

Buffeting by the Unholy Trinity

Thailand's Military Coups

Bhanupong

Lecture 7

Asian Economic Papers 5(2), 2006

The Thai Economy after the 2006 coup

Syllabus

Lecture 7

- We discuss the consequences of the Avian Influenza, the 2005 Asian tsunami, and the oil price shock in 2005.
- We examine the impact of the 2006 military coup
- A shift in fiscal spending pattern took place after the coup. In 2007, Thai economy grew at the lowest pace among countries in the region.
- How have the coups changed the Thai economy?

Readings

Lecture 7

- “The Thai economy after the coup,” in John Funston (ed.) *Divided over Thaksin*, Institute of Southeast Asian Studies. 2009
- “The buffeting of Thailand by the unholy trinity of Avian Influenza, tsunami, and the oil price shock” *Asian Economic Papers*, Vol. 5, no.2, 2006.

Key words

- The Avian Influenza
- The 2005 Asian tsunami
- The oil price shock in 2005
- The 2006 military coup
- Tanks versus hospitals
- The latest coup: May 2014

Bird flu (2004), Tsunami (2005), the 2005 oil shock

Buffeting of Thailand

Table 1. Estimates of the economic costs of the three shocks

	Crisis year	GDP growth (percent)	Financial loss (billion baht)	Loss of life
Avian influenza	2004	-0.1	20	14
Tsunami	2005	-0.3	65	5,400
Oil shock	2005	-2.0	90	

Sources: Estimates are from the Ministry of Finance, the Bank of Thailand, and the Tourism Authority of Thailand.

Massive Culling



Bird flu

Avian influenza (AI) broke out in Thailand in December 2003 and killed 14 people in the following 12 months.

The Thai poultry industry had just recovered from the loss of Generalized System of Preferences (GSP) status in Europe in 1999

And the import ban on Thai chicken in 2002, due to the detection of antibiotic residues (Nitrofurans).

The damage from the bird flu

The spread of bird flu (AI) caused heavy damage to the industry because of massive culling and a temporary decline in domestic consumption.

The fear subsided by October 2004, and domestic chicken consumption returned to its rising trend.

The Ministry of Finance estimated that AI reduced GDP growth by 0.1 percentage points in 2004

Why so little impact?

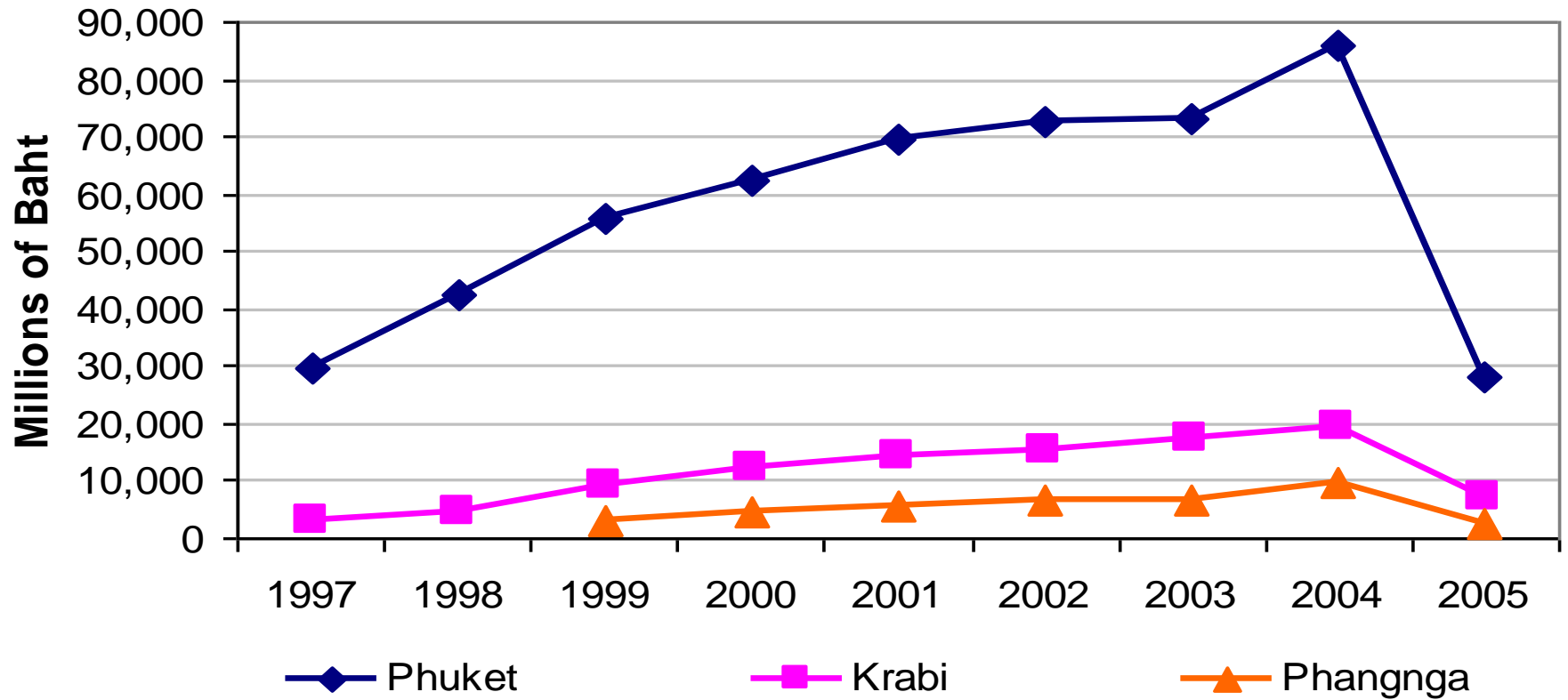
December 26, 2004



The Asian Tsunami

- AI has caused less damage in Thailand than the tsunami that hit six southern provinces of Thailand on December 26, 2004, killing 5,394 people—half of them foreign visitors.
- The tourism industry was badly affected, in particular, the hotel business on the Andaman Coast. Fisheries were also affected by the tsunami, as a result of the destruction of fishing boats and shrimp farms.
- Estimates show that the tsunami reduced GDP growth in 2005 by 0.3 percentage points

Tourism Revenue from Visitors in Three Provinces

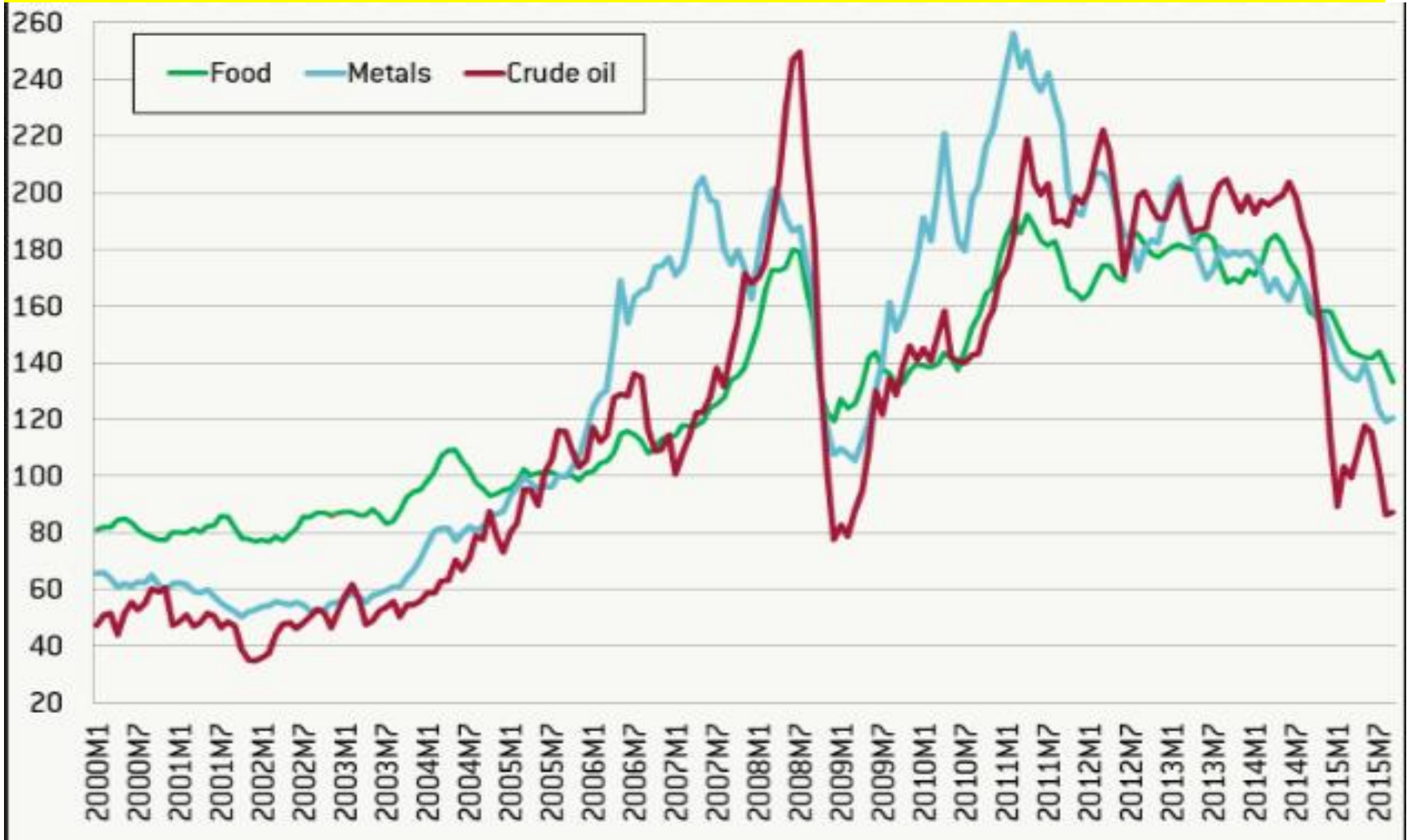


Source: Tourism Authority of Thailand

Shocks after shocks

- World recession 1991
- Asian financial crisis 1997
- SARS and Iraq war in 2003
- Avian flu (H5N1) 2004
- Tsunami (Dec 26, 2004)
- Coup d'état (Sep 19, 2006)

The oil shock in 2005



The oil price shock

- The oil price shock of 2005 did not lead to loss of life, but its impact on economic growth in Thailand was the greatest among the three unholy trinity shocks.
- It caused a decline of 2 percentage points in the GDP growth of 2005.
- The oil fund deficit caused by an existing oil price subsidy carried **a fiscal cost** of more than 90 billion baht.
- *(Was it worth the subsidies: Okun Gap vs. Harberger's Triangles)*
- The oil price shock had an adverse direct impact on the tourism industry by raising the cost of traveling.
- The slowdown in world output growth aggravated the slump in the industry

Among the three oil price shocks

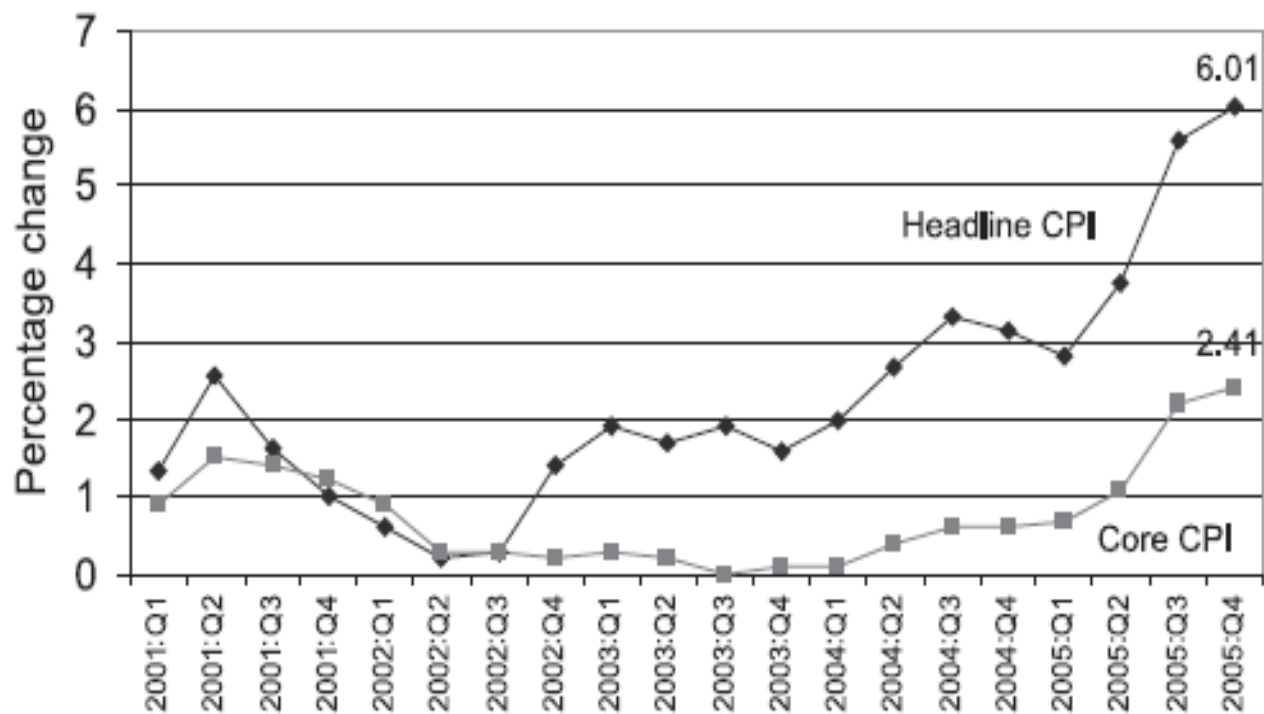
Table 2. Macroeconomic impact of the three oil price shocks (percent)

	First oil shock		Second oil shock			Third oil shock	
	1973	1974	1978	1979	1980	2004	2005
GDP growth	9.9	4.4	10.4	5.3	4.8	6.1	4.5
Inflation	15.5	24.3	7.9	9.9	19.7	2.7	4.5
Current account/GDP	-0.5	-0.6	-2.8	-4.9	-6.4	4.5	-4.8
Trade balance/GDP	-1.7	-2.4	-3.1	-4.4	-6.1	2.3	-2.1
World oil price index	3.3	11.6	12.9	30.1	35.9	37.7	54.2

Sources: Bank of Thailand, International Monetary Fund.

Core vs. headline inflation

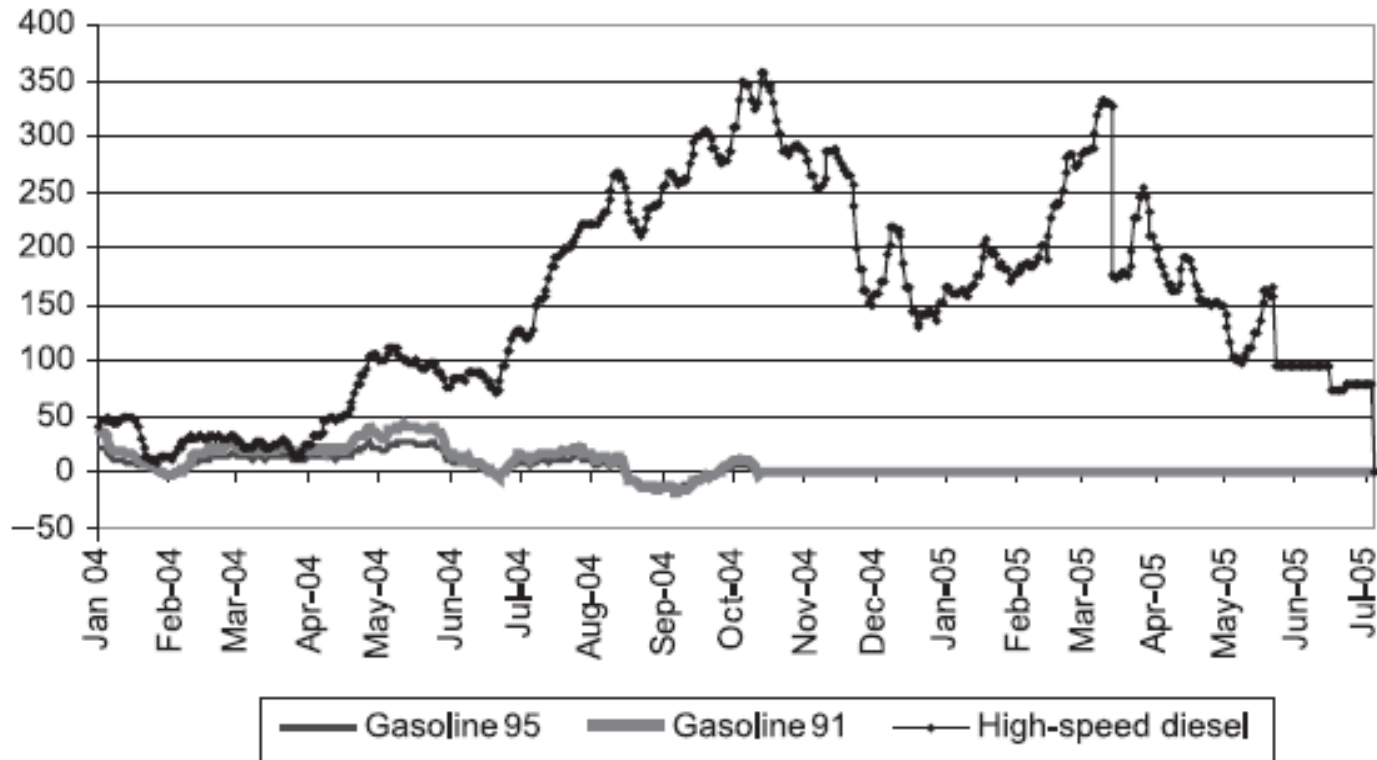
Figure 4. Inflationary impact of the third oil price shock



Source: Bank of Thailand.

Diesel vs. gasoline subsidies

Figure 5. Oil subsidies per day (million baht)

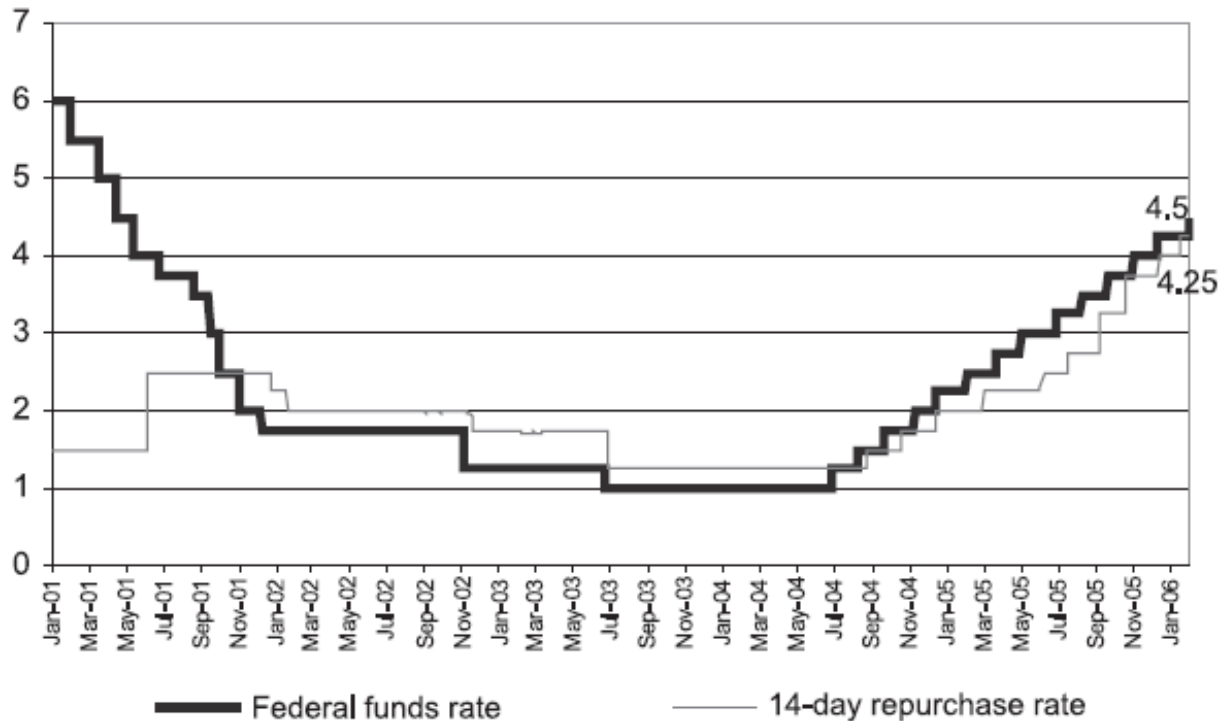


Source: Energy Policy and Planning Office.

Still subsidize energy until these days?

Gradual approach to interest rate adjustments: Follow the Fed

Figure 6. Federal funds and repurchase rates



Sources: Bank of Thailand, Federal Reserve.

Appropriate policy responses to shocks

The establishment of realistic exchange rates and positive real interest rates by reducing the degree of price intervention will induce economic agents to adjust properly to cushion the impact of external shocks.

Nominal exchange rates must be allowed to depreciate to maintain competitiveness.

Price controls must be employed *temporarily* to avoid market disruptions and to calm inflationary expectations.

More Shocks (still counting)

- Bangkok bombing (Jan 2007)
- Global (Great) recession (2009)
- Type-A(H1N1) (2009)
- Red shirts (UDD) uprising (April 2009, March 2010, April and May 2010)
- Japan quake (March 2011)
- 2013 Bangkok shutdown
- 2014: Military Coup
- 2015: Erawan shrine bombing

PAD uprising and airport shutdowns (2008)



Thailand's main international airport cancelled all flights on Wednesday (November 26, 2008) as thousands of protesters swarmed the complex in efforts to bring down the government, stranding tourists and dealing a blow to the country's already-fragile tourism industry.

Bangkok airport under siege, thousands stranded

Nov 26 2008,



The airport takeover was one of the boldest gambles yet by the People's Alliance for Democracy in its four-month campaign to topple Prime Minister Somchai Wongsawat, whom it accuses of being the puppet of a disgraced fugitive predecessor, billionaire Thaksin Shinawatra.

The Thai economy after the coup: 2006-2008

- Coups d'état and the vicious cycle
- The importance of capital formation
- Animal spirits of investors

Coups galore

- There have been 20 military coups since June 24, 1932, when absolute monarchy was replaced by constitutional monarchy.
- Only ten coups succeeded.
- June 20, 1933: Phraya Phahol toppled the government led by Phraya Manopakorn.
- Nov 8, 1947: Gen Pin Choonhawan overthrew the government of Thawan Thamsrongdhnawasavad

Timeline of coups d'état

The 1958 Coup

General Plaek regime (1948-58) was overthrown by
General Sarit (1959-63)
General Thanom (1964-1974)

1971 Coup (Nov 17) by Field Marshal Thamom against
his own government.

Another coup, another constitution, and another election

Oct 14, 1973

PM Sanya (1974)

PM Kukrit (1975)

Oct 6, 1976 PM Thanin

Coup 1977 (October 20) by Adm Sa-ngad Chaloyu
overthrew the government of Thanin Kraivichien

General Kriangsak, General Prem 1981,

Coup 1981,

Coup 1985

PM Chatchai **Coup 1991**

A vicious cycle

And we thought that we had seen the last coup in 1991

Between 1991 and 2005, the absence of coup provided stable environment and economic prosperity under five PMs:

Anan, Chuan, Banharn, Chawalit, Chuan, and Thaksin

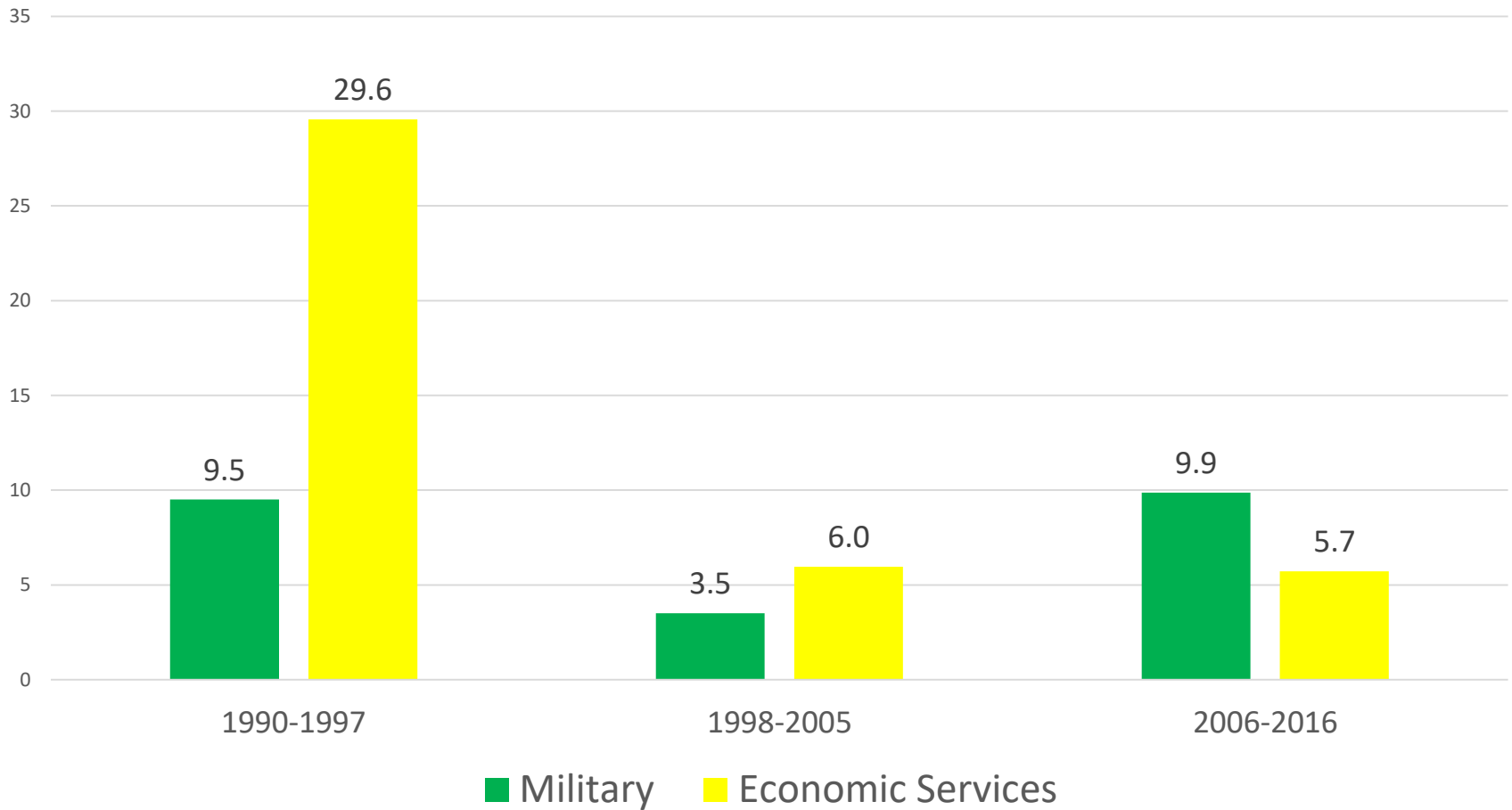
Then came 2006 coup to topple down PM Thaksin: General Surayud

Fiscal budget under the military-backed government (General Surayud: The coup leader in 2006)

	FY 2007	FY 2008	% Change in value
Defense	7.3	8.6	17.8
Education	18.0	18.1	0.56
Public health	4.0	3.9	-2.56
Central fund	12.6	14.8	17.4
Agriculture	4.1	3.9	-4.88
Total amount (billon baht)	1566.0	1660.0	6.0

Defense budget expanded
public health and agriculture contracted

Fiscal expenditures (annual percentage change)



Grossman, Michael (1972)

*“On the concept of **health capital** and the demand for health”*

Journal of Political Economy

- Health can be viewed as a durable capital stock that produces an output of healthy time.
- Individual inherit an initial stock of health that depreciates with age and can be increased by investment.
- The “shadow price” of health depends the price of medical care, rising with age if the rate of depreciation rises over the life cycle and falls with **education** if more educated people are more efficient producers of health.

Thailand's perennial problems

- Weak governing institutions: Absence of the rule of law
- Military and judicial coups threat and political disturbances
- Fluctuations of world business cycle
- The southern violence

Capital formation

- Investment causes short-term fluctuations in GDP by affecting aggregate demand.
- Investment also enhances long-term growth by increasing potential, or full-employment national income.
- Investment improves living standards.
- Opportunity cost of growth is precious heritage of natural resources and pollution.

Why growth is good for the poor

- Growth increases the ability to redistribute income among people and reduce unemployment.

- Okun's Law

$$g_t = \alpha - \beta \Delta u_t$$

- For every 1% of increase in unemployment rate, GDP will be lower by roughly 2% (In USA).

Animal spirits

- Akerlof and Shiller (2009) extend Keynes' animal spirits from investor confidence to fear, blind faith, corruption, and a concern to fairness, and the stories we tell ourselves about our economic fortunes.
- These are the factors which adversely affect investment
- *We must uphold fairness and social justice: no more double standards*

Foundation of long-term growth

- Institutions are quality of formal and informal sociopolitical arrangement—from legal system to political institutions.
- Good institutions provide property rights, appropriate regulatory structures, the quality and independence of the judiciary and bureaucratic capacity.
- Institutions that provide dependable property rights, manage conflict, maintain law and order, and align economic incentives with social costs and benefits are the foundation of long-term growth.

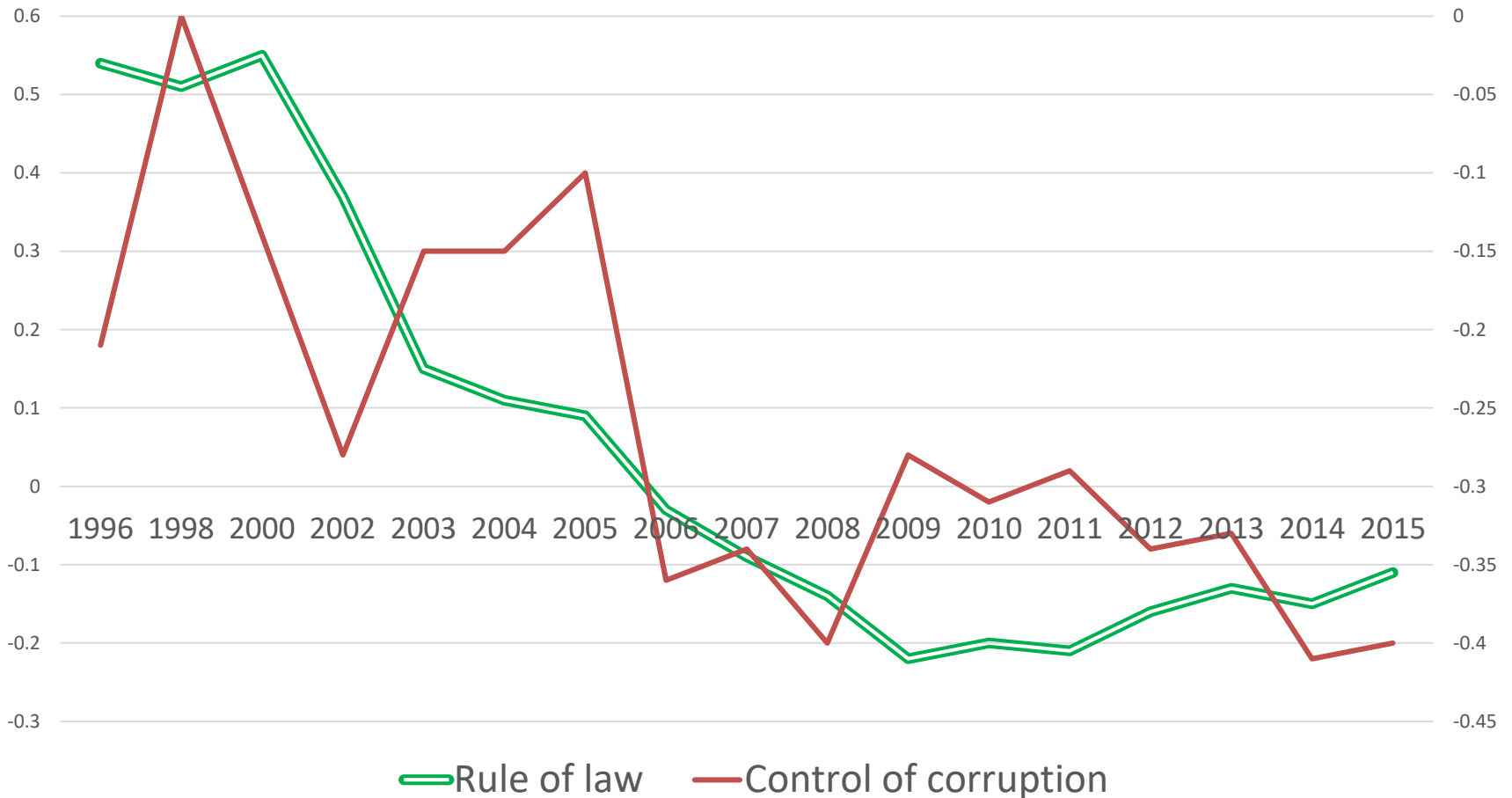
The coup and the abandoning rule of law

- The overthrow of the legitimate government by the military coup cost considerable damages in terms of economic losses.
- **The rule of law**, good governance and good institutions, both legal and democratic infrastructure are required to nurture economic environment suitable for long-term development to raise living standards.

Deteriorating rule of law

losing corruption control

Source: Worldwide Governance Indicators



Past coups were different from the two recent coups

- In Thailand, the military coups in the past did not destroy the confidence of the business sectors; thereby leaving intact the country's economic strength.
- The coup in 2006 , however, had destroyed the democratic underpinning of the stability of political and economic structure; thereby sapping the economic strength of the economy.

The Thai Economy after the 2006 coup

- The long-term growth and social welfare is threatened as the government budget is allocated to non-productive spending. Infrastructure public investment and human capital-related spending was curtailed for the sake of defense.
- The Thai economy has stepped backward, losing opportunity to grow when the world economy expanded in 2007.
- Alas, the September 2006 was not the last one.

**SHUT
DOWN
BANGKOK**

REFORM BEFORE ELECTION

13 JANUARY 2014

**FIGHT FOR
THE SAKE OF
THAILAND**

Thailand's Coup Just One Sign of Southeast Asia's Regression From Democracy



Demonstrators march as riot police officers and soldiers block a street during a protest against military rule in central Bangkok on May 24, 2014. Former prime minister Yingluck Shinawatra was in a "safe place" on Saturday, an aide said, after being held by Thailand's army following its seizure of power this week, as opposition to the coup grew among her supporters and pro-democracy activists (Athit Perawongmetha/Courtesy: Reuters).

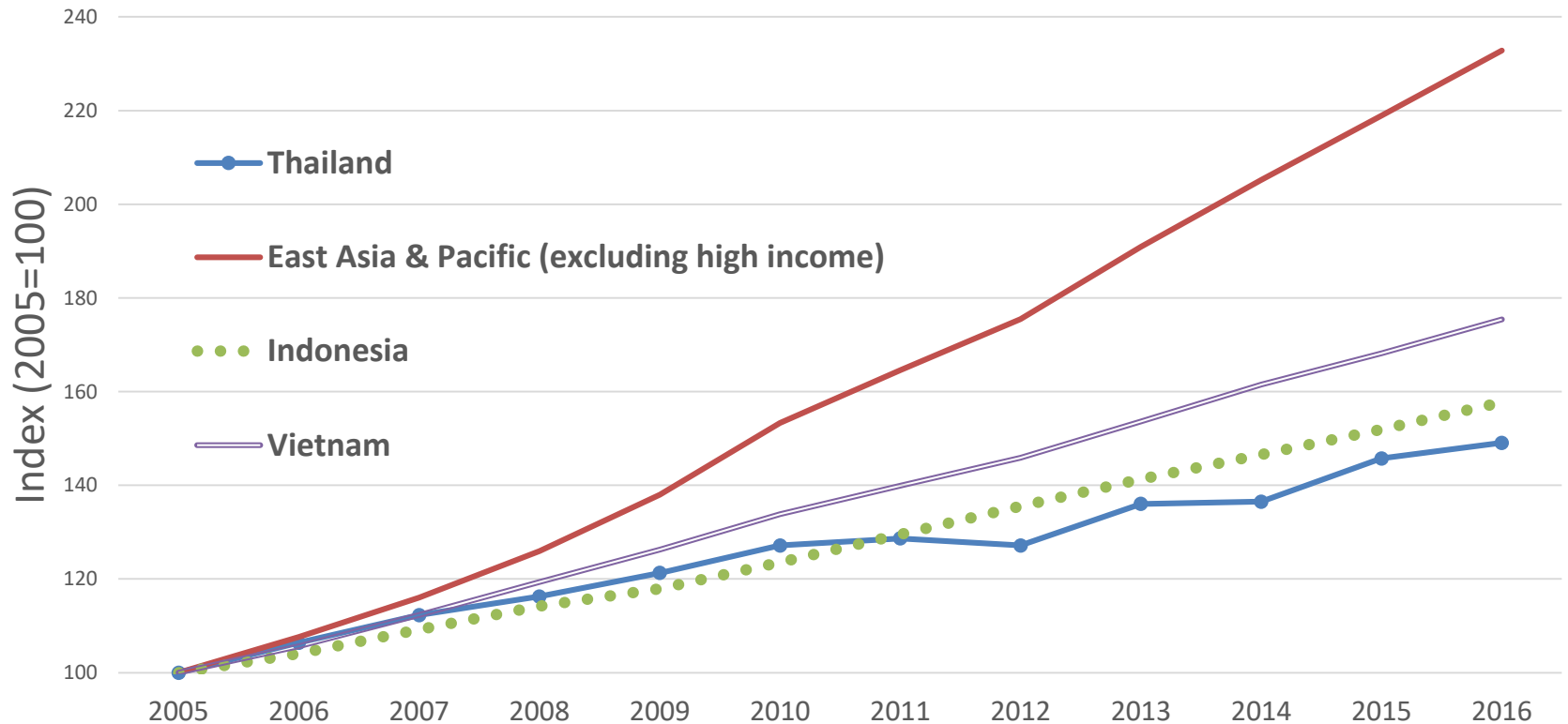
The 2014 military coup

- Thailand's economy was already struggling before the country's military seized power in a bloodless coup on 24 May 2014, saying it needed to restore order after six months of protests aimed at ousting the elected government.
- The military takeover, the second since 2006, could ensure stability in the short term.

More challenges for economy after the coup

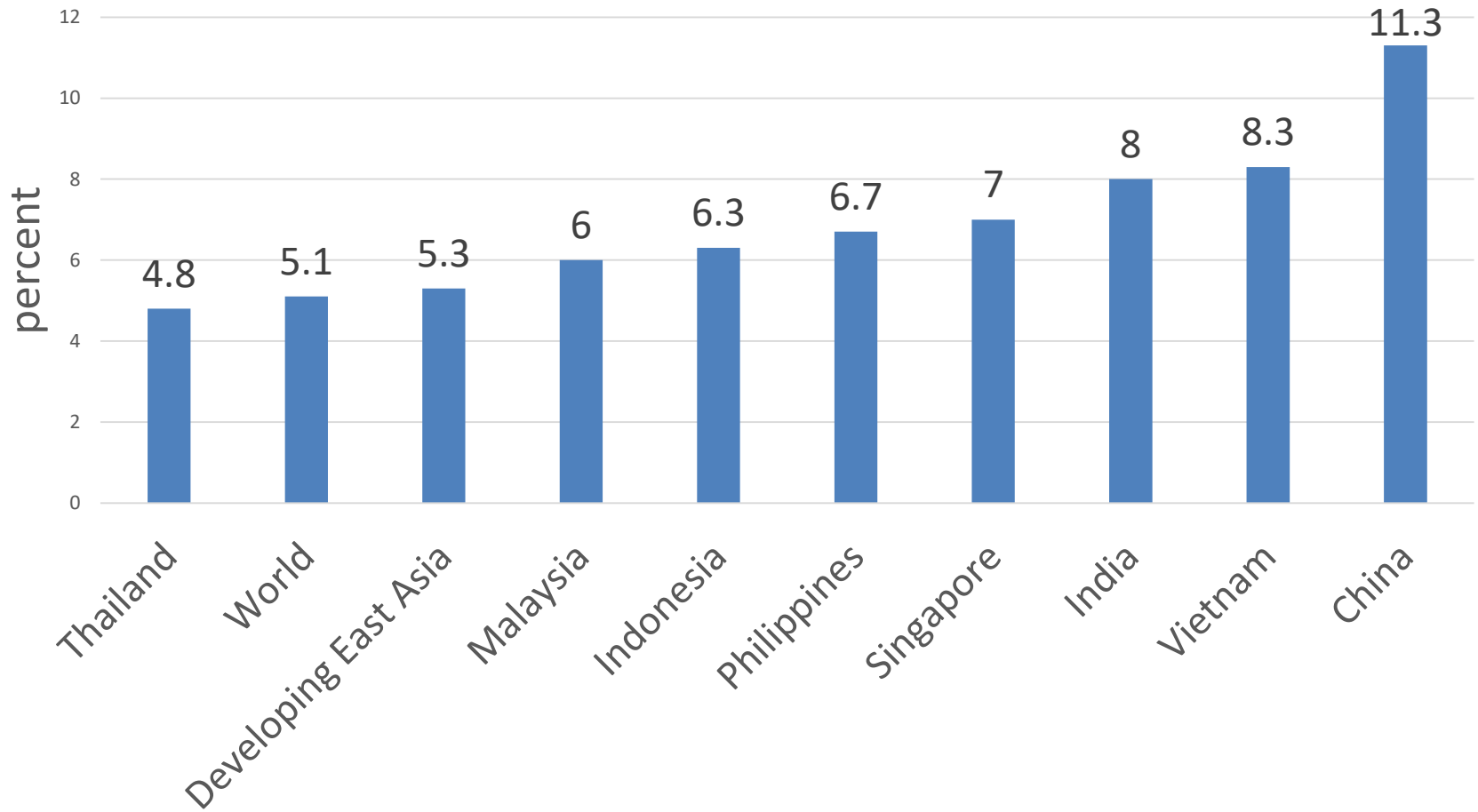
- But analysts fear the army's intervention will result in Thailand's political divide becoming even sharper, holding back the economy and living standards in the longer run.

GDP per capita (PPP constant 2011 \$)

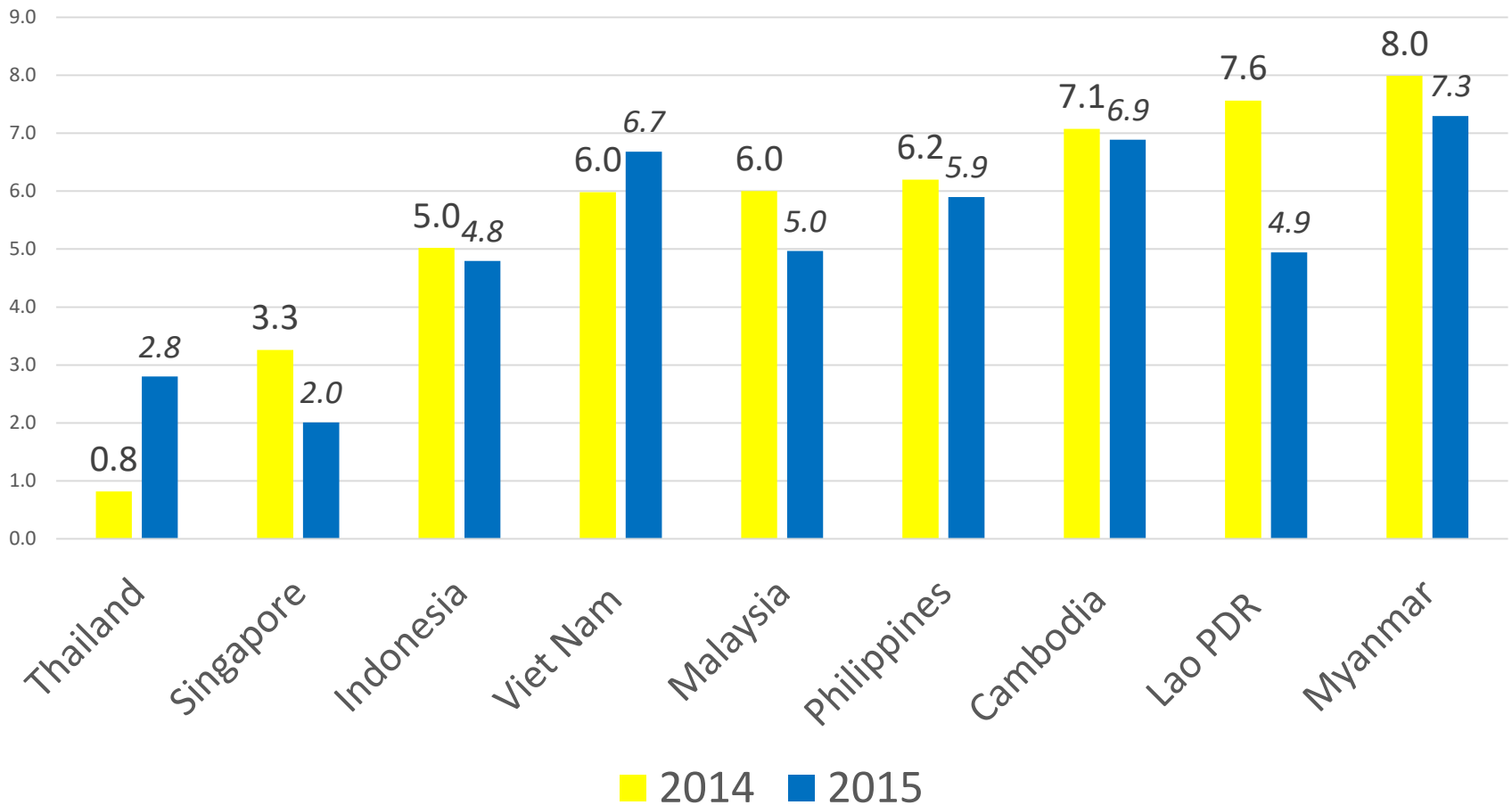


Comparison of 2007 GDP growth

After the November 2006 coup

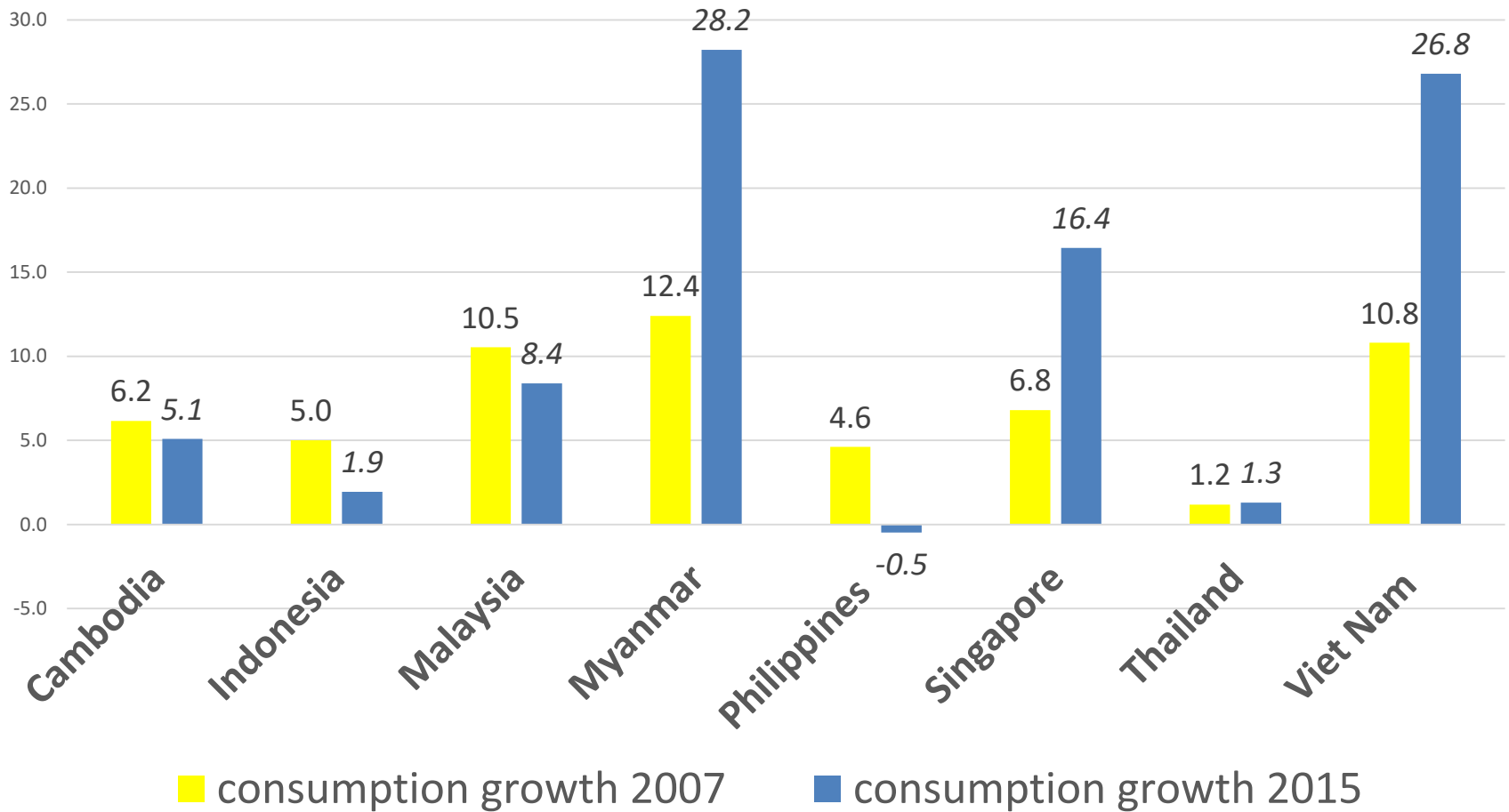


Comparison of ASEAN growth After the May 2014 coup

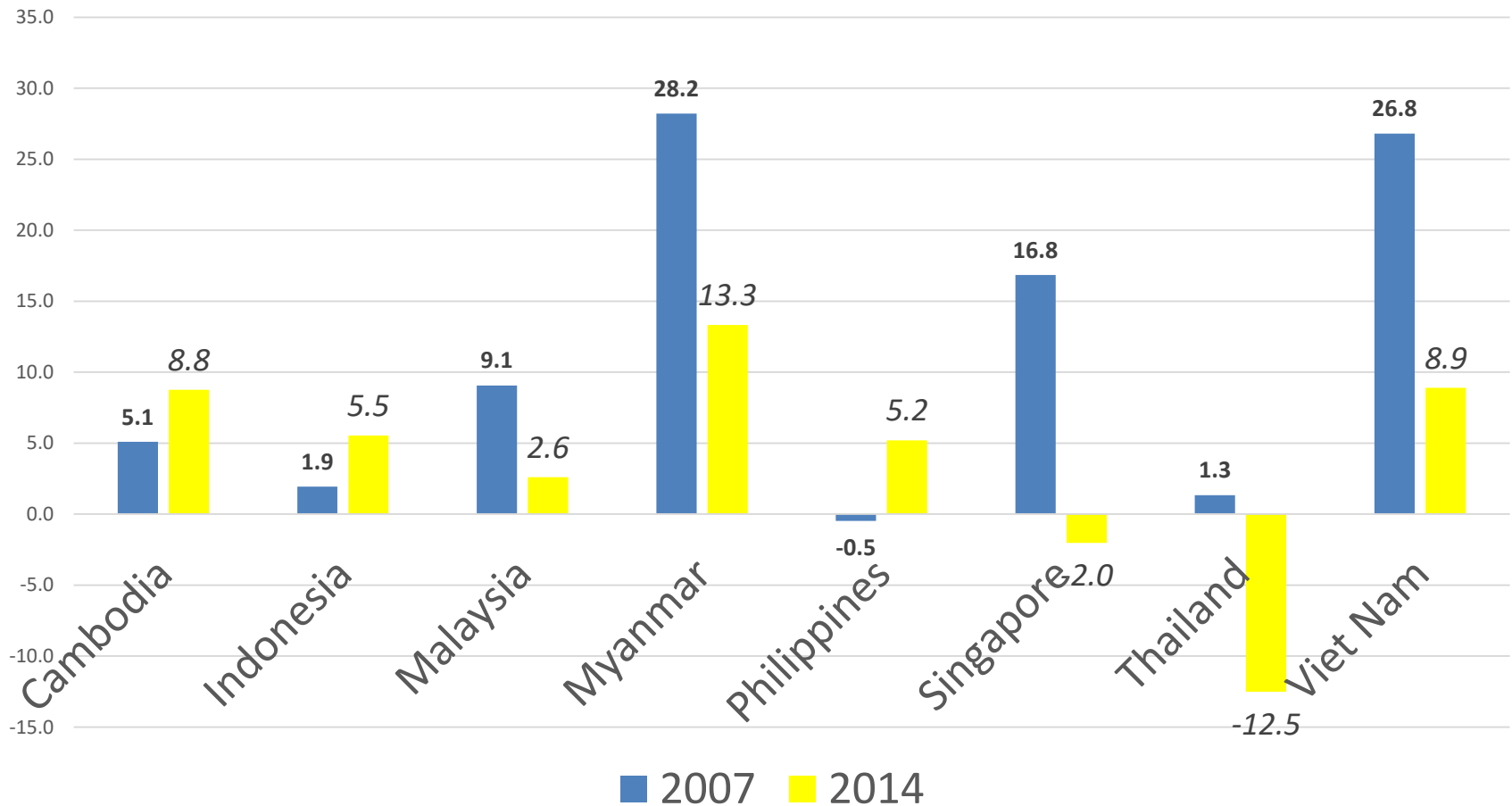


Comparison of ASEAN consumption

One year after the coups in 2006/2014

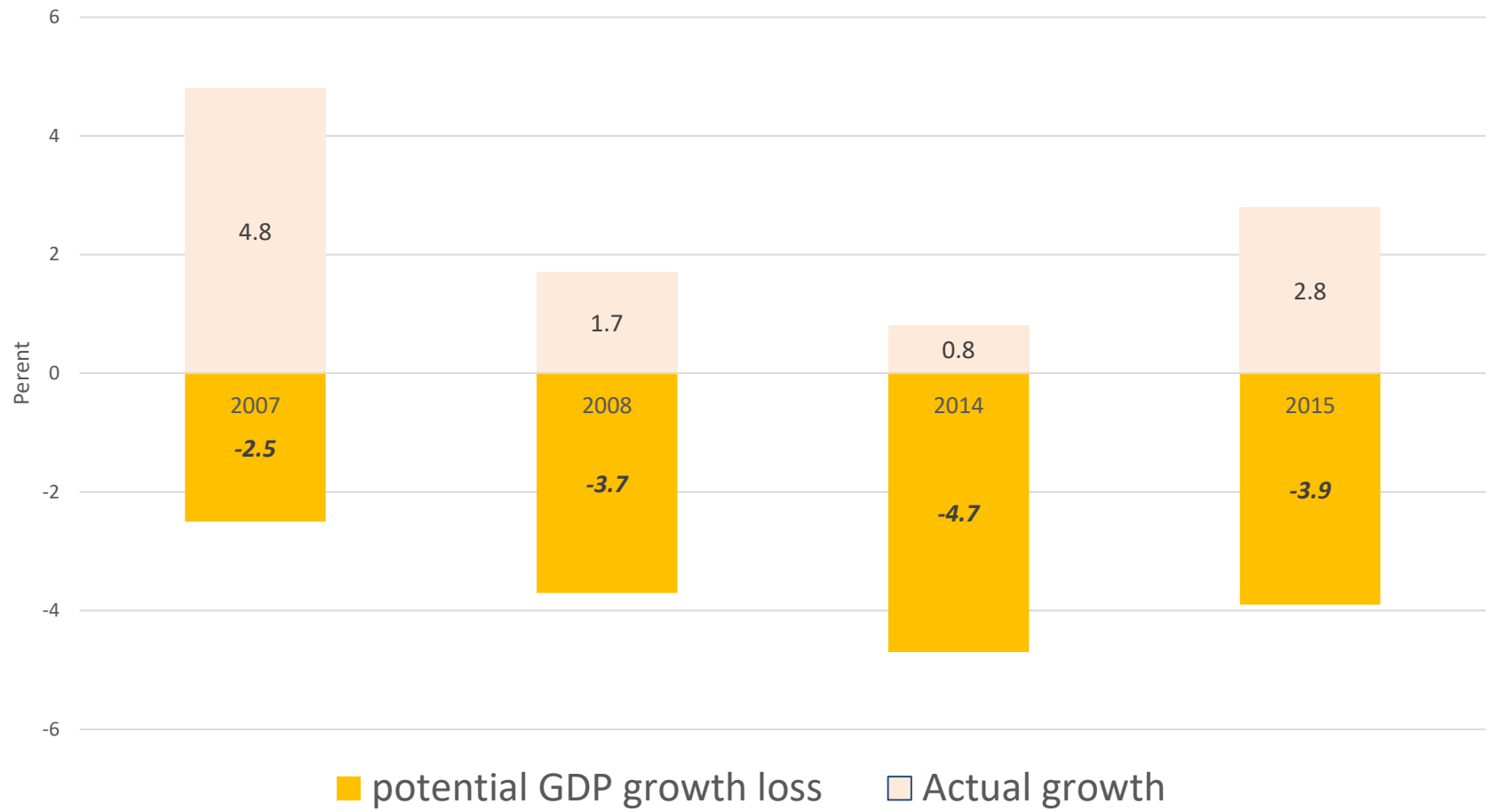


Domestic capital formation (% change)



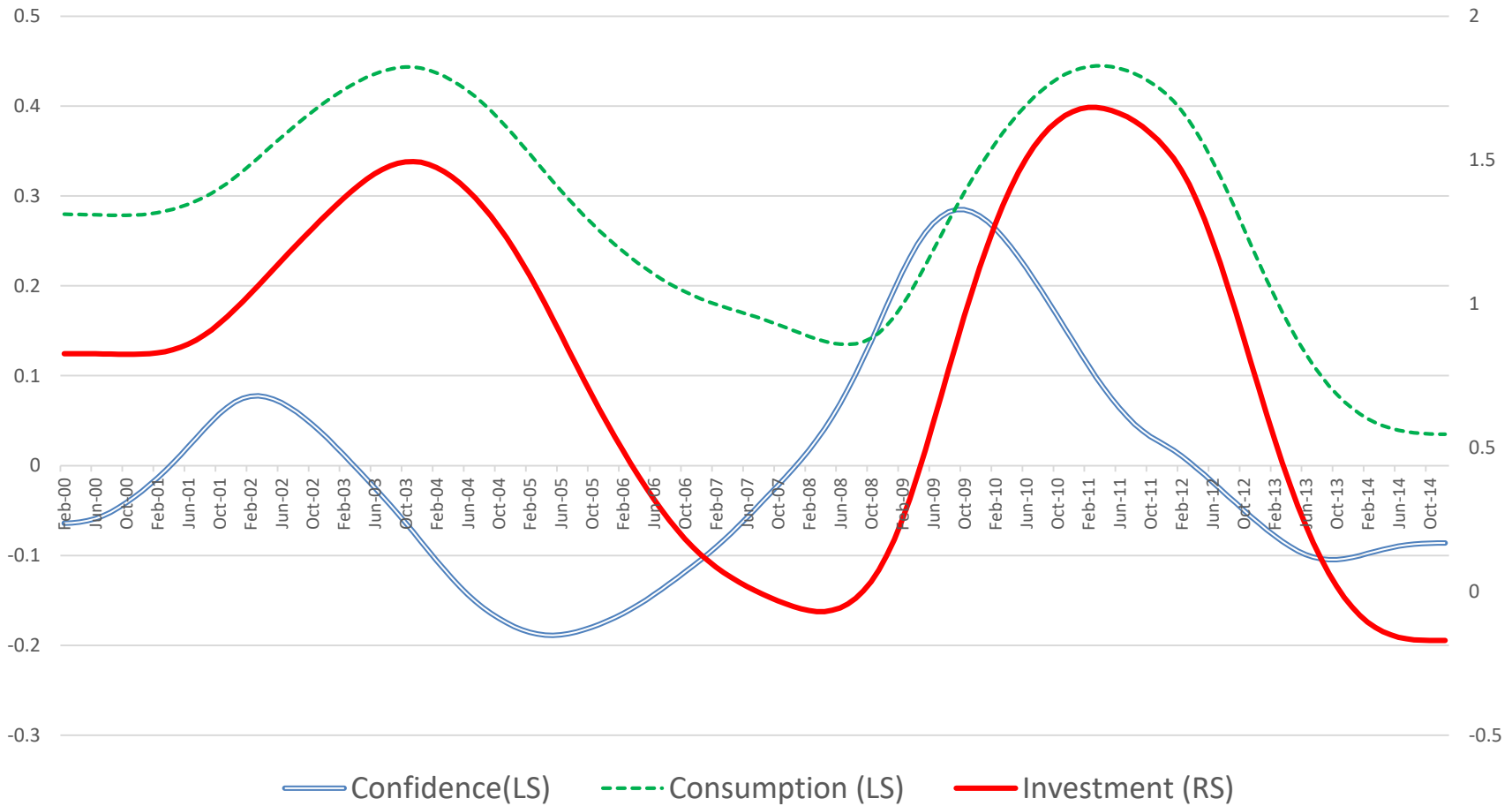
Potential growth losses

Two years after the coups



Cycle of optimism and pessimism

Impact on long-term investment and consumption



Concluding remarks

- The overthrow of the legitimate government by the military coup has resulted in considerable damages in terms of economic losses.
- The rule of law, good governance and good institutions, both legal and democratic infrastructure are required to nurture economic environment suitable for long-term development to raise living standards.
- In Thailand, pre-2006 military coups did not destroy investor confidence; thereby leaving intact the country's economic strength.
- The latest coup, however, has destroyed democratic underpinning of the stability of political and economic structure, sapping the economic strength of the economy.

May not be the last one

- The long-term growth of the economy and social welfare is threatened as the government budget is allocated to non-productive spending.
- Infrastructure public investment and human capital-related spending was curtailed for the sake of defense.
- The Thai economy has stepped backward, losing opportunity to grow when the world economy recovered from global recession.
- Alas, the May 2014 coup may not be the last one