor earnings declined by about -7.6 percent in 1998, which was less than the decline of -10.0 percent in GDP. In contrast, wage labor earnings declined nearly three times as much as GDP in Korea and Indonesia. That the share of wage labor earnings in GDP increased in Thailand during the crisis period suggests that capital and land owners fared worse in a proportional sense than workers during the economic crisis.

(v) Previous studies on the labor market outcomes in Thailand and other East Asian economies are misleading with regard to “price” (wage) effects because of aggregation problems and because they confound changes in hours worked in their purported measures of changes in real wage rates.

(vi) Thai labor markets are not as flexible as those in some low-income countries, such as Indonesia, where virtually none of the adjustment to the economic crisis occurred on the unemployment side. The apparent limited wage flexibility in Thai labor markets is somewhat of a surprise given the absence of indications that governmental policies or unions introduce much rigidity.

(vii) The impact of the crisis on labor markets was not over at the end of the data analysis in this report. While unemployment stopped increasing in the third quarter of 1999, the unemployment rate still was significantly higher than it was before the onset of the crisis and most of the major labor market outcomes remained relatively far on the recession side of the secular trends in that quarter.

DIFFERENTIAL EFFECTS ON LABOR MARKET OUTCOMES FOR GROUPS DEFINED BY GEOGRAPHY, TYPE OF EMPLOYERS, AND INDIVIDUAL WORKER CHARACTERISTICS

Most previous studies on the impact of the Thai crisis have concluded that in most dimensions labor market outcomes worsened in the sense that they tended to impact more negatively on lower-income labor force participants—though with some exceptions, particularly regarding how women fared relative to men. This report provides a more nuanced characterization of these distributional effects by considering more labor market outcomes and by directly including among those

outcomes the changes in real hourly wage rates. It finds, as in the previous literature, that the shifts on net probably were regressive. But there also were a number of important relative shifts in the opposite direction, such as relative total employment gains by agriculture relative to manufacturing, services relative to banking and migrants relative to nonmigrants; relative wage rate gains by agriculture relative to services, construction relative to services, primary schooling relative to secondary schooling, production workers and craftsmen relative to professional and technical workers, and private employees relative to government employees; and relative real average monthly wage earnings shifts to services from banking and to primary schooling from secondary schooling. Thus the data suggest a number of progressive aspects of the relative labor market outcomes that resulted. They also suggest that the one progressive shift emphasized previously, from males to females, may not have been very large and in certain important respects may have favored males. Therefore this examination leads to a somewhat different understanding of the extent to which there were regressive shifts in labor market outcomes than that presented in the previous literature. As a result, the net effect of the different changes was to generally worsen the overall distribution of wage earnings in the population. However, the magnitude of the change was small; the Gini coefficient of wage labor earnings increased only by 1.5 percent during the crisis.

THAI POLICIES RELATED TO LABOR MARKETS

Thai governmental roles in the labor market are reviewed with respect to general labor protection, minimum wages, severance pay, the employee welfare fund, the social security fund, labor market information, various ad hoc short-term public measures to mitigate the crisis effects on workers, and regulations concerning unionization. These policies are placed into a broader historical perspective in order to be able to better understand changes subsequent to the initiation of the crisis in 1997. The report then considers how governmental policies related to labor markets changed during the crisis—with particular attention to minimum wages, severance pay, social security coverage, unionization, employment creation policies and public sector employment—and addresses the adequacy or inadequacy of the government’s responses to the crisis. We include multivariate exploration of what geographic, firm and individual characteristics are associated with access to a number of these programs.

(i) *Minimum wages*: The proportion of Thai workers earning less than the minimum wage did not change substantially during the economic crisis but remained large (about 30%). Since payment of the minimum wage is a legal requirement at least for formal sector employers under Thai labor law, there is obviously widespread disregard for this law. The non-compliance

with the minimum wage law is greatest in the construction and agricultural sectors, in the North and Northeast regions, and in rural areas. Female workers, younger workers and workers with less schooling are at the greatest risk of being paid wages that are below the minimum wage. One implication of the limited effectiveness of minimum wages pertains to public employment generation programs. An important requirement of well-targeted (to the poor) rural employment creation programs is that they offer compensation that is less than prevailing wages in the rural areas. This automatically limits participation in these programs to the genuinely poor. However, job creation programs that were implemented in Thailand during the crisis paid workers at least a minimum wage. This means that these programs must have attracted a large number of the nonpoor, as a very large proportion of Thai workers earn less than the minimum wage. A significant proportion of the poor may not have been able to obtain employment in these public works programs.

(ii) *Severance pay*: Thailand relies on severance pay requirements as opposed to an unemployment insurance scheme. The relevance of severance pay as a form of insurance against unemployment is limited in Thailand owing to the small proportion of workers covered by severance pay benefits. Obviously, only wage employees, who constitute less than 40 percent of all Thai workers, can avail of severance pay benefits. But even among these wage employees, the proportion actually covered by severance pay benefits is small—fewer than a third of all wage employees in the country and only 13 percent of private sector wage employees reported having severance pay coverage in the third quarter of 1999. Some of the most vulnerable workers from the perspective of being laid off during the crisis were more likely to have severance coverage (e.g., those in manufacturing). But those identified to be in many of the most vulnerable groups to be laid off had average or less than average probabilities of severance coverage (e.g., those in the North, service and clerical workers; and those working in construction and commerce). And schooling, which is not related to the probability of being laid off, is strongly associated with the probability of severance coverage. Therefore, the extent to which severance coverage provided more protection to those who were at greater risk of being laid off is limited, and in many cases it provided more protection to those who were at lesser risk of being laid off. In fact, severance pay coverage is strongly biased in favor of high-wage workers. It is thus clear that extending the severance pay requirement from six months to 10 months did not affect the vast majority of Thai workers.

(iii) *Social security*: The social security system had been in place since 1990 but in late 1998, a significant change was initiated, establishing pension and child allowance schemes for private sector employees. Due to the crisis and hardships on employers and workers, the implementation plan will phase in the full contribution rates over several years, so as to minimize

the contractionary impact of the new system. Questions remain about the long-term financial viability of the scheme, given the mandated benefits and contribution rates. A child allowance scheme uses general government revenues to finance benefits for children of only enrolled families, a relatively better-off group. The 1999 LFS data indicate that only 15 percent of Thai workers reported being covered under the Social Security Act (SSA), with wide variations across different types of workers. Not surprisingly, reported coverage is higher among private-sector employees than among state-enterprise workers and government employees, as public employees are already covered by the Civil Servants' Pension Scheme and the Civil Servants' Medical Benefit Scheme. Generally within the private sector, social security coverage currently favors better-off workers. The Thai government plans to expand the social security program next year to cover employees of companies with 10 or fewer employees. The expansion would add an additional 3.6 million workers to the program, boosting coverage to 9.3 million workers. These moves will go some way toward bringing low-wage employees into the folds of the social security program. However, it is clear that simply enacting laws will not achieve much, as current rates of compliance are poor.

(iv) *Unionization provisions and coverage*: Labor unions can protect some worker interests in an economic crisis. However, labor union penetration is very low in Thailand, and collective bargaining has not played an important role in Thai labor markets, especially after unions in state enterprises were disbanded after the 1991 military coup. In addition, state enterprise workers are forbidden to form unions, although the Thai parliament in mid-February 2000 passed the State Enterprise Labor Relations Act, which reinstates the right of workers in state enterprises to form unions and allows them to bargain collectively. The LFS data indicate that, as of August 1998, 4.6 percent of all private-sector wage employees in the country had a labor union in their workplace. Even fewer—2.9 percent—reported being members of a union. These are among the lowest rates of unionization anywhere in the world. Even these low numbers may overstate the importance of Thai labor unions in influencing the “social dialogue” among labor, industry, and government because the number of collective bargaining agreements—a better indicator of labor unions' influence—is much smaller than the number of labor unions in Thailand. The low rates of unionization are the result of significant obstacles to union organizing that are codified in Thai labor law and Ministerial regulations. For instance, there is no protection of a worker wishing to organize a union until he/she has successfully organized that union and is formally elected an executive board member of the union. In addition, unionization faces a significant “free rider” problem in Thailand, since current Thai law states that a negotiated work agreement applies to all workers in the factory, regardless of whether they are members of

the union that negotiated the agreement or not. Thai workers are thus able to benefit from union-negotiated contracts without being members of a union and contributing dues to it. The fact that unions are more commonly found in large establishments implies that there is a greater tendency for the better-off workers in Thailand to have access to and be members of labor unions.

(v) *Employment creation programs:* The government's 1999 economic stimulus package placed priority on creating employment and increasing incomes for those severely affected by the crisis in both rural and urban areas through a set of employment creation programs, including the so-called Miyazawa package, which was by far the largest of the job creation interventions. The objective was to spend the money quickly to stimulate the economy through job creation and productive investments, while at the same time cushioning the poor from the crisis and creating a foundation for future competitiveness. The Miyazawa package has provided employment to 88,967 educated employees and to 3.5 million workers equivalent to 319,182 person years. With such a large number of beneficiaries, one would expect the impact of the job creation programs to show up in reduced unemployment numbers for the country in mid to late 1999 (as the Miyazawa package began to be implemented only in April 1999). An examination of the August round of the LFS 1999 confirms this: unemployment in Thailand fell from 1.14 million persons in August 1998 to merely 0.99 million in August 1999—a decline of nearly 14 percent year-on-year. This was the first such decline in unemployment year-on-year since the onset of the crisis. Of course, it is unlikely that the Miyazawa package accounted for all of the decline in unemployment in August 1999. The improving economy and the other employment generation programs also likely contributed to the decline in unemployment. Real GDP had increased by 7.4 percent year-on-year in the third quarter of 1999 (after a 2.6% increase in the second quarter). Detailed data on the characteristics of individuals who obtained employment under these programs are not readily available. This information would be important in calculating the distributional effects of these interventions to see if these interventions provide employment and income assistance to the poor or to better-off workers. Given that these projects paid at least the minimum wage and about 30 percent of Thai workers receive less than the minimum wage, it seems unlikely that they effectively targeted the poor. These programs also were developed and implemented rather slowly, more than a year and a half after the start of the crisis, and appear to have had relatively low labor intensity.

(vi) *Public sector employment:* Though the private sector dominates in Thai labor markets, public sector employment also is important, particularly among wage employees. The pre-/post-crisis comparison indicates that total employment increased substantially for public sector workers—11.3 percent for government

workers and 27.5 percent for state-enterprise workers—in sharp contrast to the decline of -9.6 percent for private wage employees. Thus the substantial expansion in relative terms of public sector employment offset a little of the large drop in private wage employment (but only a little because private sector employment is so much greater than the public sector). For government employees, average real wage rates declined by -6.3 percent, despite the increased average schooling in this sector. This decline in the real wage rates of government employees probably reflects the fact that new part-time, contract hires were paid much lower wages than existing permanent employees. In contrast, real hourly wage rates for state-enterprise employees increased by 18 percent, much more than the increase of 1 percent for private wage employees. This large increase partly reflects a composition shift toward more-schooled and more experienced (or at least older) workers. But still it is striking in light of the increase of over a quarter in the number of state-enterprise employees and the general tendency documented in this report for marginal workers moving in or out of particular sectors to be lower-than-average wage recipients. It is all the more striking because state-enterprise employees tend to be much more highly paid than employees in the government sector or the private wage sector.

CONSIDERATIONS FOR FUTURE POLICIES

Current policies seem to provide very limited social protection for most of those affected adversely by changes in labor markets, some dimensions of what protection is provided have become available only with a considerable lag, and generally those who are covered best by such protection are those who are better off, not the poorer members of society. At the same time traditional social safety nets, such as the agricultural sector and unpaid family work, appear to have but limited capacity for providing such protection in response to the crisis that started in 1997. As the Thai agricultural sector and labor markets develop further, the agricultural sector and unpaid family labor status are increasingly going to be unable to absorb other workers laid off in an economic downturn. This also means that there will be an increasingly greater need for developing formal safety nets for workers laid off at such times. Further, as far as can be discerned from the pre-/post-crisis periods comparisons, real wage rates do not seem to have adjusted downward in response to the crisis—despite evidence that suggests that neither governmental regulations nor unions introduce the kind of rigidities into downward wage adjustments that are common in many other countries.

One implication of these factors is that it would be desirable to consider changing policies so as to offer meaningful social protection to vulnerable workers. One route to do so might be to attempt to ensure compliance by employers with existing laws, as suggested, for

example, in a recent World Bank review of the impact of the crisis on Thai labor markets. But it is not clear that with present laws the benefits of making current legislation much more effective will outweigh the costs. The costs include the potential of making labor much more expensive. For example, about 30 percent of current wage earners earn less than the minimum wage and only about an eighth of those employed (a third of wage earners) are in fact covered by severance pay provisions. Making effective for all workers (or for all wage workers) minimum wage and severance pay coverage would seem to increase substantially the cost to employers of hiring workers and exacerbate the current possible problems of limited downward wage flexibility—probably with significant costs in terms of economic growth and adjustment capacities to respond to changing markets and technologies. From this perspective, if there are to be efforts to strengthen the effectiveness of minimum wages and severance pay provisions, care should be taken to assure that they are not at such high levels so as to be very costly.

An alternative to deal with the effects of downward shocks is to introduce unemployment insurance. This is a contentious possibility, with unions, employers, government agencies, and non-governmental organizations taking different sides on the need for such insurance. While there is some merit to the argument that the concept of unemployment insurance may not be required due to traditional Thai values of self-help and reliance on the family and community, it is also the case that traditional support systems have been slowly breaking down in Thailand, as they have in other countries, as a consequence of rapid industrialization, urbanization, marketization of labor and modernization. As rural-urban migration continues, employment in the agricultural sector declines, wage labor markets expand, and Thai society continues to experience structural change, the need for augmenting the current system of informal social safety nets with more formal safety nets like unemployment insurance will increase. At the same time, there are a number of economic and administrative issues that determine whether or not unemployment insurance is feasible in Thailand at this time. Unemployment insurance schemes are not always feasible (or equitable) for labor markets characterized by relatively small formal sectors, though part of the argument above is that the formal labor market is likely to expand. In addition, there are questions about whether the existing infrastructure is capable of administering unemployment insurance effectively. At the very least, however, a comprehensive study on the economic and administrative feasibility (as well as equity implications) of having an unemployment insurance scheme in Thailand is warranted.

Unemployment insurance schemes also do not deal with the possibility that earnings of many who are employed are inadequate to cover what society deems to be a minimum standard of living. Unemployment insurance schemes moreover are often financed out of

revenues that are tied to employment, and thus raise the cost of hiring workers (though there is no reason why this has to be the case). For such reasons it will be worth considering having a comprehensive study on the economic and administrative feasibility and the equity implications of having other form of income-support schemes, including employment projects at low wages for those capable of working and welfare transfers for those not capable of working. The better such systems work, of course, the less reason there is to intervene directly in labor markets in ways that are likely to make most labor more expensive for employers—and, thus, effectively to tax employment creation. There are many questions about various dimensions of such possibilities, which is all the more reason why systematic consideration would be useful to clarify what are the magnitudes of potential costs and benefits.

Another important implication of the factors described above is that better information about labor markets would be desirable. Information has basic public good characteristics in the technical sense, which means that there is a strong efficiency case for the public sector subsidizing the production and dissemination of information. Limitations in current information about labor markets probably has been an important factor in the slowness of some policy responses and in the limited extent to which real wage rates apparently have fallen to facilitate adjustments in the labor market to the crisis. Indeed, an important indication of the need to improve information is that the current LFSs do not permit knowledge of whether in fact real wage rates fell for the same individuals. In this case, changing the LFS sample design to have a rotating panel design as in many countries would improve substantially the capacity for understanding what happened to individuals over time without inferences being confounded by compositional changes among various groups. But the information question is much broader than to provide a better foundation for historical analysis of the sort in this report. The payoffs in terms of private and public sector adjustments to changing conditions may be quite high from providing better and more timely information about a multiplicity of aspects of labor markets. Though there has been some recent consideration of how labor market information could be improved, the returns from substantial efforts to improving such information further are likely to be high.

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The New Foreign Economic Policy of Thailand and Its International Implications*

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The landslide win by the Thai Rak Thai Party in the general election of Thailand in early January this year has imbued many Thais with a heightened sense of intrigue toward impending policy changes. The Thai foreign economic policy is no exception, especially with a new, young foreign minister at the helm of the foreign ministry. Many questions can be asked with respect to the impending changes in the new foreign economic policy. What has been promised by the new administration? Is it really a new policy? Who are actually involved in the making of Thailand's foreign economic policy? And, perhaps most important of all, would the 'new' policy change the practice and outlook of Thailand with regard to its international economic behavior, commitments and obligations? These questions will be discussed in turn.

THE 'NEW' FOREIGN ECONOMIC POLICY

What could be considered a new foreign economic policy is contained in Section 4 of the Official Government Policy Statement. Although it is true that some elements of foreign economic policy can also be found in other parts of the official policy statement as well, such as those on agricultural policy and communications policy, the main thrust of the new foreign economic policy is found in this Section 4. Let us take a look at this section.

The first impression one gets from reading this section is that the new government and the new foreign minister are very serious about their pre-election campaign promises to change the foreign economic policy of Thailand from the one based on 'traditional diplomacy first, economic matters second,' to the one that stresses 'overall economic gains first and everything else second.' This is obvious from the opening statement in this Section, which says that ... "The Government is determined to elevate the international trade policy from one solely emphasizing the acceleration of exports at all levels to one focused on developing a global marketing

network system able to respond to the rapidly changing needs of consumers, thus integrating the Thai economy as part of a powerful global economy in a borderless world." Then the policy moves on to divide the issues into trade and finance. On trade, the government would like to develop Thailand into a center for global trade in goods and services, and to do so, it has to be able to develop its own products (agricultural as well as manufacturing) and services (including tourism and communications systems) that are world-class and world-recognized. This orientation toward global outreach, to go beyond traditional trade with traditional partners, could be the most vivid intention of this new policy.

Once the goal is set, the next step is how to reach it. Again, the government came with a clear answer: the local private sector or private businesspeople will be promoted to do the above. The government will promote Thai businesses to be able to obtain technology and intellectual property from all sources, and develop them to create value-added by enabling such businesses to diversify their production. If we can accept what could be perceived as an existing situation that the Thai business sector is not very innovative and Thai businesspeople and entrepreneurs often buy and use foreign technology for their own quick financial returns without too much concern for their own innovations, then what is aimed here by the new government is a new policy. We can find similar reference to this same Thai-owned or Thai-initiated value-added in other parts of the policy statement too. For example, in the sentence following the one referred to above, the government plans to promote the establishment of a fund to provide the opportunity for Thai investors and entrepreneurs to develop and utilize unique Thai know-how and indigenous intellectual property rights with full treaty protection. In agriculture, the new government wants to develop Thailand as a center for the production of organic agricultural products. In industry, the government will support measures to increase value-added in industrial production, and will support the growth of new entrepreneurs in small- and medium-sized industrial businesses in the new

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knowledge-based economy. In services, the government will help local businesspeople by instituting zoning measures and relevant regulations to counter the threat of takeovers and dominance by large-scale retail businesses which are mainly owned by foreign companies.

On international finance there is no clear statement in the new policy. The government did say in the economic policy part that it wants to implement exchange rate policies that facilitate economic recovery as well as the process of income creation for the people from all levels. No further details or elaboration are given anywhere. But it seems that whatever international finance issues that may be forthcoming, the government's direction is clear: that it will try to do what it can to protect local business interest as against foreign interest. The concern for local business interest is paramount and shows up here and there throughout the official policy statement.

WHAT IS AND WHAT WILL BE: POLICY THAT IS NOT IN THE OFFICIAL STATEMENT

Perhaps what the new government has said it wants to do in writing and what it wants to do in reality may not be the same. So, what the policy is and what the real action will be may have to be considered together. This is the case for looking beyond the policy statement to other indications for policy directions. In this connection, the 'body language' of those who are involved in shaping the foreign economic policy, the Prime Minister himself, or the Foreign Minister, or other ministers or party leaders, may reveal the true intentions not found in the policy statement. There are some indications about the change in foreign economic policy that can be gleaned either from relevant interviews or public comments by these ministers or leaders, or from other activities.

On Myanmar

Both Drs. Thaksin Shinawatra and Surakiart Sathirathai visited Myanmar in June last year—well before the general election—in order to acquaint themselves with Myanmar's military leaders and perhaps in preparation for the pursuance of their new Myanmar policy if and when they got into power. Soon after the election result was known with Dr. Thaksin expected to be the new prime minister, he had indicated that he would make an official visit to Myanmar as his first foreign visit in the region.¹ Why Myanmar is so important in the eyes of these two political leaders? For one thing Myanmar offers a potential base for economic expansion of Thailand. In the past several years, especially during the government of Mr. Chuan Leekpai, the relationship between Thailand and Myanmar was lukewarm at best because the former foreign minister in the Democrat Party did not like the way the Myanmar military regime conducted its domestic political policy. This had

prevented any serious economic cooperation while other East Asian countries, namely Singapore, Malaysia and Korea were securing strong and extensive economic foothold in Myanmar already. So, in order to fulfil the objective of making Thailand the center for trade in goods and services in the region the economic relations with Myanmar must improve, and that requires the change of basic policy from political engagement to economic engagement.²

On China

Again the two leaders went to China in October last year after their visit to Myanmar. They recognized, rightly perhaps, the important role that China will play in the East and South-East Asian regions in the near future. In China, they had asked for the same trade concessions that China gave to its southern neighbors, claiming that Thailand also shares the same Mekong River. More importantly, the Thai Rak Thai leaders were informed of the new economic plan of China which encourages Chinese investors to invest in foreign countries and under which a special fund has been set up for the promotion of investment in ASEAN countries, especially Thailand. Obviously the two leaders would like Thailand to be the first place where these Chinese investors will land. Closer economic relationship between Thailand and China may be a result of a likely prospect that China will soon become a world economic power, and Thailand wants to maintain even closer relations with this giant northern neighbor.

On IMF and WTO

That the International Monetary Fund (IMF) liked the way the former government handled the management of the economic crisis was no secret. So it is only natural that the Thai Rak Thai will do things differently from the Democrats. Both Drs. Thaksin and Surakiart had indicated that they would negotiate with the IMF for the readjustment of the debt payment schedule so as to avoid repercussions on the country's foreign reserves and balance of payments account. The new government also supports the setting up of the Asian Monetary Fund (AMF) backed by Japan, an idea that was originally opposed by the IMF. As for the World Trade Organization (WTO), the government probably would not propose anything that will bring about more free trade obligations unless it can be proven that the liberalization process will not harm Thai businesses, society and the recovery of the Thai economy (See more on this point later).

PERMANENT BUREAUCRATS AND TRANSIENT POLITICIANS

As transient politicians are not the only ones who decide and run foreign economic policy in Thailand, some attention must also be given to others who also

have a part in deciding and running foreign economic policy of Thailand: the permanent bureaucrats in various economic ministries and government agencies. Of course policy directives from politicians take precedence over bureaucratic preference and practices, and it would be folly for any bureaucrat to openly challenge the power of politicians.³ However, if the politician-designed policy runs counter to the perceived or traditional stance of the permanent bureaucracy, these bureaucrats will either try to delay the implementation, feed in wrong, inaccurate or outdated information to policy maker politicians, or give incomplete advice, or all of these, which may result in the wrong policy being adopted or implemented. This is a well-known way by which the bureaucrats can get even with the politicians if they disagree with them.

Fortunately for Thailand, disagreements between transient politicians and permanent bureaucrats with regards to Thailand's basic or fundamental foreign economic policy have rarely happened in the past and at present. These basic or fundamental positions include such policies as the acceptance of the general principle of globalization, the opening up of trade and investment, the commitments to international standards and obligations, the support and promotion of regional and international cooperation, the observation of international practices, international laws and international diplomatic protocols, and so on. Therefore, as long as the new government's foreign economic policy does not deflect too much from the above norm, we can see full cooperation between these two groups of players in laying out and implementing the foreign economic policy of Thailand. The three policy issues that are likely to be maintained and closely followed are, the policy to support free trade in the international arena, the policy that emphasizes the proactive role of Thailand in international trade negotiations, and the policy that supports and advances the free trade policy of the ASEAN Free Trade Area (AFTA).

Is there any possibility of conflict in the implementation of the foreign economic policy between the politicians and the permanent bureaucrats? The answer is probably yes. It is clear from the above that this government favors a bigger role of the private sector in the running of the government. Many present government leaders themselves have been successful businesspeople before entering politics and they would be inclined to maintain the superior position of the private business.⁴ Assuming that the permanent bureaucrats do not have any direct, personal connection with private businesses but work for the general interest of the public, it is possible that these bureaucrats will act as a buffer against policy that favors specific business interest at the expense of public interest. Examples abound in Thailand where information on the incumbent government's stand on certain policies was leaked to members of the opposition who used it effectively in a parliamentary censure motion. The usurpation of the freedoms of the bureaucracy by tinkering with its normal practice can also be a source of conflict. It was reported that the diplomatic

emphasis of the role of the Ministry of Foreign Affairs will be reduced under the new government, to be replaced or supplemented by the emphasis on economic affairs. There will be even plans to recruit economic ambassadors from among businesspeople, technocrats and pensioners, but not government officials. Several private advisers have been drafted from outside the Ministry of Foreign Affairs to work with the new Foreign Minister inside the Ministry. It is hoped that this has not created a sense of slight among the bureaucrats of the Foreign Ministry. Otherwise the implementation and coordination roles of these officials could be adversely affected.

CONCLUDING REMARKS: THAI FOREIGN ECONOMIC POLICY IN THE REAL WORLD

It may be concluded that altogether the transition of Thailand's foreign economic policy from the old to the new government has been quite smooth despite some differences in the style of management. The basic outlook of the Thai foreign economic policy in its support of the international economic system should remain unchanged. Thailand will still be a good and conscientious player in international economic cooperation. It will maintain its international obligations and participate fully in international organizations. One thing that has remained true throughout its modern history is that whenever there is an international image or international commitment issue involved, the Thais will always give it top priority. Thus it is unlikely that Thailand will become an economic outcast in the world arena.

But is it not true that this government supports local, national businesspeople as against foreign interest? Is this a change that is different from the past fundamental economic policy of open market and non-discrimination? Perhaps not. The psychology of this new policy is that it was conceived and put in place by people who are successful businesspeople themselves. They truly believe in themselves and their colleagues. The new government is certainly not 'anti-foreigners.' It simply believes that, given equal opportunity, the local businesspeople (*a la* their own groups) could compete with any foreigners. This is an obvious manifestation of self-confidence rather than new economic nationalism. But whether the outcome of this pro-local business will better benefit the Thai people as a whole compared to the policy of the past is something we are all waiting to see.

ENDNOTES

¹ He later changed his mind after many protests from various quarters for giving in to the military regime of Myanmar. Normally, a new Thai prime minister will make his first foreign visit to ASEAN neighbor countries first. Visiting Myanmar first is still not against the traditional practice as Myanmar is now an

ASEAN member, but to go there first would still convey an uneasy sense of appeasement.

² It is possible that the interest of the Thai Rak Thai leaders in Myanmar is a natural reflection of their personal economic interest in the neighboring countries. Dr. Thaksin himself, through Shin Corporation, a telecommunications company that he used to own, has had extensive investment and other telecommunications business activities in Myanmar, Laos and Cambodia. Dr. Surakiart himself was involved in the natural gas deal with Myanmar when he was the chairman of the Petroleum Authority of Thailand. But the general interest in Indochina, not just Myanmar, may come from more than just these two Thai Rak Thai leaders. There are many in the policy-making group in the Thai Rak Thai now, such as Mr. Pitak Intrawitayanunt and Mr. Pansak Winyarat, along with Dr. Surakiart himself, who used to be economic advisers to former Prime Minister General Chatichai Choonhavan, who became famous for his pro-Indochina stance in the late 1980s by wanting to 'turn the battlefield into the market place.'

³ Indeed, the Prime Minister has told top bureaucrats of all ministries soon after assuming office that they toe the government's lines and cooperate rather than obstruct its main policy.

⁴ Dr. Thaksin himself was a successful businessman in telecommunications businesses. Dr. Surakiart, the Foreign Minister, although he started his career as an academic, quickly left it to join politics and business enterprises. He ran a successful law and business consulting firm of his own before becoming the Foreign Minister, and was at one time the chairman of the Petroleum Authority of Thailand, a state enterprise. Dr. Adisai Bodharamik, the Commerce Minister, was Chairman of Jasmine International, another successful telecommunications company. Mr. Pracha Maleenont, the Deputy Communications Minister was the owner of Channel 3 television station. Industry Minister, Mr. Suriya Jungrungreangkit was also a successful businessman in the engineering field.

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An Assessment of the Role of Board of Directors in Building Good Governance: The Case of Thailand*

Deunden Nikomborirak**

INTRODUCTION

Since the recent economic crisis that sent many companies into a deep financial mire, the Thai corporate sector has been slowly getting back on its feet. With the ruins of reckless lending and risky investment still looming in the form of non-performing loans (NPLs), the public expects companies that have survived to improve their corporate governance. Indeed, the spotlight has now been focused on the board of directors, which is often accused of being involved in connected transactions and of having turned a blind eye on the company's blatantly unfair and in some cases even fraudulent corporate practices. To this end, the Securities and Exchange Commission (SEC) and the Stock Exchange of Thailand (SET) have recently introduced several rules and regulations to help promote more effective supervision of management by boards of directors. These include, for example, the mandatory audit committee consisting of at least three independent directors, and greater disclosure requirement for connected dealings.

Besides regulatory bodies such as the SET and the SEC, foreign investors have also played an important, even if indirect, role in the development of corporate governance among Thai companies after the crisis. To remain afloat during the difficult times, many listed Thai companies need to mobilize foreign capital as domestic funding has virtually dried up. Some have plans to be listed in overseas stock markets; others have taken road shows to promote the issuance of their new stocks or bonds. To be able to attract foreign investors, these companies are pressured to improve their corporate

governance infrastructure, which often includes the board of directors.

The premium foreign investors place on good corporate governance is indeed high. According to the report by McKinsey & Company,¹ foreign investors are willing to pay 27 percent more for equity shares of SET-listed companies with good governance standing. Good governance also pays in terms of superior corporate performance. A corporate governance survey conducted by the CLSA in 2001² found a positive correlation between good corporate governance and superior financial performance among SET-listed companies. Further, the survey reveals that five-year share prices also correlate with the quality of governance. Thus there is no doubt from these surveys that good corporate governance does pay, if not in the short run, then in the long run.

Despite the evidence supporting good governance, many listed companies, most of them family-run, have failed to improve their governance. Claessens et al. (1998) noted that over 60 percent of SET-listed companies are family-owned. The figure may have declined somewhat over the years, but are nevertheless likely to remain significant. It is therefore difficult to make general statements or analyses about the characteristics of local corporate governance. The development in this area appears to be progressing on two different tracks: a fast track for companies that need to mobilize foreign capital, and a slow track for those that do not. It is hoped, however, that through time, increased investor sophistication as well as increased awareness about good governance among family

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businesses will help raise the standard of corporate governance in all corporate entities.

LEGAL FRAMEWORK

Rules and regulations governing listed company are dictated by the Public Company Act of 1992 (PCA), the Civil Code, the SET and the SEC.

The PCA stipulates that a public company can have as many directors as stated in the article of association but not less than five persons. A 1999 survey by the Thailand Development Research Institute (TDRI) of the top 100 listed companies (in terms of registered capital) showed that the average board size is 12.29 members.³

As for the minimum requirements to serve as a member of the board, the law stipulates that the person (1) must be at least 18 years old; (2) must not be a bankrupt individual; (3) must not have been imprisoned for fraud or embezzlement; and (4) must not have been removed from government office for fraud. Legal entities are allowed to be board directors. Board directors do not normally own shares in the company, but can be, and usually are, representatives of various groups of block shareholders.

Directors are elected by shareholders at the shareholders' annual meeting. 'One share, one vote' normally applies, although it is not mandatory. Cumulative voting is the default voting scheme stipulated in the PCA, but companies are allowed to establish their own voting rules in the article of association. Few, if any, allow cumulative voting.

The length of a director's term may vary from two to four years. However, for firms that choose to have their own election rules, a staggering term is mandatory, with one third of the board randomly re-elected each year. Employees do not participate in the election of directors.

Since evaluation of a director's performance is extremely rare among Thai companies, reappointment of

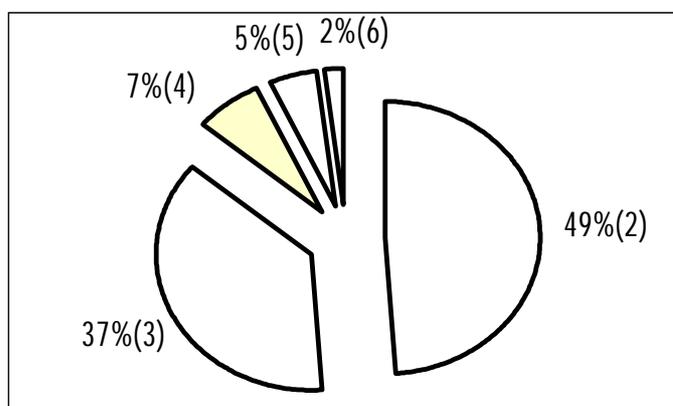
directors is often automatic, unless the individual director caused obvious damage to the company. However, in a very few, remote cases where a nomination committee exists, reappointment of directors and executives is not automatic but relies on the assessment of the committee.

There is no requirement in the PCA for public companies to appoint independent directors. However, the SEC and the SET require listed or publicly held companies to appoint at least two outside directors who are independent of the major shareholders and the management. The objective is to have directors who are able to provide effective and unbiased oversight of the way in which the company is managed. Independent directors are supposed to safeguard the interests of the company, which includes minority shareholders, against any abuse by the management. They are required to give opinions on the connected transactions and provide comments in the annual report.

According to a recent survey conducted by the TDRI, almost half of the companies surveyed have only two independent directors, which is less than the minimal requirement of three (Chart 1). This is because many listed companies are still unable to find three independent directors who are also willing to take up the responsibility of an audit committee. Many are discouraged by the amount of responsibilities involved and the rather stringent qualifications required by the regulation. Also, many directors are still unfamiliar with the role and responsibilities of an audit committee. Indeed, the task appears to be particularly daunting now that most companies are still caught in a deep financial crisis.

For the above reasons, only 37 companies surveyed met the minimum requirement of three independent directors. The remaining 14 have more independent directors than the regulation requires. It should be noted that only two companies surveyed have independent directors as a majority on the board (Chart 1).

Chart 1: Percentage of Firms with (x number) of Independent Directors on the Board



Source: TDRI Survey of top 100 listed companies in 2001; based on end of 1999 data.

COMPOSITION OF THE BOARD

In most Thai companies the board is still dominated by the executive director, who, in most cases, has personal ties with large shareholders. Foreign directors are rare, unless the company has a significant foreign equity share. However, with the need to mobilize capital from overseas, many Thai companies have begun looking for professional directors to help push the company forward in order to meet the expectations of, or the commitments made with, foreign investors. An appointment of an internationally recognized director can provide an immediate boost to the image of the company.

High-ranking bureaucrats—retired or still in the middle of their career—also make popular board of directors for Thai companies, in particular for companies that operate within a heavily regulated environment. Indeed, connections can prove much more valuable than competence in a culture of patronage and in an environment where the rule of law is unclear and not properly enforced.

Independent directors are a relatively new phenomenon in Thailand since the SEC has mandated that every listed company must have at least three independent directors who will also become audit committee members. Most companies are still struggling to decide whether to shun them or appreciate them, while regulators struggle to find out how to legislate “independence.” The definition of independence according to the SEC is as follows: (1) not an employee of the company, its subsidiary or part of the same conglomerate; (2) does not own more than 0.5 percent of the equity share; and (3) not a relative to have special relations with insiders that may obstruct impartiality in performing duty. Indeed, it is difficult to legislate “independence,” as one can never exclude all types of personal ties, especially in an environment where patronage is a way of life.

There is an ongoing discussion on whether the number of independent directors in a board should be increased to at least half of the total number of directors so that these directors will not be easily outvoted. Such a proposal should be considered carefully, however, for several reasons.

First, the expected role of outside directors should be reconsidered. Their role is to offer impartial and independent views and oversight that can be valuable to the company’s management, not dominate the decision-making process of the board. Moreover, as part of the common business practice, there is no real vote taken in board meetings anyway. Attention should thus be focused instead on ensuring that the environment is conducive to these independent directors in contributing to the company; i.e., access to accurate, timely and adequate information. If the two independent directors can fulfil their expected role effectively, the company will no doubt recognize their contribution and may voluntarily choose to recruit more independent directors.

Second, there is a severe shortage of qualified directors in the market.⁴ The crisis has disqualified many prominent executives and directors, in particular, those involved in the failed banking and finance companies. These people have been marked by the public as belonging to the “old regime” where cronyism and nepotism prevailed.

Third, most outside directors are prominent persons whose integrity is well recognized by the public. While their presence on the board can help boost the image of the company, these individuals do not necessarily make good directors. Also, many are heavily over-committed with both private and public tasks. Good reputation is of little use if the amount of time and business skills these directors can contribute to the company are very limited.

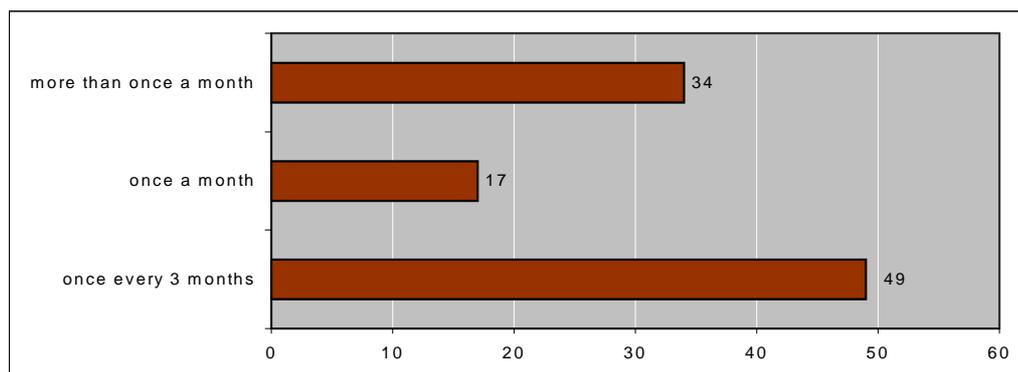
Fourth, outside directors are often not familiar with the management of the company and will have to rely on executive directors and the management for information. Their decisions, though impartial, well intentioned and independent, may not necessarily be optimal for the company. To have outside directors controlling the decisions of the board may, therefore, not necessarily be preferable.

RESPONSIBILITIES OF THE BOARD

According to the law, listed companies must hold a board meeting at least once every three months. According to the survey conducted by the SET in 1999, almost half of the companies surveyed were found to hold board meetings once every three months, while in another 17 percent the board meets once a month and in the remaining 34 percent, the meetings take place more than once a month on average (Chart 2).

Normally, large companies meet at least once a month. For smaller companies, the frequency of the meetings may be once every two or three months. Board meetings usually last one to two hours. Most Thai companies have an executive board that meets more often, two to three times a month, depending on the amount of work that needs to be accomplished. Executive board meetings are usually longer, lasting normally three hours. Executive directors are the ones who execute and monitor tasks in coordination with the management, while the board of directors approves tasks, work plans, strategies that have been pre-screened and pre-assessed by the executive board. The main responsibility of the board is to oversee the company’s business strategy and business plan and to ensure that the management of the company is consistent with the shareholders’ resolution and in compliance with the law.

With the presence of independent directors and an audit committee as mandated by the SEC, boards of directors in Thailand are playing an increasingly active role in overseeing the management of Thai companies.

Chart 2: Frequency of Board Meetings

Source: The SET, The Corporate Governance Report 2001.

The idea of independent directors was initially shunned by the corporate sector. Many still believe that it is impossible to legislate independence and that these so-called “independent directors” will be nothing more than those with close personal ties with major shareholders. However, several companies did try to recruit genuinely independent directors with good professional track records. These companies are finally beginning to appreciate the contributions these outside directors have made to the company.

Audit committees have also become an important tool for boards of directors. With the committee reporting directly to the board, directors can better perform the tasks of overseeing how the company is managed. The audit committee is expected not only to be involved with the audit of the company’s finance and connection transactions, but also to perform “compliance audit” to make sure that decisions made by the board of directors are properly carried out by the management. Thus, the audit committee has become one of the main ingredients of the board to ensure the “best interest of the company,” which often refers to the bottom line of the company’s income statement. According to the TDRI survey, all except two of the top 100 companies surveyed had established audit committees by the end of 1999 – the deadline set by the SEC and the SET for that purpose. However, most are still unable to find three independent directors who will be on this committee.

Another key ingredient that contributes to the board’s ability to ensure the best interest of the company is the quality of the business plan and strategy proposed by the Chief Executive Officer. If these plans and strategies are clear and well thought out, it will be easy for the directors to “steer” the company in the right direction. Otherwise, it would be difficult for the directors to assess the situation and they would spend more time questioning the validity and soundness of the proposed plans and strategies.

While boards of directors of a number of companies have taken major steps toward improving

their effectiveness in performing their tasks as representatives of shareholders, many still maintain the same bad habit of not taking their duties seriously. On this matter the legal environment is of little or no help in ensuring the accountability of these directors.

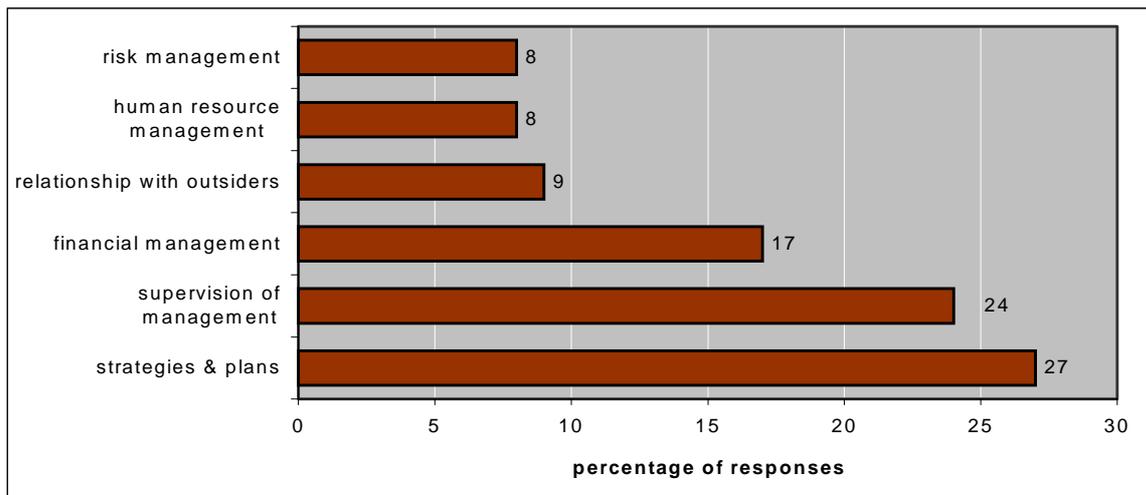
Section 85 of the PCA stipulates that directors have to perform their duties in compliance with all laws, the objectives and the article of association of the company and the resolutions of the shareholders meetings, with care and honesty in order to preserve the interest of the company. However, there are no clear interpretations of what may constitute care and honesty. Because of the vagueness of the words of law, there has been very few cases—if any—of directors being convicted for neglecting fiduciary duties.

In order to lift the standard of the board of directors among listed companies, the SET has established a code of best practice for directors. Each year, companies are expected to report on whether they have complied with the code according to their own monitoring. Whereas not complying with the code does not constitute a violation of the law, false report of compliance is a criminal violation. It has been recommended that fiduciary duties of directors be codified in the law and that audit committees assess compliance to the code.

DECISION MAKING PROCESS

Duties of the Board of Directors

According to the Corporate Governance Survey conducted by the SET, more than a quarter of the respondents saw the most important role of a board of directors to be the laying out of business strategies and plans. This was a consistent opinion of both the management and independent directors. Another 24 percent emphasized the supervisory role, while further 17 percent believed that the board should contribute to the company’s financial management (Chart 3).

Chart 3: Roles of the Board of Directors

Source: The SET, Corporate Governance Report, 2001.

The ability of the board of directors to perform its duties efficiently depends mainly on the quality of the management's report and the efficiency of the board's secretariat in preparing documents. On this note, it is worth mentioning that the term "company secretary" is often unheard of among Thai companies. The crucial role of the secretariat is something that is often overlooked. Secretariat functions are often treated only as "extra duties" that the staff perform in addition to their regular work. Thus, little attention is paid to the quality of the work beyond what is required by the SEC or the SET. For example, if the board's decisions are not properly recorded and circulated well before the following meeting, directors may end up spending most of their time debating the content of the decisions instead of dedicating their time to more meaningful matters. Likewise, if the agenda of the meeting is not properly defined well ahead of time, it may lead to questions and issues being raised unexpectedly during the meeting, and directors will not have enough information or time to make optimal decisions.

While the management and the secretariat play important roles in supplying corporate information to directors, directors themselves need to demand information. Sometimes it is difficult to determine what kind of information the directors would require. Usually outside directors are less familiar with the company's business and style of management. Therefore, these directors may require more information than do their peers. They are therefore expected to pose questions to the management who may have unintentionally omitted vital details in its reports. It is thus the individual director's duty to "ask as many questions" as he/she can. In some cases, outside directors are paid "too much" or "too little" to play such an inquisitive role. A question then naturally follows. Can such directors be held liable for their failure to perform their duties according to the law?

Liability of Directors

According to Section 85 of the PCA, directors who fail to perform their duties with honesty and prudence are *individually liable*. Other directors who are not aware of the violation cannot be held liable. Directors can also be held individually liable for misinformation, which is considered a criminal violation. However, it must be proven that the individual director had the "intention" of falsifying the information and that damage has been done, which is often difficult. However, shareholders may file a lawsuit for compensation under the Civil Code if negligence can be proven.

Several sections of the law stipulate *collective liability* of directors. These include Section 91 of the PCA that holds directors jointly liable for:

- (1) damages to the company caused by a director's failure to perform fiduciary duties stipulated in section 85
- (2) approval of loans to directors or employees that is in violation of the law
- (3) illegitimate remuneration for directors
- (4) disbursement of dividends that is in violation of the law; i.e., in the case where the company sustains a loss unless it can be proven that the decision was made with honesty and based on the information or financial report that has been certified by the financial officer or the auditor of the company
- (5) negligence in keeping accounts, documentation, and registration according to the requirement of the law unless it can be proven that best efforts have been placed to avoid violation of the law
- (6) use of proceeds from sales of equity without proper approval

- (7) demands of payments or transfer of assets from sales of securities without proper approval.

Section 94 of the PCA also stipulates that directors are jointly liable for damages that result from the following acts, unless it can be proven that none of them was involved in any of the following acts that constitute a violation of the law:

- (1) Misinformation about or concealment of financial status and performance record of the company during the sale of company shares or bonds
- (2) Submission to authorities of documents that are false or inconsistent with the company's account, registration or other official documents
- (3) Falsification of income and financial statements, shareholders meeting reports or board-of-directors reports.

While the law provides ample opportunities for shareholders to file lawsuits against directors for compensation, the strain, in terms of both time and money, of going through a court process poses a formidable obstacle for shareholders in exercising their rights. It has been recommended that to save time and money, class-action filing should be allowed for such cases and that the director or directors bear at least some part of the cost if found guilty. Alternatively, a foundation for small shareholders may be set up. Small shareholders may deposit shares with this not-for-profit organization that will monitor boards and managements or even undertake lawsuits against directors on behalf of shareholders. Indeed, the SEC may partially contribute funding to support such an organization.

Conflict of Interest at the Board Level

Besides lack of information and accountability, conflict of interest is another major element that can impede effective decision-making by the board. This problem is particularly severe among Thai companies which often lack transparency and adequate supervision in the way in which they are managed. There are several provisions concerning conflict of interest at the board level in the PCA. The law:

1. Prohibits directors from holding a position or owning shares in competing companies.
2. Prohibits directors from borrowing funds from the company. Violation of this particular clause will hold all directors who approved such transactions jointly liable for both civil and penal action. The latter includes a fine twice the amount of the illegal loans or 20,000 baht, whichever amount is greater.

3. Prohibits the company from providing financial or non-financial compensation to directors beyond what is specified in the company's rules, unless the decision is endorsed by at least two third of shareholders present at the shareholders meeting. Violation of this particular section will hold all directors who approved such transaction jointly liable for both civil and penal action. Again, the latter includes a fine twice the amount of the illegal loans or 20,000 baht, whichever amount is greater. In practice, however, directors are compensated in terms of free trips, for example, whose expenses are filed under the category of meeting expenses.
4. Requires that conflict of interest dealings be approved by the board of directors, while the individual director with the potential conflict-of-interest must abstain from voting.
5. Requires that the following types of dealings obtain approval from the shareholders:
 - *Sale or transfer of ownership of the business or a significant part thereof to another individual,*
 - *Purchase or transfer of businesses from other private companies,*
 - *Amendment, signing or canceling of major contracts,*
 - *Decision to allow some other entity or individual to manage the company, and*
 - *Mergers for the purpose of profit sharing.*

Additionally, signing of all contracts with directors implicated in the conflict-of-interest must be announced in the company's annual report.

There are several loopholes in the law. First, connected transactions require approval from the board of directors. This would be futile if most or all directors are associated with the same group of block shareholders as is the case for many SET-listed companies. Second, most connected transactions are negotiated not by the directors themselves, but through nominees. Since the prohibitions do not cover cases when directors have indirect interest in the connected transactions, connected dealings negotiated by middlemen are beyond the reach of the law. Third, large shareholders are not considered as a party whose interests may be in conflict with that of the company. That is, doing business with large shareholders does not constitute a connected transaction. The SET realized the shortcomings of the PCA and therefore established rules that demand greater disclosure of connected dealings. These rules are as follows:

- *all connected dealings must be published in a newspaper (one Thai, one English) and recorded in annual reports giving the size of each transaction*

- *dealings with large shareholders or with legal entities in which large shareholders own a controlling share must also be disclosed*
- *all connected dealings with substantial value must obtain approval from three quarters of shareholders. In addition, in calling a shareholders meeting to request for such resolution, the company must provide the opinion of an independent financial advisor on the suitability of such transaction.*

While the more stringent SET rules are likely to be better able to deter undesirable connected transactions, it is not clear, however, whether failure to comply with the SET requirements in itself constitutes a violation of the law. Of course, directors can be held jointly liable should the company be delisted from the Stock Exchange. However, delisting is not an attractive form of sanction for the SET since it would potentially hurt small shareholders. While the latter can file for damages in court, time and cost considerations, as pointed out earlier, are often a deterrence. Thus, class action needs to be facilitated and the burden of the cost must be borne at least in part by the guilty party.

It is recommended that the PCA be amended to provide clearer and more extensive definitions of connected transactions. Strengthening the role of the audit committee may also help deter fraud cases arising from connected dealings.

RELATIONSHIP AMONG BOARD MEMBERS AND BETWEEN THE BOARD AND OTHER BODIES

The board of directors in listed Thai companies has a one-tiered structure. As mentioned earlier, it is often dominated by executive directors. However, according to the TDRI survey of the top 100 listed companies, only 11 had the CEO as the chairperson of the board. According to the SET's opinion survey cited earlier, 52 percent of independent directors believe that the chairperson of the board should be a representative of the large shareholder, while another 45 percent think that the chairperson position should be held by an independent director.

The PCA does not mandate any committee but the SEC and the SET require all listed companies to set up an audit committee consisting of at least three independent directors each of whom does not directly or indirectly hold shares in the company worth more than 0.5 percent of its paid up capital. However, the current definition of independence does not exclude (1) executives, employees, workers or consultants who receive salary or other regular benefits from affiliated companies; and (2) those that may have past direct or indirect financial or other interest in the management or the business of the company or its affiliates in such a way that the person cannot make independent judgement. It can therefore be assumed that the audit committee may not be independent from the management, although it must report directly to the board.

A remuneration committee is not required by law or by SEC regulations. Remuneration of directors requires a vote of three fourths of the shareholders. But since many listed companies are still family run, small shareholders often own less than 10 percent equity share and thus are not able to regulate the compensation of directors. In such companies, large shareholders are thus able to provide excessive compensation to friends and families or "shadow directors." However, several companies that have a significant foreign holding are voluntarily introducing remuneration committees for greater transparency and efficiency in personnel management. According to the TDRI's survey of top 100 listed companies, none had officially set up a remuneration committee as of end of 1999.

A nomination committee is also not required. It has been mentioned in a prior section that a large number of listed companies are still controlled by various groups of large shareholders. Directors and high-ranking executives, most of whom are friends and family of large shareholders, often have their term automatically renewed with little concern for performance. Again, the story is different for companies with a significant foreign equity share. The Siam Commercial Bank, for example, has voluntarily established a nomination committee that will assess the performance of directors and senior executives, as well as screen potential applicants to assist the board in its decisions concerning personnel.

According to the TDRI's survey of 100 largest listed companies, only five had a nomination committee as of 1999-end. This is hardly surprising, considering that the SET opinion survey showed that 74 percent of the respondents believe that a nomination committee is not necessary and that the task can be effectively undertaken by the board itself.

In theory, these committees should consist of independent directors. The current practice is diverse, however. In large organizations, outside directors often become involved in these committees to ensure independence from management. This, however, does not mean that these committees should consist entirely of outside directors. After all, the committee will have to rely on the company's staff, be they from the audit department or from the executive office. It is important that committee members are familiar with the staff and the working environment of the company. It is probably optimal to have a mix of outside directors and executive directors as committee members.

BOARD REMUNERATION AND TRAINING

Directors are often provided with a per-meeting honorarium. Compensation in the form of equity shares or warrants are still rare, but gradually becoming more popular. Table 1 shows the number of listed companies that have provided equity shares or warrants as compensation for their directors.

Table 1. Listed Companies Providing Equity Shares or Warrants as Compensation for Directors

Year	Equity shares	Warrants	Total
2000	4	25	29
1999	4	12	16
1998	1	6	7

Source: The Stock Exchange of Thailand.

Very few directors have had any professional training since until recently there was not an institute that would offer such training. Since its inauguration in October 1999, the Institute of Directors Association (IoD) has been offering two programs: Directors Certification Program and Chairman Program. The IoD has produced over 200 certified directors so far.

The question whether every director should be certified has been raised a number of times in the past. In most countries, a director’s certification remains voluntary, except in a few countries such as Australia where it is mandatory. For Thailand, the voluntary option would probably be more realistic at this stage as there are presently very few certified directors. Mandatory certification would imply that most directors would have to enroll in the IoD’s course, which can prove to be quite costly for some companies, particularly, smaller ones. A suggestion would be to require that all directors specify, as part of their credentials, whether they have undertaken training courses for directors.

CONCLUSION

The face of the board of directors in many Thai companies is undergoing major changes as a result of

both commercial necessities, increasingly stringent rules and regulations as well as greater awareness and appreciation of good corporate governance. Yet, there are many other companies whose boards still function in the same old ways with little accountability to peripheral shareholders. It is only through time that the change in the business culture and market discipline will help companies recognize that having qualified and competent directors actually “pays.” Only then can we hope to raise the quality of the board of directors across the board.

ENDNOTES

- ¹ Coombes, Paul, and Mark Watson. 2000. “Three Surveys on Corporate Governance.” *The McKinsey Quarterly* No.4.
- ² CLSA. CG Watch: Corporate Governance in Emerging Markets. April 2001.
- ³ The figure is based on the last quarter of 1999 data.
- ⁴ As of August 2001, the Institute of Directors Association had produced in total about 215 certified directors.

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