

# CHAPTER 1

## 1. Introduction

In the age of globalization where one country economy integrates with another country's economy causes the stipulation and bestow of the foreign currencies involvement. It exhibits the transaction between both economies in terms of foreign exchange currencies with the help of major parties such as central banks, commercial banks, hedgers and speculators (Argy, 2010).

Presently, the exchange rate between Thai Baht against other currencies are a total of 48 local currencies up from 35 currencies from April 2008 onwards (Source: The Average Exchange rate of the Commercial Banks in Bangkok Year 2003 - present: The Bank of Thailand, 2015).

This study aims to study the influence of the critical factors to the exchange rate of Thai Baht currency against US dollar. The foreign exchange brings many issues along within from the international trade perspective and it can create a negative impact on the functioning of the country such as the adverse impact on the wages, fluctuation in interest rates, declining employment opportunities, sickening production levels. This explains that the understanding of the market efficiency of currency is utmost important in order to understand that the behaviour study of exchange rates is highly important especially when two countries are dealing with each other (Saeed et al., 2012).

The study of the market efficiency of currencies enables to identify the global value of country's position in the field of international trade by measuring imports and exports, international reserves, government debts, the balance of trade and terms of trade. When there is a shift in exchange rate or imbalance in any country international trade can influence the currency to appreciate or depreciate (Zwanzger, 2008). The aim of this paper is to investigate the previous

five years interrelation trade relation between Thailand and United States of America and their currency movement's trends to inference the Valence of Thai Baht and US dollar. There are various other researchers (Salikupod and Khongsawatkiat, 2013) who have worked in order to deduce the international trade relations and exchange rate movements based real and nominal interest rate, money supply, international reserves, interbank transfer, inflation rate, current bank account.

In 1997, Thailand has changed its foreign exchange mechanism from fixed exchange rate to floating or managed exchange rate and allowed other currency to fluctuate in accordance. This change had brought vastly change in foreign exchange rate between US dollar and Thai baht

This paper will elucidate the different models which can be used to assess the currency movement in order to understand the market efficiency of Thai Baht and US dollar based on the last seven years (from 2010 to 2017) and also the study of the international trade relations between both the countries. The main study of this paper will be macroeconomic indicators and the indicators that are going to be studied in this paper are terms of trade, interest rates, manufacturing production index and international reserves of both countries. Moreover, these indicators will be justified by Vroom's valence model.

### **1.1. Rationale of the study**

The primary basis for doing this study is to analyse the movement and valence of currency trade between Thai baht and US dollar from international trade outlook. It also analyses the factors associated with the international trade over the last seven years. Moreover, this study focusses on the change in currency movement between both these countries because of the change in terms of trade, interest rates, manufacturing production index and international reserves. This study constitutes the positive and negative valence of both these currencies with the help of detail study of the above macroeconomic indicators. This study needs to be done in order to safeguard the investors to see and check

which currency pairs are correct enough to be invested in the future. Furthermore, this study is also very important for one country to understand about its economic growth so the cause for this study is to know about Thailand and US exporters & importers and economy situation previously and with that available information to forecast in the future (Baneda, 2009).

## 1.2. Purpose of the study

This topic will encounter the issues are associated with currency trading and exchange market. It will give the investors of Thailand who are exporting or importing trading goods and services from the USA to know the valence of Thai baht in comparison with US dollars for the future trading references and vice versa. This study will analyse the previous seven years international trade transaction between both countries and provide the detail investigation of macroeconomic indicators of Thailand economy with USA economy. This study will identify the movement of the exchange rate between US dollars and Thai baht and it will also pinpoint the causes of movement along with the current scenario (Bodnar and Gentry 2010).

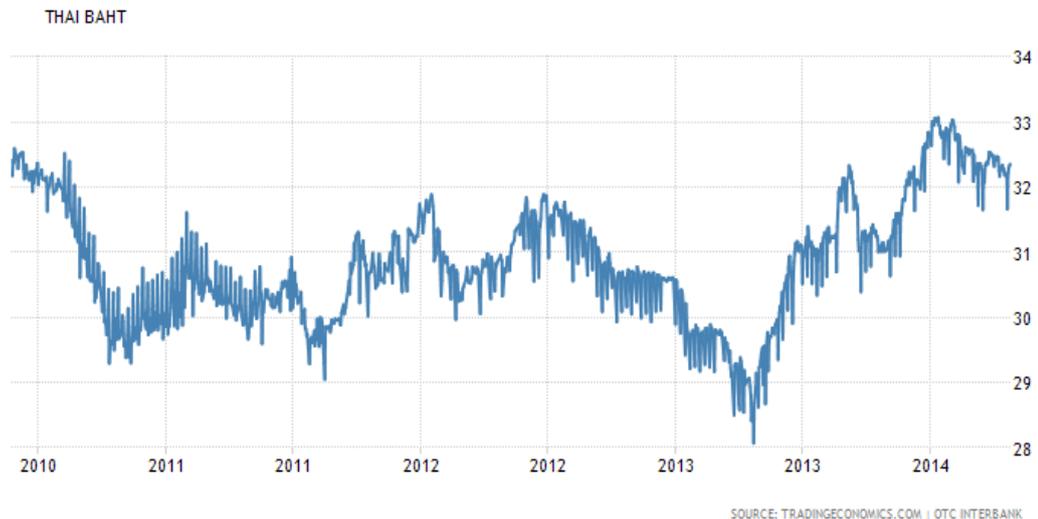
## 1.3. Background of the topic

Thailand had adopted a fixed exchange rate system and it lasted until 2<sup>nd</sup> July 1997, when Thailand transited from fixed to floating exchange rate system. The main intention of this to Thai baht move freely and steadily with other currencies. The below table shows the historical date of US dollar exchange rate with Thai baht from the period of July 1998 to July 2002. It shows that after the inception of managed exchange rate system Thai baht was getting weaker as it had touched more than 55 against one dollar and later gradually had started to decline and scaled a level of 35 to 37 baht against on dollar and in this scenario Thai baht was getting stronger. It also explains a very important factor is that when Thailand economy was getting stronger and better the exchange ratio with US dollar was getting stronger and better as well. Furthermore, this also explains

the policy regarding the exchange rate is very vital to maintain economic firmness.



**Figure: Thai baht exchange rate with US dollar from July 1998 to July 2002**



**Figure: Thai baht exchange rate with US dollar from 2010 to 2014**

The above chart explains the Thai baht exchange rate with US dollars from the period 2010 to second half of 2014 and it shows that in 2013 the Thai baht traded for 1 US dollar was in 28-30 which advocates that Thai baht was the strongest in 10-15 years and it reflects that economics situations were better as well. In early 2013 it had started to decline gradually and then skyrocketed up to more than 3baht against one US dollar.



**Figure: Thai/US exchange rate**

The chart indicates the exchange rate between Thai baht and US dollars from the year ending 2014 to 2017. It shows that in early 2014 to 2015 it was in the range of 32-35 baht against one dollar and then it has crossed more than 36 baht in late 2015 and early 2016. During this period Thai baht was the weakest in a long time and economic situation was on turmoil stage. The exchange rate from the period 2016 to 2017 was stable between in the range of 34-36 Thai baht against one dollar and from 2017 onwards it has started to become stronger gradually as from the table its evident that it has moved from 36 to 32 baht against one dollar.

#### 1.4. Research aim and objectives

The main aim of this research paper is to understand the macroeconomic factors (terms of trade, interest rates, manufacturing production index, international reserves) which affected the valence of Thai baht trading with US dollar in international trade between both countries during the period of 2010 to 2017. This study will provide an overview of interrelated trade between Thailand and U.S.A and how their trade decision affecting the attractiveness of Thai baht and USD. This overview understanding will also provide an opportunity to analyse the issues faced by the Thailand Exporters and Importer using macroeconomic indicators. The aim of this study can be achieved only through

mounting with objectives and that can achieve with detail study of this topic. This brings the following objectives considering the subject and its issues from 2010 to 2017.

- ❖ To probe the international trade relation between Thailand and the USA.
- ❖ To explain the macroeconomic factors such as terms of trade, interest rates, manufacturing production index, international reserves of both countries.
- ❖ To pinpoint the macroeconomic factors that impact the valence of the Thai baht.
- ❖ To pinpoint the macroeconomic factors that impact the valence of US dollar.

### 1.5. Research questions

- ❖ Discuss the international trade relations and the activities between Thailand and USA from 2010 to 2017.
- ❖ Discuss the terms of trade, interest rates, manufacturing production index and international reserves of both countries from 2010 to 2017.
- ❖ Discuss and analyse the factors that impact the valence of the Thai baht.
- ❖ Discuss and analyse that factors that impact the valence of the US dollar.
- ❖ Discuss the recommendations and conclusions for the international trade relation parties.