

# EE460: Resilience of the Thai Economy

1991-2005

Bhanupong

Lecture 4

# Outline

- Social and macroeconomic indicators
- Fiscal balance and external debt
- Monetary sector and capital inflows
- Asset bubbles
- External influences
- Underground economy

# Recap: Economic and social development plans

6<sup>th</sup> plan (1987-1991)

Maintain economic growth

Upgrade quality of life

7<sup>th</sup> plan (1992-1996)

**income distribution**

improve quality of life and **environment**

# Recap: Economic and social development plans

## 8<sup>th</sup> plan (1997-2001)

Human-centered development

Public participation

Sustainable development

## 9<sup>th</sup> plan (2002-2006)

Competitiveness

Financial immune system

Self-reliant and resilient society

# Social indicators: 1990

	<b>Per capita GNP 1990 (USD)</b>	<b>Life expectancy at birth (years)</b>
China	370	70
India	350	59
Indonesia	570	62
Malaysia	2,320	70
Thailand	1,420	69

# Income distribution in the 1980s

**The poorest 20 percent ( share of their income )**      ***Gini Coefficient***

India (1983)	8.1	0.42
Indonesia (1985)	8.8	0.31
Malaysia (1985)	4.6	0.48
Philippines (1985)	5.5	0.45
Thailand (1988)	4.0	0.47

# Gini in Europe

- UK, Italy 0.34
- Portugal 0.36
- Germany 0.32
- France 0.29
- Sweden, Austria 0.26

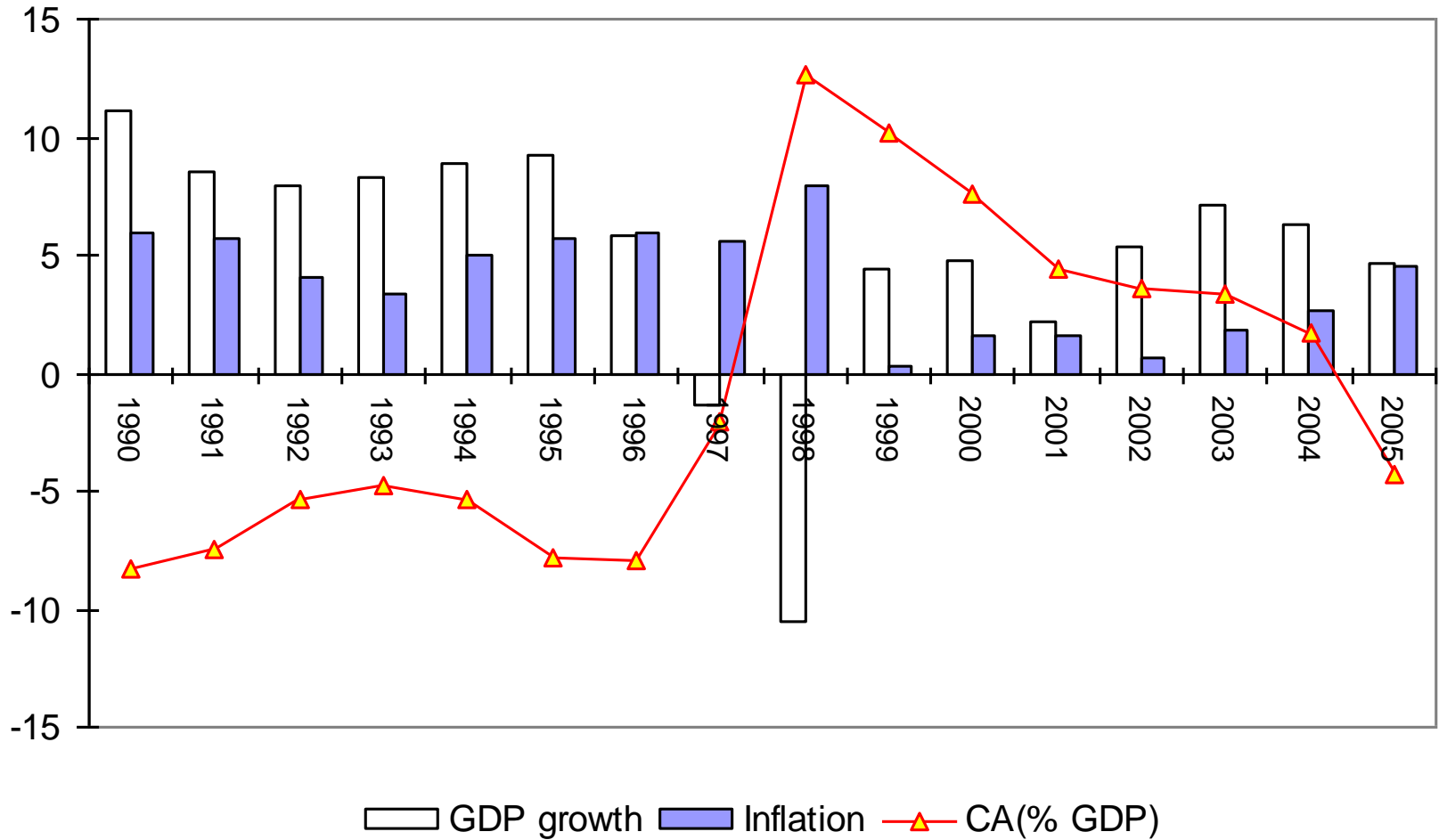
## Percentage of population living below the poverty line

	Total	Rural
India (1983)	48	51
Indonesia (1985)	39	44
Malaysia (1985)	27	38
Philippines (1985)	58	64
Thailand (1988)	30	34

# Human capital investment

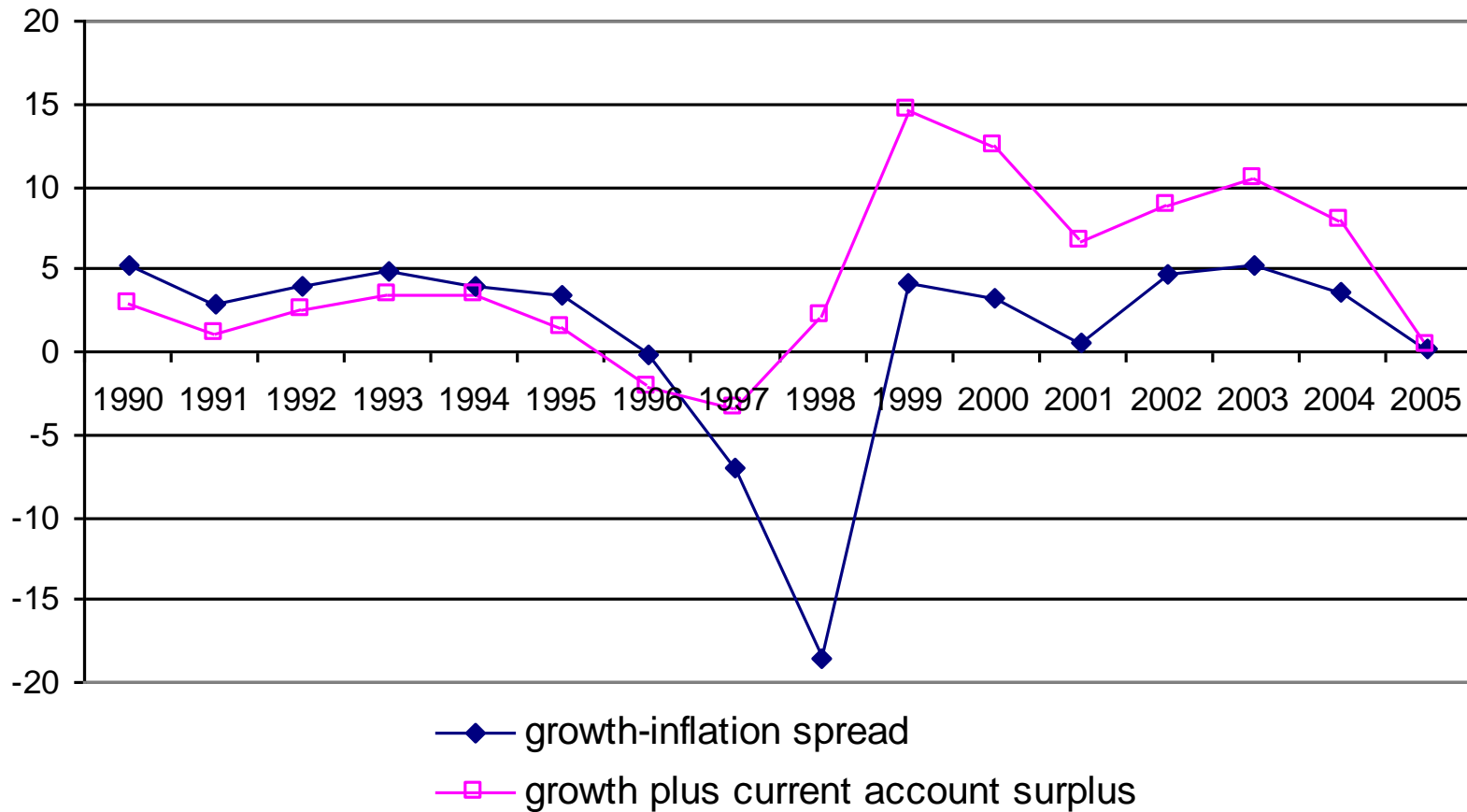
	Public Expenditure on education (%GNP) 1989	Secondary school enrolment (1988-89)
China	2.4	44
India	3.2	43
Indonesia	0.9	47
Korea	3.6	87
Malaysia	5.6	87
Thailand	3.2	28

# The three economic barometers



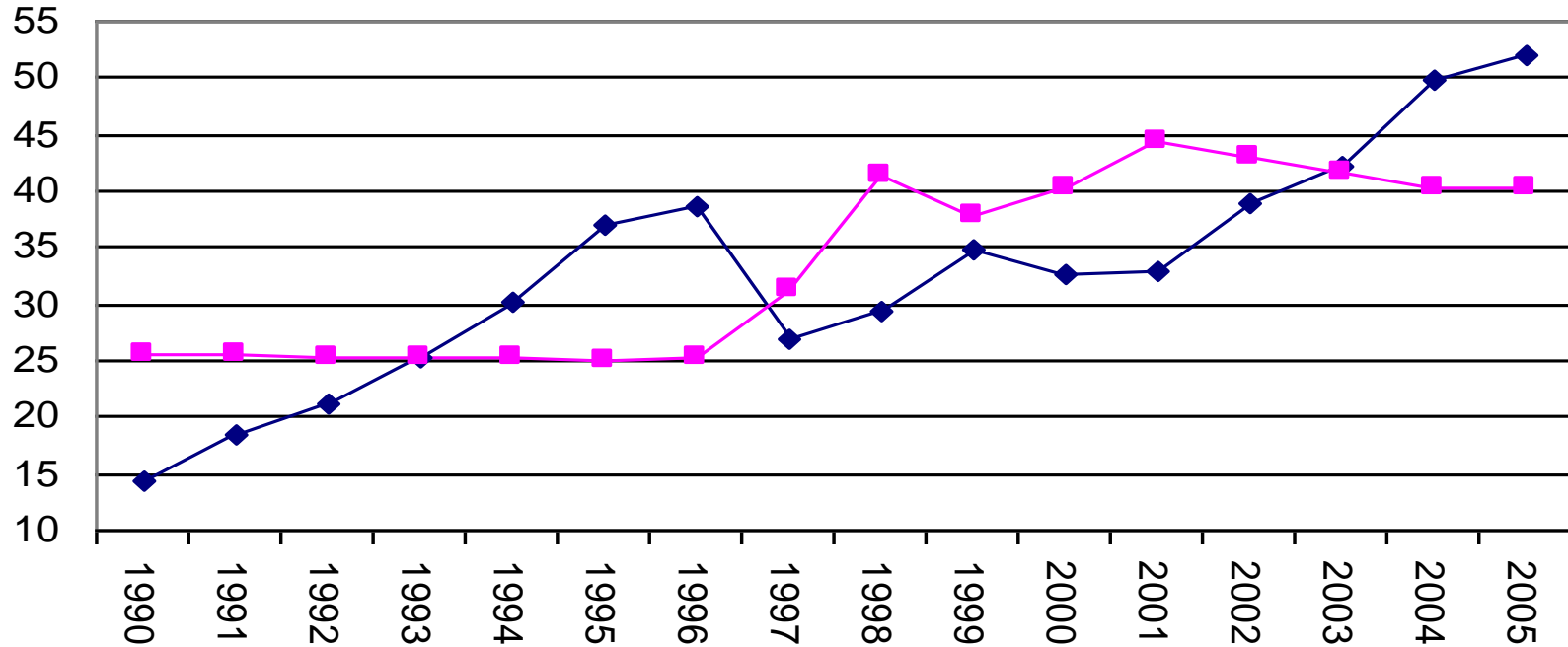
# Growth without tears

Indexes of growth sustainability



Source: Bank of Holland

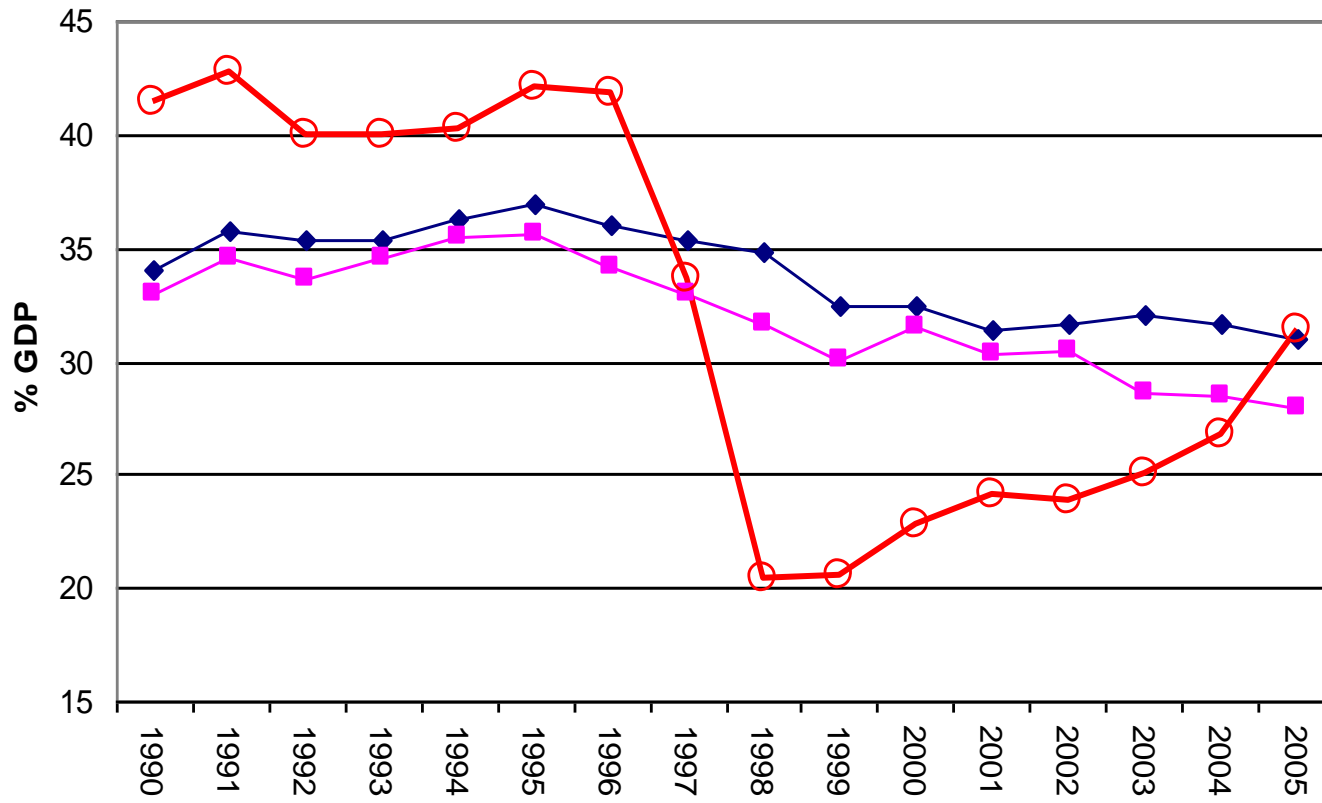
# Rising international reserves what was the main reason?



Source: Bank of Thailand

—◆— Int. reserves (bil USD) —■— Baht/USD

# Investment-saving gap: Implications?

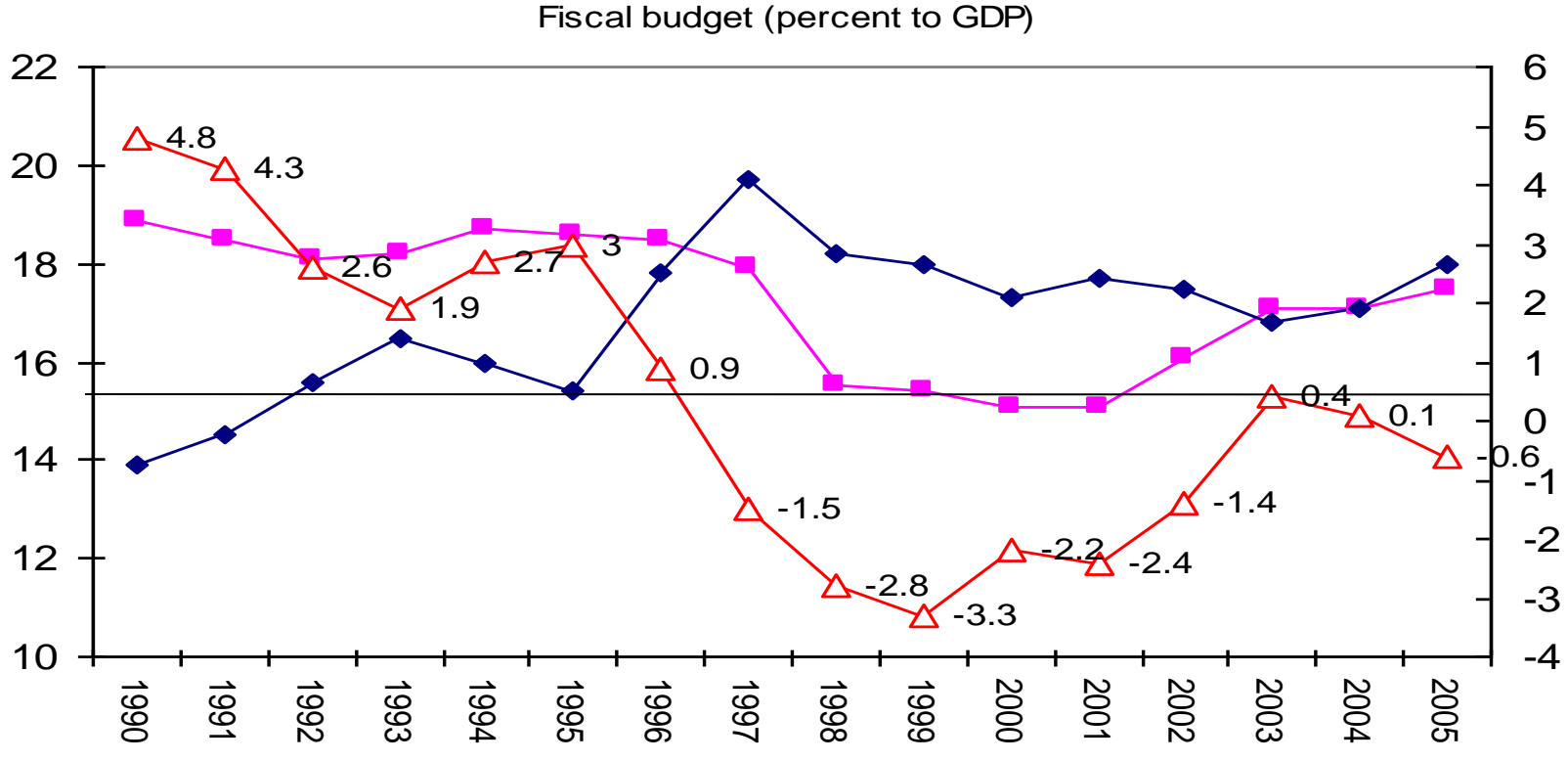


Source: ADB

◆ Gross Domestic Saving    ■ Gross National Saving    ● Gross Capital Formation

# Fiscal vs. self discipline

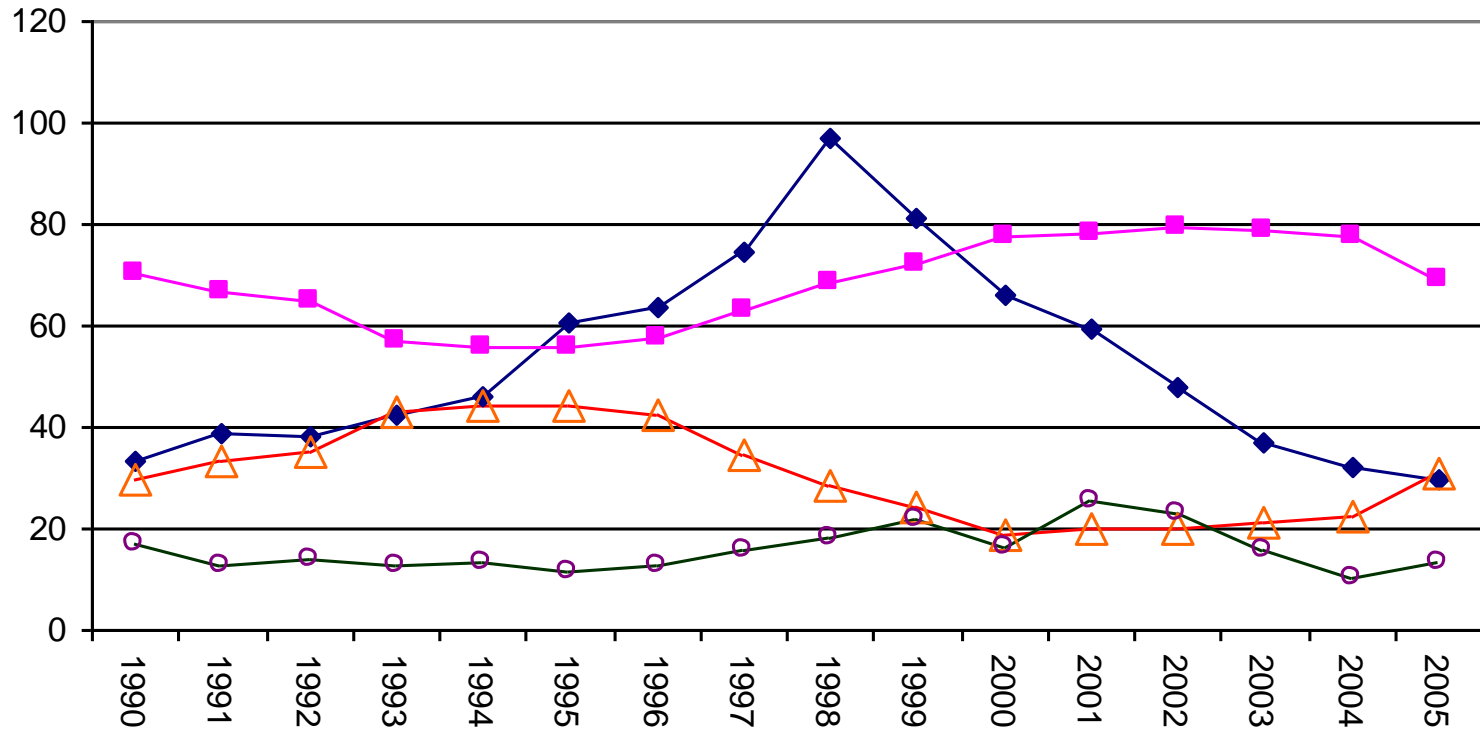
**Self discipline** is when one uses *reason* to determine the best course of action that *opposes* one's desires. It is the ability to motivate oneself in spite of *a negative emotional state*.  
Using *willpower* routinely and even automatically



Source: Bank of Thailand

—■— Revenue —◆— Expenditure —△— Surplus/deficit (RHS)

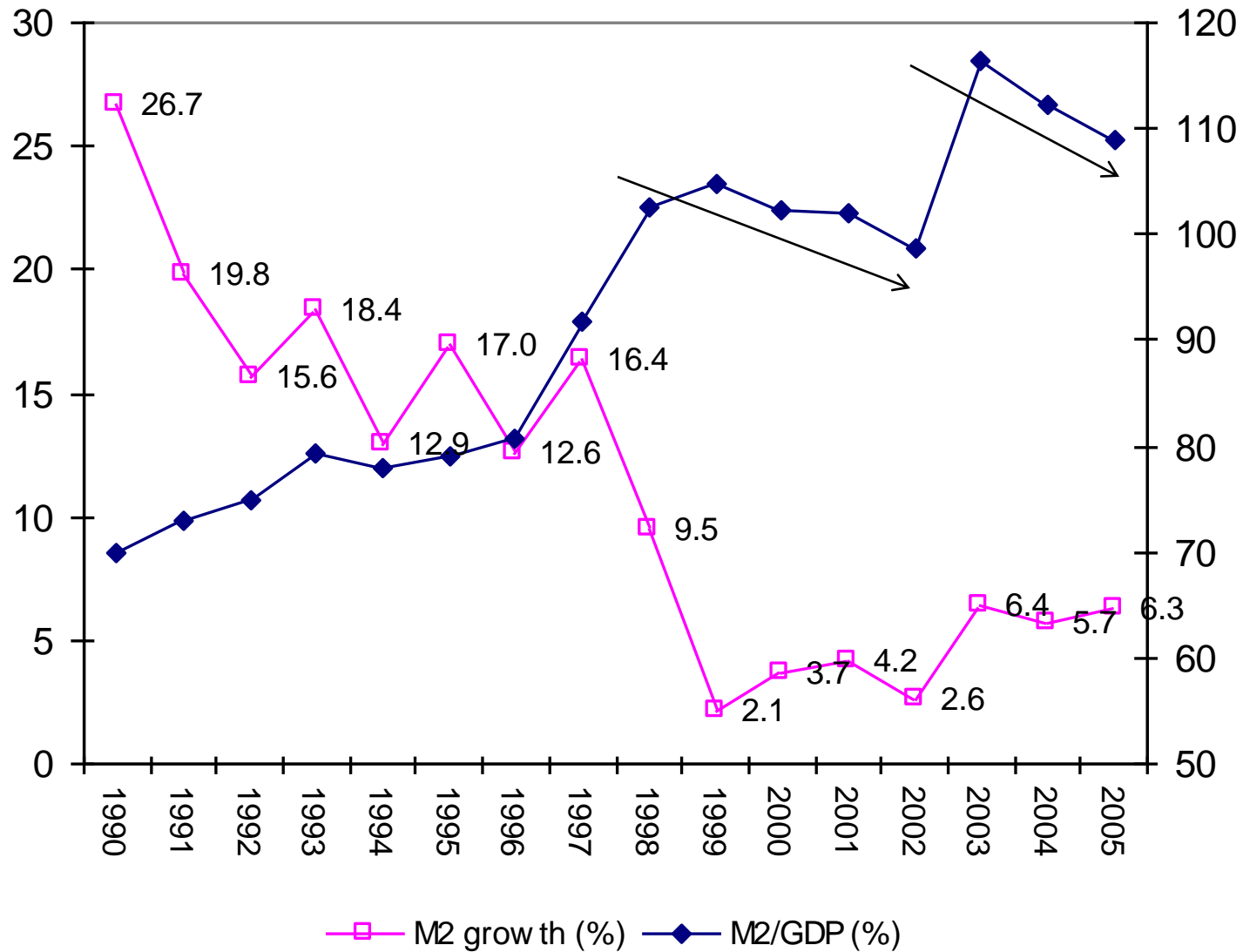
# External debt structure



Source: Bank of Thailand

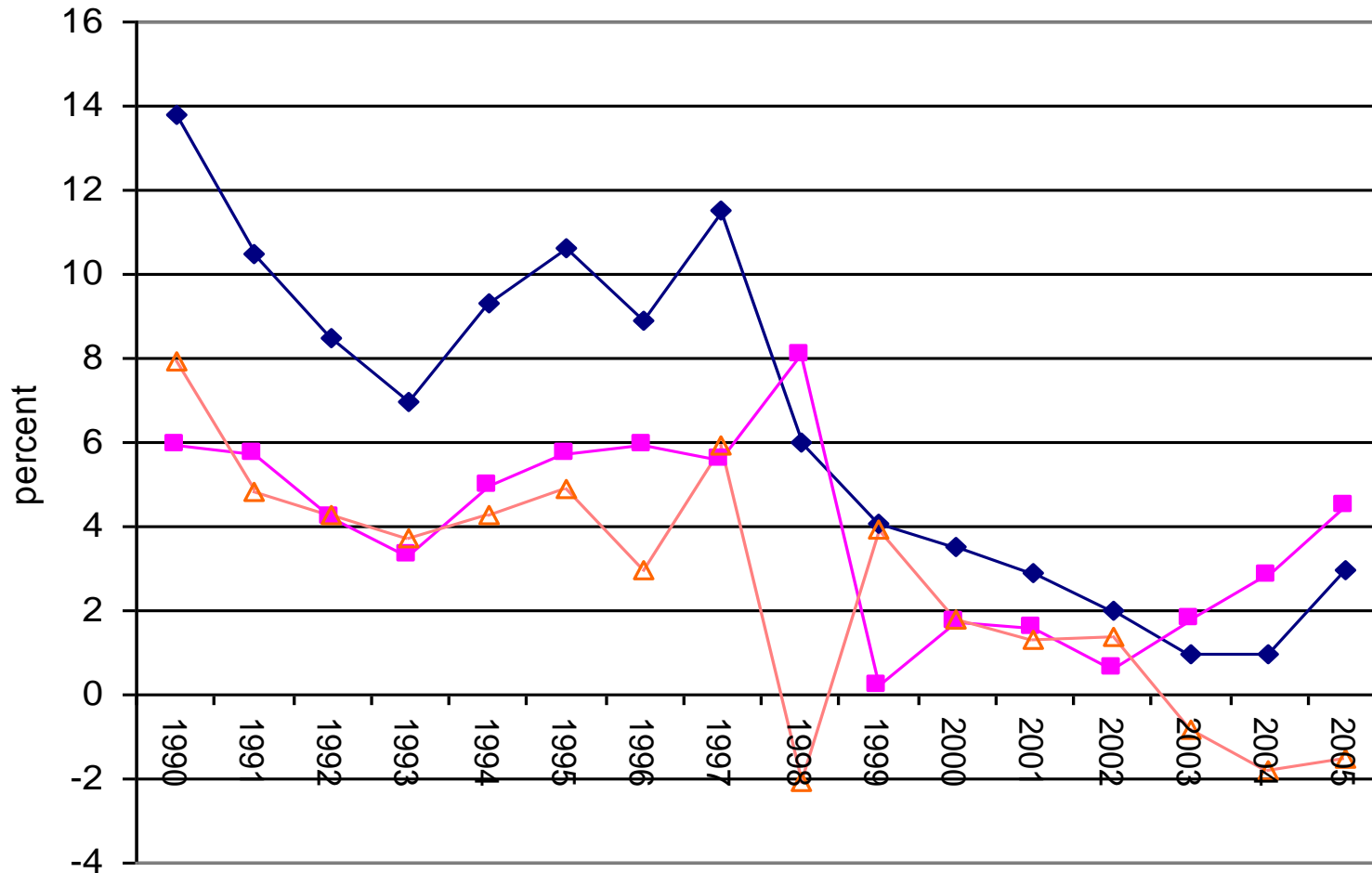
- ◆ External debt (%Gross National Income)
- Long-term Debt (%total debt)
- ▲ Short-term debt (%)
- Debt service ratio

# Monetary growth slowdown



# Incentive for financial savings

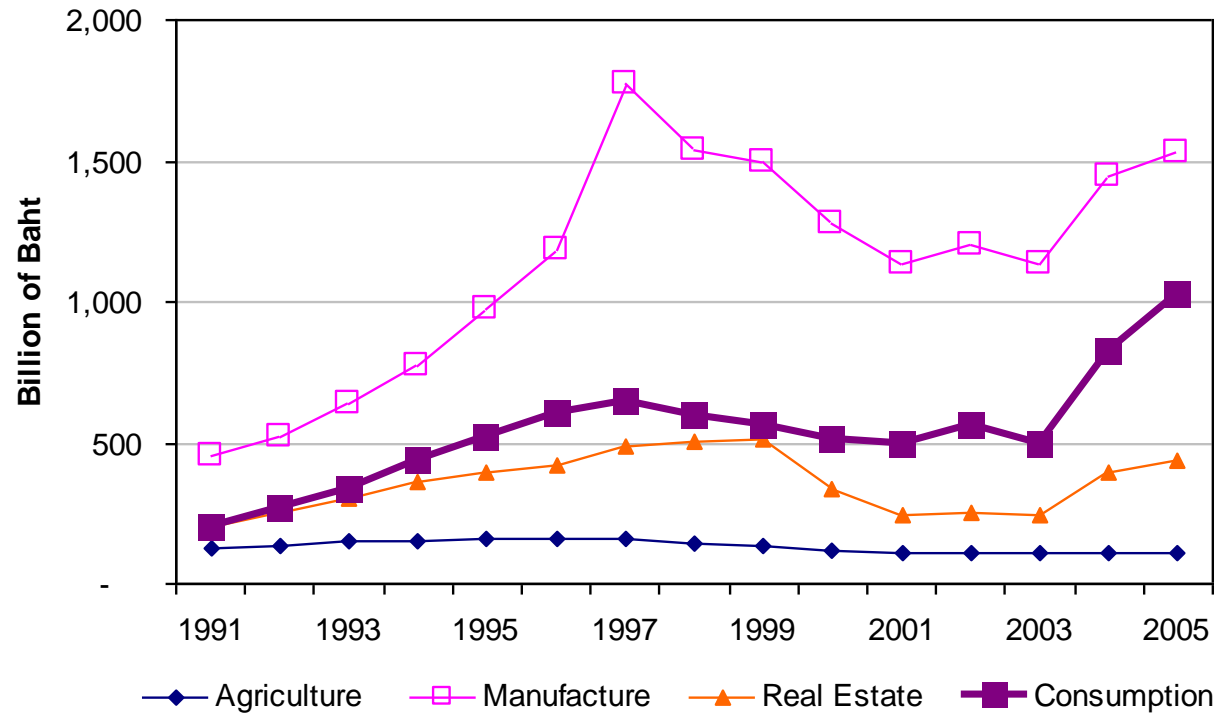
Fisher Effect?



Source: ADB

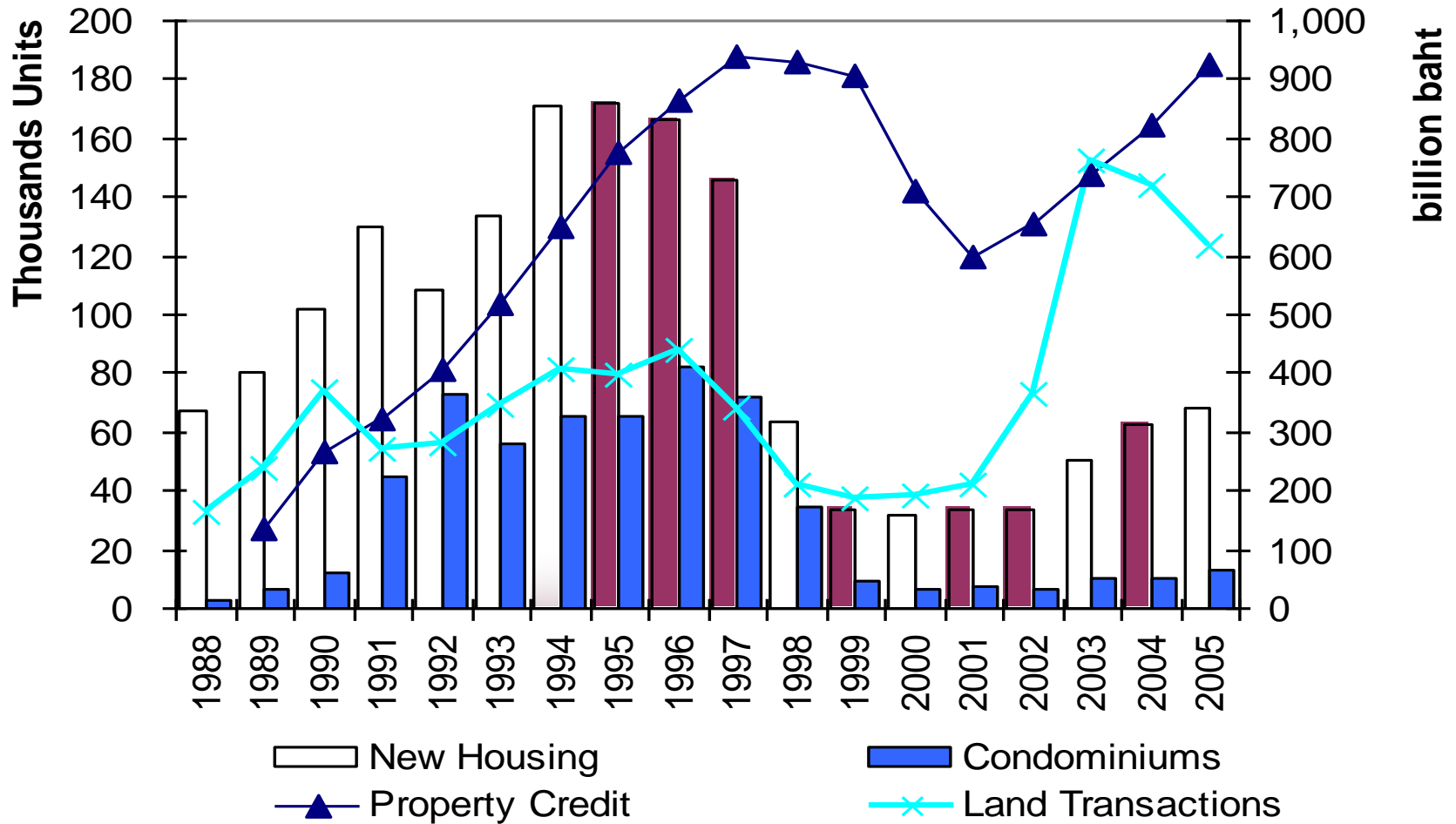
◆ Deposit Interest rate (12 months)    ■ CPI    ▲ Real interest

# Bank loan extension



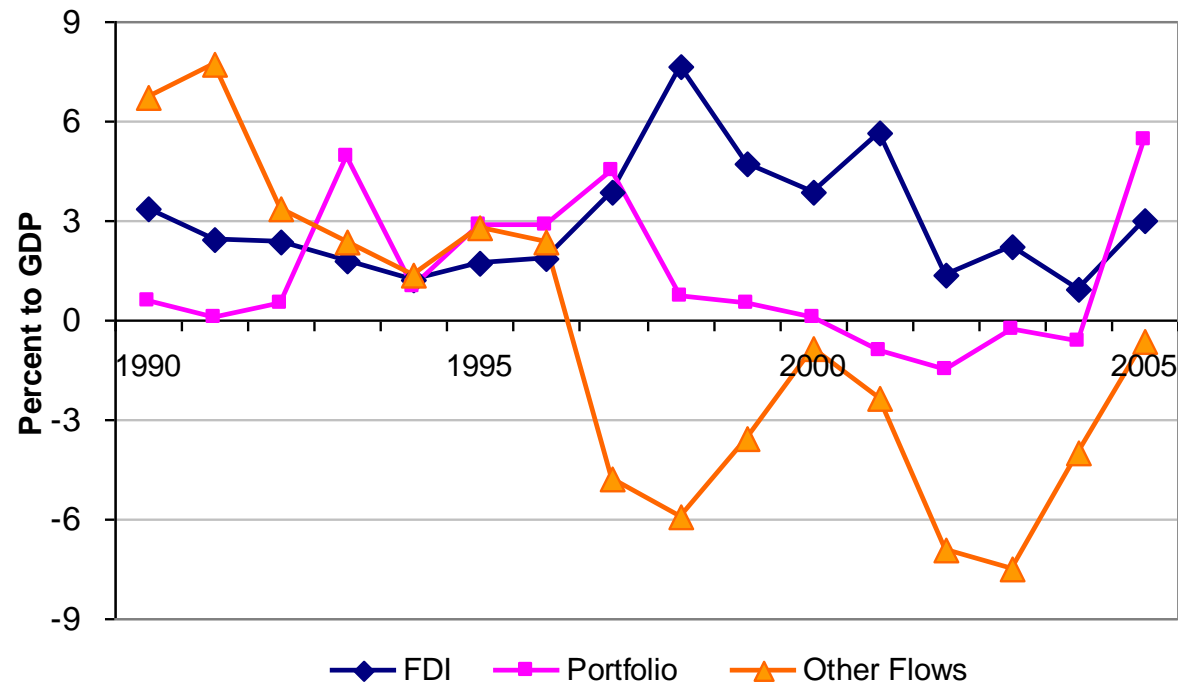
Source: Bank of Thailand

# Property bubble



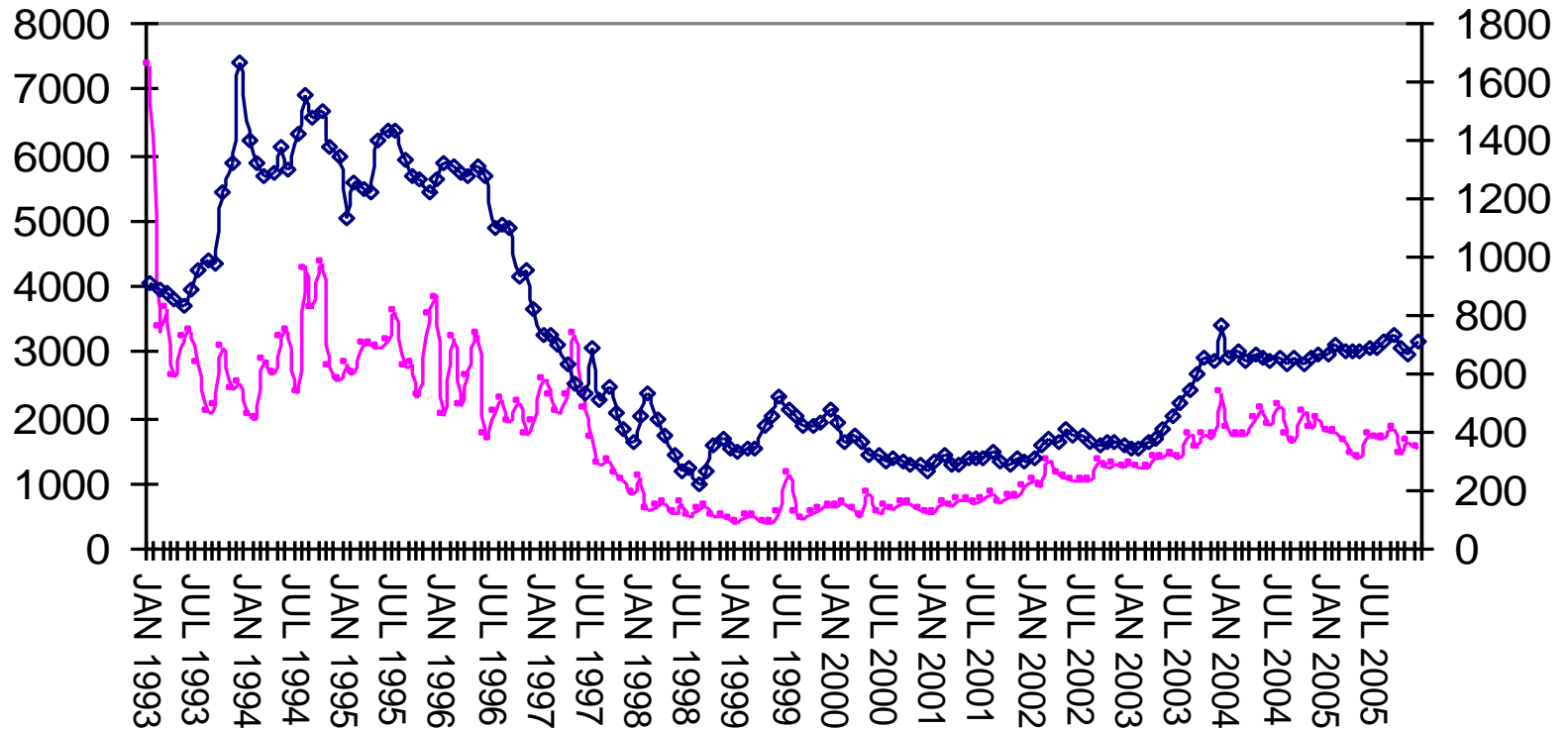
Source: Bank of Thailand

# Hot and cold capital flows



Source: Bank of Thailand

# Property and stock bubbles

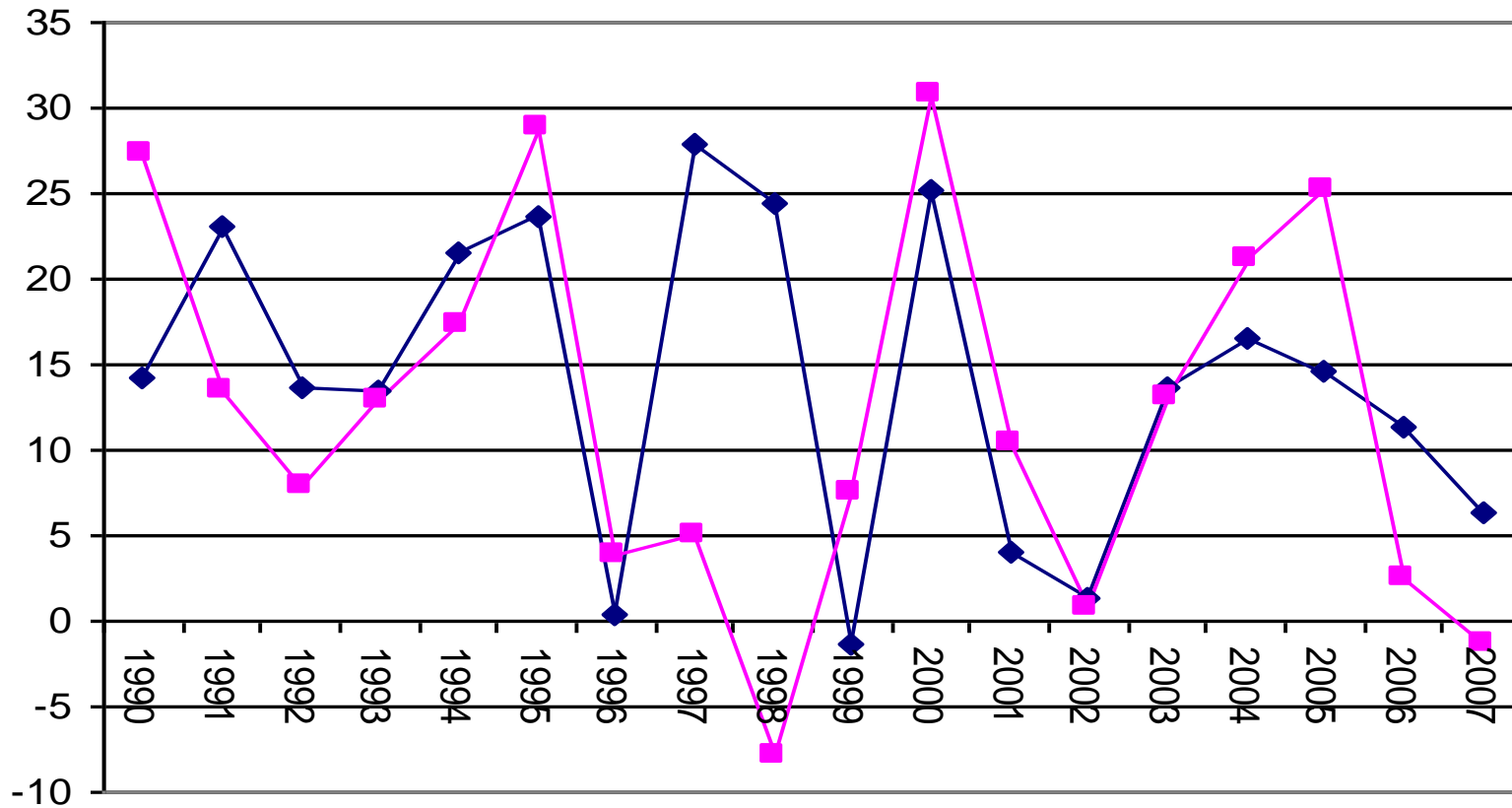


Source: Bank of Thailand

— Construction Areas Permitted in Municipal Zone (1,000 sq.m) — SET Index (RHS)

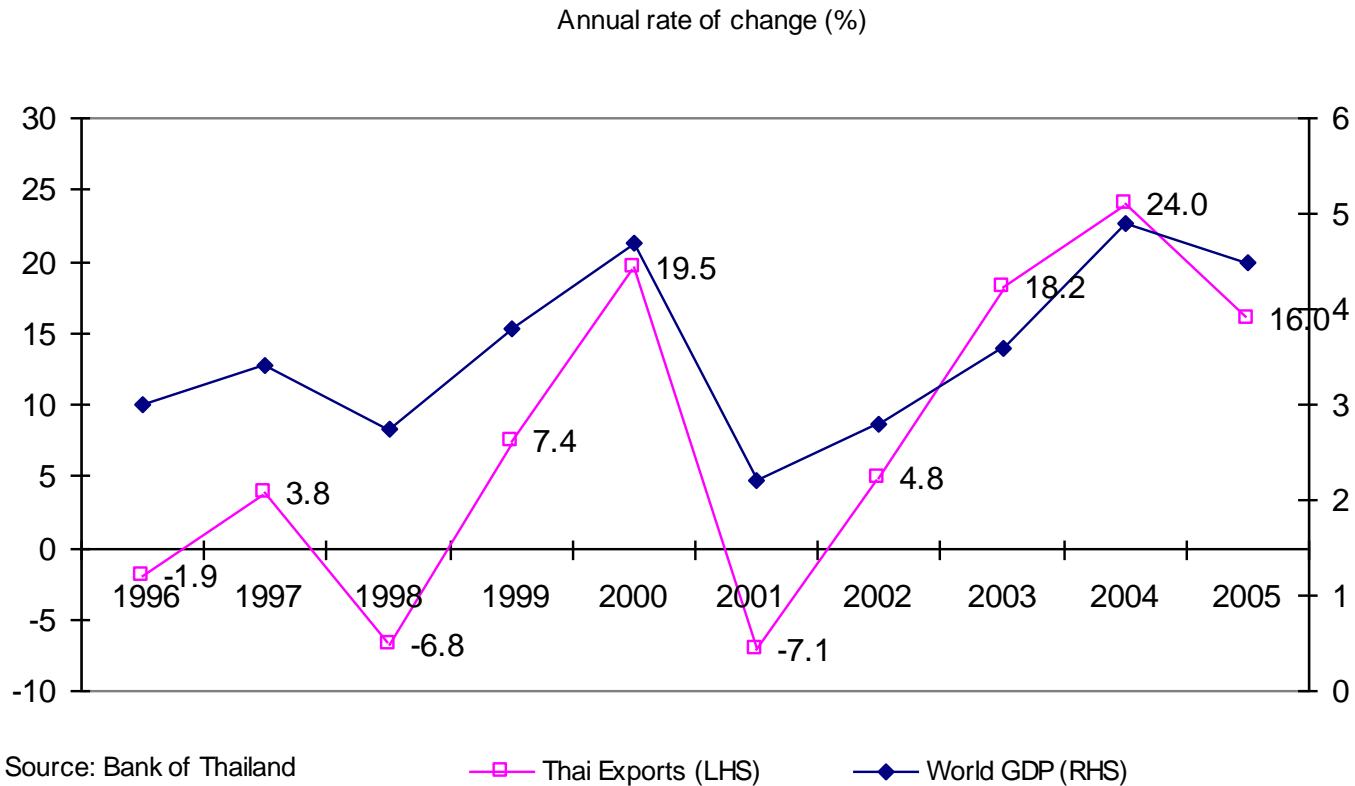
# Co-movements

## Exports and Imports (% change)



Source: Bank of Thailand — Exports — Imports

# Compare and contrast fluctuating effect of world business cycle on the Thai exports: 1990-1995 and 2006-2010



# Conclusions

- Resilience of the Thai economy had been demonstrated after the financial and exchange rate crises in the period 1997-98.
- Realistic exchange rates are the key for successful external imbalance adjustments.
- Fiscal balances and external debts depend on fiscal discipline.
- Capital flows are related to exchange rate movements.
- Asset bubbles are associated with expectations and monetary expansion.
- External influences on the Thai economy increase with the degree of globalization.

# Research questions

- Has the Thai economy become less resilient since 2006?
- Are we experiencing a property and asset bubbles? If so, explain why. If not, why not? Should the Central Bank prick asset bubbles?
- How far can a country rely on domestic demand stimulus?

# Underground economy

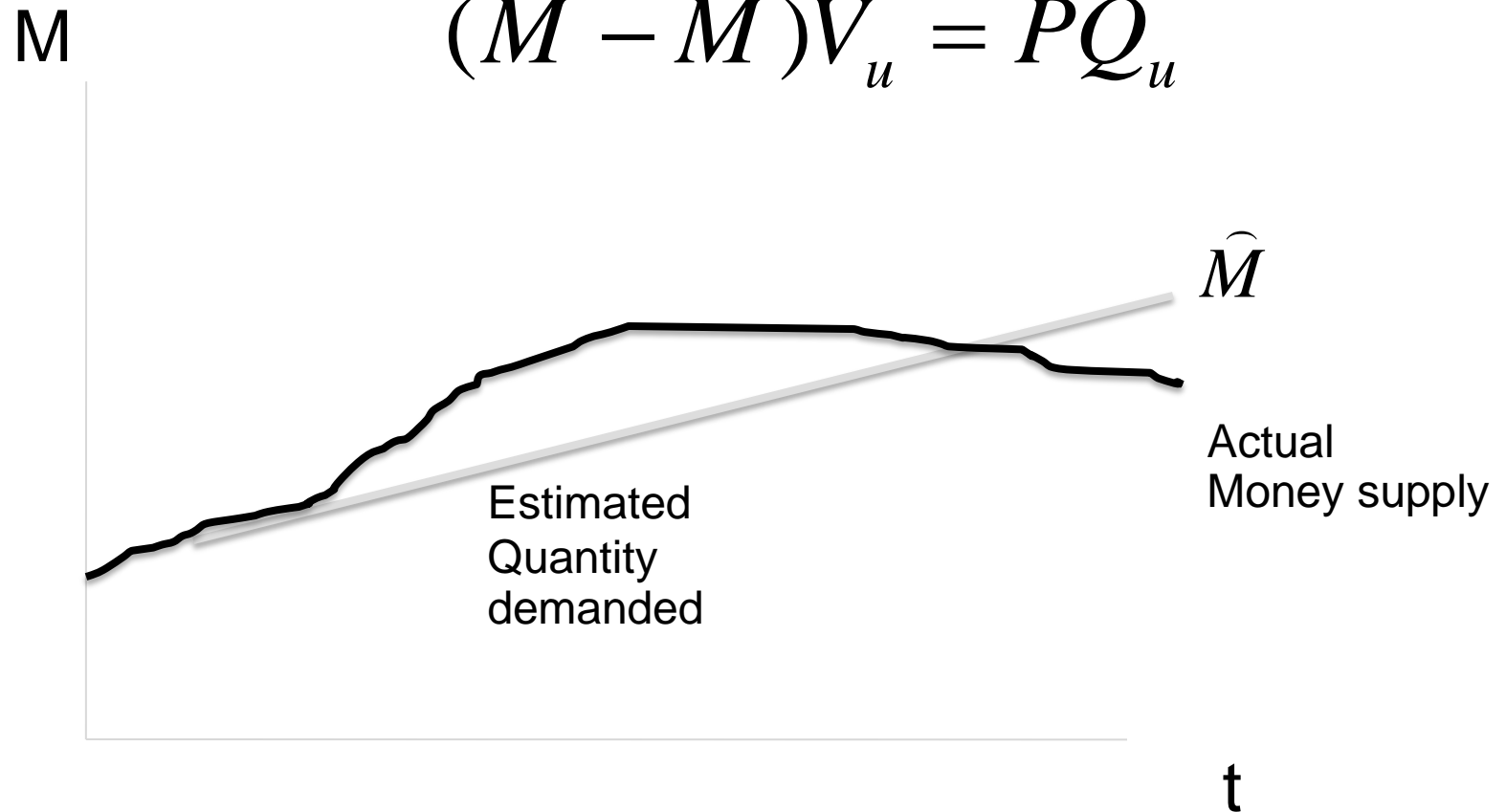
- In the shadow economy (informal sector, or underground), business goes off the books.
- The shadow economy is spreading, including both legally earned income and illicit activities, such as drug dealing, prostitution, and gambling.
- The government knows less about what is really going on in the economy
- The underground economy overstates the actual level of unemployment
- The government has difficulty taxing those earned income.

# Missing quantity of money

- Friedrich Schneider, a professor at Austria's Linz university, estimated unreported activities in **17** rich countries by examining the amount of **unexplained** cash sloshing around the economy.
- The basic assumption is that the shadow economy works on cash, so more unreported transactions mean greater demand for cash.
- Schneider estimated that the shadow economy account for more than one-fifth of GDP in Belgium, Italy and Spain.

$$MV=PQ$$

$$(M - \hat{M})V_u = PQ_u$$

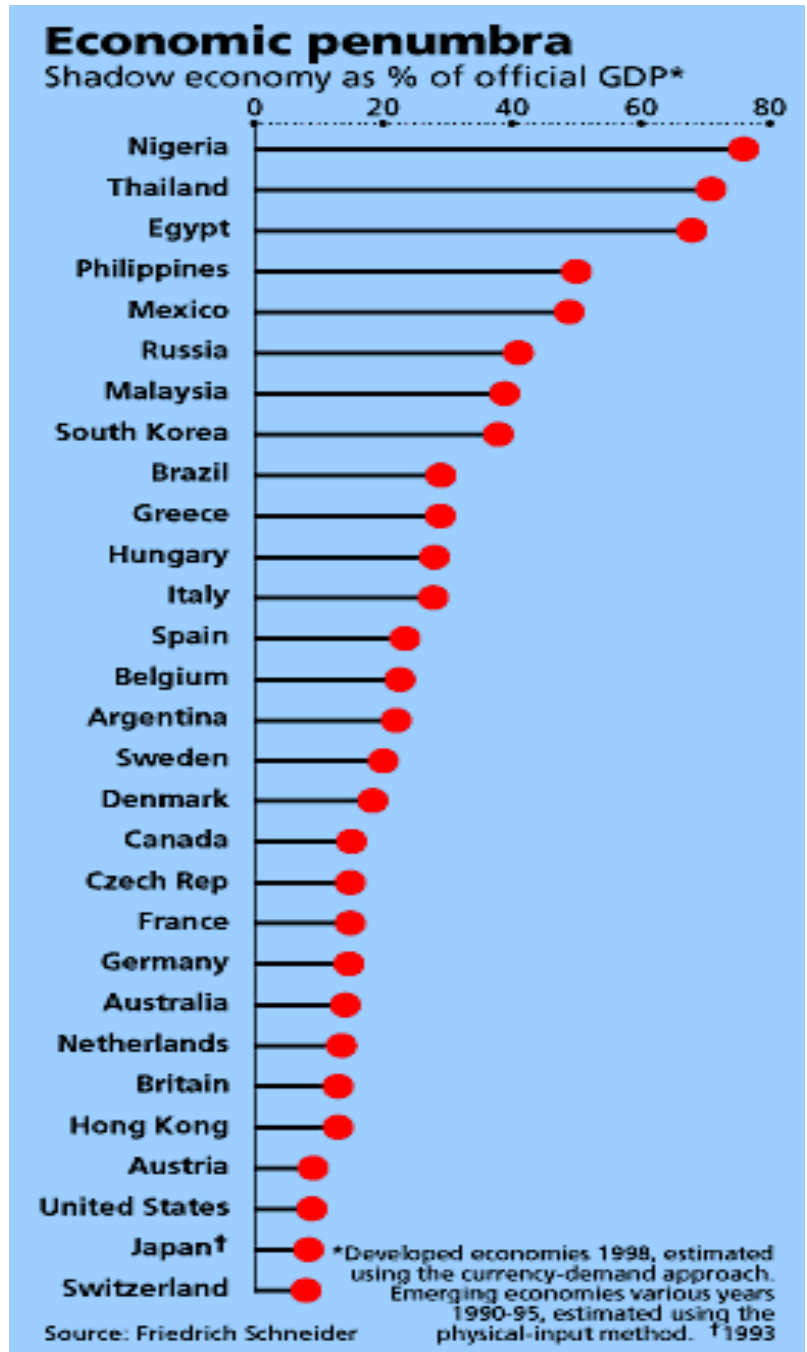


## The size of the underground economy

(% official GDP)

*Emerging economies: 1990-95*

*Developed economies: 1998*



# Tax burden and tax evasion

- Nigeria and Thailand had the world's largest black economies, accounting for more than 70% of official GDP.
- Note that China was excluded from the study.
- The shadow economy is not so much driven by the incentive to evade taxes as by a desire to evade the law. **True, false, or uncertain?**
- **How many Thais pay income tax? How many people pay at the 37% tax bracket and how many percent of total income tax revenue?**

# Cash approach

- Thailand's thriving shadow economy largely consists of crime: gambling, narcotics and the sex industry (according to Prof. Schneider).
- Thailand was ranked ahead of Egypt, Philippines, Mexico, Russia, Malaysia, South Korea, Brazil and Greece.
- Shadow economy in the OECD countries is usually attributed to high taxation and onerous labor regulation.
- In transition economies and LDCs, the driving forces of shadow activities are usually tax and regulation avoidances, corruption, and general distrust by citizens of the political system.

# Substitution or complement to above ground activities ?

- According to Schneider, the underground economy would mark a turnaround in its fortunes after nearly a decade of decline.
- He estimated the value-added of the shadow economy in 21 of the 30 OECD countries.
- On average, it was equivalent to 16.8% of GDP in 1999.
- By 2008 that figure had fallen to 13.3%.
- In 2009 he forecast it would rise to 14%.
- Is there any relationship between GDP growth and the size of the underground economy? Will the underground economy in Thailand expand or contract in 2014?

# Discussion questions

- In his recent study, Mr. Schneider's calculations exclude illegal activities.
- The size of the underground economy is equivalent to less than 8% of GDP in the United States, whereas in Greece it reaches 25% and in Italy 22%.

Source: The Economist, April 2, 2009

*Thailand's underground economy expands during recession and contracts during recovery (True, false, or Uncertain?)*