

A Critical Review of the Economic Freedom of the World Index, with Reference to Thailand and the Freedom to Exchange with Foreigners*

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I. INTRODUCTION

The *Handbook of Freedom* (DFN 2004) defines economic freedom as “the right of man to engage in voluntary economic activities (e.g., trade) for his benefit.” There are a number of other definitions and measures of such economic freedom. The Fraser Institute and other institutions annually publish the *Economic Freedom of the World* report, which contains various indices to measure *economic freedom*. This publication forms the basis for our review. Economic freedom is not a new term but an adaptive dimension for rating how residents of a country assess the freedom of their personal choices and voluntary exchanges, their freedom to compete, and the protection of their person and property from incidental shocks.

Representative government is the political corollary of the market economy. The same philosophic movement that created modern capitalism substituted elected officeholders for the authoritarian rule of absolute kings and hereditary aristocracies. It was this much-decried bourgeois liberalism that helped to bring about today’s freedom of conscience, of thought, of speech, and of the press, and put an end to the intolerant persecution of dissenters. The governmental as well as political institutions providing the infrastructure and necessary foundations of society therefore protect individuals and their property from violence and coercive forces. In preparing the *Economic Freedom of the World* report, Gwartney and Lawson (2003) found a positive high correlation between the economic freedom index and per capita income and economic growth. In addition, the index is comparable to other leading social indicators, such as the illiteracy rate, the percentage of the population having access to improved sanitation facilities, and the expectation of life.

The *Economic Freedom of the World* index adapts third-party data to measure the degree of economic freedom of countries in five areas: (1) size of government, (2) legal structure and security of property rights, (3) access to sound money, (4) freedom to

exchange with foreigners, and (5) regulation of credit, labor, and business. This paper is aimed at analyzing and qualifying the degree of freedom under *Area 4: Freedom to Exchange with Foreigners*, as it relates to the policies of Thailand and their implications.

Area 4 encompasses one of the most important issues of economic freedom in the global context, i.e., the freedom to exchange among a nation’s residents and those living outside its national boundaries, a process that contributes to better living standards. The freedom to exchange with foreigners therefore involves the elimination or amelioration of restrictions that would otherwise be an obstacle to international trade, such as tariffs and quotas, non-tariff barriers, hidden administrative costs of exchange, exchange rates and capital controls. These economic freedom indicators are therefore notified and adapted using the current situation of Thailand as well as the current policy implications to support these indices.

Based on the economic freedom indices for Area 4, the evidential and policy implications will be discussed according to the following economic freedom ratings (see Gwartney and Lawson (2003) for details on how the indices are computed):

- A: Taxes and international trade
 - (i) Taxes as a percentage of exports and imports
 - (ii) Mean tariff rates
 - (iii) Variability of tariff rates
- B: Regulatory trade barriers
 - (i) Hidden import barriers
 - (ii) Cost of importing
- C: Actual size of trade sector compared with expected size
- D: Difference between official exchange rate and black market rate
- E: International capital market controls
 - (i) Access to foreign capital
 - (ii) Restrictions on foreign capital transactions

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Section II provides an overview of economic freedom ratings under two major issues: trade liberalization and financial/capital liberalization, both of which are related to the freedom rating of Area 4. Section III discusses the current status of Thailand's policies and their implications, especially under the current governmental administration, based on the above ratings. Section IV provides a conclusion.

II. THAILAND'S ECONOMIC FREEDOM TO EXCHANGE WITH FOREIGNERS: AN OVERVIEW

Thai people gained greater freedom in the twentieth century than had ever been the case previously. Thai citizens are free from proactive controls by government agencies and are free to move about at their own discretion. They also generally enjoy freedom of speech, which is a constitutional right, and the government generally respects these rights in practice. However, although the government may restrict these rights to preserve national security, maintain public order, preserve the rights of others, and protect public morals, in practice this rarely has been done.

Thailand was ranked 44th among 123 countries in 2001 for overall economic freedom; its rating then was 6.7. A rating of 10 is the highest score. In 1975, Thailand was rated 5.8 (rank 24th), a level that has generally varied little over the years. The freedom index for Thailand reached its highest level in 1995, i.e., 7.1 (rank 26th). If only the index of freedom to exchange with foreigners is considered, Thailand's rating increased considerably, i.e., from 6.0 in 1975 to 7.7 in 2001 (Table 1). The freedom to exchange with foreigners therefore provides insight into the country's progress in increasing economic freedom with regard to international relations in the global context.

Thailand's freedom to exchange or to trade with foreigners when compared with that of some countries in Asia is reflected in Table 2.

The results show that Thailand has achieved the strongest level of freedom with regard to (1) the actual vs. expected size of the trade sector and (2) the

difference between the official and black market exchange rates, the ratings for which reached the highest level, i.e., 10. However, these two indices are not surprisingly different from those of other countries in Asia. The sub-section with the lowest rating for Thailand concerns restrictions in foreign capital market exchange; Thailand's rating was only 1.5.

Table 1 Economic Freedom Index for Thailand

Year	Overall economic freedom rating	Freedom to exchange with foreigners
1975	5.8	6.0
1980	6.0	6.1
1985	6.1	6.2
1990	6.8	6.6
1995	7.1	6.9
2000	6.6	7.6
2001	6.7	7.7

In overview, the freedom to exchange with foreigners in Thailand's context is generally divided into two parts: (1) freedom to trade with foreigners, or trade liberalization, and (2) freedom in capital market exchange with foreigners, or international financial liberalization.

2.1. Trade Liberalization

The freedom to trade with foreigners, or trade liberalization issues, are currently distinguishable policies that the Thai government aims to implement with other trading partners. Trade liberalization involves the freedom of countries to trade without any tariff or non-tariff barriers. Preferential free trade arrangements have strengthened the freedom of Thailand to exchange with foreign countries, thus also making development among nations more sustainable. The preferential trade arrangements, both bilateral and multilateral that have been signed, purposed, or under negotiation with various country groups are summarized in Table 3.

Table 2 Area 4's Economic Freedom Rating in Selected Asian Economies, 2001

	Hong Kong	India	Indonesia	Malaysia	Thailand
Ai Tax as percentage of exports/imports	9.8	4.4	9.5	9.0	9.0
Aii Mean tariff rates	10.0	3.5	8.3	8.1	6.7
Aiii Standard deviation of tariff rates	10.0	5.0	5.7	0.0	4.4
A Tariffs	9.9	4.3	7.8	5.7	6.7
Bi Hidden import barriers	8.9	5.5	4.2	6.3	5.8
Bii Costs of importing	9.6	7.0	8.1	8.6	8.8
B Regulatory trade barriers	9.2	6.2	6.1	7.5	7.3
C Actual vs. expected size of trade sector	10.0	6.0	9.9	10.0	10.0
D Difference between official and black market exchange rates	10.0	10.0	10.0	10.0	10.0
Ei Access of citizens to foreign capital markets/foreign access to domestic capital markets	9.9	4.0	8.1	6.6	7.0
Eii Restrictions on foreign capital market exchange	9.2	0.0	1.5	0.8	1.5
E International capital market controls	9.6	2.0	4.8	3.7	4.3
Freedom to exchange/trade with foreigners	9.8	5.7	7.7	7.4	7.7

Table 3 Preferential Trading Arrangements Involving Thailand and Other Countries: as of May 2004

Partners	Type of arrangements	Status
<i>Regional level</i>		
ASEAN	Free Trade Area	Implemented
ASEAN+3	Comprehensive Economic Cooperation	Official discussions
ASEAN-EC	Comprehensive Economic Cooperation	Official discussions
ASEAN-Canada	Comprehensive Economic Partnership	Implemented
ASEAN-China	Comprehensive Economic Partnership	Implemented
AFTA-CER	Comprehensive Economic Partnership	Official discussions
ASEAN-Japan	Comprehensive Economic Partnership	Official discussions
ASEAN-India	Comprehensive Economic Cooperation	Official discussions
ASEAN-USA	Trade and Investment Framework	Official discussions
BIMST-EC	Free Trade Area	Implemented
<i>Bilateral level</i>		
Thailand-China	Free Trade Area	Implemented
Thailand-Bahrain	Closer Economic Partnership	Implemented
Thailand-USA	Free Trade Area	Official discussions
Thailand-Australia	Free Trade Area	Will sign in July 2004
Thailand-Sri Lanka	Free Trade Area	Proposal/study
Thailand-India	Free Trade Area	Implemented
Thailand-New Zealand	Closer Economic Partnership	Proposal/study
Thailand-Peru	Free Trade Area	Implemented
Thailand-Japan	Closer Economic Partnership	Official discussions

Source: Summarized by International Economic Relations Program, TDRI.

A number of preferential trading arrangements in regional agreements have been extended from the regional trading partners of the ASEAN Free Trade Area (AFTA) to a wider area. Moreover, Thailand has encouraged regional economic partnership within the Asia-Pacific Economic Cooperation (APEC) forum, Asia-Europe Meetings (ASEM), Bangladesh-India-Myanmar-Sri Lanka-Thailand Economic Cooperation (BIMST-EC), and the Greater Mekong Subregion (GMS) to liberalize more rapidly and extensively in the context of regional trading arrangements, because of its conviction that liberalization should assist economic recovery. However, the trade liberalization policies that the Thai government has signed or is negotiating with many individual countries or country groups may be complicated to implement owing to the intra-linkages among those agreements. Figure 1 shows the intra-linkages in various preferential trading arrangements involving Thailand and other countries or groups of economies.

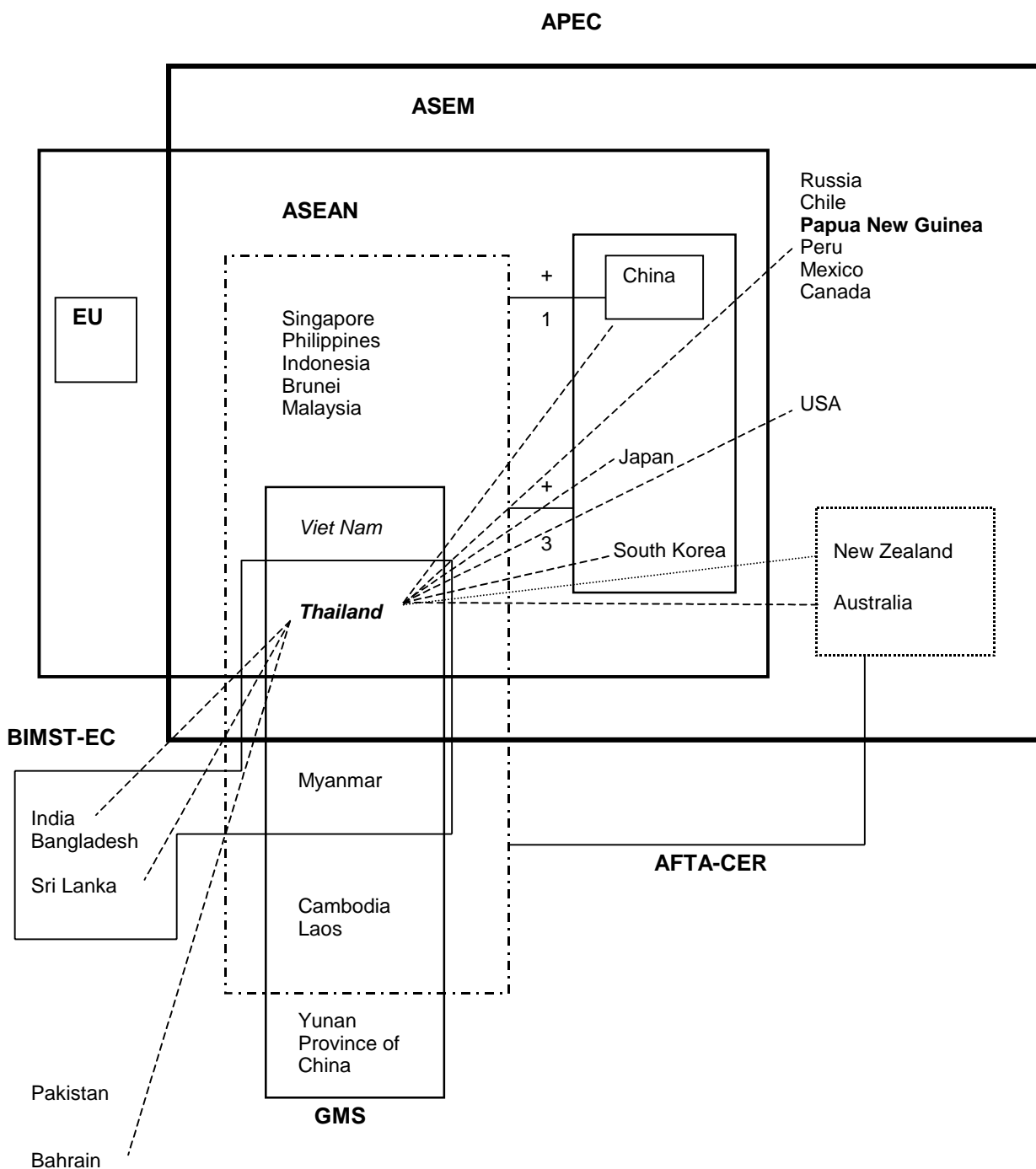
The likelihood of establishing free trade areas involving Thailand and other countries is therefore one of the main issues for building up the economic freedom of the nation. However, with regard to taxes on international trade and regulatory trade barriers, especially in specific sectors, the free trade areas are still not so effective that it would be possible to conclude that Thailand's economic freedom will be improved. The rating ranges from 4.4 to 8.8 under the various areas listed under tariffs and regulatory trade barriers provide useful indicators of what areas need adjustment to improve Thailand's trade liberalization policies. (More specific details for each topic under these areas will be presented in section III.)

2.2. Capital and Financial Liberalization

The financial liberalization of Thailand was one of the hottest issues during the country's financial reform process. During the period from the late 1980s to 1991, Thailand's economy underwent deep structural changes, including the liberalization of its financial sector and the integration of its economy with global financial and product markets. The management of the economy during this period of rapid structural change and the large capital flows that started in 1988 was a major challenge for the Thai authorities. Thailand maintained relatively open current and capital accounts, with liberal treatment of foreign direct and portfolio investments. Foreign borrowing by Thai residents was allowed, but was subject to registration with the Bank of Thailand (BOT). Starting in 1985, both current and capital account transactions were significantly liberalized. By the end of 1994, Thailand was free of foreign exchange restrictions on current account transactions, and had a very open and favorable regime for foreign investment. Thai investment overseas, in particular by financial intermediaries and banks, was also restricted.

Hardin and Holmes (1997) ranked the degree of liberalization among countries in terms of its support of foreign direct investment (FDI) inflows to business, communication, distribution, and financial sectors. Their *FDI Restrictiveness Indices* showed that Thailand still provided a relatively low degree of liberalization, especially in the services and financial sectors (Table 4).

Figure 1 Preferential Trading Arrangements



Source: Summarized by International Economic Relations Program, TDRI.

Table 4 Financial Liberalization: FDI Restrictiveness Indices

Country/area	Business	Communication	Distribution	Financial
Thailand	78	81	78	88
China	36	82	28	45
Hong Kong	2	35	5	23
Indonesia	56	61	33	55
Japan	6	35	5	36
Malaysia	32	42	8	61
Philippines	48	76	48	95
Singapore	26	32	25	38
South Korea	57	69	63	88

Note: The higher the score, the lower is the degree of liberalization, or the higher is the degree of restriction. Maximum score is 100.

Source: Hardin and Holmes (1997).

The most important change in Thailand's financial liberalization before the 1997 financial crisis was the establishment of the Bangkok International Banking Facility (BIBF) in 1993. BIBF was an offshore financial market, which provided supportive tax and regulatory advantages aimed at fostering the development of Bangkok as a regional financial center. The establishment of BIBF was due mainly to two factors: (1) BIBF institutions were granted considerable tax advantages, and (2) many Thai firms which could not directly access overseas capital markets were able to borrow through BIBF. As a result, BIBF increased foreign borrowing; rapid credit growth resulted in high leverage economy-wide as well as an asset price bubble. This therefore led to a rapid increase in foreign exchange exposure and a shortening of the maturity structure, rendering the economy vulnerable to reversals in capital inflows and downturns in economic activity, which led to the 1997 financial crisis. Other liberalization measures adopted during the 1985–1996 period included subjecting non-resident Baht accounts at domestic commercial banks to lower reserve requirements and gradually eliminating restrictions on the purchase of foreign exchange by residents and on the transfer of the Baht overseas.

To survive after the 1997 crisis, the Thai government, especially under the control of BOT, has been implementing capital controls and financial resolution measures. For example, in 1998, BOT tightened regulations on loan classification, provisioning, and reporting standards, with the aim of upgrading local financial institutions. Thai authorities have implemented a number of financial-sector restructuring measures to restore financial stability and address structural weaknesses. The restructuring measures have been based on both market-driven and state-led mandatory approaches. Veerathai (2003) categorized the restructuring measures into (1) those intended to address financial institutions' insolvency and capital adequacy issues, and (2) those intended to address non-performing loans and distressed assets.¹

The recent financial crisis therefore clearly demonstrates the powerful influence of market forces and capital flow regulations across borders. The control of capital flows and exchange rates is therefore one of the main measurements of economic freedom of international exchange with foreigners in the area of capital markets. (More details about how the BOT regulates international capital market controls will be discussed in the next section.)

III. THAILAND'S ECONOMIC FREEDOM TO EXCHANGE WITH FOREIGNERS: BY CATEGORY

Thailand's economic freedom index under Area 4, i.e., economic freedom to exchange with foreigners, will be discussed under the following sub-sectors:²

- Taxes on international trade
- Regulatory trade barriers
- International capital market controls.

3.1. Taxes on International Trade

The *Economic Freedom of the World* reports that Thailand reached a rating of 6.7 in section A (Tariffs), which is high owing to the tax revenue on exports and imports. The reason that Thailand achieved 90 (Table 2) in this sub-section (Ai) is mainly because of the establishment of a number of free trade areas, especially AFTA, which is currently being implemented.³ Therefore, as a member of AFTA, Thailand should incur a significant perceived cost related to the potential loss in revenues from trade taxes associated with tariff reductions. Trade tax revenues normally constitute a significant share of total government revenue, but it is likely to fall.⁴ Nevertheless, it is believed that the reduction in tariffs over time will increase economic growth and thereafter stimulate imports. Therefore, less tariff revenue will be collected on each good imported; in the meantime, the increase in the volume of imports should mitigate the fall in revenue in the aggregate. In addition, the reduction in tariffs and other trade barriers is likely to reduce the incentive to engage in illegal cross-border trade, i.e., smuggling. Where the volume of illegal or informal cross-border trade is perceived to be low, smuggling may decline in response to a lowering of tariff barriers, after which the share of trade on which tariffs can be applied will increase. The revenue from international trade taxes therefore depends on (a) the size of tariff reduction, (b) the possible switch from an informal to a formal trading system, and (c) the growth in imports as a result of tariff cuts.

Table 5 provides evidence of the amount of revenue collected by Thailand's Ministry of Finance from 1996 to 2003. Taxation on international trade (import duties and export duties) has been decreasing during the periods from 15.5 percent of tax revenue in 1996 to 12.2 percent of tax revenue in 2003. This indicates a trend toward tariff reduction over time. Under preferential trade arrangements between Thailand and other countries, it may decrease further in the future. The economic freedom rating for this sub-sector was 6.7. Compared with historical data, the average tariff rates of Thailand and other Asian countries have been declining. Thailand's mean tariff was 32 percent in 1984 and it dropped to 20 percent in 1996.

The first reason for the downward drift in ASEAN tariffs is mainly due to the multilateral trade negotiations resulting in the GATT and WTO agreements. Negotiations began with the Uruguay Round, which aimed at making world trade freer and at reducing tariffs. The second reason is that the unilateral tariff reforms of AFTA have limited CEPT, which is even lower than the most-favored-nation (MFN) tariff rates, so that they are now low and uniform among member countries. Nevertheless, the reduction in tariff

Table 5 Thai Government's Taxation and Tariff Revenues

Source	1996	1997	1998	1999	2000	2001	2002	2003
(Million baht)								
Tax revenue :	781,772	757,440	686,338	625,353	689,632	694,482	785,574	902,579
<i>Taxes on income and profits :</i>	<i>281,779</i>	<i>276,367</i>	<i>213,435</i>	<i>205,007</i>	<i>243,493</i>	<i>254,089</i>	<i>286,019</i>	<i>346,608</i>
Personal	107,728	111,683	123,058	91,925	90,541	97,033	104,912	116,099
Corporate	170,428	159,717	85,114	101,941	142,097	140,088	162,415	208,211
Petroleum income tax	3,623	4,967	5,263	11,141	10,855	16,957	18,691	22,298
<i>Taxes on consumption</i>	<i>357,684</i>	<i>381,495</i>	<i>335,751</i>	<i>325,802</i>	<i>319,651</i>	<i>327,802</i>	<i>379,716</i>	<i>421,466</i>
Business tax	620	305	451	95	152	133	101	86
Value added tax	150,472	152,062	144,925	138,529	139,167	126,804	147,228	150,457
Specific business tax	32,856	33,879	31,467	19,193	15,015	13,143	12,960	12,727
Excise taxes	173,735	175,159	158,908	167,986	165,317	187,722	219,426	258,196
<i>Taxes on international trade</i>	<i>121,539</i>	<i>94,826</i>	<i>60,946</i>	<i>73,424</i>	<i>85,168</i>	<i>91,496</i>	<i>98,291</i>	<i>109,882</i>
Import duties	121,533	94,814	60,928	73,355	85,080	91,403	98,116	109,628
Export duties	6	12	18	68	88	93	175	214
Other taxes	20,770	24,752	16,262	21,121	21,319	21,075	21,549	24,663
Percentage of tax revenue								
Tax revenue :	1000	1000	1000	1000	1000	1000	1000	1000
<i>Taxes on income and profits :</i>	<i>36.0</i>	<i>36.5</i>	<i>34.1</i>	<i>32.8</i>	<i>36.4</i>	<i>36.6</i>	<i>36.4</i>	<i>38.4</i>
Personal	13.8	14.7	19.6	14.7	13.5	14.0	13.4	12.9
Corporate	21.8	21.1	13.6	16.3	21.2	20.2	20.7	23.1
Petroleum income tax	0.5	0.7	0.8	1.8	1.6	2.4	2.4	2.5
<i>Taxes on consumption</i>	<i>45.8</i>	<i>47.7</i>	<i>53.6</i>	<i>52.1</i>	<i>47.7</i>	<i>47.2</i>	<i>48.3</i>	<i>46.7</i>
Business tax	0.1	0.1	0.1	0.0	0.0	0.0	0.0	0.0
Value added tax	19.2	20.1	23.1	22.2	20.8	18.3	18.7	16.7
Specific business tax	4.2	4.5	5.0	3.1	2.2	1.9	1.6	1.4
Excise taxes	22.2	23.1	25.4	26.9	24.7	27.0	27.9	28.6
<i>Taxes on international trade</i>	<i>15.5</i>	<i>12.5</i>	<i>9.7</i>	<i>11.7</i>	<i>12.7</i>	<i>13.2</i>	<i>12.5</i>	<i>12.2</i>
Import duties	15.5	12.5	9.7	11.7	12.7	13.2	12.5	12.1
Export duties	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other taxes	2.7	3.3	2.6	3.4	3.2	3.0	2.7	2.7

Sources: 1) Comptroller-General's Department.
2) Bank of Thailand.

revenues has been absorbed by increases in other tax revenues collected on income and profit, and on consumption. The proportion of tax revenue collected as excise taxes has increased from 22.2 percent in 1996 to 28.6 percent in 2003. A high rate of excise tax is collected on particular items such as gasoline (increasing from 25 percent to 31 percent), beer (from 53 percent to 55 percent), and wine (from 55 percent to 60 percent). Such taxes are also collected on luxury items such as yachts and wool carpets (50 percent).

Even though Thailand's mean tariff rates have been declining as a result of various preferential trade arrangements, its mean tariff structures are still relatively high compared with that of other countries; for example, Thailand's MFN rate is about 16.1 percent for agricultural products and about 15.9 percent for manufactured products, or about 16.5 percent for all goods. The tariff mean however indicates that the tariffs that Thailand imposes are generally higher than the world standard, i.e., 12.6 percent for low-income countries, 11.6 percent for middle-income countries, 6.9 percent for high-income countries (not associated with OECD), and only 3.7 percent for high-income OECD countries.

Although there has been a general downward trend in Thailand's tariffs, there are still major sectors hiding behind high-tariff barriers aimed at protecting infant industries. Therefore, tariffs in Thailand vary widely among sectors because some attempt to protect particular sectors with high tariffs and others, to apply lower tariffs in sectors that are less sensitive to foreign trade. Agricultural products are on the list of politically sensitive commodities, which is why the negotiations regarding this sector are generally considered separately from industrial tariffs. Frankly, the import duties on agricultural and food products applied by Thailand are quite high, perhaps the highest in ASEAN. The automobile sector is another protected sector; the combined import duties and taxes that Thailand currently imposes are among the highest in ASEAN.

In general, Thailand has been trying to reform its tariff structure since the end of 1994. On some categories of goods, tariffs are around zero percent, e.g., for medical equipment and fertilizer; 1 percent for raw materials and electronic components; 5 percent for primary and capital goods such as machinery, tools, and computers; 10 percent for intermediate goods; 20 percent for instant-print film and certain finished products; and

30 percent for goods that need special protection. This is what we call a “tariff escalator.” The situation thus described obstructs the economic freedom rating by applying various tariffs or, what we call a high “standard deviation of tariffs.”

The standard deviation of the tariff rates measures the average deviation of the tariff rates around the mean; it is calculated using unweighted tariff data. Highly dispersed rates are evidence of discriminatory tariffs that may distort economic freedom with regard to residents’ production and consumption decisions. It can be stated that sectoral tariff structures remain escalated with the highest protection given to final goods. In this sub-sector, Thailand achieved only a 4.4 rating score, which seems to be quite a low degree of economic freedom with regard to the World Development Indicators, the standard deviation of Thailand during the period 1990-1993 was about 16.9, increasing to 17.8 in 1998. Therefore, it may be concluded that the degree of protection on Thailand’s domestic industries is relatively and highly varied compared with that of other countries; therefore, it remains a major obstacle for Thailand in its efforts to foster economic freedom.

3.2 Regulatory Trade Barriers

The hidden import barriers (considered as non-tariff barriers) comprise another obstacle lowering the degree of economic freedom in Thailand. Those hidden import barriers include the combined effect of import tariffs, license fees, bank fees, and the lag time required for administrative works and handling clearance, all of which raise the cost of the importing process. In this area, Thailand achieved a 7.3 rating for regulatory trade barriers divided into two sub-sections: the hidden import barriers, for which Thailand achieved a 5.8 rating and the cost of importing, for which Thailand achieved an 8.8 rating. Hence, the index of hidden import barriers indicates a lower degree of economic freedom within this category. Hidden import barriers included in the cost of importing are treated separately in the following paragraphs.

Import license barriers

Thailand is in the process of changing its import licensing procedures to comply with WTO regulations. Import licenses are required for a number of items such as raw materials, petroleum, industrial materials, textiles, pharmaceuticals, and agricultural products. The import of some items not requiring licenses must nonetheless comply with the applicable regulations of the agencies involved, including extra fees and certificate-of-origin requirements.

Customs barriers

We have to accept that Thai customs procedures are an impediment to international trade and investment inflow. Thailand’s Customs Department has quite a high degree of autonomy, so its import regulations are

complicated, not very transparent, and inconsistently applied. The problems include excessive paperwork and formalities.

Standards, testing, and labeling barriers

In general, the importation of food, and pharmaceutical products and medical devices must meet certain standards and pass testing and labeling requirements as well as be granted certification permits from the Thailand Food and Drug Administration (TFDA). The testing procedures generate costs with regard to their duration and complexity. Food import licenses must be renewed every three years and pharmaceutical import licenses must be renewed every year, with additional payment for the fees applied. Moreover, labels bearing the product’s name, description, net weight or volume, and expiration dates must be printed in Thai and approved by TFDA. These requirements are basically for consumer safety.

Financial services barriers

Different criteria apply to the bank fees for supporting international trade. With regarding to information from the Export-Import Bank of Thailand (EXIM Bank), the minimum fee for issuing a letter of credit (L/C) for imports is 1,000 baht; the fee for amending an L/C is 500 baht; the charge for Swift/Telex is 800 baht per message, while the fee for amending such a message is 300 baht. Thailand’s banking fees are considered reasonable; they are under the strict exchange control of the BOT. The fees also include delivery and charges, import bills for collection, and outward remittance services. (Financial service barriers are considered in more detail under the topic of international capital market controls, which will be discussed in section 3.3)

In summary, the level of economic freedom in Thailand under the sub-sector of regulatory trade barriers (either hidden import barriers or cost of importing) shows the unavoidable regulatory agenda of countries, especially in terms of barriers such as standards, testing, and labeling for sensitive products related to human life such as food and pharmaceuticals. However, the hidden costs under customs procedures and governmental administration need to be improved by enhancing services for supporting international exchange abilities in Thailand and among other partner countries. Nevertheless, the overall economic freedom rating of 7.7 under Area 4 may still be considered acceptable compared with that of other countries in Asia.

3.3 International Capital Market Controls

International capital market controls can be categorized in two ways: (1) according to how citizens are able to access foreign capital markets and foreigners are able to access domestic capital markets and (2) the restrictions that exist on the freedom of citizens to engage in capital market exchange with foreigners.

Thailand achieved a rating of only 43 in this regard. Its worst rating was 15, which refers to the restrictions on the freedom that Thai people enjoy to engage in capital market exchange. Under capital control conditions, BOT began to regulate both the inflows and outflows of capital.

The restrictions on and exemptions from foreign exchange control regulations in Thailand are very tight in order to meet the requirements of the Exchange Control Act of 1992. Under the Act, Thailand regulates the manner in which money flows into, or is taken out of, the country. Based on BOT information, the foreign exchange control system encompasses the following rules:

1. All trade transactions are free of restrictions although the proceeds of exports in excess of 500,000 baht must be deposited with an authorized bank within 15 days of receipt.
2. There are no restrictions on foreign borrowing and capital investments.
3. Repatriation of investment funds, dividends and profits as well as loan repayments and interest payments, net of taxes, may be made freely.
4. Direct foreign investment by residents, or lending to affiliate companies abroad, of more than US\$ 5 million a year requires the approval of BOT.
5. Payments for service fees related to foreign trade, educational expenses or family allowances abroad may be made freely.
6. Banks in Thailand may offer foreign currency accounts to individuals and companies with a total outstanding balance for all accounts of US\$ 500,000 and US\$ 5 million respectively.
7. No more than 50,000 baht (100,000 baht for bordering countries) in cash may be taken out of Thailand.

Export transactions

In general, there are few exchange control restrictions on export transactions. With certain exceptions, exporters are required to obtain a certificate of exportation from an authorized bank, in order to authorize the Customs Department to clear the goods for export. The proceeds from exports must be collected and brought into the country immediately after payment is received and within 120 days from the date of the export.

Transactions on invisibles

All receipts from invisibles must be surrendered to an authorized bank or deposited in a foreign currency account with an authorized bank within 15 days of the date of receipt. Payments for invisibles, such as services related to foreign trade, educational purposes or family allowances abroad, can be made freely. For travel

expenses abroad, a resident can take out foreign currency without limit.

Bank facilities

The EXIM Bank is a financial institution wholly owned by the Royal Thai Government under the supervision of the Ministry of Finance. It is empowered to engage in various business undertakings and offers the facilities of short-term and long-term credits in domestic or overseas markets for which the Bank can borrow from local or overseas financial institutions.

Borrowing

There are no restrictions related to the borrowing by residents from commercial banks in Thailand; however, non-residents may freely borrow either directly or through FX Swap transactions in local currency from commercial banks to finance their underlying activities. Without underlying activities, non-resident borrowing in local currency is limited to a maximum of 50 million baht per person. Private companies may provide lending to affiliated companies abroad if they hold at least a 25 percent share in them.

Foreign and local currency

Persons living in Thailand are permitted to use foreign exchange that originates from abroad to service their external obligations. Any person receiving foreign currencies is required to sell or deposit such foreign currencies with an authorized agent within seven days from the date of receipt. In terms of local currency, there is no restriction on the amount of Thai currency that may be brought into the country. A person traveling to countries bordering Thailand and to other countries may take out local currency up to an amount permitted by current regulations.

Investment in securities abroad

Residents can invest in securities abroad as institutional investors: through life insurance companies, government pension fund, social security fund, mutual funds, provident funds, and specialized financial institutions. The securities must be issued prior to January 1, 2003 by the Thai government, or corporate and sovereign debt securities issued by non-residents with an international credit rating but limited to a total of US\$ 500. Recent demands for investment in foreign debt securities have been high, with application from a total of 105 financial institutions.

Holding shares in overseas companies

Prior approval is required in many cases in order to invest or lend abroad, but prior approval is not required in order to invest money in Thailand. Foreign investments in Thailand, which receive promotional

privileges from the Board of Investment, are accorded various incentives and special benefits. Repatriation of investment funds, dividends and profits as well as loan repayments and interest payments thereon may be made freely after settlement of all applicable taxes in Thailand.

However, with greater liberalization in the global context, international capital controls and exchange rate controls have been eased. The Bank of Thailand (2003) announced that it would ameliorate the rules on holding foreign currency deposits that previously allowed for an obligation to become due in three months; instead they would be due in six months. Moreover, it allowed Thailand's state enterprises to freely hedge Thai foreign currency debts regardless of maturity; previously, they could hedge for only up to one year.

Thai residents are also allowed to issue structured products, which link return to foreign variables such as exchange rates and foreign assets. However, such products can be sold only to institutional investors under specified conditions. The last and most recent measure to alleviate international capital controls was the establishment of mutual funds for individual investors to invest in the "Asian Bond." This idea will be further pursued by BOT to assess the demand for and the amount of funding. Therefore, capital controls on international movements are currently being relaxed, which should help to increase the degree of economic freedom under this category.

IV. CONCLUSION

This paper is aimed at providing a comparison of the Economic Freedom Indices reported in the current *Economic Freedom of the World* Annual Report under Area 4: Freedom to exchange with foreigners, with reference to Thailand. In this paper, three sections of Area 4 are analyzed and preliminary and supportive evidence of Thai policies provided as they relate to international exchange/trade among Thai residents and foreigners.

ENDNOTES

¹ By estimation, the total public costs of Thailand's financial-sector restructuring are in the range of

approximately 30-40 percent of GDP, which may raise serious concerns over the sustainability of the long-term public debt.

- ² The paper omits two sub-sectors: (1) the actual size of the trade sector compared with expected size, and (2) the difference between the official exchange rate and black market rate, for which Thailand achieved a rating score of 10.
- ³ The decision to establish AFTA was taken at the Summit Meeting of the ASEAN Heads of State in January 1992. The six original signatory countries (known as ASEAN-6) agreed to a deadline of 2008 for reducing Common Effective Preferential Tariff (CEPT) rates to 0-5 percent. In addition, they also agreed that each ASEAN-6 country would have a minimum of 85 percent of its tariff line in the Inclusion List, with a tariff of 0-5 percent by 2000; this should be increased to a minimum of 90 percent of the Inclusion List by 2001.
- ⁴ It is still uncertain whether the fall in tariff revenues will be a result of the implementation of AFTA, because other major factors, such as the economic situation and imported values, could be the cause.

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