

Buffeting by the Unholy Trinity

Thailand's Military Coup in 2006 and 2014

Bhanupong

Lecture 7

Asian Economic Papers 5(2), 2006

The Thai Economy after the 2006 coup

outline

- The 2004 Avian Influenza
- The 2005 Asian tsunami
- The third oil price shock in 2005
- The 2006 military coup
- Tanks versus hospitals
- Bangkok shutdown January 2014
- The latest coup: May 2014

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

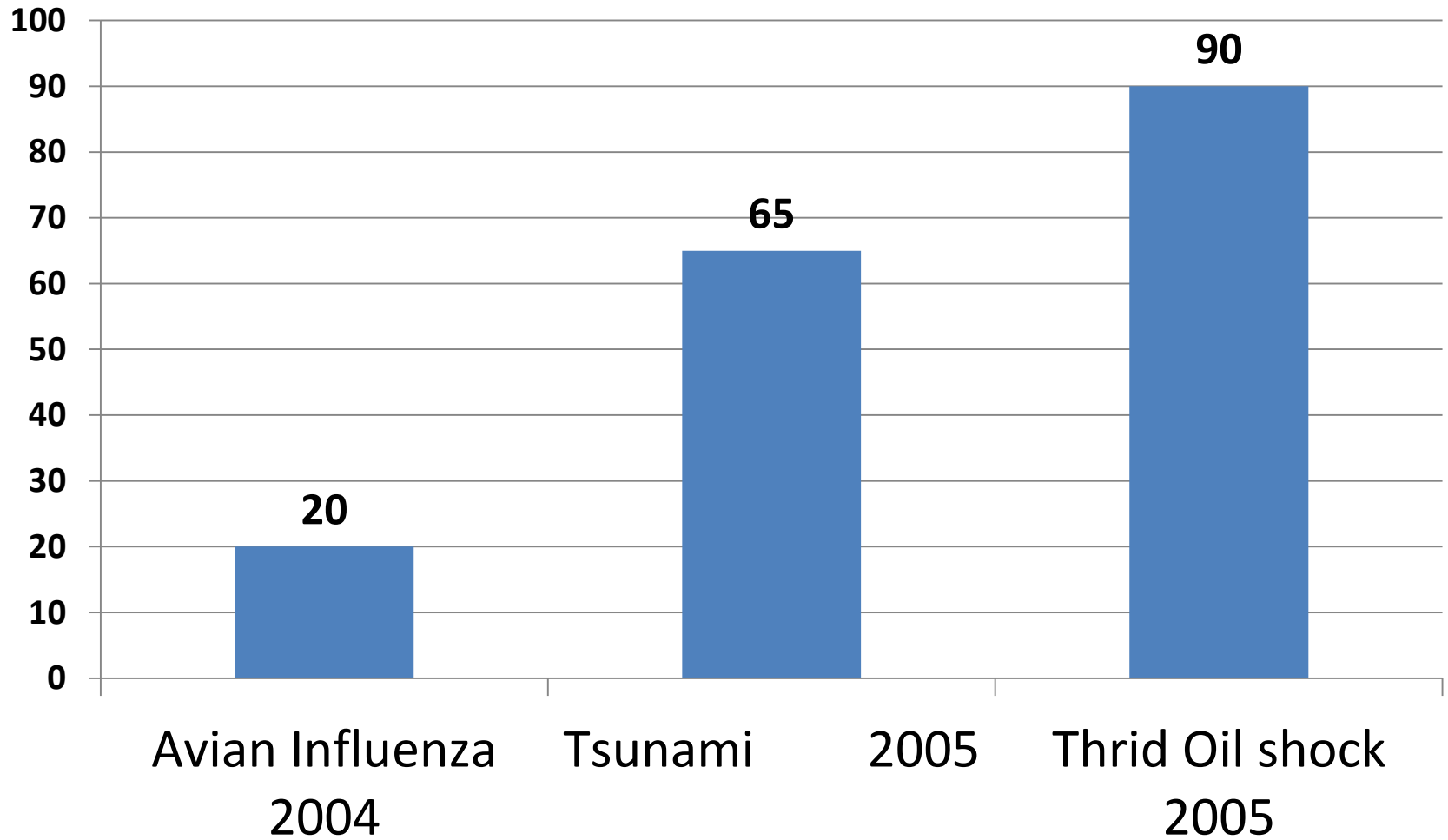
Buffeting of Thailand

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.

**Unholy Trinity: Financial damage
(billion baht)**





Bird flu (AI)

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

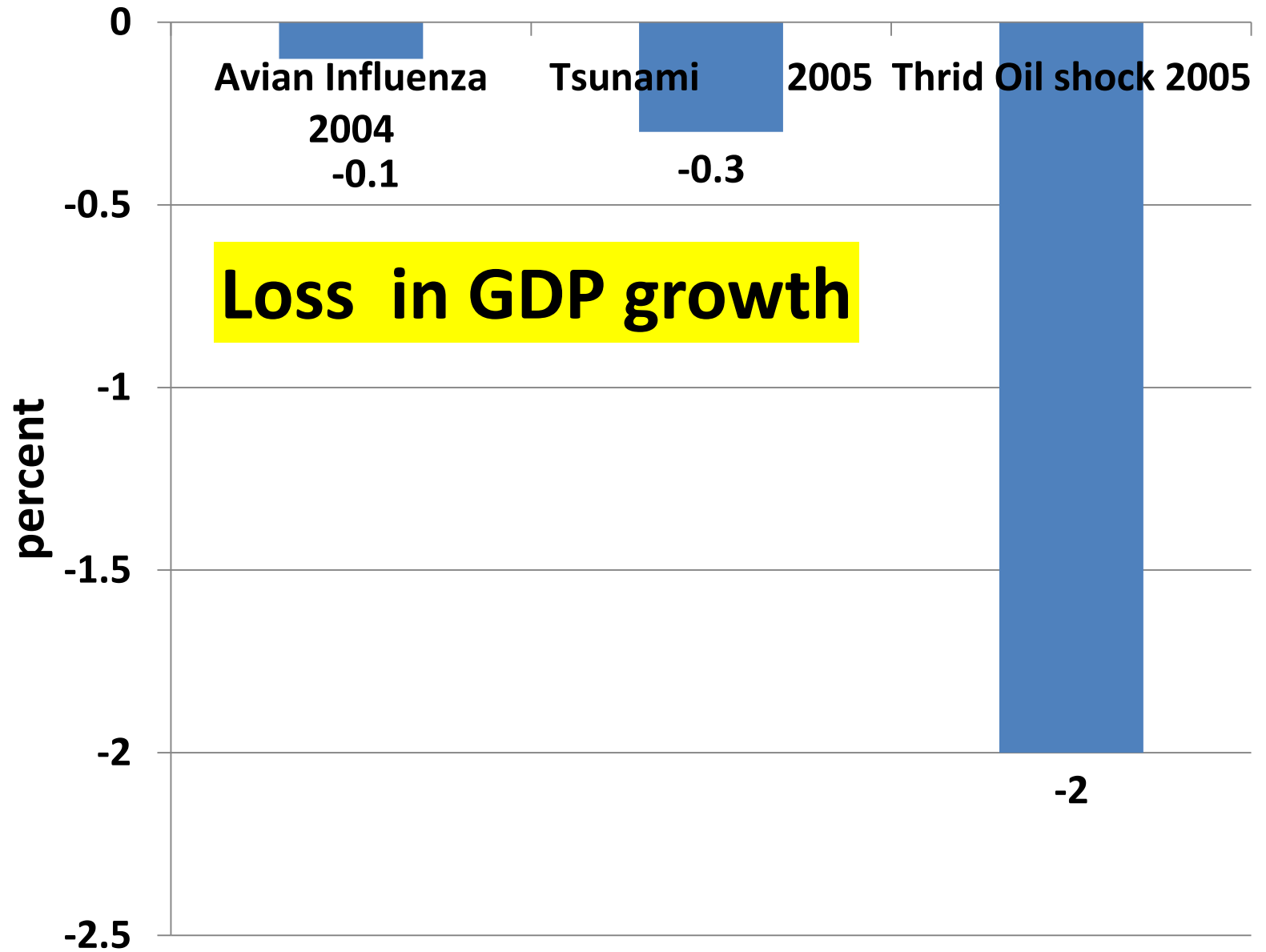
The Thai poultry industry had just recovered from the loss of Generalized System of Preferences (GSP) status in Europe in 1999 and the import ban on Thai chicken in 2002 resulting from the detection of antibiotic residues.

The damage from the bird flu

The spread of 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



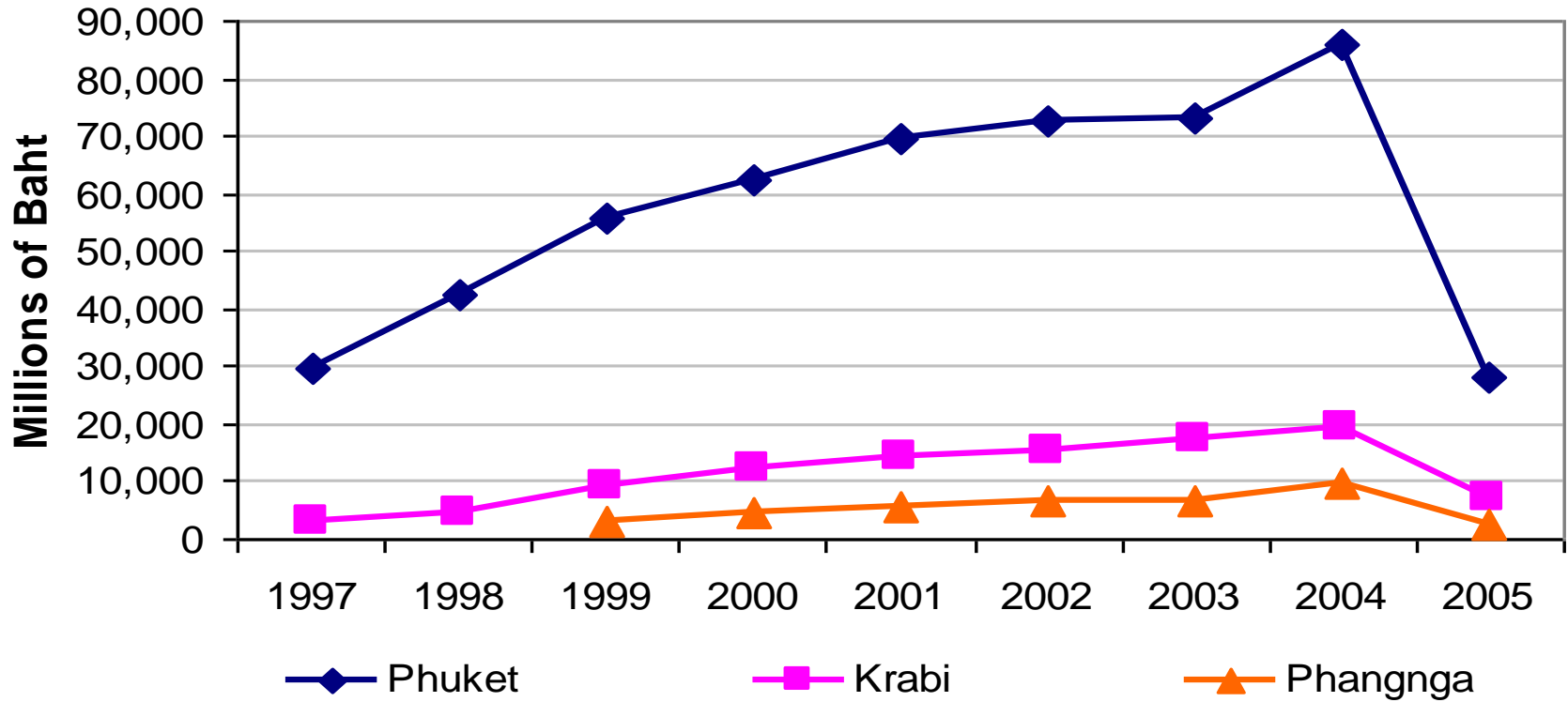
December 26, 2004: 5,394 dead



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



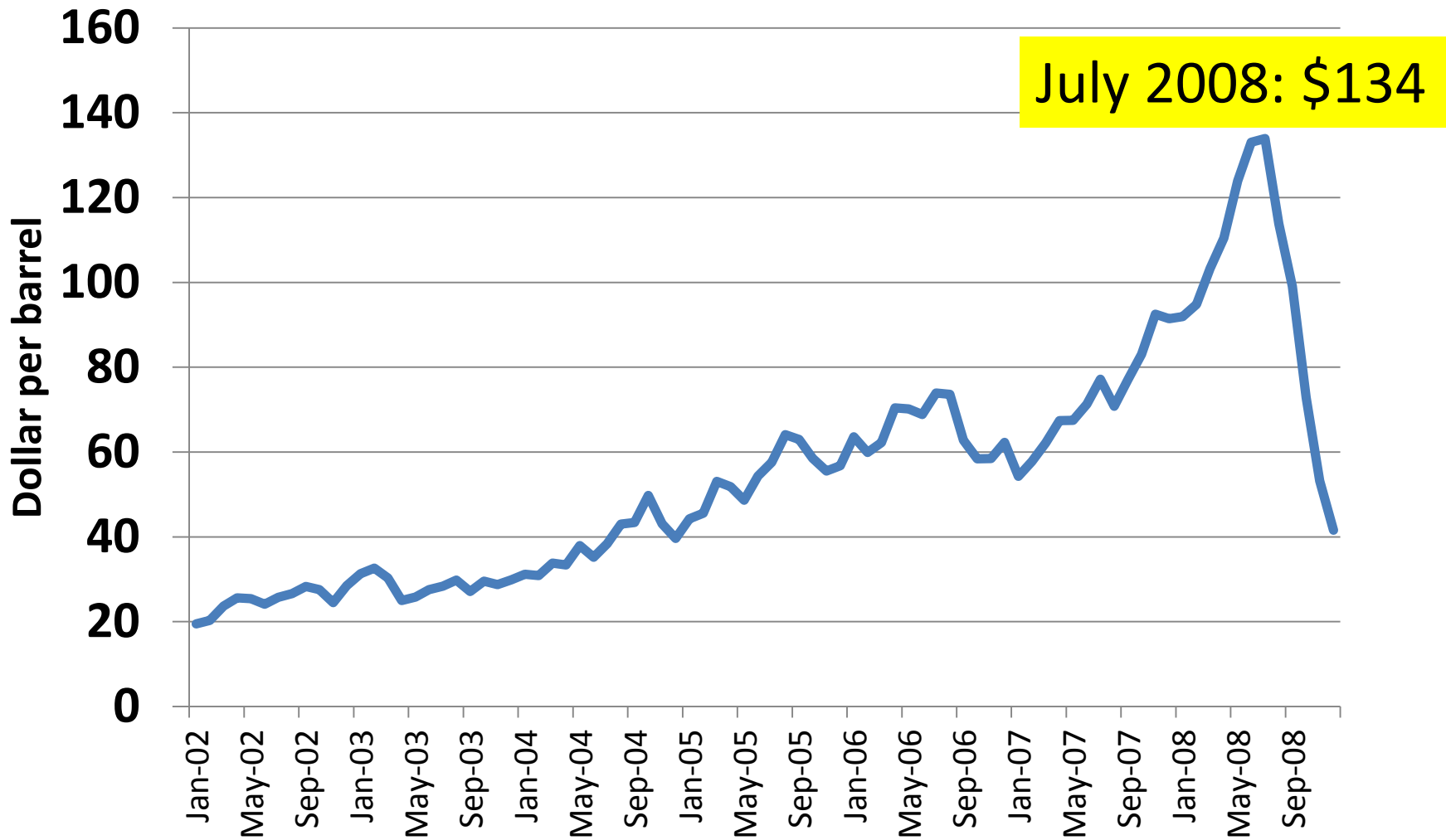
Source: Tourism Authority of Thailand

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 third oil price shock

Crude oil price (Brent)



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.
- 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

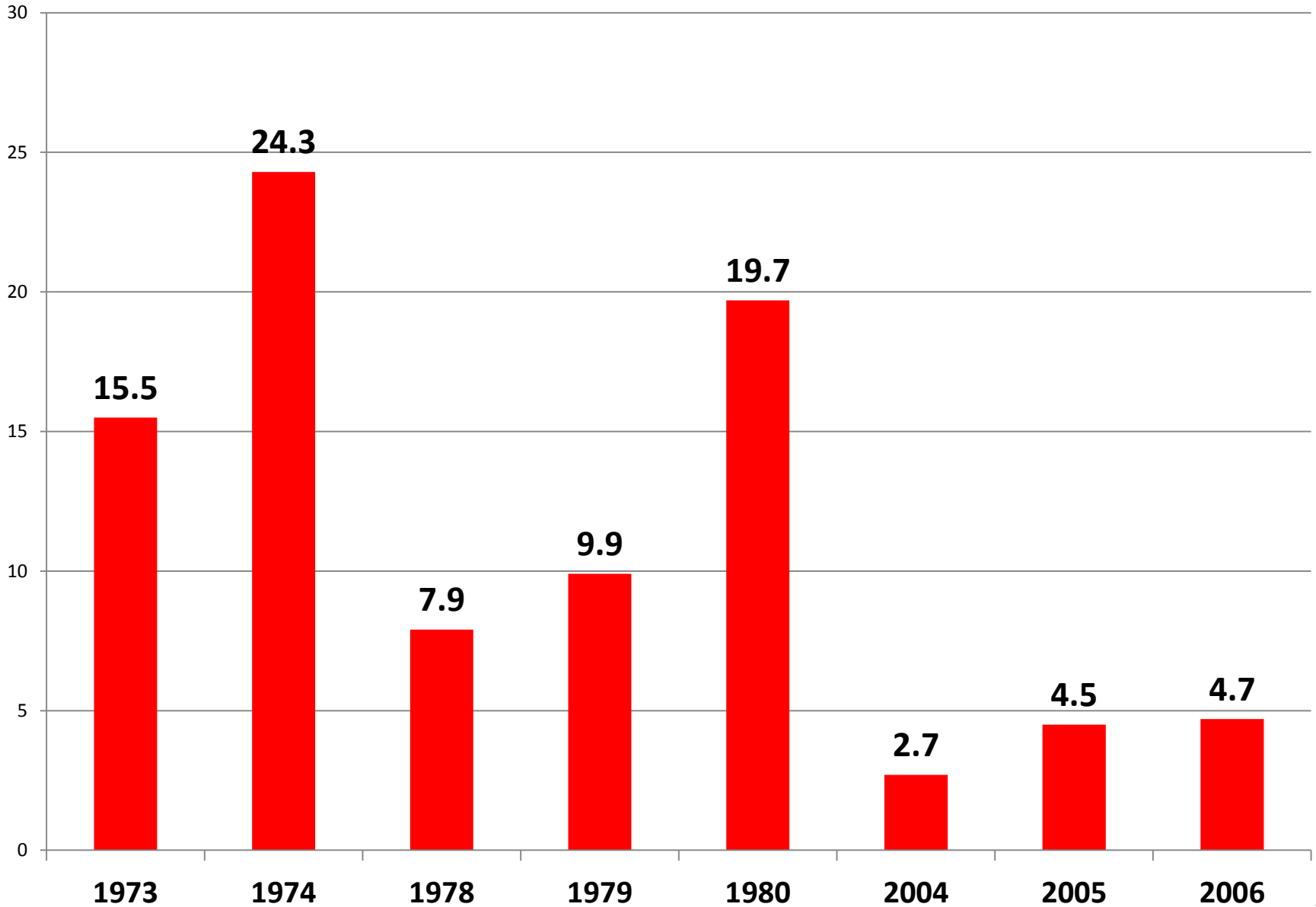
Three oil price shocks in comparison

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

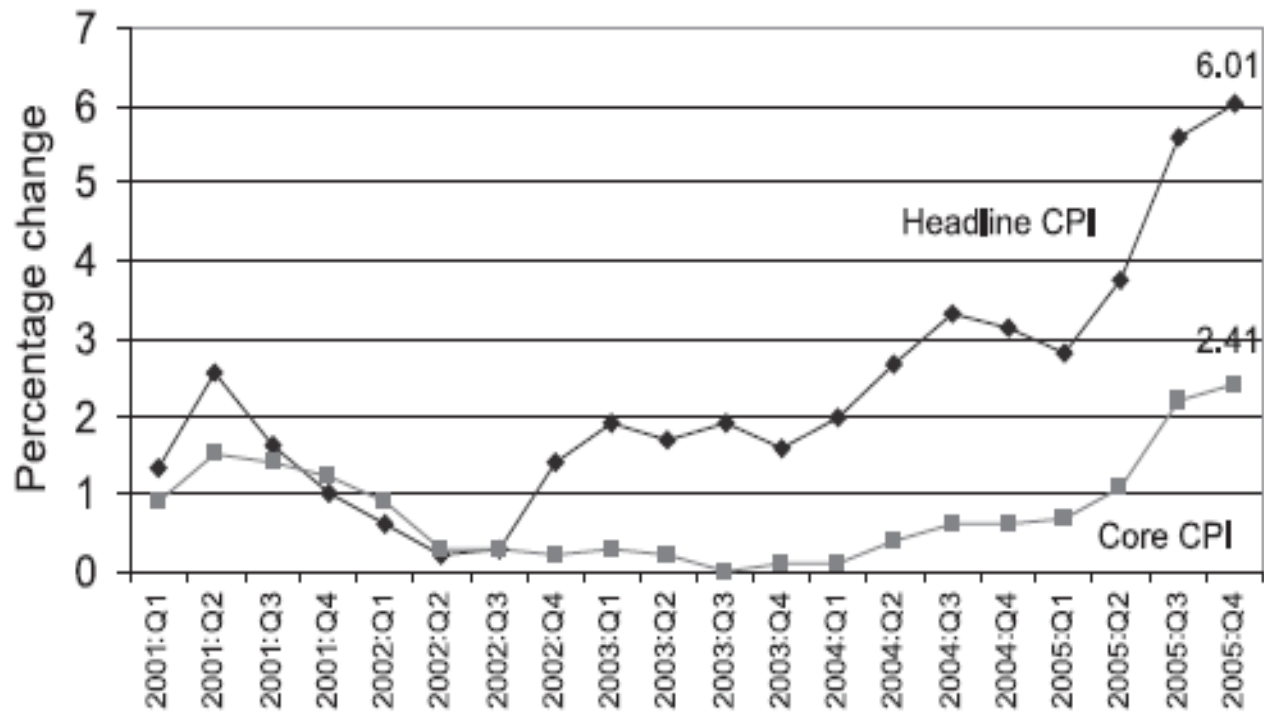
Sources: Bank of Thailand, International Monetary Fund.

inflation edged up after three oil shocks



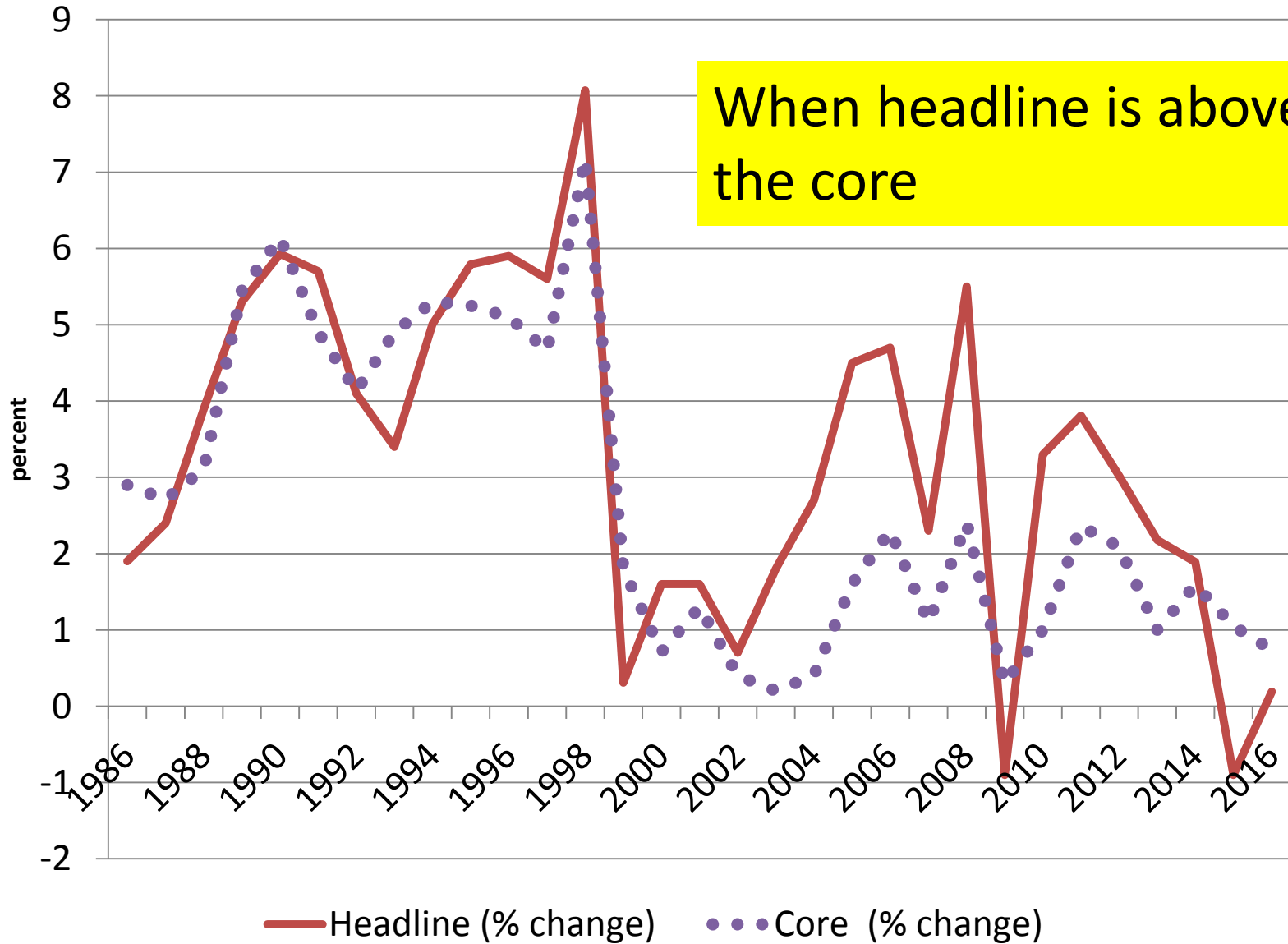
Core vs. headline inflation 2001-2005

Figure 4. Inflationary impact of the third oil price shock

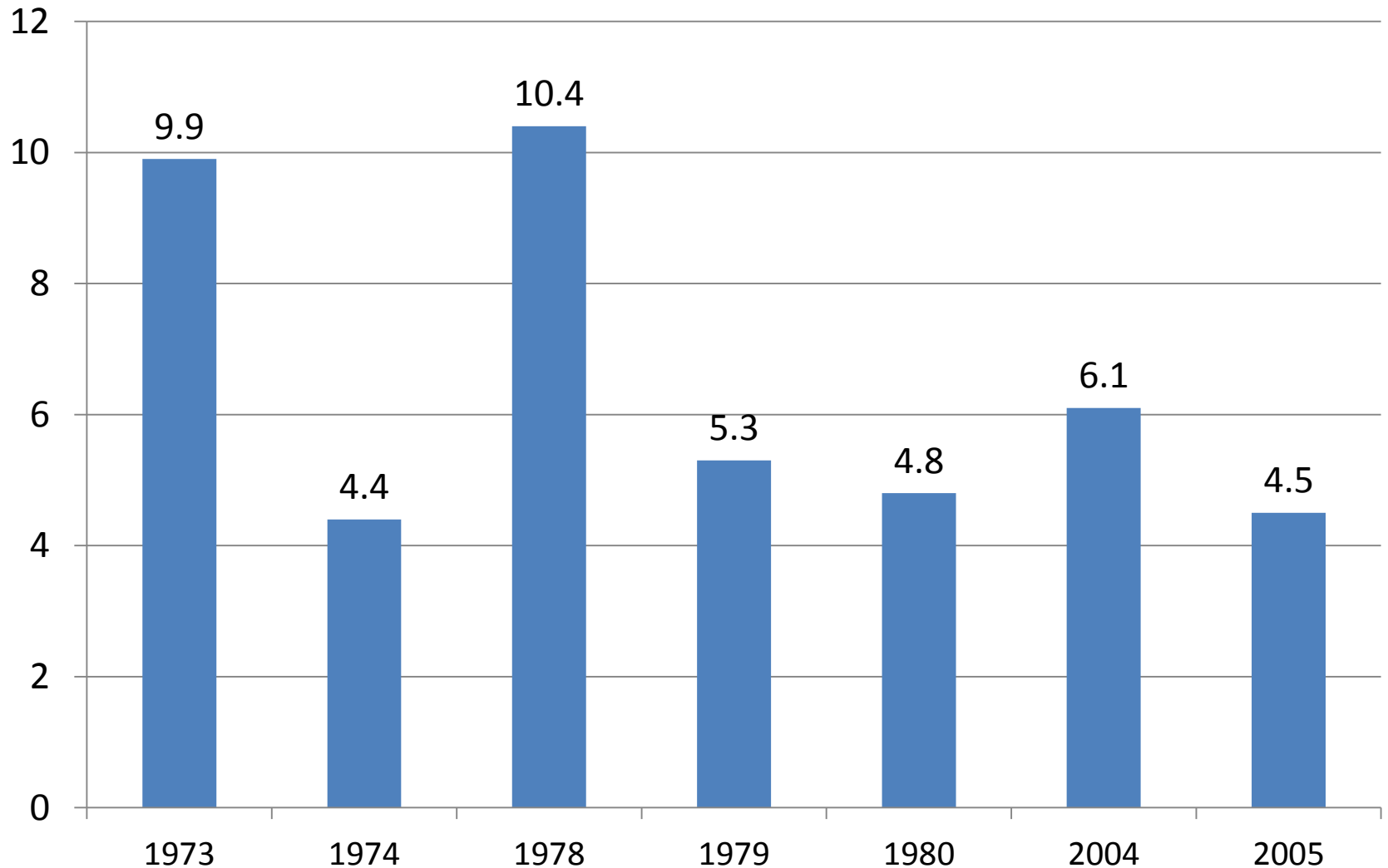


Source: Bank of Thailand.

Core and Headline during the oil shock



GDP growth slowdown after the oil shocks

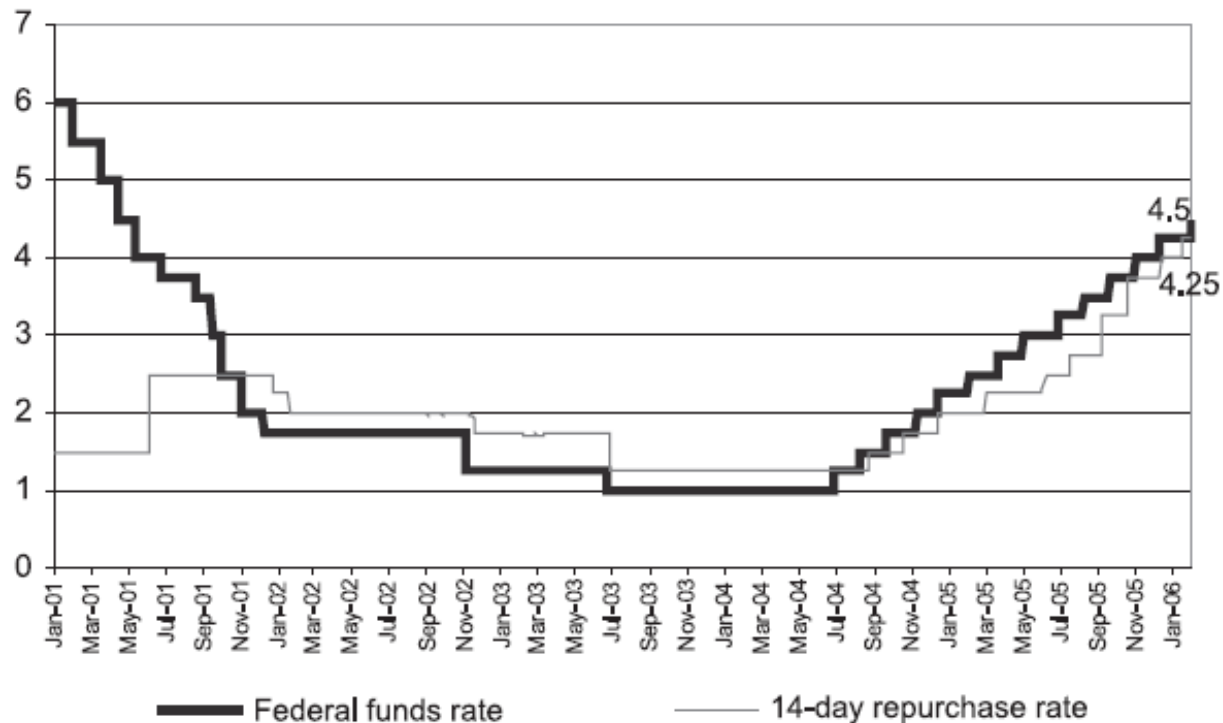


A text-book version of monetary policy response to oil shocks

- Expansionary monetary policy: interest cut
- Why didn't it lead to higher inflation?
- Oil price subsidy and price controls subdued inflationary expectations.

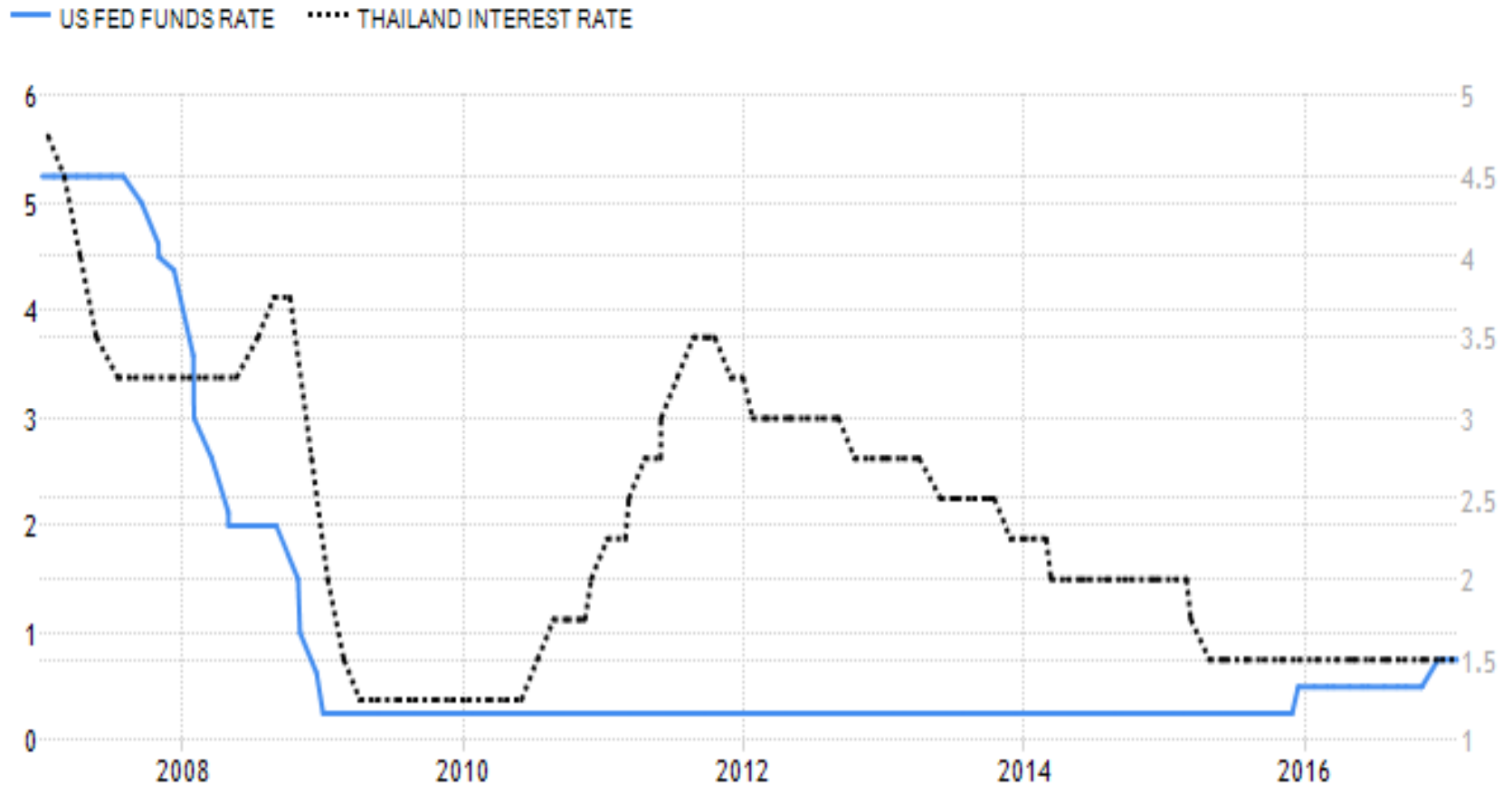
Gradual approach to interest rate adjustments: Follow the Fed

Figure 6. Federal funds and repurchase rates



Sources: Bank of Thailand, Federal Reserve.

Following the Fed?



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

A vicious cycle

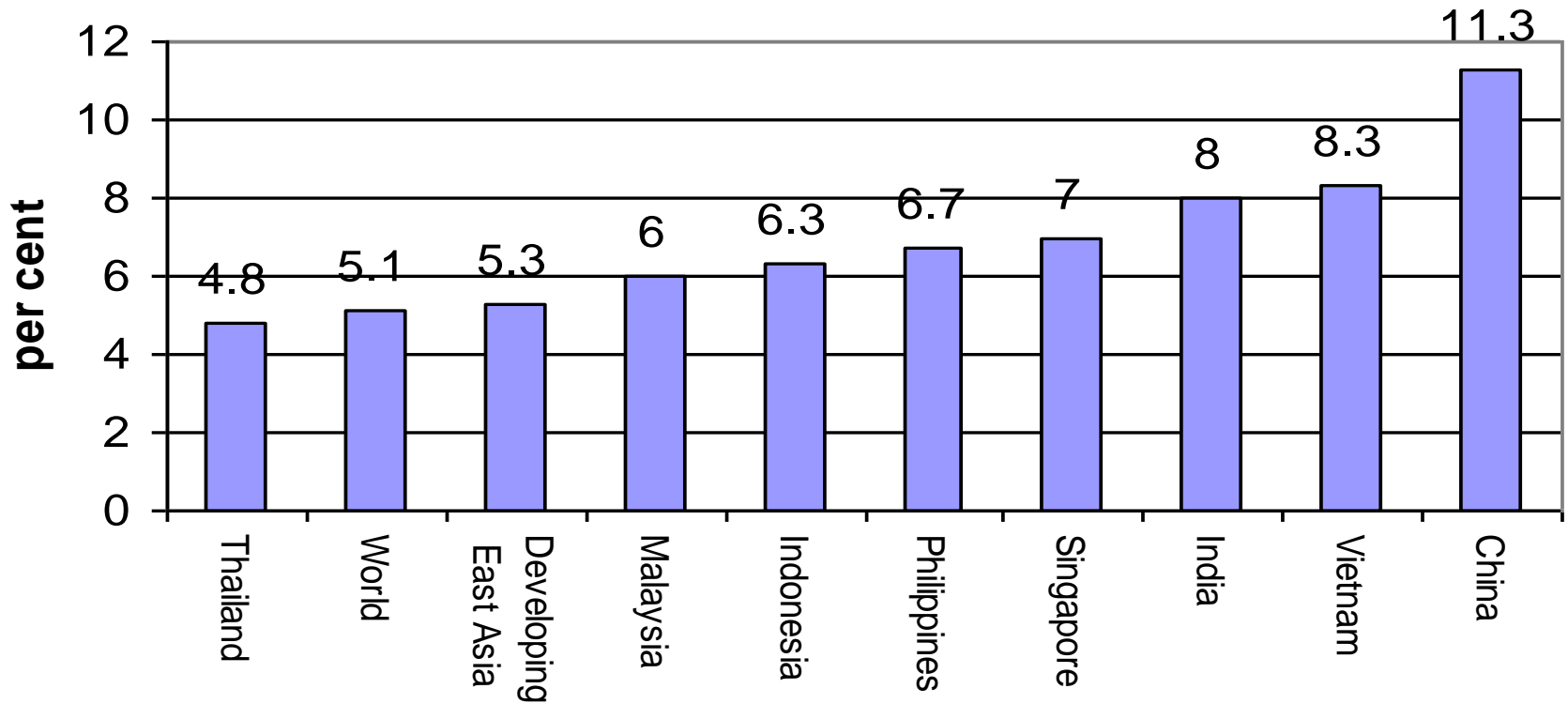
And we thought that we had seen the last coup in 1991

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

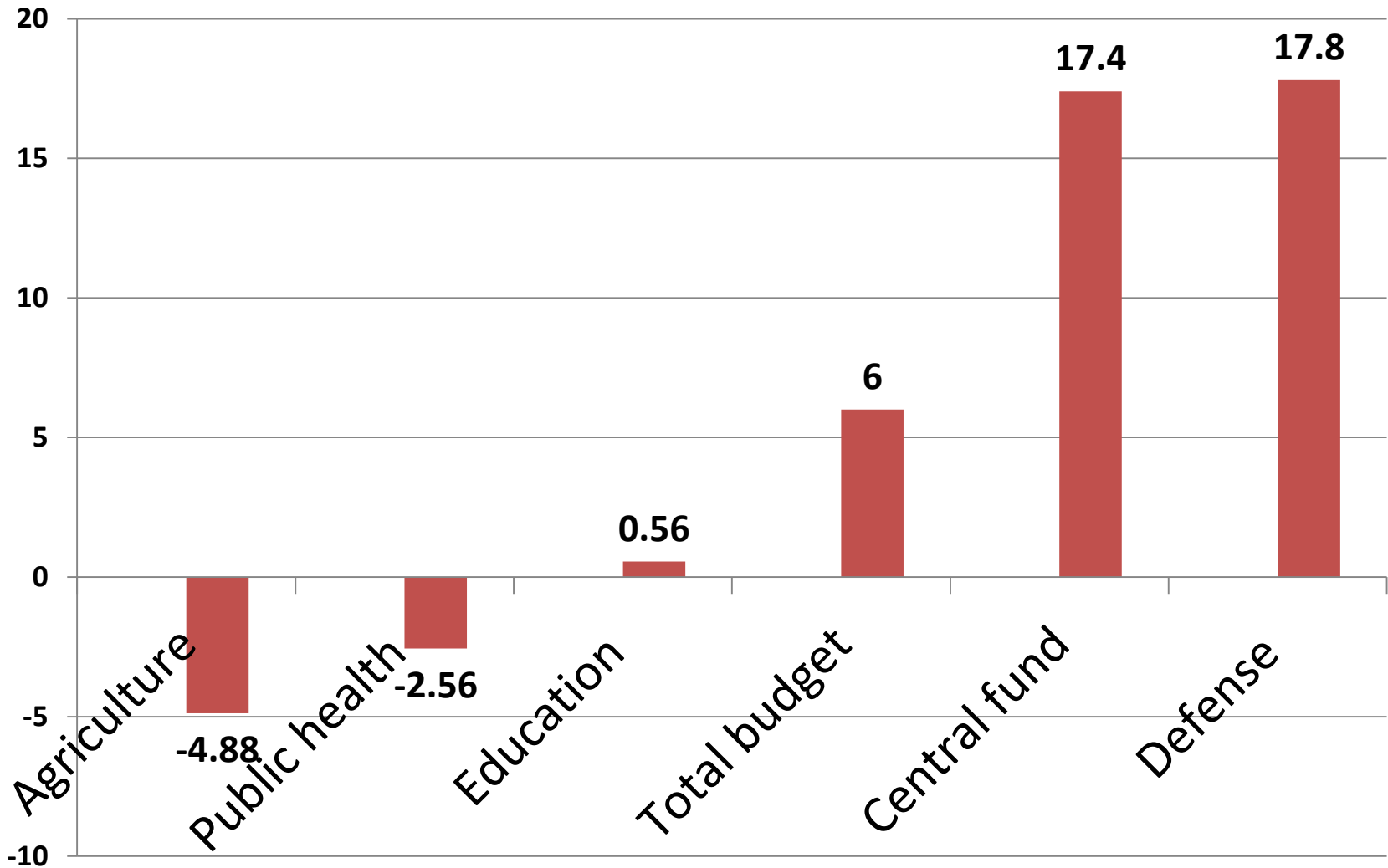
Anan, Chuan, Banharn, Chawalit, Chuan, and Thaksin

The high cost of the 2006 coup

Comparison of Growth in 2007



Percentage Change in fiscal budget in FY 2008/2007



Defense spending vs. health capital investment

- Determinants of military spending: external and civil wars, military spending by potential enemies, population, and democracy.
- Democracy is negatively related to military burden.
- Cross-country evidence shows a negative impact of military spending on economic performance.

Grossman, Michael (1972)

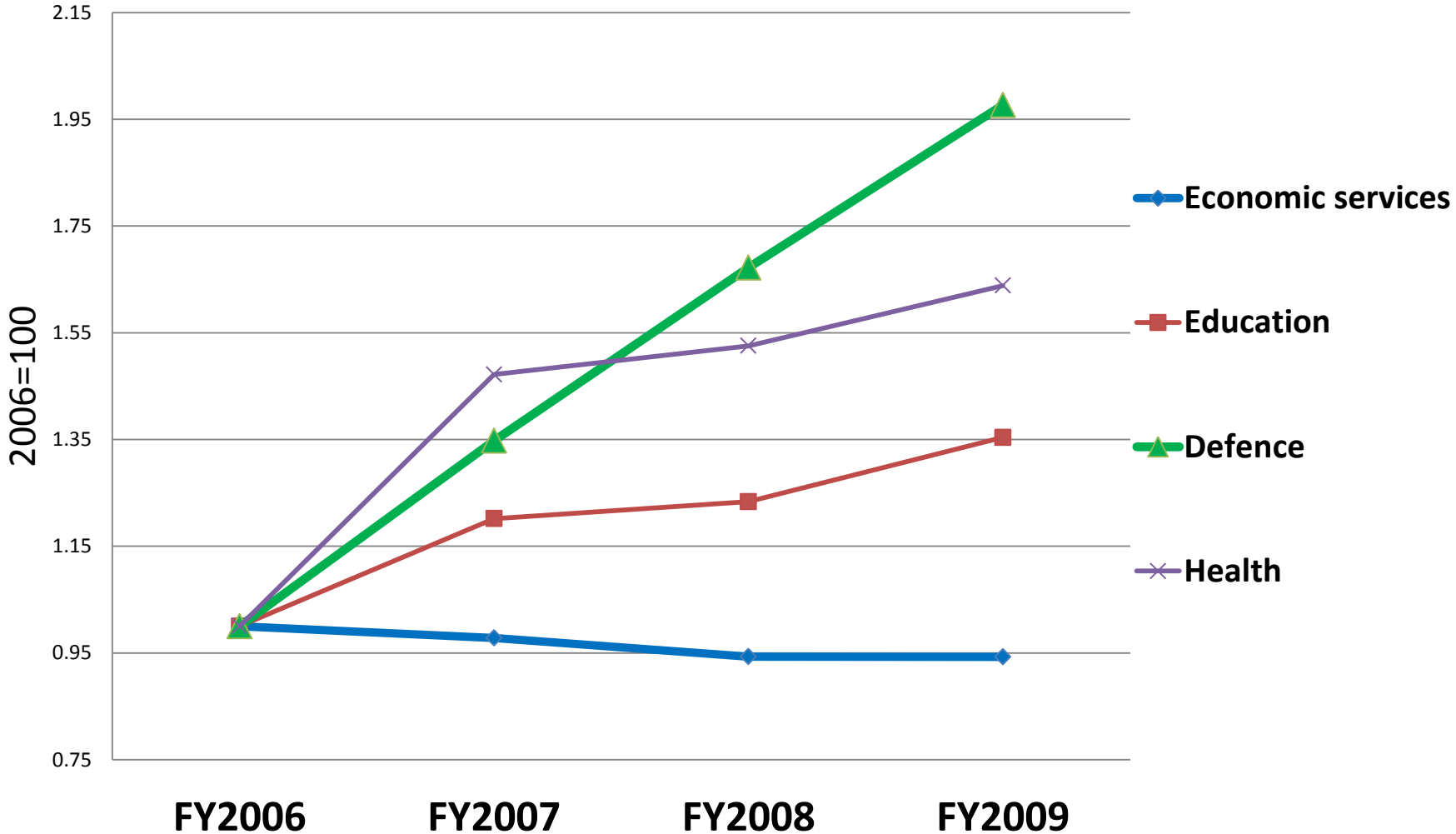
*“On the concept of **health capital** and the demand for health”*

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.

Government Budget appropriation after the 2006 military coup

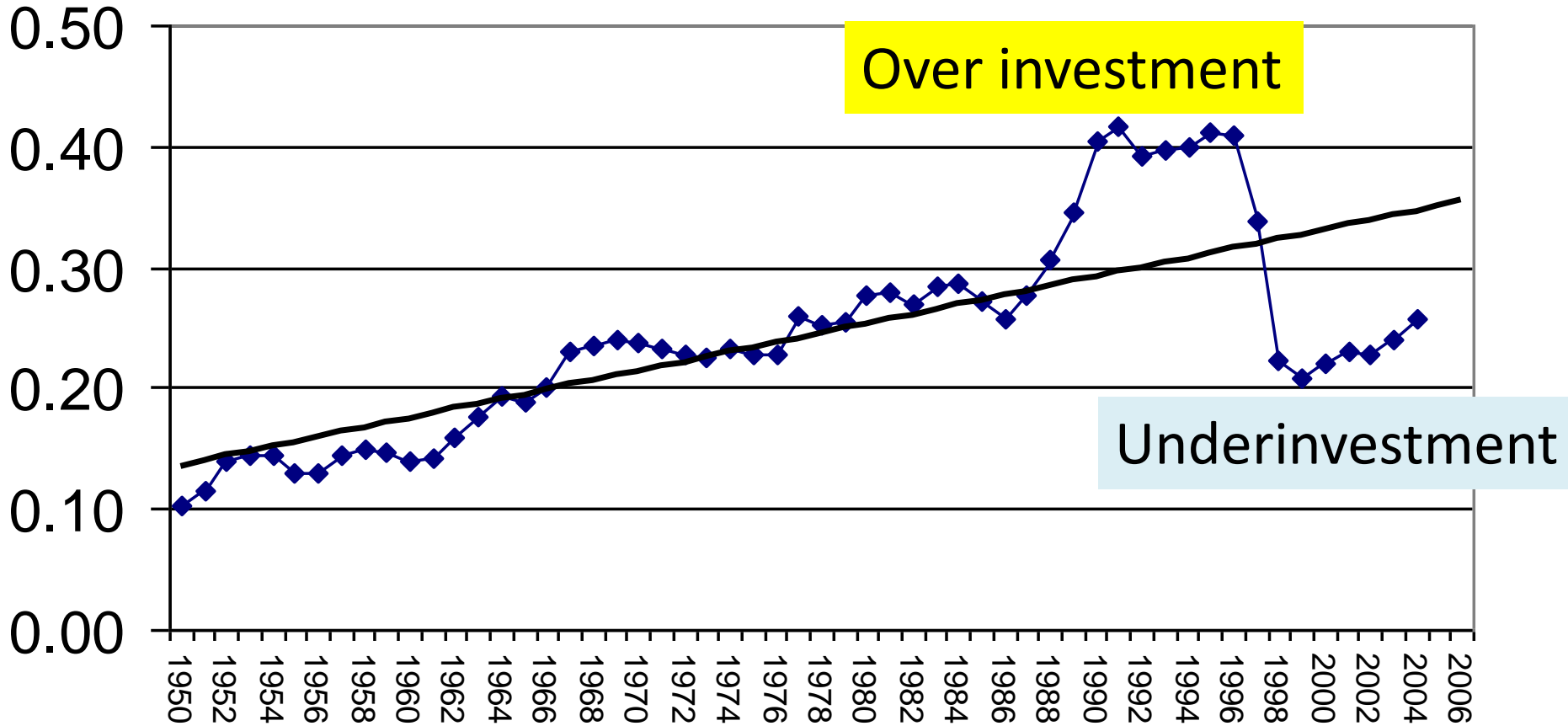
Source: BOB



Thailand's perennial problems

- Exchange rate risks
- Fluctuations of the world economy
- Weak governing institutions: Absence of the rule of law
- Military and judicial coups threat and political disturbances
- Southern violence

Share of investment in GDP



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

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

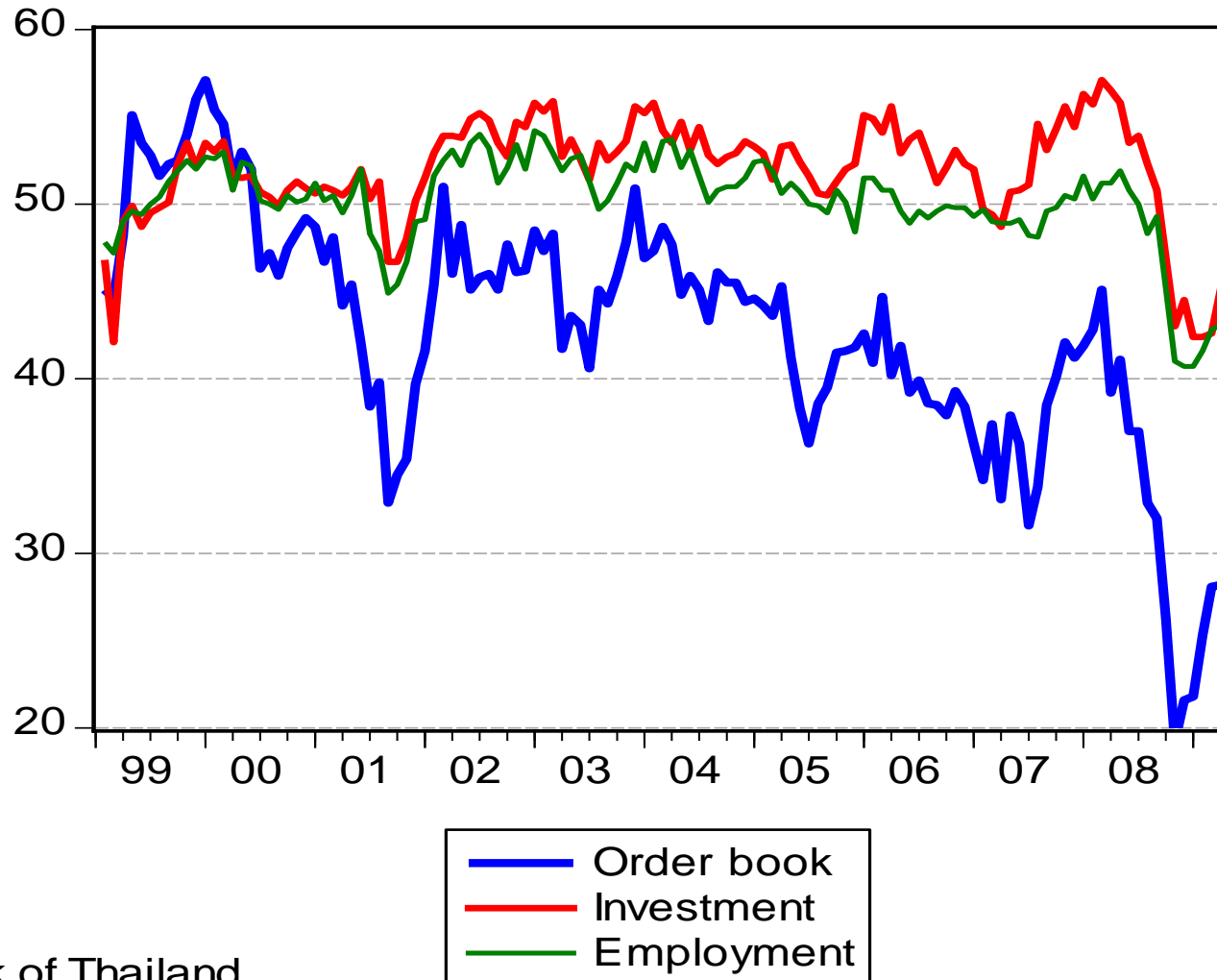
- For every 1% of increase in unemployment rate, GDP will be lower by roughly 2% (In USA).

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*

Business sentiment Index

How can we rekindle favorable investment climate?



Gold price rises during the time of uncertainties

10 Year Gold London Fix PM Daily with 60 and 200-day moving averages



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 Thai economy after the coup

- 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.

Past coups were different from the 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 may not be the last one.

January 2014



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 Thai coup in 2014

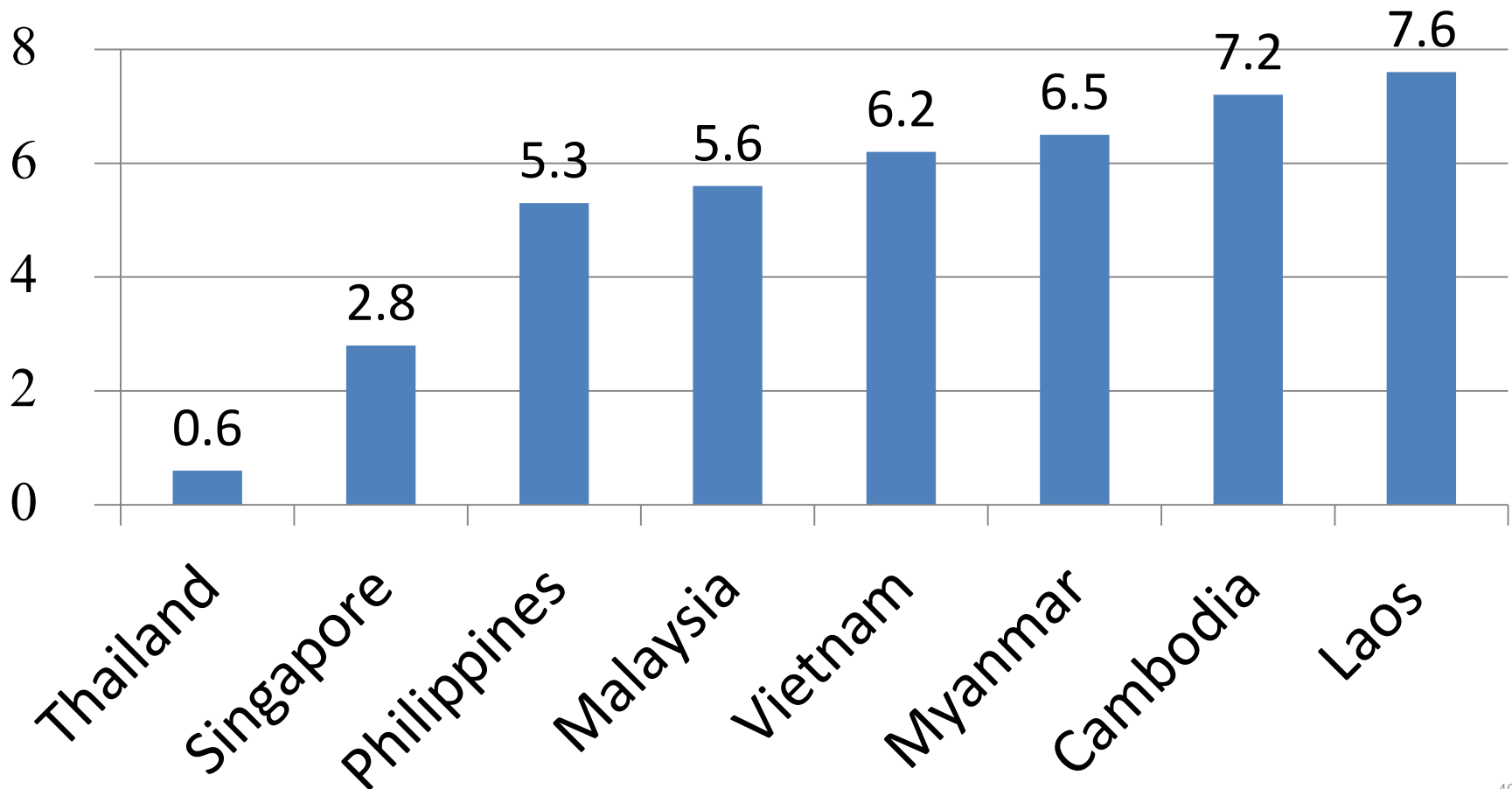
- Thailand's economy was already struggling before the country's military seized power in a bloodless coup on 24 May 2014, saying it needed to restore order after six months of protests aimed at ousting the elected government.
- The military takeover, the second since 2006, could ensure stability in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

More challenges for the Thai 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.

The high price of the 2014 coup

GDP Growth Rate (Y-o-Y) in 2014



Concluding remarks

- The long term economic cost of the coup was underestimated.
- Political instability damages economic performance and derails the return to the pre-shock growth path.
- Domestic demand could have been stimulated to offset the shortfall in exports in 2009 caused by the GFC.