Capital Market Development in Thailand

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Abstract

Capital Market Development in Thailand

After the financial crisis in 1997 domestic securities were issued in the Thai capital markets to a greater extent than before However, considerable parts of such surge were due to recapitalization of commercial banks and refinancing of private corporations' foreign debt obligations Thus, favorable growth path of the Thai capital markets may not be sustainable, especially when there were several shortcomings Most funds were tapped by a few sectors of the economy and a small number of large firms. Poor corporate governance and inadequate transparency widely prevailed Institutional and high net-worth investors, particularly the foreign ones, played a predominant role in contrast with the household sector which had little knowledge and confidence about capital market instruments Even though recently the government has undertaken numerous promoting measures, Thai corporate culture does not facilitate well, especially among small- and medium-sized enterprises the number of which is overwhelming Foreign investment in and liberalization of securities business may help accelerate the pace of capital market development in Thailand. Nevertheless, they can also bring about a larger degree of vulnerability or susceptibility to dangers or shocks, depending upon timing and how well prepared local agents have been The government therefore has to be extremely careful in choosing an optimal blend of regulations

Capital Market Development in Thailand

1 Introduction

After the Thai economy sparked off the Asian financial crisis in 1997, both her stock and bond markets seem to have experienced unprecedented growth in most regards, including issuance and turnover of securities It is thus the objective of this paper to investigate the actual path of Thailand's market development, to examine fundamental shortcomings as well as potential, and to analyze pertinent factors plus regulations The second section gives a brief description on instruments and regulations on borrowing from Thai capital markets The third section identifies market preferences and sizes. The fourth section gives some qualifications about the recent surge in the Thai securities markets The fifth section pinpoints particular weaknesses which are not only important but also intractable. The sixth section covers latest policy actions adopted by the government and concerning the path of future capital market development The final section presents conclusive remarks as well as some suggestions

2. Instruments and Regulations

The public authorities in Thailand could issue the following types of securities: (1) government bonds (2) state enterprise bonds (3) Bank of Thailand bonds (4) Financial Institution Development bonds (5) Property Loan Management Organization bonds (6) Treasury bills and (7) promissory notes Type (3) was meant for handling domestic liquidity or monetary policy, while Types (4) and (5) were intended to help resolve particular crises However, Types (4) and (5) are no longer issued. In contrast, the government and state enterprises occasionally resort to Types (1) as well as (3), and (2), respectively

In accordance with the Budgetary Act of 1959, Thai government can borrow by issuing securities only in case of budget deficit or when expenditures exceed revenues, and those borrowings cannot exceed the sum of 20% of total fiscal spending and 80% of the expenses allocated to debt amortization. On the part of state enterprises, each of them has its own regulation on borrowing but government guarantees are subject to the following conditions If the state enterprise is a company, the limit of government guarantee is four times capital funds of financial state enterprise company or six times capital funds of non-financial state enterprise company. On the other hand, there is no limit of government guarantee if the borrowing state enterprise is not a company Treasury bills are short-term securities issued by discounting process for the purpose of administering treasury balance and fiscal policy As regards maturities, timing, and auctioning methods, the borrowing public entities have freedom to select any pattern that they deem suitable for their status and/or market conditions.

Similarly, most private entities (except financial institutions) are not subject to constraints on borrowing On a short-term basis, they can issue several types of commercial papers (e.g bill of exchange, bankers' acceptance, promissory note, negotiable certificate of deposit) As for securities of longer maturities, before 1992 only public and exchange-listed companies were eligible to issue bonds Limited companies, which constituted a majority of Thai business entities, were prohibited. After the enactment of the Securities and Exchange Act in 1992, however, limited companies are allowed to issue corporate bonds

3. Market Preferences and Sizes

The central authorities truly recognized investors' *need for liquidity*. A number of secondary markets were thus established and measures undertaken to help trading of different kinds of securities. First, the Stock Exchange of Thailand (SET) was originated in 1974 for common shares. Second, the repurchase market was initiated by the Bank of Thailand in 1979 so as to temporarily accommodate financial institutions' liquidity shortage and simultaneously implement monetary policy Third, the Bond Dealers' Club (BDC) was put into action in 1994 in order to entertain secondary trading of both public securities and corporate bonds Fourth, in 1993 the first credit rating agency, the Thai Rating Information Service Co , Ltd (TRIS), was founded to help investors evaluate bond and share issuers Fifth, banks were permitted to engage in bond underwriting in 1993 Their role in this respect grew remarkably from 4% of the total value of bonds registered at BDC in 1995 to 46% in 2000 Sixth, banks became major dealers in the secondary bond markets as well between 1998 and 2000. Growing volumes of transactions and responsibilities led to enlargement of BDC to the Thai Bond Dealing Center (TBDC) in 1997. Afterwards, the statistics on secondary trading of securities rose impressively as shown on Tables 1 and 2. Trading value jumped from 72 billion baht in 1998 to 1,592 billion baht in 2001 Turnover ratio surged from 9% in 1998 to 105% in 2001. It is yet noticeable that corporate bonds still constituted a minor portion (5% of trading value in 2001), as compared with government bonds (57%) and state enterprise bonds (8%)

From an overall perspective, the total funds that private businesses mobilized from capital markets in Thailand between 1988 and 2000 remained far less than credit obtained from commercial banks As displayed in Table 3, the former averaged 118 billion baht p a or roughly a half of the latter which amounted to 242 billion baht p.a. An international comparison in Table 4 confirms such diffference. In 1988-2000 the capital markets in the U S and the U K helped private businesses mobilize funds worth 51% and 43% of gross fixed capital formation, respectively Meanwhile, the Thai capital markets contributed only 11%. When attention moves to commercial banks' credit, the picture is reversed That is, Thai bank credit added up to 26% of investment spending while the American one totaled only 15% This clearly demonstrates that most Thai businesses lagged behind in direct financing via capital markets in several respects For instance, they tended to be possessed by the owners who did not have enough knowledge or understanding about the role, responsibility, and working mechanism of capital markets, including regulations as well Consequently, most of their fund raising largely hinged upon borrowings from financial institutions, especially commercial banks

Table 1: Thai BDC Trading and Outstanding Value

(Millions of baht)

	1995		1996		1997		1998		1999		2000		2001	
	Trading value	Outstanding	Trading value	Outstanding	Trading value	Outstanding	Trading value	Outstanding	Trading value	Outstanding	Trading value	Outstanding	Trading value	Outstanding
Government	-		-			-	43 090	330 446	341 784	538 846	1 127 761	586 261	916 473	618 176
State enterprise	-					-	7 533	286 458	50 784	356 310	201 864	407 347	140 383	414 448
Guaranteed	-		-			-	6 636	253 696	42 535	309 091	191 686	345 340	123 871	357 278
Non guaranteed			-			-	897	32 762	8 249	47 279	16 176	62 007	16 512	57 170
Treasury bills	-		-	-	-	-	-	-	3 777	-	47 414	62 000	350 837	110 000
BOT FIDF PMO	931	8 500	4 833	18 500	15 235	36 500	12 579	21 000	2 732	10 000	662	4 076	93 233	112 337
Government debts	931	8 500	4 833	18 500	15 235	36 500	63 202	637 904	398 378	905 216	1 283 722	1 059 684	1 500 926	1 254 961
Corporate debts	50 597	89 228	195 775	130 189	[illegible]	132 591	8 896	125 841	32 819	179 387	73 4[illegible]	209 883	91 294	251 720
Total value	51 528	97 728	200 608	148 689	56 140	169 091	72 098	763 745	431 197	1 084 602	1 357 121	1 269 567	1 592 219	1 506 682

Source: Thai Bond Dealing Centre

Remarks: The BDC was established in November 1994 and renamed Thai BDC in April 1998 following its status upgrade to Bond Exchange. Government and state enterprise bonds have been registered after Thai BDC operated in 1994. T-Bills were registered at Thai BDC for information purpose only, not included in outstanding value of registered bonds. The outstanding value of total registered bonds is included T-Bills since October 1 2001.

Table 2. Turnover Ratios of Bonds in the TBDC*

(Percent)

	1995	1996	1997	1998	1999	2000	2001
Government	-	-	-	13 04	63 30	175 31	148 25
State enterprise	-	-	-	2 63	14 25	51 03	33 87
- Guaranteed	-	-	-	2 62	13 76	55 51	34 67
- Non-guaranteed	-	-	-	2 74	17 45	26 09	28.88
Treasury bills	-	-	-	-	-	76.47	318.94
BoT/FIDF/PLMO	10 96	26 12	41 74	59 90	27 32	16 25	82 99
Government debts	10 96	26 12	41 74	9 91	44 01	121 14	119 60
Corporate debts	56 71	150 38	68 60	7 07	18 30	34 97	36 27
Total value	52 73	134 92	62 80	9 44	39 76	106.90	105 68

Source calculated from Table 1

* Turnover ratio = Yearly trading value/Outstanding value

Table 3. Fund Mobilization in Thailand's Capital Markets and Money Markets by Business Sectors

(Unit billion baht)

	1988-1992 ave p a	1993-2000 ave p a	1988-2000 ave p a
(1) Funds mobilized via capital markets	49 08	161 47	118 24
- as % of country's investment	6 73	17 52	13.95
(2) Commercial banks' credit	262 66	229 50	242 25
- as % of country's investment	36 03	24 90	28 58
(3) - (1) ÷ (2)	18 69	70 36	48 81

Sources NESDB, BOT, SEC, SET

N B calculated from 1988 price

Table 4. International Comparison of Capital and Money Markets in Different Countries, 1988-2000

(Percent)

Countries	Funds mobilized via capital markets		Commercial banks' credit	
	to GDP	to GFCF	to GDP	to GFCF
U S A [2]	9 64	51 74	2 93	15 72
U.K [3]	7 26	43 59	0.01	0.05
Japan [4]	4 32	14 57	3 73	12.57
South Korea	8 80	25 23	8 41	24.10
Singapore	6 07	17 52	11 24	32.45
Thailand	3 87	11 68	8 62	26 01

Sources U S Census Bureau, Statistical Abstract of the United States 1998

London Stock Exchange

Tokyo Stock Exchange, Annual Securities Statistics, 1997

Financial Supervisory Board of South Korea

Monetary Authority of Singapore

NESDB, BOT, SEC and SET

N B [1] GDP = gross domestic product

GFCF = gross fixed capital formation

[2] during 1990-1999

[3] during 1994-1998

[4] during 1988-1997

4. Qualifications

Table 5 shows that after the crisis (1997) both the government and the private sector issued securities to a greater extent than before. However, such event may be somewhat misleading about capital market development so a few qualifications will be given

Table 5: Issuance of Thai Debt Securities

(Billions of baht)

	1993	1994	1995	1996	1997	1998	1999	2000	2001
Government bonds	0	0	0	0	0	400	333 7	94 1	149 2
Treasury bills	0	0	0	0	0	0	77	240 9	441 4
State enterprise bonds	60 4	57 1	55 2	57 4	49 3	46 7	95 3	111 7	57 6
- Guaranteed	0	50 8	55 2	43 1	41 3	46 7	90 1	90 4	57 5
- Non-guaranteed	0	6 3	0	14 3	8	0	5 1	21 3	0 1
FIDF/PLMO bonds	0	0	29 5	139 9	191 5	55	0	0	112
Corporate bonds	21 1	59 8	47 5	36 2	40 9	37 8	289 3	151 2	106 7
Total	81 5	116 9	132 2	232 4	281 7	539 5	795 3	597.9	866 9

Source Thai Bond Dealing Centre

On the part of the government, nine consecutive years (1988-96) of surplus on the cash balance (Table 6) did not allow issuance of securities But once financial turmoil arose, the government offered massive assistance to ailing financial institutions in many formats such as recapitalization (Table 7) via the Bank of Thailand's Financial Institution Development Fund Another reason for substantial borrowing was the government's intention to revive the prevalent economic downturn Thus, issuance of government securities, which represented a dominant source of capital market expansion in the late 1990's, may not be long-lasting, especially when there are limits as mentioned earlier

Table 6. Government's Cash Balance

(Millions of baht)

CY	Cash balance	GDP	Cash balance/GDP (%)
1985	-38,966	1,056,496	-3 69
1986	-34,150	1,133,397	-3 01
1987	-8,861	1,299,913	-0 68
1988	36,098	1,559,804	2 31
1989	65,335	1,856,992	3 52
1990	107,046	2,183,545	4 90
1991	107,707	2,506,635	4 30
1992	72,811	2,830,914	2 57
1993	59,713	3,170,259	1 88
1994	97,651	3,634,500	2 69
1995	126,117	4,192,697	3 01
1996	43,303	4,622,832	0 94
1997	-71,051	4,740,249	-1 50
1998	-129,292	4,628,431	-2 79
1999	-154,362	4,615,388	-3 34
2000	-109,869	4,900,330	-2 24

Sources Bank of Thailand and National Economic and Social Development Board

Table 7· Government Bonds Issued for Recapitalization

(Billions of baht)

Recapitalization bonds	1998	1999	2000
For FIDF	400	100	0
(% of total government bonds)	100 00	30 05	0 00
For reopened FIDF	0	149 04	0
(% of total government bonds)	0 00	44 78	0 00
For tier 1&2			
for banks	0	39 03	24 65
(% of total government bonds)	0 00	11 73	44 84
for finance companies	0	9 73	0 32
(% of total government bonds)	0 00	2 92	0 58
Total recapitalization bonds	**400**	**297.8**	**24 97**
(% of total government bonds)	100 00	89 48	45 42
Total government bonds	**400**	**332.8**	**54 97**

Source Bank of Thailand

On the part of the private sector, commercial banks underwent a rigid course of adjustment Tighter rules on loan classification and provisioning as well as write-off were ordered by the central bank after the country received assistance from the IMF It is thus unsurprising that bank credit contracted in 1998-2000 (Table 8), as commercial banks became remarkably cautious about their credit extension. Moreover, they had to recapitalize themselves either by issuing more shares or merging with foreign partners Some large non-bank private corporations also paid more attention to tapping funds from domestic capital markets not only because bank credit became less accessible but because local interest rates declined sizably while exchange rates fluctuated to a large extent These private companies therefore chose to issue domestic bonds in 1990-2000 in order to refinance their foreign debt obligations (Tables 9-10) After commercial banks' recapitalization and large corporations' debt refinancing, there is no assurance of further capital market development In other words, the booming of capital markets may not be sustainable

Table 8· Capital Market Mobilization and Changes in Commercial Banks' Credit

(Billions of baht)

	1993	1994	1995	1996	1997	1998	1999	2000
Capital mobilization (current price)	122 55	250 49	225 85	242 23	90 54	232 03	566 83	232 15
Capital mobilization (1988 price)	95 64	185 77	158 39	163 43	58 55	137 44	351 14	141 41
% of gross investment	*9 78*	*17 27*	*13 16*	*12 79*	*5 74*	*22 57*	*61 14*	*22 20*
Change in commercial banks' credit						-		
Change in commercial banks' credit								
% of gross investment	*-40 91*	*52 60*	*46 22*	*31 94*	*76 40*	*-79 90*	*11 42*	*50 35*

Source Securities and Exchange Commission

Table 9. Value of Newly Issued Securities Classified by Types of Instruments

(Billions of baht)

	1993	1994	1995	1996	1997	1998	1999	2000
Equities	60 23	138 00	138 65	106 43	49 62	194 25	245 83	64 46
(% share)	*49 14*	*55 09*	*61 40*	*43 94*	*54 80*	*83 72*	*43.26*	*27 41*
Debt instruments	21 46	82 54	70 60	92 33	38 15	31 06	313 30	163 10
(% share)	*17 51*	*32 95*	*31 26*	*38 12*	*42 14*	*13 39*	*55 14*	*69 36*
Equities-linked instruments	39 99	27 51	16 10	40.53	2.77	6 72	7 69	7 59
(% share)	*32 63*	*10 98*	*7 13*	*16 73*	*3 06*	*2 90*	*1 35*	*3 23*
Warrants	0 88	2 44	0 47	2 95	0 00	0 00	1 40	0 00
(% share)	*0 72*	*0 97*	*0 21*	*1 22*	*0 00*	*0 00*	*0 25*	*0 00*
Total	122 56	250 49	255 82	242 24	90 54	232 03	568 22	235.15

Source Securities and Exchange Commission

Table 10. Value of Corporate Bond Offerings, Categorized by Types

(Billions of baht)

Type of bonds	1995	1996	1997	1998	1999	2000	2001
Straight issues	70 6	92 33	38 15	30 05	308 17	146 92	106.67
(% share)	*81 40*	*69 49*	*93 23*	*82 90*	*97 57*	*95 17*	*99.99*
Convertible issues	16 13	40 53	2 77	6 2	7 69	7 45	0 01
(% share)	*18 60*	*30 51*	*6 77*	*17 10*	*2 43*	*4 83*	*0 01*
Total	86 73	132 86	40 92	36 25	315 86	154 37	106 68

Source Securities and Exchange Commission

Even since Thailand opened up her capital account in the early 1990's, the Thai capital markets counted upon foreign capital to a large degree (e g roughly a third of turnover in SET, see Table 21) Even though such relationship may have helped reinforce the markets somewhat, it adds undesirable elements of volatility and vulnerability to the markets because of the following reasons. Interest rate differentials became significant stimulant and so did exchange rate fluctuations together with other relevant factors (e g current account status, foreign exchange reserves) Fluctuations of stock market indices in foreign countries had more influence as well. In short, though foreign capital may have strengthened the growth path of Thai capital markets, it was highly volatile, making Thai capital markets more vulnerable to shocks

5 Crucial Shortcomings

1 Although the Thai capital markets were relied upon to a growing extent after 1997, the growth was not well diversified across different sectors Among the thirty business sectors which tapped funds from the market, only a few sectors were those funds clustered around In 1988-2000 the sectors which benefited most were financial institutions, construction, and property Altogether, they commanded 67% share of funds, far more than their GDP share of 12% (Table 11) In the meantime, the fund share of industries, imports, and exports was only 16%, roughly a half of these industries' value added to GDP or 31% The above-mentioned bias did not occur in the distribution of commercial banks' credit. Instead, their profile corresponded well to GDP composition.

Table 11 Sectoral Distribution of Fund Allocation in Thailand, 1988-2000

(Percentage share)

Business sector	GDP[1]	Capital markets	Banks
1 Industries, exports, and imports	31 58	16 85	36 65
2 Services, consumption, and public utilities	19 96	10 38	22 42
3 Wholesale and retail trade	16 54	1 98	16 71
4 Financial institution, construction, and properties	12 06	67 34	21 09
5 Agriculture	10 22	0 00	2 50
6 Mining	4 12	3 45	0 62
7 Administration and defence	3 01	0 00	0 00
8 Housing[2]	2 51	0 00	0 00
Total	100 00	100 00	100 00

N B [1]Composition of GDP at constant prices

[2]Rentals

2 As of mid-2000 there were 383 firms listed in the Stock Exchange of Thailand (SET), representing only 0 17% of all companies in Thailand (Table 12) Nevertheless, these listed firms' capital funds added up to 26 52% of all companies' Such records indicate that relatively very few Thai firms were willing to spread their ownership and minimize their cost of funds via direct financing through the capital markets A majority of Thai companies still counted upon more expensive indirect financing via financial intermediaries That was true even with large firms which had potential to be listed in the stock exchange. In 2000, there were 3,261 limited companies and public limited companies which met the SET requirements, i e having paid-up capital funds of at least 200 million baht each and long enough satisfactory profits However, up to 2,915 or 89% of those firms opted to stay out of the stock market. In terms of paid-up capital funds, those non-stock-market public or large limited firms also represented the majority (62%) of all eligible companies (Table 13) Most of those eligible but non-stock-market firms fell in the following two sectors (Table 14) manufacturing (22%), property & construction & renting & business services (24%)

Table 12 Public and Limited Companies at the end of 1999

	Number of companies	Capital funds (million baht)
(1) Public and limited companies in the whole country	226,060	4,982,221 63
(2) Listed companies in SET	383[1]	1,321,490 96
as % of (1)	0 17	26 52

Sources Ministry of Commerce, SET

N.B. [1] As of 30 June 2000

Table 13 Public and Limited Companies Having Paid-up Capital Funds of at Least 200 Million Baht Each at the end of 1999

	Number of companies	Capital funds (million baht)
(1) Public and limited companies with paid-up capital funds of at least 200 million baht	3,261	3,567,889 2
(2) Companies in (1) but not listed in SET	2,915[1]	2,211,418 4
as % of (1)	89 4	62 0

Sources Ministry of Commerce, SET

N B As of 30 June, 2000

Table 14: Companies Eligible to be Listed in SET at the end of 1999
as Categorized by Business Sectors

Business sector	Number of companies		Capital funds	
	Companies	%	mil baht	%
1) Manufacturing	668	22 9	571,482	25 8
2) Property, construction, renting, business services	700	24 0	459,550	20 8
3) Wholesale retail trade, auto and motorcycle repairs	474	16 3	372,500	16 8
4) Financial institutions	192	6 6	205,708	9 3
5) Communication, transportation, storage	73	2 5	77,979	3 5
6) Hotels and restaurants	99	3 4	48,624	2 2
7) Entertainment, personal services	49	1 7	42,914	1 9
8) Energy	30	1 0	36,238	1 6
9) Healthcare services	70	2 4	29,400	1 3
10) Agriculture	49	1 7	22,942	1 0
11) Education	18	0 6	6,916	0 3
12) Others	493	16 9	337,164	15 2
Total	2,915	100.0	2,211,418	100 0

3 The intricate issues, which have very strong impact on the capital markets and are not yet resolved, concerns good corporate governance and transparency Explicit rules cannot be implemented or even spelled out on these issues but they acutely affect performances of both listed firms and potential candidates For instance, poor corporate governance and inadequate transparency, which can easily generate negative repercussions, is prevalent in Thai businesses, even among some listed companies. Such weaknesses are partly due to culture and it can hardly be rectified by any regulation or supervision, especially in the midst of economic difficulties, because unlike money markets, capital markets involve so many parties that few regulations prove effective.

4. Regarding instruments in capital markets, Table 15 indicates that Thailand lagged behind developed countries in that its fund mobilization still counted considerably upon equity-related instruments That was primarily because bond markets in Thailand were opened up later than the stock market Nonetheless, after the

SEC Act became active (1992), more corporate bonds (straight issues and convertible issues) were offered to such an extent that the debt portion gained growing momentum (Table 16).

Table 15 Proportions of Funds Tapped via Capital Markets as Categorized by Instruments in Different Countries during 1988-2000

Unit % of total mobilization

Country	Equity-related	Debt-related
U S A [1]	17 72	82 28
Japan	11 27	88 73
South Korea	24 91	75 09
Singapore	49 19	50 81
Thailand [2]	56 14	43 86

Sources - U S Census Bureau, Statistical Abstract of the United States 1998
- Tokyo Stock Exchange, Annual Securities Statistics 1997
- Financial Supervisory Board of South Korea
- Monetary Authority of Singapore
- BOT, SEC, SET

N B [1] during 1990-1999
during 1988-1997
Equity-related include common shares, preferred shares, and warrants
Debt-related include debentures and convertible debentures

Table 16 Funds Tapped via Capital Markets as Categorized by Instruments during 1988-2000

Unit billion baht

Instrument	1988-1992	1993-1997	1998-2000
(1) Equity-related proportion (%)	51 32 90 68	99 93 53 63	168 18 48 94
(2) Debt-related proportion (%)	5 27 9 32	86 40 46 37	175 49 51 06
(3) Total proportion (%)	56 60 100 00	186 33 100 00	343 67 100 00

Sources BOT, SEC, SET

5. The supply of government bonds are limited by the above-mentioned law that allows issuance of government securities only when budget deficit arises.

6. On the investor side, institutional and high net-worth investors played a predominant role (Table 17) They commanded 98% of newly issued corporate bonds. Commercial banks, in particular, held the largest portion of government securities as a means of investment and satisfying reserve requirements (Tables 18-19) The household sector, in contrast, had less confidence and/or little knowledge about capital market instruments Bank deposits thus gained the largest and growing weight in the household savings as surveyed by the central bank (Table 20). This represents one significant drawback of capital market development in Thailand

Table 17. Investors of Newly Issued Corporate Bonds

Investors	1995		1999	
	Millions of baht	%	Millions of baht	%
Institutional investors and high net-worth investors	**84,103**	**96.97**	**314,652**	**99.62**
Domestic investors	27 214	31 38	287,801	91 12
Foreign investors	56 889	65 59	26,851	8 50
Retail investors	**2,627**	**3 03**	**1,206**	**0.38**
Domestic investors	1 619	1 87	1,201	0 38
Foreign investors	1 008	1 16	5	0 00
Total	**86,730**	**100 00**	**315,858**	**100.00**

Source Securities and Exchange Commission

Table 18 Investors in Government Debt Securities (Amounts)

(Millions of baht)

	1995	1996	1997	1998	1999	2000	2001
Bank of Thailand	12,301	20,608	75,232	214,942	153,120	129,101	146,296
Commercial banks	166,303	157,795	136,949	282,475	414,498	446,999	457,466
Government Savings Bank	14,184	24,460	21,838	47,748	148,129	187,761	169,999
Financial institutions	70,763	75,402	41,680	72,023	61,791	60,456	53,368
Insurance companies	6 785	6,511	14,632	31,040	62,198	93,768	126,767
Others	10 909	11,646	17,692	64,805	124,914	201,142	268,208
Total	281,245	296,422	308,024	713,034	964,650	1,119,227	1,222,104

Source Bank of Thailand

Table 19: Investors in Government Debt Securities (% Shares)

(Percentage share)

	1995	1996	1997	1998	1999	2000	2001
Bank of Thailand	4 37	6 95	24 42	30 14	15 87	11 53	11 97
Commercial banks	59 13	53 23	44 46	39 62	42 97	39 94	37 43
Government Savings Bank	5 04	8 25	7 09	6 70	15 36	16 78	13 91
Financial institutions	25 16	25 44	13 53	10 10	6 41	5 40	4 37
Insurance companies	2 41	2 20	4 75	4 35	6 45	8 38	10 37
Others	3 88	3 93	5 74	9 09	12 95	17 97	21 95
Total	100 00	100 00	100 00	100 00	100 00	100 00	100 00

Source calculated from Table 18

Table 20 Pattern of Household Savings in Thailand

(Percentage share)

Type of Savings	1993	1998
Deposits	74 9	94 5
Life insurance	18 9	1 4
Equity	1 3	0 3
Provident funds	0 3	2 1
Others	4 6	1 7
Total	100	100

Source Survey of the Bank of Thailand, 1993 and 1998

7 Worse yet, non-bank institutional investors, e.g insurance companies, provident funds, mutual funds, are (for prudential purpose) restricted on corporate bond investment And these regulations affect their trading activities in the secondary bond market.

7 1 Insurance companies

a) Investment in any particular company's corporate bonds must not exceed 10% of the total value of bonds issued by the company

b) Investment in corporate bonds issued by insurance companies must not exceed 10% of total assets

c) Investment in corporate bonds issued by non-insurance companies must not exceed 30% of total assets.

7 2 Provident funds

Investment in any company's cooperate bonds must not exceed 5% of total funds

7 3 Mutual funds

a) Investment in any company's corporate bonds must not exceed 5% of total net asset value

b) Investment in corporate bonds that are not rated in the first four rankings from a credit rating agency are subject to an investment ceiling not exceeding 15% of total net asset value

8. Table 21 and Figure 1 display one vulnerable feature of SET Roughly a third of turnover value in the Thai stock exchange were up to the discretion of foreign investors That represents formidable vulnerability to volatility because foreign investors have gigantic funds, tend to know little detail about local scenario, and are inclined to move in consonance with capital markets abroad. Their movements of huge investment funds also strongly affect exchange rate of the baht after the baht was floated in 1997 Ever since Thailand opened up its capital account in the early 1990's, portfolio moves of foreigners have become a primary determinant of SET index. An adverse and strong repercussion from such situation is that local investors are often discouraged or even scared off, except the speculative ones Another repercussion is on the real sector via exchange rate fluctuations because of varying foreign portfolio investment

Table 21: Turnover Value of SET Classified by Groups of Investors

(Millions of baht)

	1993	1994	1995	1996	1997	1998	1999	2000	2001[1/]
Net turnover value[2/]									
Foreign investors	52,419	-41,737	47,302	13,377	55,437	30,227	-3,134	-33,068	-6,426
Local institutions	23,928	13,405	-756	-17,056	-22,453	-3,239	-2,872	-948	-538
Retail investors	-76,346	28,332	-46,546	3,680	-32,984	-26,987	6,006	34,016	6,963
Percentage of total turnover value[3/] (%)									
Foreign investors	16.97	20.94	26.33	34.25	43.25	34.62	29.41	32.19	18.62
Local institutions	7.77	9.55	13.07	12.41	9.94	5.64	4.90	5.69	3.95
Retail investors	75.27	69.51	60.60	53.34	46.81	59.75	65.69	62.12	77.43

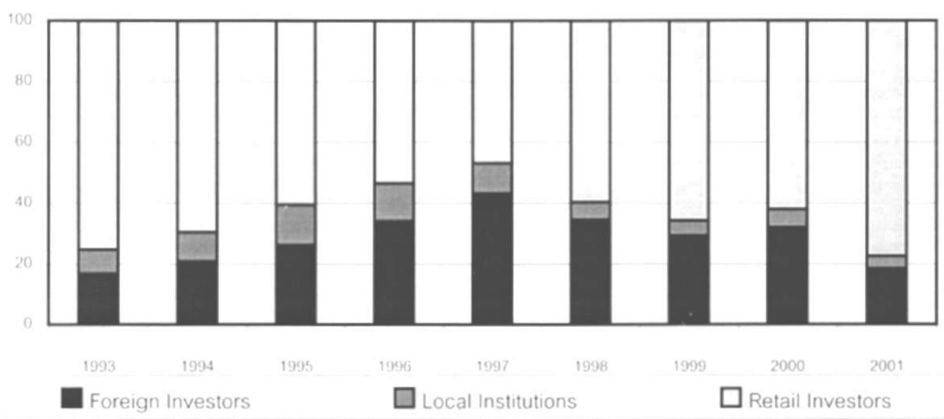
Source: Securities and Exchange Commission

Note : [1/] preliminary data

[2/] net turnover value = buying value - selling value

[3/] percentage of turnover value $= \left(\dfrac{\textit{buying value} + \textit{selling value}}{\textit{total buying and selling value}}\right) x100$

Figure 1: Turnover Value of SET Classified by Groups of Investors (% Shares)



6. Recent Policy Moves

Towards the end of 1990's the government believed more in market discipline, which claims that if market forces function efficiently, movements of securities prices will reflect most relevant data or status of the firms. Market forces should therefore be allowed to function freely, since securities prices would then serve as prompt signals to both regulators and firm owners as to whether there are any emerging problems or not. This growing belief gave rise to a series of policy actions, as follows

1 Since 1997 the SEC has already allowed investors to conduct short selling and securities lending Short selling provides investors an opportunity to make profits when the market goes downwards, whereas securities lending is meant to support short selling activities

2 Recognizing the fact that a large number of business entities in Thailand are small, in June 1999 the SET established another market for small- and medium-sized enterprises (SME) called "Market for Alternative Investment" or MAI Its trading and settlement as well as trading hours are the same as those of the main market, but the minimum paid-up capital for companies listed in MAI is lowered to 40 million baht from 200 million baht as in the main market Besides, the authorities further motivate SME to resort to MAI by lowering MAI corporate income tax to only 20% from 25% on SET-listed firms and regular 30% corporate income tax on non-listed companies

3 In order to enhance liquidity and facilitate transactions in the secondary debt market, the government authorized the organization of interdealer brokers in 2000.

4 In June 2000 the SET modified its listing criteria to provide greater flexibility for prospective companies to be listed in the market The requirement of no accumulated losses was revoked and prospective companies have three options profit based (net profit of at least 30 million baht in the pre-listing year), sales based (sales revenues of at least 2 million baht in the pre-listing year), market capitalization based (market capitalization of at least 1 5 billion baht)

5 Earlier, the clearing and settlement system at SET was based on payment by cheques and electronic book entry system in the delivery of securities among clearing members Since September 2000 the system was changed into a delivery-versus-payment Under the new system clearing members which are custodian banks can make or receive payments directly to Thailand Securities Depository through the Bank of Thailand's BAHTNET system

6. In October 2000 brokerage commission fees were liberalized so as to create intense competition and equip investors with more alternatives whose rates may vary in accordance with the services provided

7. As a means to upgrade the quality of securities supply, the authorities coordinated efforts to expedite privatization of some state enterprises such as electricity power plants, petroleum authority, Thai Airways The first one (Ratchaburi Electricity Power Plant) was listed at the end of 2000.

8 To cultivate investors, in 2000 the SEC set up a capital market information center from which investors can search for necessary information to support their investment decisions. The SEC promotes activities on information access, education and training, and investor protection The agency has also developed capital market information on a website

9 In January 2001 the SET launched the regulations on internet trading, under which securities companies with computer supports and information security systems may be permitted to give internet trading services to their customers. Afterwards, the SET organized a new company called "SETTRADE COM" to provide internet trading services for securities companies in order to promote securities trading via the internet and to help reduce securities houses' risks and investment expenses

10 In February 2001 Fitch Ratings was approved as the country's second credit rating agency, because investors are perceived to need more assistance in credit rating information so that they can assess risks of and return to their investment with more confidence and accuracy.

11 In order to encourage listing of private companies, the SEC eases the process of application for companies which have won promotion from the Office of the Board of Investment, commencing March 2001

12 Along with other liberalization measures, the SEC in March 2001 permitted securities companies to expand their scope of businesses to include the following: life

insurance broker, back office provider, computer vendor, and mutual fund business via subsidiaries.

13 In 1997 some mutual funds, e g Thai Trust Fund, were established as a means to help foreigners invest in companies which have already reached their limits on foreign shareholding. Similarly, in mid-2001 non-voting right depository receipt (NVDR) was introduced as a new type of securities providing holders with all rights to which shareholder are entitled, except the voting right

14 Foreseeing the importance of long-term institutional investment as shock absorber, the SEC supported long-term savings for retirement by establishing retirement mutual funds (RMF) in the last quarter of 2001 If savers satisfy certain conditions in this RMF (e g having invested for at least five years, first redemption allowed only after owners' ages have arrived 55 years old), they will be given similar tax privileges to those of provident funds.

7. Concluding Remarks

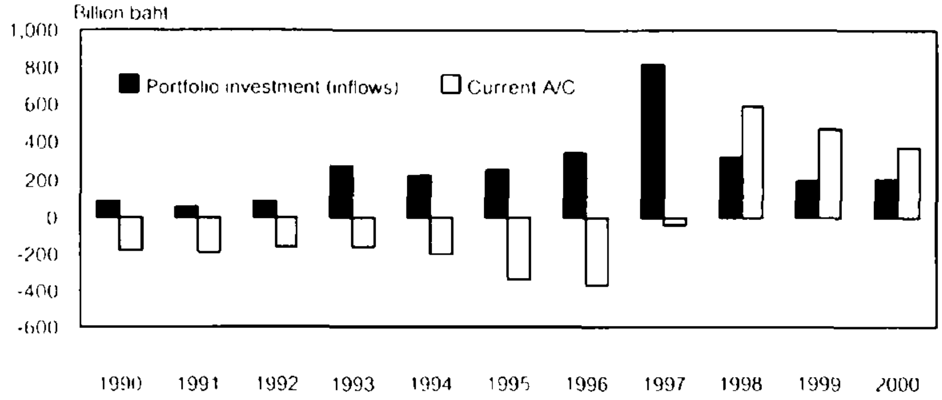
The statistics and stories in the past decade (1990's) may suggest satisfactory performance and ruling in Thailand's capital markets, as hinted by the volume of debt securities issued by the public and private sectors (Table 5), the turnover value of foreign investment (Table 21), and a series of recent liberalization measures. However, detailed investigation may not similarly give a positive impression

In the public sector, the stringent rules on borrowing create uncertainties in bond issuance, debt rollover, maturity profile, benchmark yield curve, and actual uses of funds The government can issue bonds only for deficit financing, not for other purposes such as allocating or channeling or lubricating capital flows On the part of lenders or investors, the reserve requirements that the government imposes upon financial institutions leave the general public and the secondary markets with fewer government securities to trade Worse yet, the implementation of monetary policy in the official repurchase market further distorts the genuine market forces

In the private sector, even though the SEC Act of 1992 allows limited and not necessarily public companies to issue corporate bonds, actual issuances were pursued only by large and leading firms, as corporate bonds tend to be a costly source of funds once the issuing size is not large enough Corporate bonds also need adequately good credit rating So small- and medium-sized enterprises (SME) are left out What is more worrying is that in Thailand SME account for more than 90% of the total number of businesses And even after the authorities set up MAI exclusively for SME, only very few SME resorted to MAI, demonstrating that the Thai corporate culture does not favor listing or public ownership. Or, family circles mean very much. Besides, for the sake of stability, the authorities impose some restrictions upon institutional investors' extent of corporate bond investment and trading activities in the secondary bond market. What is more worrying is that these institutional investors (e g insurance companies, provident funds, mutual funds) play far more important roles than households in capital market development

Though foreign capital may be one alternative source of stimulus in the market, it could generate an excessive degree of volatility because of the following reasons First, foreign investors tend to diversify their portfolios of investment in various countries Whenever there is any shock in one country, these investors may move investments in other countries so as to cover their losses or positions. Consequently, dependence upon these investors means bringing in an additional and unnecessary degree of market fluctuations Second, ordinarily foreigners have less acquaintance with domestic corporations or local incidents. These foreigners thus tend to be too gullible and sensitive What is more frightening is that foreigners' volumes of transactions are gigantic, as evidenced by the sizes of Thailand's aggregate portfolio investment when compared with those of current account (Figure 2) Therefore, capital flows due to foreigners' decisions certainly have strong impact upon both stock market sentiment and exchange rate in the current flexible regime And that has powerful repercussions upon both the real and financial sectors

Figure 2. Portfolio Investment (Inflows) VS Current Account



Liberalization of securities businesses can be a double-edged sword, depending upon how well prepared the concerned local agencies are. Having more freedom to undertake new businesses may mean more income and growth of domestic securities firms or banks. It could bring more competition and welfare to consumers as well. However, it will definitely lead to more risks. The crucial question is whether those domestic securities firms or banks are ready or mature enough to handle those risks or not. Financial liberalization of immature commercial banks and finance companies in the early 1990's, which led to financial bubbling and crisis in 1997 ultimately, serves as a sorrowful lesson for improper timing of liberalization. To cope successfully with enormous and volatile transactions, securities firms and commercial banks unquestionably need adequate experience and expertise. Otherwise, they could easily overexpose themselves as some did in the past.

Altogether, foreign investment in and liberalization of securities business may accelerate the pace of capital market development in Thailand. Nevertheless, they also bring about a greater degree of vulnerability or susceptibility to dangers or shocks in one format or another, depending upon how well prepared local agents have been.

Liberalization immediately leads to controversial issues of regulations. Different sectors deserve different rules, and so do different objectives. Target sectors and objectives therefore should be explicitly spelled out and ranked in their significance before any rule could be properly designed. In this context, at certain times one sector or objective may be more important than others. But at other times their degrees of urgency may be reversed. That is, time dimension should also be taken into consideration Regulations on different sectors or agents should also be optimally coordinated so that neither loopholes nor biases arise in favor of or against certain groups or agencies

Corporate culture is another constraint that deserves attention. Some rules or regulations in particular cultures or countries may not be compatible with other cultures or countries In those cases, modifications or compromise should be devised so as to fit with the prevalent business or corporate culture In this regard, SME are clear-cut examples of southeast Asian nations' businesses which hesitate to publicize their ownership or debts as a means to tap needed funds. Since they prefer to revolve around narrow circuits of friends in the same professions or communities, some cooperatives, representing groups of SME, could be formulated and may be listed in the capital markets counting upon aggregate performance of each cooperative's members If listing or issuance criteria are properly designed and met, recycling funds in domestic arena to SME via capital markets may be achievable in both senses, i e compatible with SME's preference while sufficiently productive plus stable from the viewpoint of pertinent investors.

In summary, the issues of SME, foreign *portfolio investment*, and liberalization of securities business clearly demonstrate that the central authorities are caught in several dilemmas in issuing or relaxing regulations. Coercive or stringent rules upon entry for the sake of stability or safety will have negative impact upon SME and foreign investors In this respect, distress is severe because of the huge number of SME and colossal volume of potential foreign investment. On the other hand, loosening rules upon these entities could give rise to company failures and rapid or wild market fluctuations. Therefore, the government has to be extremely careful in choosing the optimal blend of regulations along the path of capital market development

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