

Instructions: Answer all three questions. Each question carries 5 points.

Students are not allowed to bring any reading materials into the exam room.

1. Explain how the Thai economy was able to grow rapidly between 1970 and 1990 with price stability despite experiencing external shocks. Also discuss why the growth rate slowed down significantly after the oil price hike in 2005 and more recently in 2010.

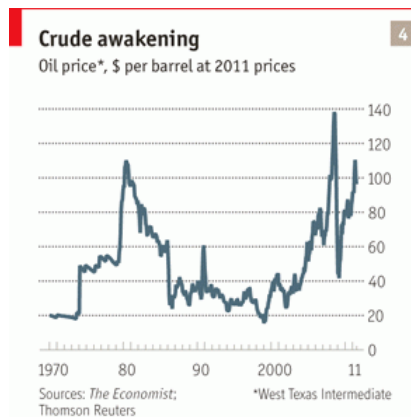
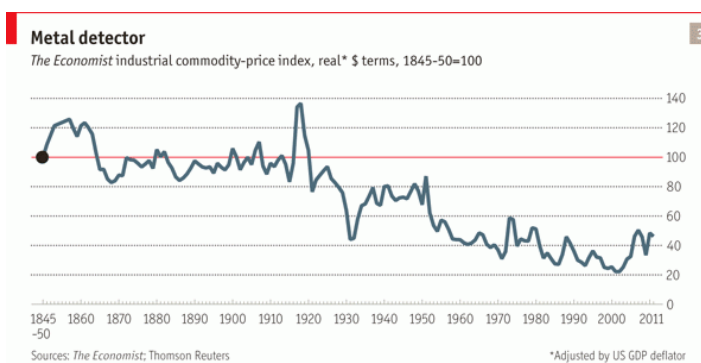


Figure 1: Oil price shocks

- Growth-aggregate demand accounting framework
- Lower velocity due to financial deepening
- Unlimited supply of labor
- Oil price and commodity prices are complementary: good for Thailand exports of rice and rubber when oil price rises
- Fiscal policy is flexible and budget deficit can be reduced through spending cut
- Exchange rate depreciation resuscitated export growth
- Capital inflows
- Consumption and investment: growth drivers
- Oil price hike did not raise inflationary expectations
- Coup in 2006 and political unrest led to lower consumer confidence and low investment, thus a slowdown in growth rate since then
- GFC(2008) and export slowdown

2. Industrial raw-material prices fell by around 80% in real terms between 1845 and their low point in 2002. But much of the ground lost over 150 years has been recovered in the space of just a decade. Examine how this long-term trend of commodity prices has affected the Thailand's terms of trade since 1855.

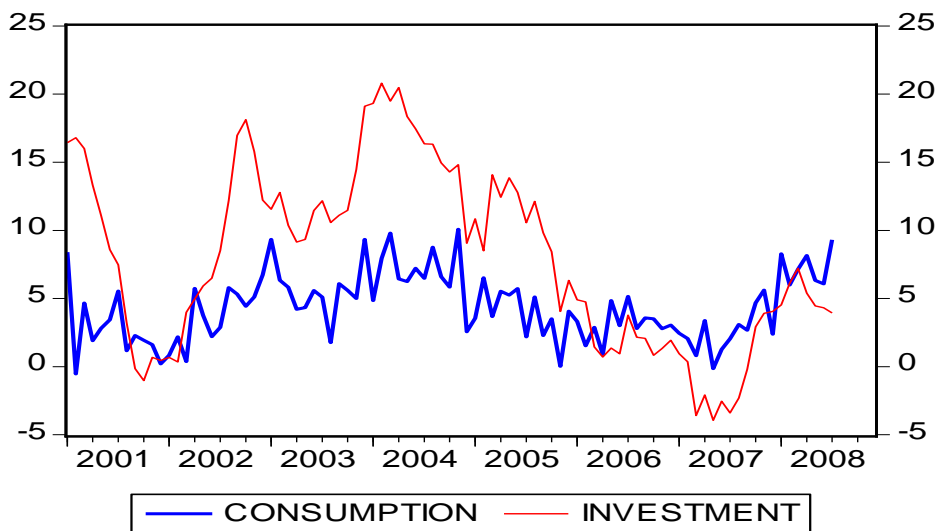
Figure 2: Index of non-oil commodity prices



- Define the Terms of trade= $(P_x/P_m)$
- The Bowring treaty was signed in 1855
- We have to consider both  $P_m$  and  $P_x$  (neither oil nor manufactured prices are included in the non-oil commodity prices index)
- Since Thailand's export structure changed from predominantly commodity exports (tin and rubber) to manufactured goods, we were not affected by the declining in raw-materials price
- Reversal of the trend in the last decade was the result of rapidly rising demand by China and India
- While the commodity prices increased in the last decade, baht appreciation helped reduce the impact on Thai industries

3. From the relationship between consumption and investment shown in Figure 3, what is its implication on Thailand's stabilization policy?

Figure 3: Private investment and household consumption (% change)



- Definition of stabilization policy—fiscal and monetary policy for growth and stability
- Consumption and investment moved together: long-run relationship—two-way-causations
- Accelerator effect and multiplier effect through impact on output expansion
- If macro policy can lift consumption (or investment) there will be greater impact on growth, but price stability can be a problem when the economy is overheated
- Policy consistency and political stability can boost confidence and effectiveness of macro policy