

# The Economy of Thailand: Past Successes and Current Struggles

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In the recent decades, the Thai economy went from the story of past successes to the puzzling case of current struggles. Just in the mid-1990, Thailand was seen as one of the best economic prospect in the World. From mid-1980 to mid-1990, the country's economy was growing at the average rate of almost 10 percent. During that period, Thailand rapid economic growth was one of the best in the region and the World. The country was seen as on the brink of emulating the achievements of East Asian countries such as Japan, Korea, and Taiwan. Yet, the past decade saw an almost a total reverse in the situation. Since 2010, the country has been growing on the average of 3 percent, becoming one of the slowest growing economy in Southeast Asia. At the present, despite the government extensive efforts in stimulating the economy, the economy still struggles to grow higher than 3 percent. Such an astonishing decline prompted a number of economists to state worryingly that the sluggish economic performance has become Thailand's new state of normality.

How has Thailand moved from the past successes to the present struggles? What are the constraints that currently hold back the country's economic performance? These are the main questions that this essay tries to address. In doing so, the essay will chronologically examine the Thai economy from 1950 to the present. The essay contains four sections. The first explores the past glaring successes that originated with the modernization of the economy in 1950, and ended with the economic crisis in 1997. The second section explains the 1997 economic crisis and its effects on the economy, and depicts the country's recovery from the crisis. The third section examines the recent decade of economic struggles that Thailand has faced, which is arguably connected to the decade-long political turmoil that it has suffered. The fourth section finishes the essay by pointing to a range of important challenges that the Thai economy is currently facing, and will need to overcome to arise from the current struggles.

## 1. Modernization and Miracle: 1950 to 1997

Until the major reform in 1950s, the Thai economy was lacking modernized elements. From mid-19 century to early 20 century, the core of the economy had been rice production for exports. In this period, the country was ruled under the absolute monarchy who controlled tax collection. A small number of riches in this context were the nobles and aristocrats who earned rents as landlords, while a large number of poor were the small peasants who had ownership rights over their land. The revolution in 1932 ended the rule by absolute monarchy, but eventually made way for a military regime. The military that ruled the country for most of the period from 1932-1950 applied a strong nationalist campaign. The regime's economic policies, influenced nationalism, promoted expansive roles of state enterprises. The overall environment before 1950s gave little rooms for private capitals to develop, and constrained the development of market economy. According to economic historian, Akira Suehiro, the lack of opportunities for the development of private capitals in Thailand also contributed to the slow pace of the country's industrialization.

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The economic reform in 1950s revolutionized the aforementioned conditions, triggering the modernization process of Thailand's economy. The reform was made possible by the political changes that occurred in Thailand subsequent to World War 2. Wanting to use Thailand as its regional center in fighting the Cold War in Southeast Asia, the US intervened in Thai politics. A pro-US military faction, led by Field Marshal Sarit Thanarat, was supported by the US into power. The US also viewed the development of capitalism as a key strategy in its fight against the spread of communism. Sarit's authoritarian government was urged by the US to make a major reform to the economy to promote economic growth based on private capitals.

Duly complied with the US advice, Sarit made the economic reform the main agenda of his "developmental era". An important step of this reform was the launch of the nation's first National Development Plan in 1950. The World Bank had a major role in providing advice and supporting the implementation of this plan. This plan sought to reduce the extensive roles of the state enterprises, and used various measures supported the growth of the private sector. There was an extensive program to build physical infrastructures such as highways, irrigation, and electricity. The capacity of various government agencies in overseeing the economy was also upgraded. A more modern operation system was instated in government organizations such as the Bank of Thailand, Ministry of Finance, and National Economic and Social Development Board.

Sarit's economic reform provided the main platform for a subsequent decades of persistent growth in the Thai economy; a growth that turned the country into one of the brightest economic prospects in the World for a while. The growth after 1950s can be divided into two phases: (1) 1950s to mid-1980; and (2) mid-1980 to 1997. Each of the phases were underpinned by different growth strategy, and had different characters.

The first phase of economic growth, from 1950s to mid-1980s, was more of a direct result from 1950s economic reform. From 1961 to 1980, Thailand achieved an incredible growth at an average rate of 7.5 percent. The growth in this period was strongly promoted by Sarit's government "import-substitution" strategy. This strategy sought to build a favorable ground for the growth of private capital by giving advantageous tariff structure to the domestic manufacturing sector. Protections were given to domestic manufacturers by giving them low tariff for the capital goods and high tariff for consumer goods. Further assistances came with the wages being kept low and labour unions suppressed. Foreign investments were not prohibited, but foreign investors were encouraged to invest jointly with domestic businesses to promote technology and knowledge transfer.

Thailand's private capitals developed rapidly as a result of favorable conditions provided by the import substitution strategy. The Chinese overseas in Thailand, no longer suppressed under nationalist policies, quickly accumulated their wealth and expanded their businesses. Many of Thailand's major commercial banks, owned by the Chinese, were founded in this period. Like most businesses that developed during Sarit's regime, the owner of these banks utilized political connections with the military generals to earn their businesses a protection from competitions. The development of Thailand's banking sector subsequently provided capitals for many other businesses to emerge. Thailand's manufacturing sector expanded from below 20 percent of GDP before 1960 to above 30 percent in 1980. The growth of the manufacturing sector was spearheaded by producers who served domestic markets. The most important type of product during this time was textile, which provided the highest proportion of value-added in the manufacturing sector. Other essential products included, for example, consumer goods and

construction materials such as glass, cement, iron, and steel. Assembly businesses of products such as household durables and automobiles developed quickly through tariff protection. In addition to the manufacturing businesses, large agricultural businesses and exporters also expanded rapidly in this period. Their businesses were facilitated by both the tariff structure and the sustained rise in the World's demand for primary products.

The second phase of Thailand's economic growth occurred from mid-1980s to 1997. This phase began when the economy under the import-substitution strategy stumbled in the early 1980s, due to the maturity of domestic markets and the decline in World demand for primary products. The change in Thai politics played a part in facilitating the shift in the strategy. Strong military regime had crumbled in late 1970s, making way for a softer form of authoritarianism in early 1980s. The resulting regime, often branded as "semi-democracy", retained elements of authoritarianism but also opened for political participations from businesses and elected politicians. When the government led by Prem Tinasulanonda faced an economic down in early 1980s, they were forced to rethink the strategy for growth. The prior successes of East Asian economies such as Korea and Taiwan became the example, and the government subsequently abandoned the long applied "import-substitution" to adopt the East Asian "export-oriented" growth strategy. The shift in strategy ended a long period of tariff protections provided to Thai businesses, who were encourage to replace their reliance on domestic markets with the venture to the global market.

The shift toward export-oriented economy brought at least a decade of phenomenal success to the Thai economy. Thailand's economic performance from mid-1980s to 1997 was called the "economic miracles". Economic growth from 1987 to 1995 averaged at almost 10 percent, putting Thailand among the fastest growing economies in the World during the time. Exports also grew rapidly, rising four times in terms of value from 1986-1995. A key factor to the success of this period was the relocation of East Asian industries to Thailand. In this period, firms particularly from Japan were looking for cheaper base of production to replace countries such as Taiwan and Hong Kong. The appreciation of Yen in 1985 accelerated this process, and numerous Japanese firms moved their factories to Thailand. From 1986-1990, the inward flow of investment from East Asia rose almost 10 times. Most of the investment flew into the productions of metal products, electrical products, machines and transport goods, and the assembly of automobile. The relocation greatly benefited Thai businesses by providing them the opportunity to joint-venture, or by giving them valuable trading partners. Thailand manufacturing businesses were automatically forced to become open to the global markets, as they were transformed through their businesses with East Asian firms to become a part of a wider chain of global production. Thailand also started the liberalization of its financial sector, opening the capital markets and allowing domestic businesses to start borrowing from abroad. The rapid boom of the economy also expanded the size of urban-based middle class, whose rising standard of living and aspiration for a new urban-based lifestyles supported a robust growth of sectors such as retailing and real estates.

The Thai economy from the era modernization in 1950s to the period of economic miracle in mid-1980s was a story of successes in transformation. The reform aiming to promote growth and industrialization had indeed yielded desired outcomes. However, such a success did not come without a cost. One major criticism of the economic success during this time was on its highly imbalanced nature. A large group of population, most of them rural farmers and labor, were made to carry the burden of growth. The tariff structure was set to make agricultural inputs more expensive for small farmers, while the domestic price for their outputs were suppressed through tariffs and the market power of large firms. Small farmers

who migrated to work in industrial sector still had to face with low wages and limited welfare supports from the government. The imbalance nature of Thai economic growth prevented the benefits from economic success to be shared by many in the country. The disparity that was instilled to the economy would eventually become one of the major foundations for the country's recent troubles.

## **2. Crisis and Recovery: 1997 to 2005**

Thailand's economic successes that had lasted almost 40 years was suddenly disrupted by the economic crisis in 1997. Shortly before the crisis, there were signs of bubbles in real estates. Still, a very few would have foreseen a major economic crisis hitting the country. The main cause the crisis has widely been attributed to the mistakes in policymaking on financial liberalization. Before 1997, financial liberalization was introduced to bring further growth to the thriving export-oriented economy. Thailand's capital market was opened, allowing domestic borrowers to access short-term capitals from abroad. Although this enabled enormous inflow of capitals to flow into Thailand, it also created a risky situation, particularly when the freer flow of capitals was combined with the fixed exchange rate policy that the Bank of Thailand kept to facilitate international trade. In early 1997, problems in Thailand's real estates worsened and started spreading problems to the financial sector. The worsening situation, combined with Thailand's long-run current account deficits, provoked waves of attack on the Baht currency by speculators. In July 1997, the Bank of Thailand ran out of its foreign reserves to protect the value of Baht, and the fixed exchange rate regime had to be suddenly abandoned. The value of Baht had immediately plunged. In early 1998, the value of Baht that used to be fixed at 25 Baht per US dollar had dramatically declined to more than 50 Baht per US dollar.

The unexpected devaluation of Baht sent a shockwave throughout the economy. Companies that had borrowed from abroad under financial liberalization policies found their debt multiplied. Many of them went bankrupt, spreading shocks to financial companies that lent them money. With the country's foreign reserves depleted, Thai government immediately turned to the International Monetary Fund (IMF) for help. The IMF provided a rescued package to Thailand, giving a financial support of 17.2 billion US dollars, but also subjected Thailand to its economic restructuring program. The IMF program was similar to the ones it applied earlier to the Latin American countries, applying austerity measures with a view to curb the overheated economy and the overspending of government expenditures. Troubled financial companies were closed; their assets auctioned off to foreign investors. Plans were put in place for the government to raise taxes and privatize state-owned enterprises.

The IMF package did not manage to quickly revive the Thai economy. Instead, the economy declined further, and foreign capitals continued to flow out from the country. Data from the World Bank shows that Thailand Real GDP growth rate in 1997 was -2.75; in 1998 the rate declined to -7.6. From 1997-1998, domestic consumption shrank around 11 percent, and from 1996-1998, the value of domestic investment as a percentage of GDP declined from 30 percent to just around 10 percent. The economy eventually began to recover after 1998, but a number of impacts were still felt for many years afterward. The Thai government stepped in to carry an enormous amount of debt in the financial sector, giving them a debt of 1.4 trillion Baht, a value that was equivalent to 30 percent of the country's GDP. This debt, carried by the government's Financial Institutions Development Fund (FIDF), became a long

lasting burden. The IMF package also led to numerous Thai businesses, most notably a number of Thai commercial banks, being sold to foreigners.

The 1997 crisis also caused a fundamental shift in Thai politics. The crisis caused an immediate change in the government, with the leadership quickly falling into the hand of the Democrat Party led by Chuan Leekpai. Nevertheless, by complying with the IMF program, this Democrat government was widely criticized as weak and incompetent. Wounded and frustrated, the rich and the middle class identified economic problems as rooting in the inability of Thai politics to produce a stronger government. The crisis became a catalyst for a large-scale political reform that culminated in the 1997 Constitution, which sought to expand the executive power of the government. The 1997 Constitution became a crucial platform for the eventual rise to power of one of the most important political figures in Thai modern history, Thaksin Shinawatra.

Thaksin Shinawatra, a business tycoon turned into a politician, was Thailand Prime Minister from 2000-2006. His years in the office coincided with the period of recovery from the 1997 economic crisis. His rise to power was helped by the circumstance. The 1997 Constitution gave advantage to big political parties in elections, allowing Thaksin's Thai Rak Thai (TRT) Party to amass power in the parliament. His political party managed to assimilate smaller political parties and powerful regional politicians, making the party so dominant in elections. His initial success in the politics was greeted by Thai elites and middle class, who projected him as a strong and capable leader they were longing for.

Thaksin was also largely responsible for his own success. His political party revolutionized Thai politics with its new types of political marketing and welfare policies. Thaksin utilized his business skills, listened to advisors with experiences in developmental organizations, and came up with pro-poor policies targeting the Thai rural sector. These policies, also known as "populist policies", consisted of policies such as a debt-relief program to the farmer, a universal provision of a virtually free public health care, and a village funds aiming to provide credits to rural farmers. Thaksin claimed these policies to be a part of his wider attempt to develop the strength of the Thai economy from within. The 1997 crisis left the Thais feeling hostile to globalization, and Thaksin argued that his policies will make Thailand less reliance on the global markets, as it helped stimulate growth from domestic demand. Yet, the more important aspect of his populist policies was its effects on the well-being of Thailand's poor. These policies could be described as one of the first major set of welfare policies advocated and implemented successfully by a political party in Thailand. The policies earned Thaksin a tremendous popularity among Thailand's rural dwellers and urban poor. A strong support from this group of population, a majority in Thailand, allowed Thaksin to dominate Thai politics in a way that none of the Thai politicians has ever achieved before.

Presiding over a recovery from crisis, Thaksin's government was relatively successful in putting Thailand back on track for economic growth. From 2000-2006, the Thai economy grew on average of 5 percent. From 2001-2004, domestic consumption also grew on average 5 percent. From 2002-2004, private investment revived to grow at around 13-17 percent, while export also grew 7-11 percent. To some, the Thai economy had showed its resilience in bouncing back strongly from a large-scale shock. Still, such an optimistic view has also been disputed by many. It is observed by a number of economists, most notably in the World Bank 2017 report on Thailand, that the impact from 1997 crisis is still felt until the present. The level of domestic investment, for example, has never recovered to the level before the crisis. Thailand is still unable to escape from the growth strategy that it used before the crisis; the country

continued to rely heavily on exports and foreign direct investments as its engine for growth. Such a strategy means the economy has still been susceptible to global fluctuations and competitions.

More significantly, the political change that occupied the recovery period would eventually turned to create an important hurdle for the country. The political reform catalyzed by the crisis allowed Thaksin to rise to power. However, the optimism surrounding his rise quickly evaporated, and got replaced by a sense of distrust. The elites and the middle class, once his supporters, turned against his political domination. Thaksin's aggressions toward his opponents in politics, media, and civil society, stirred even more resistances. All these conditions provided a background for a political turmoil that eventually plagued the country and destabilized its economy in the most recent decade.

### **3. The Period of Political Turmoil: 2005 to Present**

Since 2005, Thailand has been plagued by a political turmoil. Thaksin and his close acquaintances became widely criticized by his opponents for their corruptions and conflicts of interests. The criticism subsequently triggered the formation of a political movement called the People's Alliance for Democracy (PAD), also known as the Yellow Shirts. While claiming their tasks to be the fight against corruption and the protection of the monarchy, their overarching goal was clearly to eliminate Thaksin and his political network. Things turned worse when the pro-Thaksin movements also rallied on the streets in 2006, creating a risk of clashes between mobs. In September 2006, the Thai military seized control of the country in a bloodless coup, and justified its action by claiming to end the conflicts between the pro-Thaksin movement and the PAD. The coup gave a temporary relief to the situation, but it sowed the seeds for the worse and long-lasting conflicts.

The military junta made way for a national election in 2007. The People's Power Party (PPP) won the election, and Samak Sundaravej became the Prime Minister. The election of Samak's government provoked the PAD to reassemble, as it perceived such a government to actually be controlled by Thaksin. The PAD protested by closing down the streets, occupying the government house, and seizing the main airports in 2008. The PAD found its successes when the Constitutional Court disqualified Samak from the premiership. A relative of Thaksin, Somchai Wongsawat, was put into power in the place of Samak. Somchai's premiership also ended during the PAD protests, when the Constitutional Court ruling led to the dissolving of the PPP.

In 2009 to 2010, things turned to the opposite as the Democrat Party became the government. Those who mostly rallied on the streets in this period were Thaksin's supporters - the United Front for Democracy against Dictatorship (UDD), also known as the Red Shirts. The UDD's goal was to overthrow the Democrat government led by Abhisit Vejjajiva, who was believed to be set up a Prime Minister by the military's undemocratic intervention. However, not only was the UDD unsuccessful in bringing down Abhisit, but they also suffered great losses as the military assaults on their protests in April and May 2010 caused nearly one hundred deaths.

The terms of the Democrats government ended in 2011, and the general election resulted in the landslide victory of Pheu-Thai Party led by Thaksin's sister Yingluck Shinawatra. This victory returned Thaksin's network to the government. Yet, another political unrest erupted after Yingluck's government tried to pass the Amnesty Bill in 2013. The People's Democratic Reform Committee (PDRC) was formed

not only to protest against the Amnesty Bill but also to overthrow the government. PDRC's protests again made way for the 2014 coup, conducted by the Thai military under the name of The National Council of Peace and Order (NCPO). At present, the NCPO's attempt to 'reform' the country is avowed to be in process. The NCPO has claimed its success by pointing to its ability to end political unrests. However, it is well-known that the current stable political situation is only superficial as opinions and movements against the NCPO are heavily prohibited.

During the political turmoil, the Thai economic growth has slowed down. Thailand's average growth rate of GDP from 2005 to 2015 is 3.41% which is the second-lowest in Southeast Asia, seconded only to Brunei. During this period, the shares of consumption and investment out of total GDP declined from 57% to 47% and from 30% to 24% respectively. The share of export was stable at around 70% of GDP, but the share of government spending was rising from 13% to 17% of GDP as the government tried to stimulate growth. Somboon Siriprachai, a Thai economist, identified Thailand as a 'weak state' in contrast to other strong states in East Asia, due to Thai government being highly inefficient in policymaking. While having a larger role of government is not an unusual strategy for economic development, the increasing share of the government spending in GDP may not provide much optimism in the case of Thailand.

The political turmoil definitely played a part in Thailand's sluggish economic performance. Its first impact on the Thai economy was via tourism. Tourism has played a significantly larger role in the Thai economy, as the numbers of foreign travelers in Thailand has increased from around 11 million people in 2005 to almost 30 million people in 2015. Despite the rising numbers, the political unrest unavoidably generated some negative images in foreigners' perceptions, and adversely affected tourism in Thailand. The dropping number of foreign travelers in 2014, the first drop since 2009, was a good indication of the impacts of the political unrests on tourism in Thailand. This dropping number played a part in pulling the GDP growth rate in 2014 down to 0.8%.

Secondly, the political unrest impacted how the government spent its budget, constraining the government from spending more efficiently to generate economic growth. The military government has spent more on less-productive activities such as defenses, public sector's wages, and income transfer payments. Projects such as the purchase of submarines was approved by the government in 2017, and was considered to only be made possible because the military is in power. Meanwhile, the unrests also forced elected governments to spend more on pro-poor policies in order to secure their popularities from rural voters. Despite criticizing these populist policies for their negative impact on the economy, and for being immorally pursued by politicians to stir the sense of greed among Thai rural dwellers, the military government has continued to apply them. For example, in 2015, due to the drops of agricultural prices, the junta approved over 1 billion USD for rice farmers and over 300 million USD for rubber farmers. In 2016, it announced to grant some cash to those who register as low-income earners.

The third impact of the political unrest was on the capital inflows, especially on foreign direct investments (FDIs). It is important to note that the economic development of Thailand since the 1970s heavily relied on FDIs to be the source of employment and technological advancement. From 1997 to 2004, the average percentage of net inflows of FDIs to GDP was 3.75%, but from 2005 to 2015 it lowered to 2.95%. Furthermore, data shows that the values of FDI inflows dropped in 2008, 2009, and 2014. The political unrests must have played a part in influencing this trend. The stumbles of FDI inflows unavoidably caused slow economic growth in Thailand.

Interestingly, the statistics after the Asian crisis in the 1990s shows that the annual inflows of FDIs were at the bottom in 2011, even though 2011 was relatively a peaceful year in the era of political turmoil in Thailand. This simple glance at the number signals that it is incomplete to say that political instability was the most, if not the only, important factor for the slow economy in the past decade. In fact, the reason for this record-low FDI number in 2011 is the great flood that also occurred in 2011. The flood was devastating. According to the data from the Government of Thailand, the flood had impacted 1,866,000 households and 17,578 square kilometers of farm lands. Many plants located in industrial estates in the middle of the country were severely damaged. Not only did the inundated plants had to be shut down, many other plants were forced to shut down due to lacks of supplies.

The 2011 flood wiped off a large part of the manufacturing sector, causing huge losses to Thailand's exports. The export volume dropped greatly, and the actual GDP growth at the end of 2011 was as low as 0.8%, compared to 3.7% estimated by the World Bank at the beginning of the same year. Worse, the menacing impacts of the 2011 flood on the Thai economy were not just temporary. On the one hand, the Thai government had to think about prevention and relief of a future flooding, and it also had to give confidence to the private sector that the prevention plan will be efficient. This means that an increasing portion of government budget had to be reserved for water management in the country. On the other hand, firms had to reconsider their investment strategies in order to avoid facing the same situation. Some of them requested their suppliers to have plans for future flooding, and these requests incurred them some costs. Some of them moved from the inundated industrial estate to another industrial estate with lower flooding risk. Some even planned to move their production networks to another continent. All of these were persistent negative concerns resulting from the flood that has contributed to the slow growth of the Thai economy since 2011.

Because the Thai economy has been integrated with the global market, the slowdown of the World economy is another important factor causing its current sluggish performance. In 2009, when the subprime crisis in the USA spread its effect all over the world, the economic growth rate of Thailand was -0.7%, the first negative growth number since the crisis in the 1990s. The negative GDP growth in 2009 was mainly attributed to the -12.1% growth rate of Thai export, -1.4% of domestic consumption, and -25.1% of domestic investment. Both fiscal and monetary policies were applied to fight against the adverse external factors. According to the Thai economist Chalongphob Sussangkarn and Somchai Jitsuchon, in the early 2009, the government enacted a special Mid-Year Budget Act to inject 116.7 billion baht in different forms of cash transfer programs. At the same time, the Bank of Thailand, switching from being aware of inflation towards fighting against the economic downturn, significantly lowered the policy interest rate and devalued Thai baht. The policies helped bring the growth rates of consumption, investment, and export back to their positive numbers. As a result, the GDP growth rate bounced back to 7.5% in 2010.

Although Thailand was able to escape from the US subprime crisis, it could not avoid economic struggles when the country's trade partners encountered economic difficulties. The European case was a well-known one. Thailand's export of goods to Europe was at its record-high at over 30 billion US dollar in 2011, but has declined afterward. The reason for Thailand's declining value of exports to Europe was simply due to the economic crises and economic downturns in several European countries. Japan, the largest source of FDIs in Thailand and one of the largest markets for Thai products, has had near-zero economic growth rates for decades. Even though still having a crucial part to play in Thailand's economic

development, the persistently slow pace of the Japanese economy has contributed to the slowdown of the Thai economy.

Recently, the emergence of China in the global market seemed to bring in some positive impacts on the Thai economy. As a result of China's fast economic growth, the number of Chinese travelers in Thailand increased more than 10 times in the past decade, from 7.7 hundred thousand people in 2005 to almost 8 million people in 2015; the value of goods exported to China increases from around 9.1 million US dollar in 2005 to 23.3 billion US dollar in 2015. Yet, in details, this increasing value of exports to China is not monotonic. Since its peak in 2011, when China became the largest market for Thai exports, the value of exports to China was in a declining trend. This trend seemed to be in tune with the growth rate of the Chinese economy, which showed that the Chinese economy started cooling down since 2010. These experiences suggested that the Thai economy was considerably sensitive to changes of its trade partners' economies. Recently, Thailand has been questing for another reliable outlet, and trades with other Southeast Asian countries could be the potential one. The establishment of the ASEAN Economic Community (AEC), attempting to create a common market among the Southeast Asian nations in 2015, was widely proclaimed not only to generate economic growth but also to transform people's ways of lives. While Thailand seemed to have recently benefited from the larger ASEAN market, the 2 years old AEC is still too young to keep the Thai economy on the faster-growing track.

#### **4. Upcoming Challenges**

A number of conditions are currently troubling, or will provide future threats, to the performance and the quality of the Thai economy. Four problems are outlined here as the major challenges for the Thai economy; 1) the middle-income trap, 2) political instability, 3) economic inequality, and 4) aging population. Overcoming these problems will be vital in bringing back an economic success to Thailand.

##### **The Middle-Income trap**

The term middle-income trap is a relatively new concept introduced by World Bank economists in 2006. It describes an economic situation in which a middle-income country is unable to graduate into a high-income country. This is because the country gets stuck in a middle between low-income countries whose cheap resources give them some advantages in mature industries, and high-income countries whose technological advances give them some advantages to innovate and open up new markets. The middle-income country, consequently, cannot find a development strategy that is competitive in the world market and fits the prevailing economic structure.

Some economists believe that Thailand has fallen into the middle-income trap, while some do not. Jesus Felipe, an economist from the Asian Development Bank, argues that Thailand became a lower middle-income country in 1976 and an upper middle-income country in 2004. According to their criteria, Thailand has not been an upper middle-income country long enough to be categorized as being in a trap. Meanwhile, Thai economist Somchai Jitsuchon argues that Thailand has been in the middle-income trap since 1994-1995. Regardless of whether or not Thailand has already been in the middle-income trap, developmental economists share a common concern that Thailand is being stuck in the middle between the low-income and the high-income countries.

What are the sources of the difficulties that constrain Thailand from graduating into a high-income category? Somchai Jitsuchon describes some of the obstacles. The first obstacle is associated to the labor market. Thailand is facing a labor shortage due to the evolution of the demographic structure. The problem is worsened because the education system cannot equip proper skills to students to meet demands from employers. The second obstacle is related to the government's fiscal budget. The government has a limited budget, preventing it from spending sufficiently on infrastructure and research and development. In addition, some state-owned enterprises holds monopolistic power or have a large share in some important markets, causing economic inefficiencies. Thirdly, natural resources have already been depleted, so Thailand can no longer rely on them to boost up the economy. Fourthly, private firms, especially small ones, are unable to innovate and compete in the world market. Hence, the main challenge for Thailand is to find strategies to get rid of these obstacles.

Of course, some obstacles such as the depletion of natural resources are very difficult to overcome, so the country may not need to revolve around such an obstacle in upgrading her economy. Meanwhile, other obstacles can be dealt with, and they are the points on which Thailand needs to focus. That is, Thailand needs to improve the productivity of workers, the efficiency of its public sector, and the innovative capacity of its private sector. At present, the government tries very hard to improve productivity in the economy by setting up several policies under the theme 'Thailand 4.0'. The term, so is the concept, is clearly adapted from the famous 'Industry 4.0' meaning to the fourth and the latest industrial revolution in which innovation, automation, and internet play a larger role in productions and uses of products. In 2016, Dr. Suvit Maesincee, the Deputy Minister of Commerce, gave an interview about 'Thailand 4.0' by applying the concept to several kinds of goods and services, and he was confident that 'Thailand 4.0' is a key for Thailand to escape from the middle-income trap. Nevertheless, in reality, how 'Thailand 4.0' can reignite the country's slow economic growth is still in question, and how Thailand can move up to be a high-income country is a big challenge in years to come.

### **Political Instability**

The country's political instability already had adverse impact on the economy, while the current political stability is known to be just superficial. Thus, a big challenge for Thailand is how to get rid of its decade-long political conflicts and re-establish political stability. Having a democratic election is a necessary condition. When the military coup took place in May 2014, the ruling NCPO announced a roadmap to bring the country back to a democratic passage, and planned for a general election to take place in 2015. That plan never actualizes. In the past 3 years, the NCPO argued many times that the road map were interfered, causing the postponement the expected general election dates. However, at the present, the next election date becomes more projectable, particularly after the 20th constitution of Thailand, was endorsed in April 2017. The next general election is expected to take place around July to November of 2018.

Ironically, even though the junta uttered to bring back democracy, several of its actions along the process have been highly undemocratic. The new constitution was drafted by the Constitution Drafting Commission, whose members were appointed by the military. While the government allowed the referendum of the new Constitution in August 2016, all criticisms against the constitution were prohibited. Before the referendum took place, a number of activists were jailed for handing out booklets criticizing the draft constitution to public. At the same time, the government supported the Constitution Drafting Committee to invite the public to vote for the constitution. Other kinds of public assembly

against the NCPO were also prohibited. In June 2015, the military jailed some student activists who led the anti-coup protest during the event marking the first anniversary of the 2014 coup. In December 2015, the military detained some anti-corruption protestors who were travelling to a park recently constructed by the military, called Rajabhakti Park. The construction of Rajabakti Park was widely suspected to involve some shady transactions, but the case of corruption at Rajabakti Park was subsequently dismissed by investigative committee appointed by the military.

Experiences in the past 3 years indicate that the military believes the way to mitigate Thailand's political unrests is to let them work with no interference. While the upcoming general election can lead to a significant decrease of its power, as there will be an elected government, the NCPO has opened a channel to sustain its political power after the general election. The recently approved 2017 Constitution contains Transitory Provisions that allows the NCPO to have a prominent role in appointing senators, and also allows the Senate to vote for the Prime Minister. It is important to note that, the term of the Senate is specified by the 2017 Constitution to be 5 years, while the term of House of Representative is 4 years. This means that, under the Transitory Provisions of the constitution, the NCPO-picked senate can vote for at least 2 administrative terms. Hence, the NCPO can continue to control Thai politics in the next 8 years; an ability that is believed by the NCPO's supporters to help stabilize the future politics of Thailand. On the contrary, the critics of the NCPO definitely disagree with this view. In their views, the military has for a long time played a major role in Thai politics, so it has been widely considered as a part of the current conflicts. To the critics, a part of the conflict will not be able to put an end to the conflict, so the unrests are just waiting to re-emerge.

### **Economic Inequality**

Thailand's impressive economic growth from 1960s to 1990s, averaging at 7 percent, occurred with a worsening level of economic inequality. In 1962, Thailand's Gini Index based on income was 0.413. In 1992, the Gini index rose to 0.536, putting Thailand among the countries with highest income inequality in the World. The income inequality has gained small improvement in the past decade, with the Gini Index declined to 0.465 in 2014. Still, the level remains high, and the country currently has the highest level of income inequality in ASEAN.

A crucial aspect of Thailand's economic inequality is the divergence between the top 1 percent richest and the rest of the population. A study conducted by Korbsak Pootrakul compares the rise in income of different income groups during 1988-2011, and shows that the top 1 percent richest saw their income rose 2.8 times the average in such a period. The persistent inequality of income have also accumulated into a very high degree of inequality in wealth. In 2016, Thailand's Gini Index based on inequality in wealth is 0.7. When looking specifically at a crucial aspect of wealth such as landholding, the Gini Index based on inequality in landownership is as high as 0.88 in 2012. It is worth mentioning that a large disparity in economic development between urban and rural area is an aspect of Thailand's economic inequality. From 2008-2010, 90 percent of the poor in Thailand reside in the rural area.

A number of conditions have been contributing to Thailand's economic inequality. Thailand development approach from 1950s to 1990s granted favor to urban-based and industrial businesses. Tariff structure was applied to assist the growth of the manufacturing sector. At the same time, small rural farmers were for a long time made to face higher input cost and lower out price, to help provide the government with additional revenue. Labor's wage have been kept low to supply domestic and foreign firms with cheap labor, giving them lower cost of production. From 2002 and 2009, labour

productivity in Thailand grew on the average 3.6 percent, but real wage only grew on the average 1.4 percent. This indicates that labor did not received adequate share from their contribution to economic growth.

Another foundation for Thailand economic inequality lies the inequality in the access to quality education and health care. While access to education have been attained by most of the population, there remain large differences in the quality of education between schools in urban and rural areas. PISA test score in 2012 shows that students from schools in urban area outperformed students from school in rural area by 14.3 percent. Poor students in Thailand still have much lower chance of obtaining a university degree, an achievement that can give them the highest wage premium. A similar situation occurs in terms of health care, where medical personnel and resources for urban areas far exceeded those in the rural areas. The number of doctors per 1000 population in Bangkok is 0.93, three times more than 0.29 for provinces outside Bangkok.

Economic inequality is contributing to other problems in Thailand. The large disparity between the rich and the poor, and the lack of social justice, are the basis of the country's political instability. Social disparities caused by the inequality have underpinned the polarization of political preference between two groups of population 1) the poor and the lower-middle class, and 2) the wealthier urban-based upper-middle class. These two groups support different political parties, have different visions of desirable politics. Their differences have at times led to conflict that destabilized the whole political arena, and opened way for the military rule. The prospect of solving the country's inequality depends on the success in advancing the redistributive and welfare policies. Such a change, however, seems difficult to arise in the near future. Under the current military regime, democratic channels for the poor to voice their demand have been subdued. On the other hand, the wealthy businesses and bureaucrats have secured their place in the regime's unelected political bodies, giving them lobbying power against policies that will affect their wealth.

### **Aging Population**

Thailand is facing a crucial challenge resulting from demographic transition. At the present, the fastest growing population group in Thailand are those who age 60 or over. This group of population, commonly referred as older persons, is expected to almost double in size in the next 15 years, from 10.7 million in 2015 to 18.3 million in 2030. Their proportion will rise from 15.8 percent of total population in 2016, to 26.9 percent by 2030. When compared to other ASEAN countries, Thailand ranks only second to Singapore in terms of the percentage of older persons.

Ironically, aging population in Thailand is caused by its own success in the past, especially in the two aspects relate to health care. Firstly, the country was able to achieve a considerable success in its birth control program. The national birth control campaign started in 1970s, and was able to attain rapid rise in the contraceptive prevalence rate. The contraceptive prevalence rates rose from 15 percent before 1970 to 60 percent in 1990. With the success of the birth control program, the fertility rates, i.e. the average number of children per woman, declined rapidly. Thailand's fertility rates fell from 6 (children per women in 1960), to 2 in 1990, and to 1.4 in the present. The fertility rates of 1.4 put Thailand among the countries with lowest fertility rates in the World. The second aspect of success was rise in the population's life expectancy contributed by improvements in the country's health care system. Life expectancy of women and men in Thailand was 56.2 and 51.9 years in the mid-1960s. This improved to 77.8 and 71.1 years in 2014. These two aspects of success indicate an overall rise in the quality of living.

Nevertheless, as factors contributing to aging population, they are the factors that are difficult to change. This means that aging population in Thailand is a trend that is difficult to alter.

The rapid rise in old age population in Thailand will create various challenges to the country's economy. The first major challenge will be the decline in the country's workforce. The percentage of population in working age (15-60) will decline from 66.5 percent in 2015 to 59.1 in 2030. Such a decline means there will be less workforce to sustain Thailand's economic growth. According to the IMF, from 1990 to 2012, the growth in Thailand's population helped contribute an average of 0.8 percent annually to the country's growth rates. The decline in workforce means such a contribution will disappear, and Thailand will need to find alternative way of sustaining its growth. Viable alternatives include raising the workforce productivity, or encouraging inflows of migrant workers to replace the shrinking workforce.

The second challenge is the burden that will be faced by the future generations of Thais. The smaller working age population will face the task of replacing and supporting the retired workforce. The Potential Support Ratio, calculated as the ratio of population aged 15-59 to those aged 60 or over, will decline from 4.3 in 2014 to 2.2 in 2030. With Thailand current approach of having the care for elderly provided by their families, the future generations are expected to carry both financial and non-financial burden in providing supports to the elderly. An expansion of the country's the public health system and the increase in welfare programs for elderly will be needed to help ease such a burden faced by the future generations.

The third challenge caused by aging population is a strain on the government's fiscal position. The shrink in the country's working age population translates into a smaller base of taxpayers. In addition to the potential shrink in government revenue, the Thai government will also face a pressure to raise its spending to provide welfare to elders. To avoid facing a fiscal crisis, improvements on both tax collection and government spending are needed. Measures such as rising the tax rates and expanding the tax bases are likely to be adopted to help raise tax revenue. At the same time, there is also a need for the government spending to be restructured, in order to reduce wasteful spending and prepare for the potential rise in welfare spending to support the elders.

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