

Buffeting by the Unholy Trinity and Thailand's Military Coups

Bhanupong

Lecture 7

Syllabus

Lecture 7

- Consequences of the Avian Influenza (2004), the Asian tsunami (2005), and the oil price shock in 2005.
- Impacts of the 2006/2014 military coups
- How have the coups changed Thai economy?
- How badly hurt is Thailand by the coronavirus in 2020?

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.
- Nidhiprabha (2018) ***Chapter 3***

Key words

- The Avian Influenza
- The 2005 Asian tsunami
- The oil price shock in 2005
- Okun's law
- Health capital: The shadow price of health
- Animal spirits (Alkerlof and Shiller)

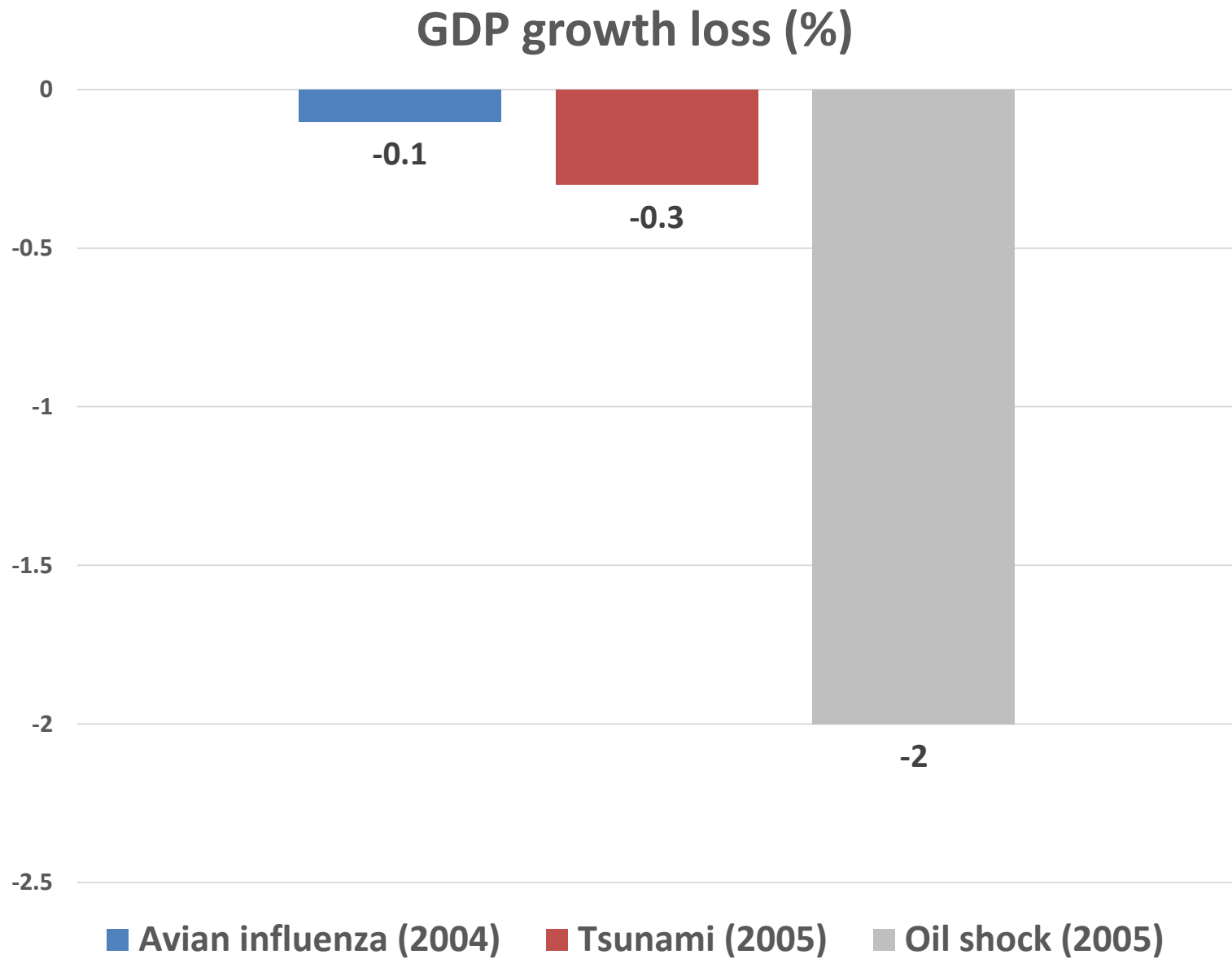
Bird flu (2004), Tsunami (2005), the 2005 oil shock

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 (H5N1)



The bird flu

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

In 2002, import ban on Thai chicken, due to the detection of antibiotic residues (*Nitrofurantoin*).

In ***December 2003***, Avian influenza broke out in Thailand and killed *14 people* in the following 12 months.

Damages from the bird flu

The spread of bird flu 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 the flu reduced GDP growth by 0.1 percentage points in 2004

Why so little impact?

H7N9



China reports bird flu outbreak near epicenter of coronavirus

February 2, 2020



The fatal illness — known as H5N1 virus — causes “a highly infectious, severe respiratory disease in birds,” according to WHO.

The flu can be transmitted to humans.

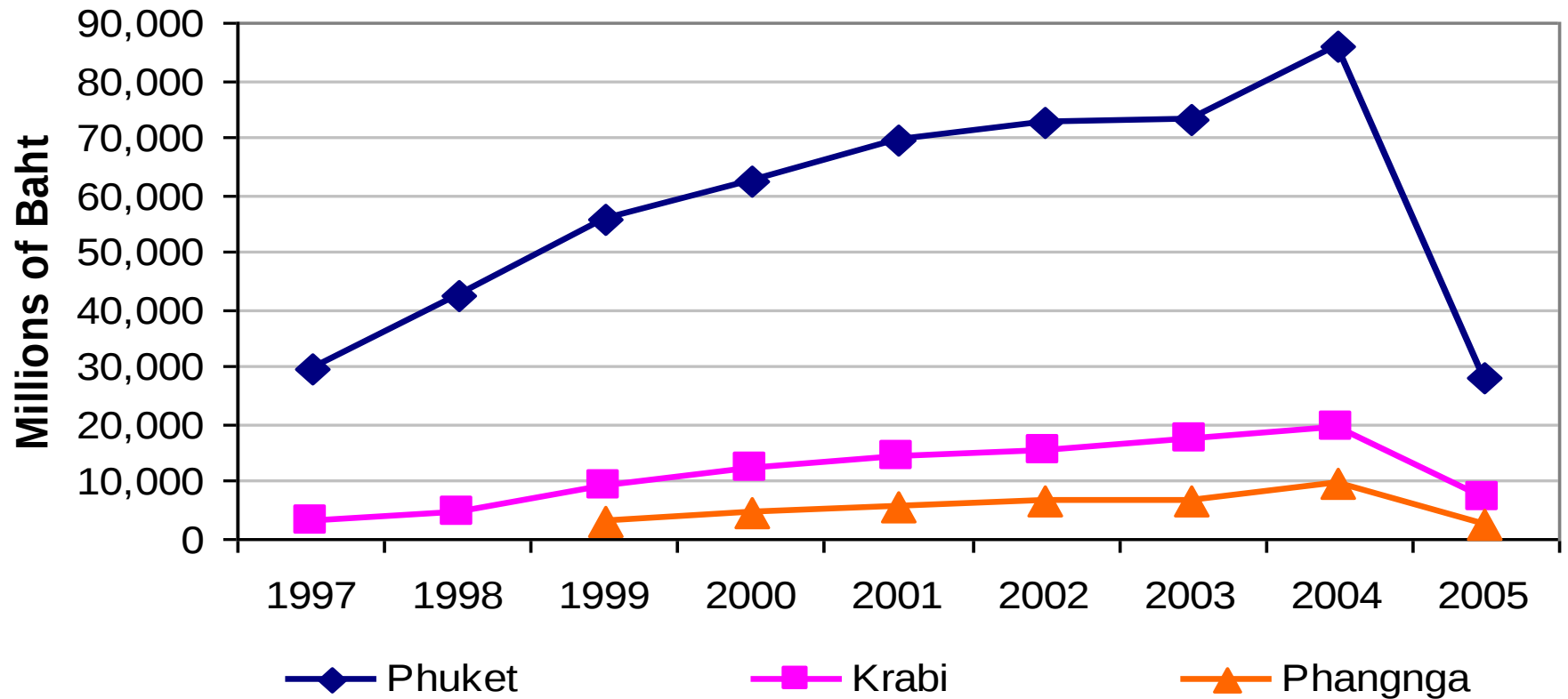
H5N1: Low Epidemic

- China's Bird Flu Surge Is a Low Epidemic Threat, (W.H.O.)
- **H5N1**, a strain that sparked widespread fear of bird flu in 2003, still occasionally kills a few people each year, and
- **H5N8**, is widely circulating in poultry in Europe and the Middle East.
- But no H5 or H7 strain has ever been transmitted easily among humans.

December 26, 2004



Tourism Revenue from Visitors in Three Provinces



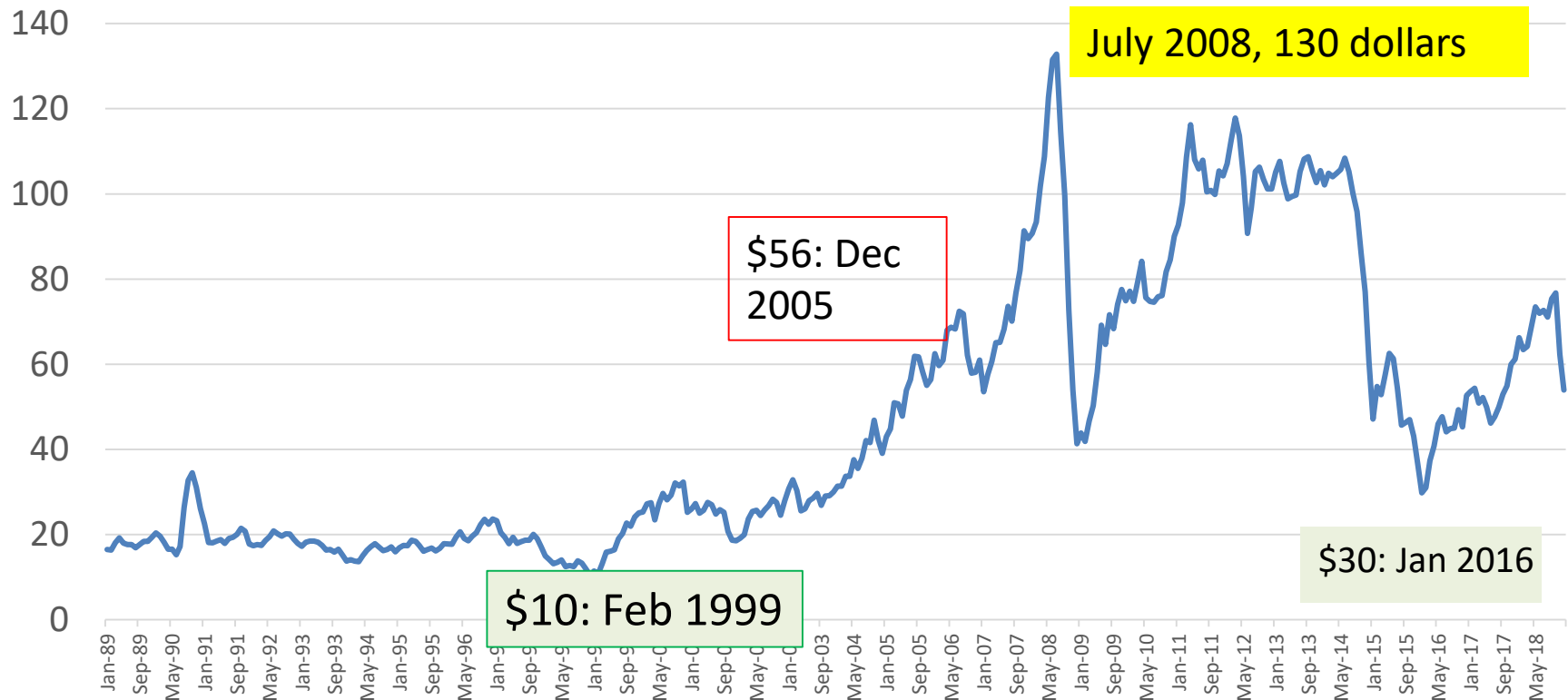
Source: Tourism Authority of Thailand

Shocks from 1991 to 2006

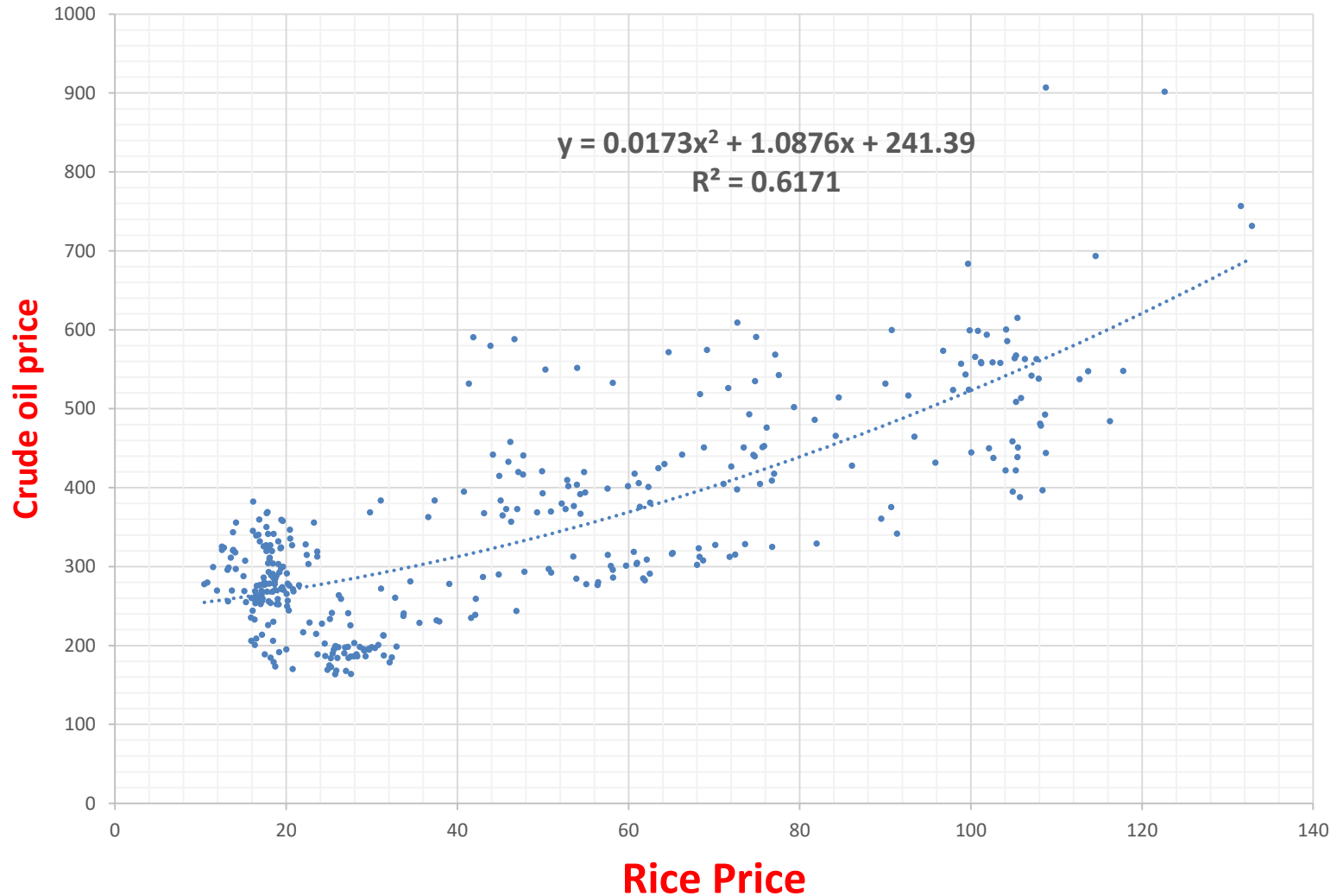
- World recession 1991
- Asian financial crisis 1997
- SARS and Iraq war in 2003
- Avian flu (H5N1) 2004
- Tsunami (Dec 26, 2004)
- The third oil shock (2005)
- Coup d'état (Sep 19, 2006)

The oil shocks

Average Spot Price
of Brent, Dubai, West Texas Intermediate
(US dollars per barrel)



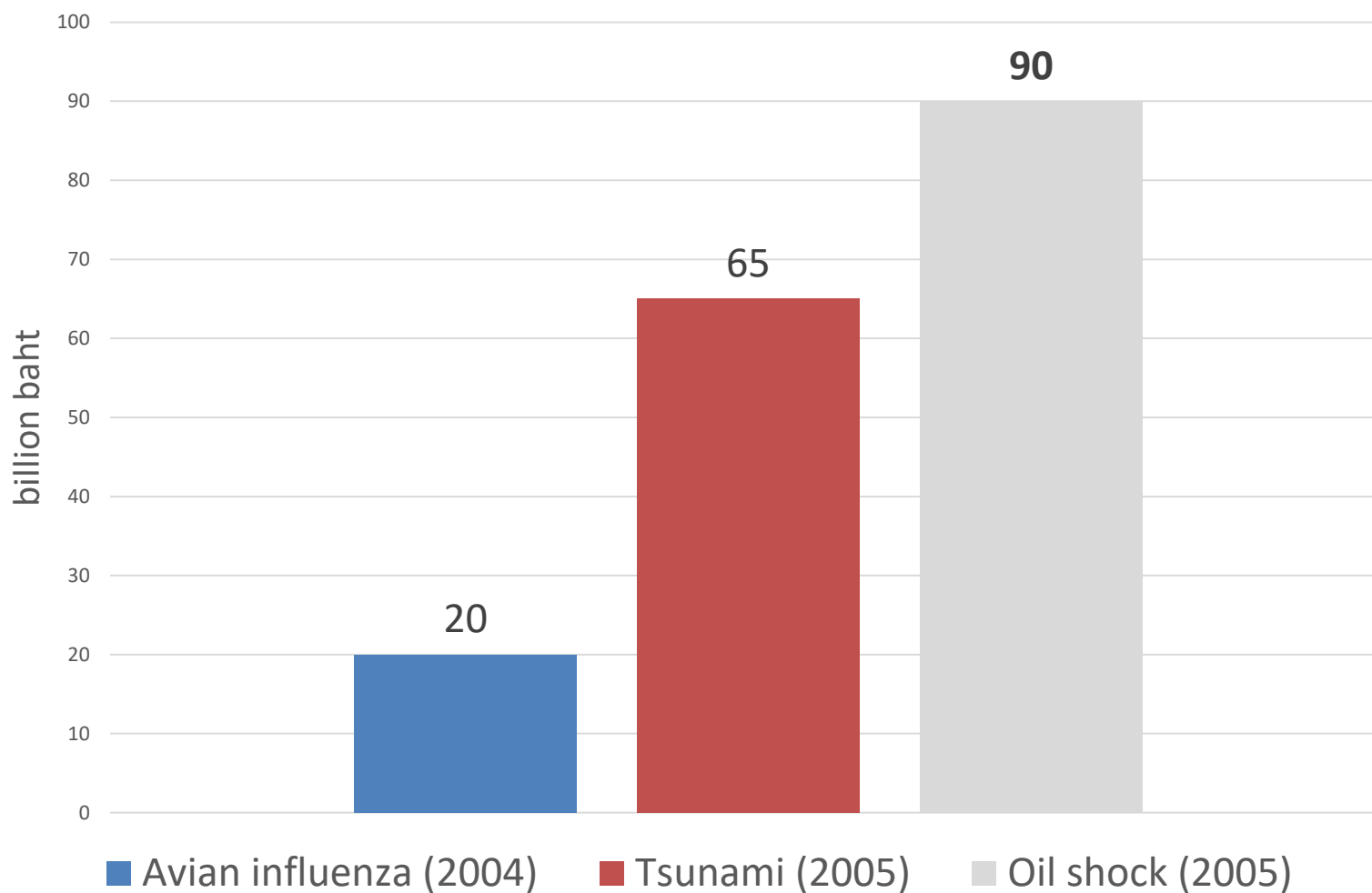
The thirty-years-old relationship



The 2005 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 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 tourism industry
- 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*
- It takes a heap of Harberger Triangles to fill an Okun Gap (James Tobin, 1977)

Comparison of financial losses



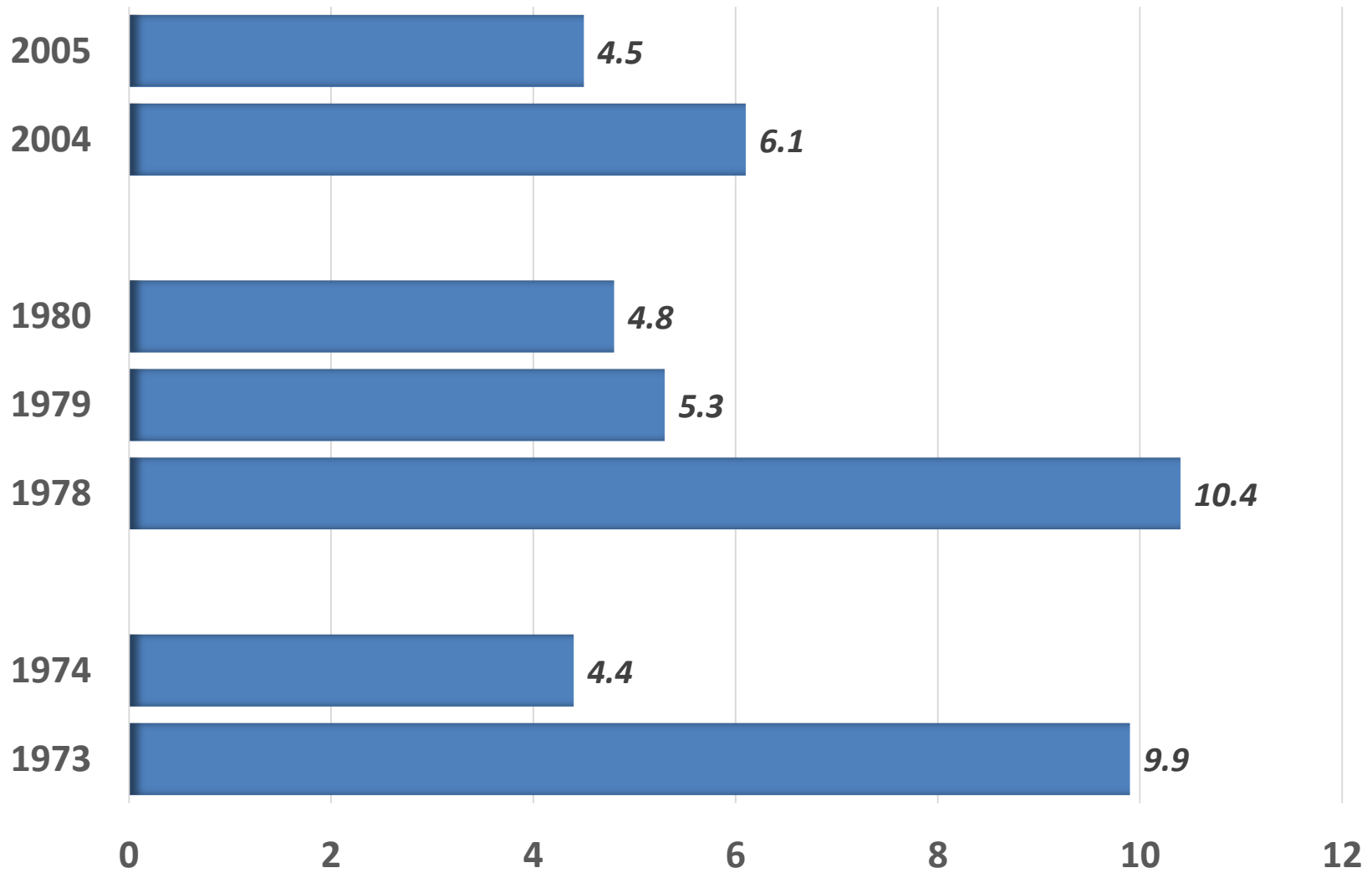
Comparing the three oil price shocks

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

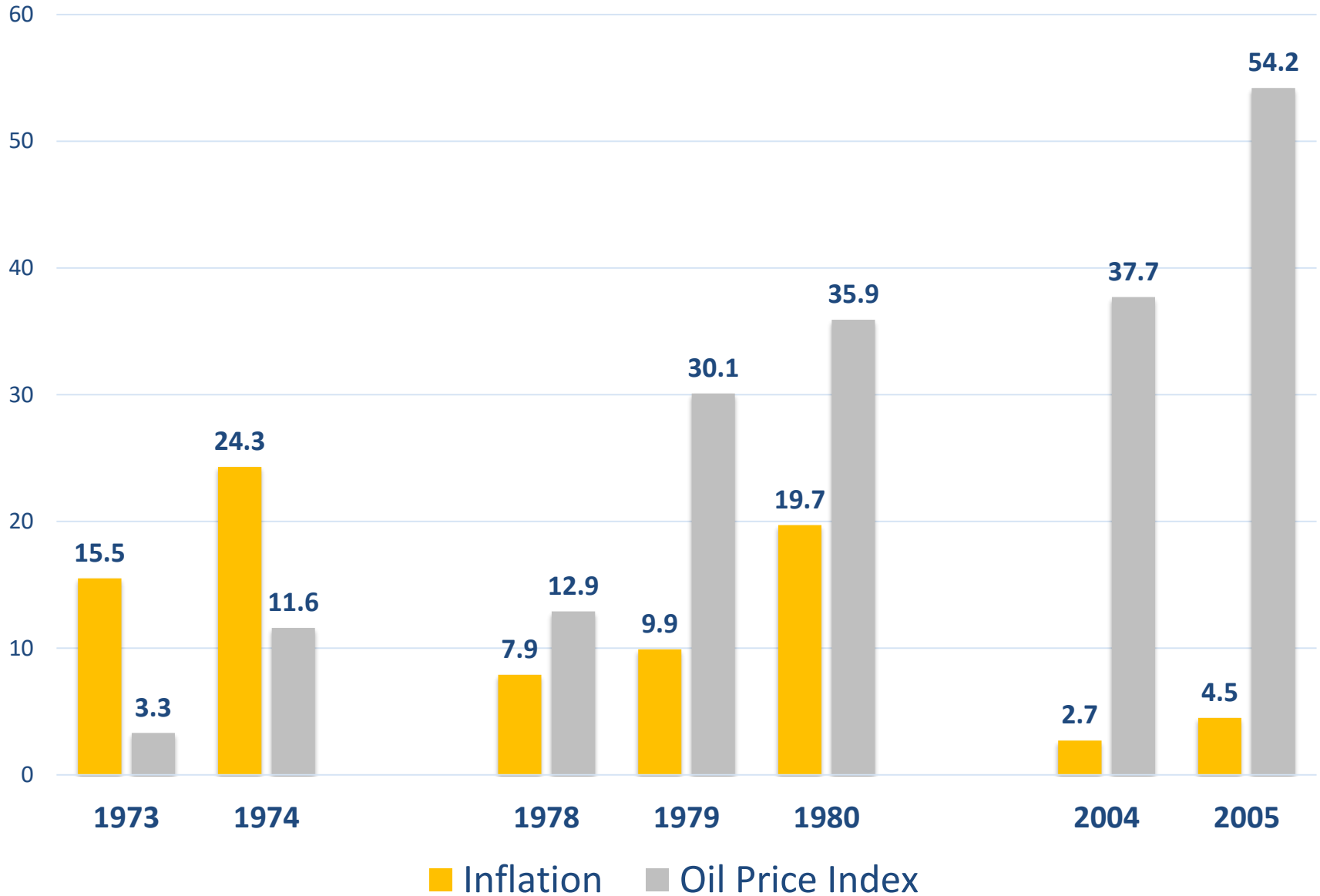
	First oil shock		Second oil shock			Third oil shock	
	1973	1974	1978	1979	1980	2004	2005
GDP growth	9.9	4.4	10.4	5.3	4.8	6.1	4.5
Inflation	15.5	24.3	7.9	9.9	19.7	2.7	4.5
Current account/GDP	-0.5	-0.6	-2.8	-4.9	-6.4	4.5	-4.8
Trade balance/GDP	-1.7	-2.4	-3.1	-4.4	-6.1	2.3	-2.1
World oil price index	3.3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

Sources: Bank of Thailand, International Monetary Fund.

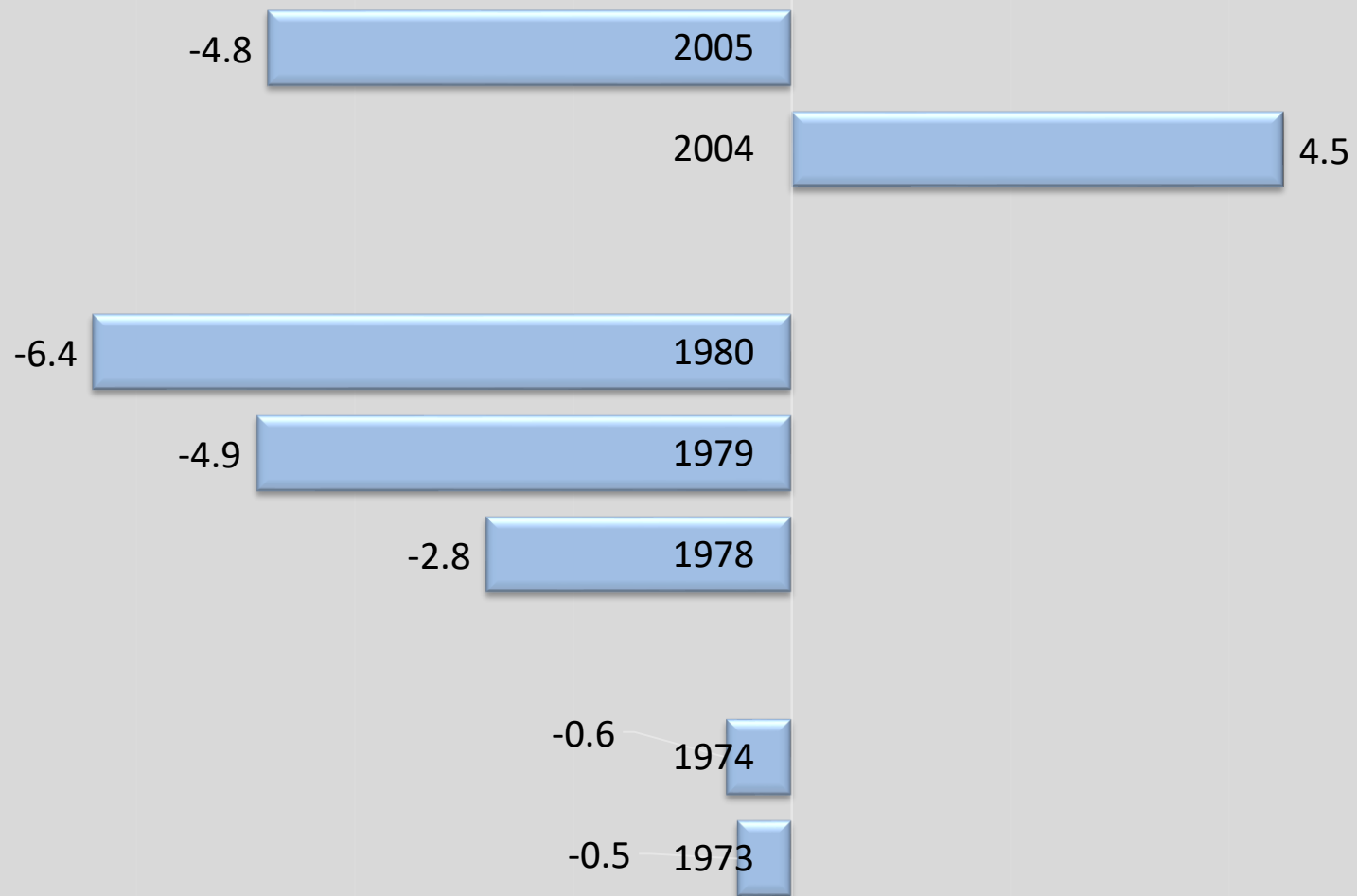
GDP growth during the three oil shocks



Oil Price shocks and Inflation rate

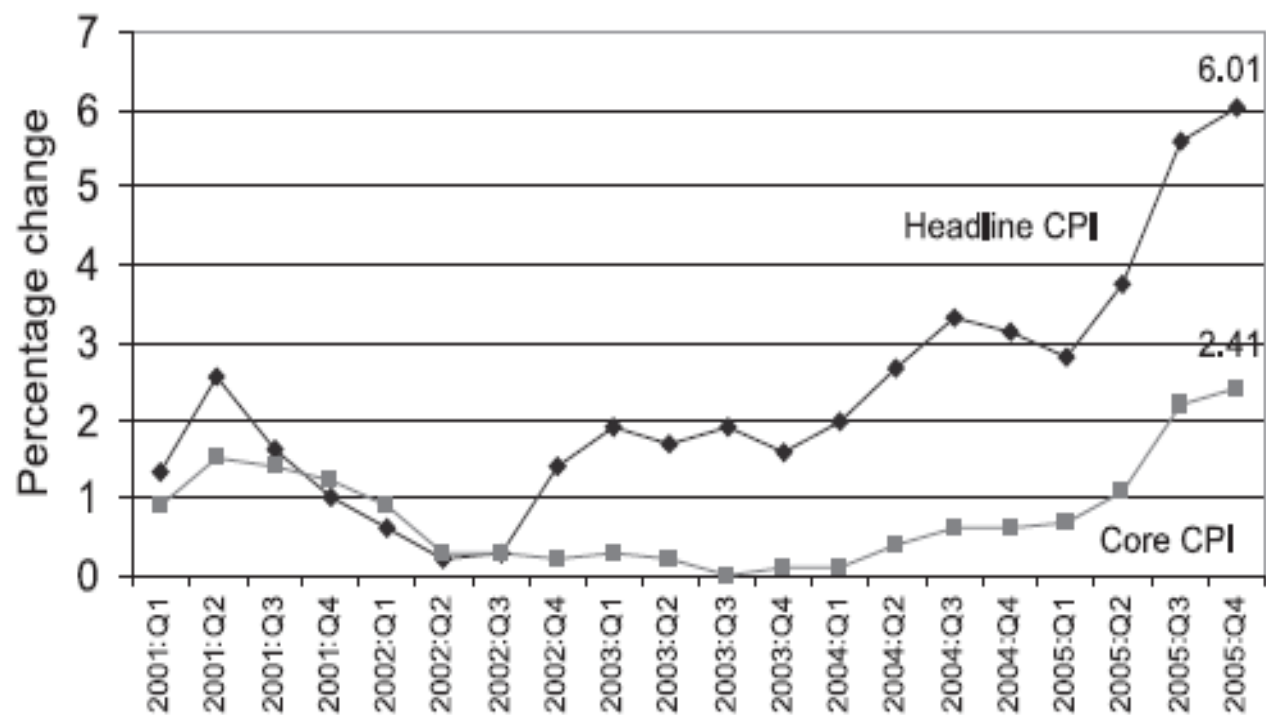


Current Account After the Oil Shocks (%GDP)



Core vs. headline inflation

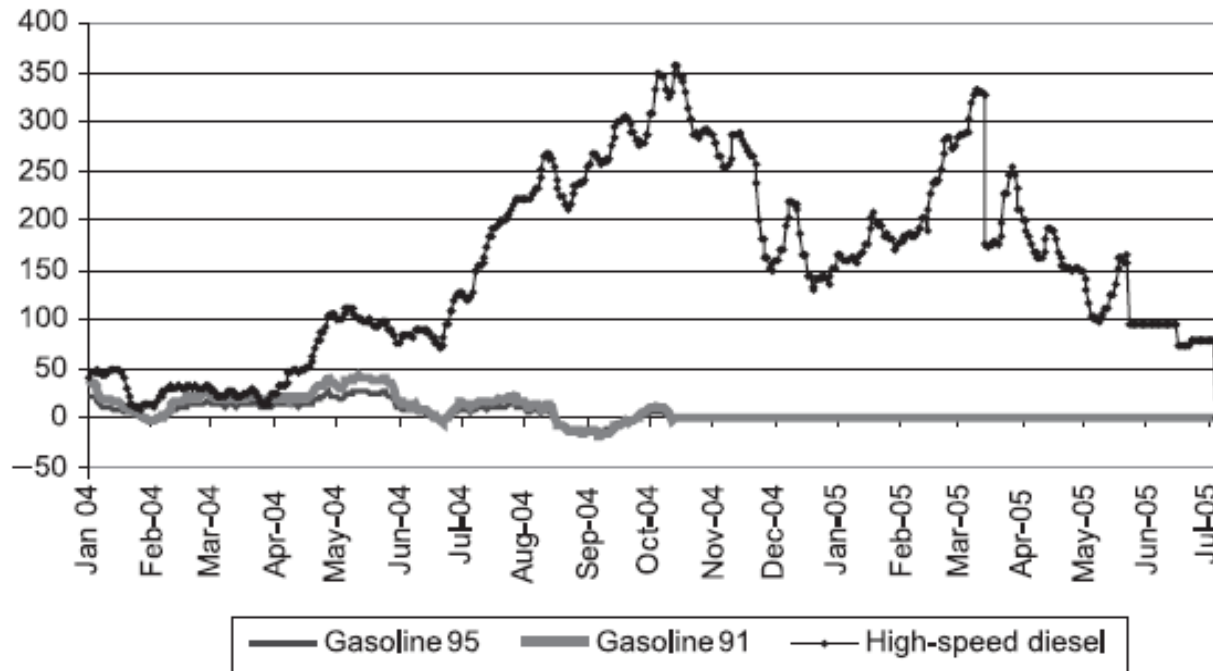
Figure 4. Inflationary impact of the third oil price shock



Source: Bank of Thailand.

Diesel vs. gasoline subsidies

Figure 5. Oil subsidies per day (million baht)

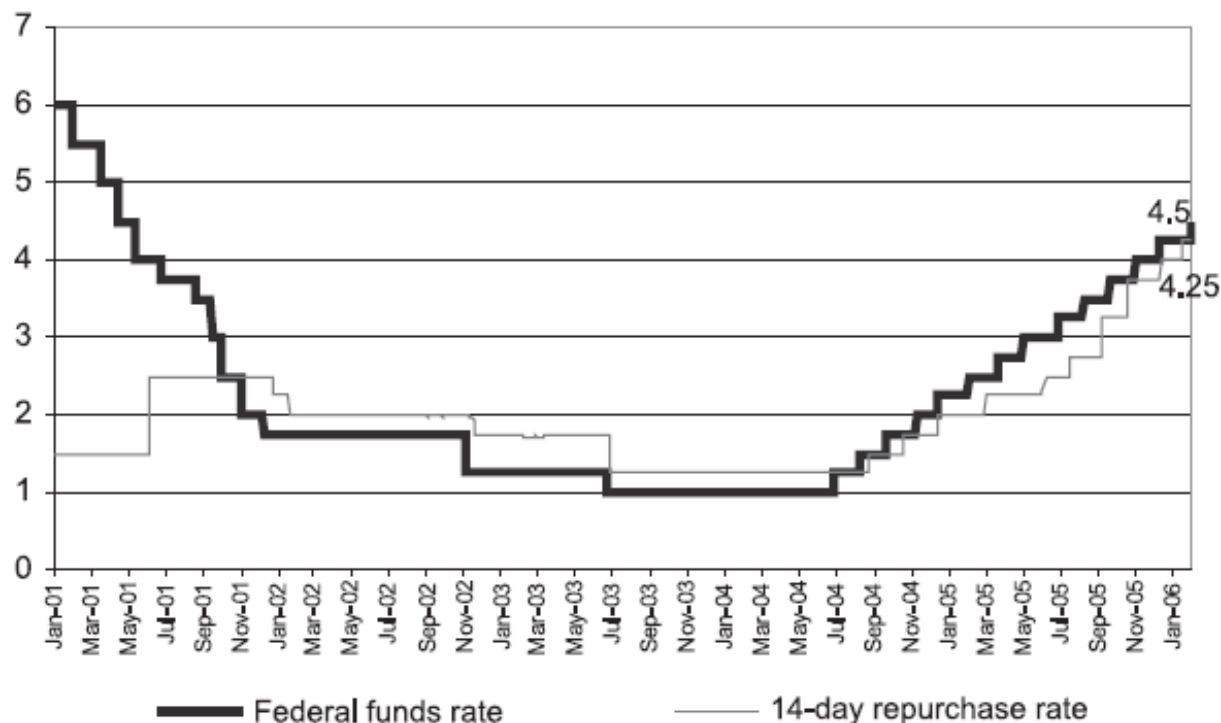


Source: Energy Policy and Planning Office.

Why does the government subsidize energy until these days?

Gradual approach to interest rate adjustments: Follow the leader (the Fed)

Figure 6. Federal funds and repurchase rates



Sources: Bank of Thailand, Federal Reserve.

Appropriate policy responses to shocks

1. Transparency is important for government's credibility
2. 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.
3. **Price controls** must be employed *temporarily* to avoid market disruptions and to calm inflationary expectations.

More Shocks since 2007 (still counting)

- Bangkok bombing (Jan 2007)
- Airport shutdown (2008)
- Global Financial Crisis (2009)
- Type-A(H1N1) (2009)
- Red shirts (UDD) uprising (April 2009, March 2010, April and May 2010)
- Japan quake: Fukushima Nuclear Power plant (March 2011)
- 2013/2014 Bangkok shutdown
- 2014: Military Coup
- 2015: Erawan shrine bombing
- 2020: Coronavirus (Global slowdown and international travel bans)

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.

Another disruption in 2014



The Thai economy after the coup: 2006-2008

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

Coups galore

- There have been 21 military coups since June 24, 1932, when absolute monarchy was replaced by constitutional monarchy.
- Only ELEVEN 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

A vicious cycle

And we thought we had seen the last coup in 1991

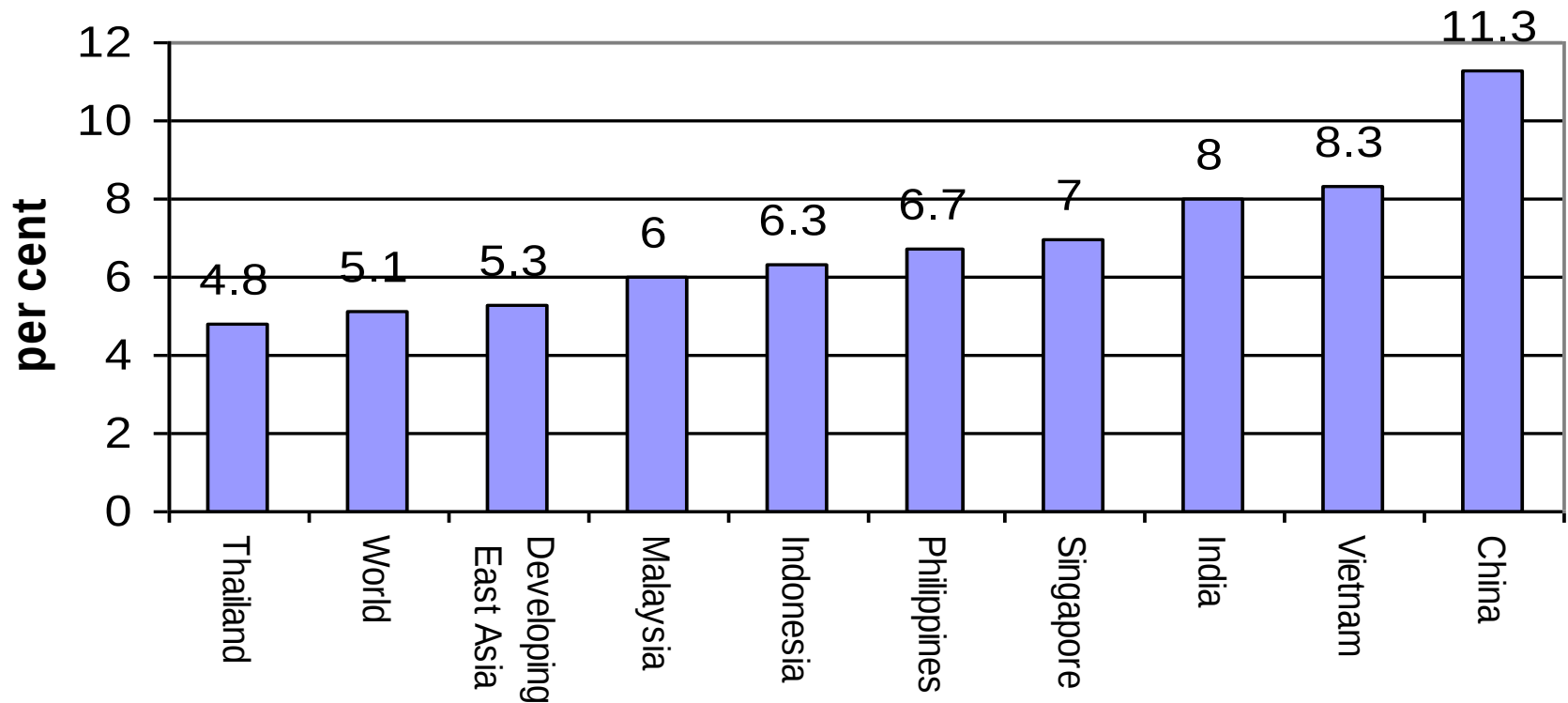
Between 1991 and 2005, the absence of coup provided stable environment and economic prosperity under five PMs:

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

Almost all coup attempts, successful or failed, occur in countries that are relatively poor and have political regimes that mix features of autocracy and democracy.

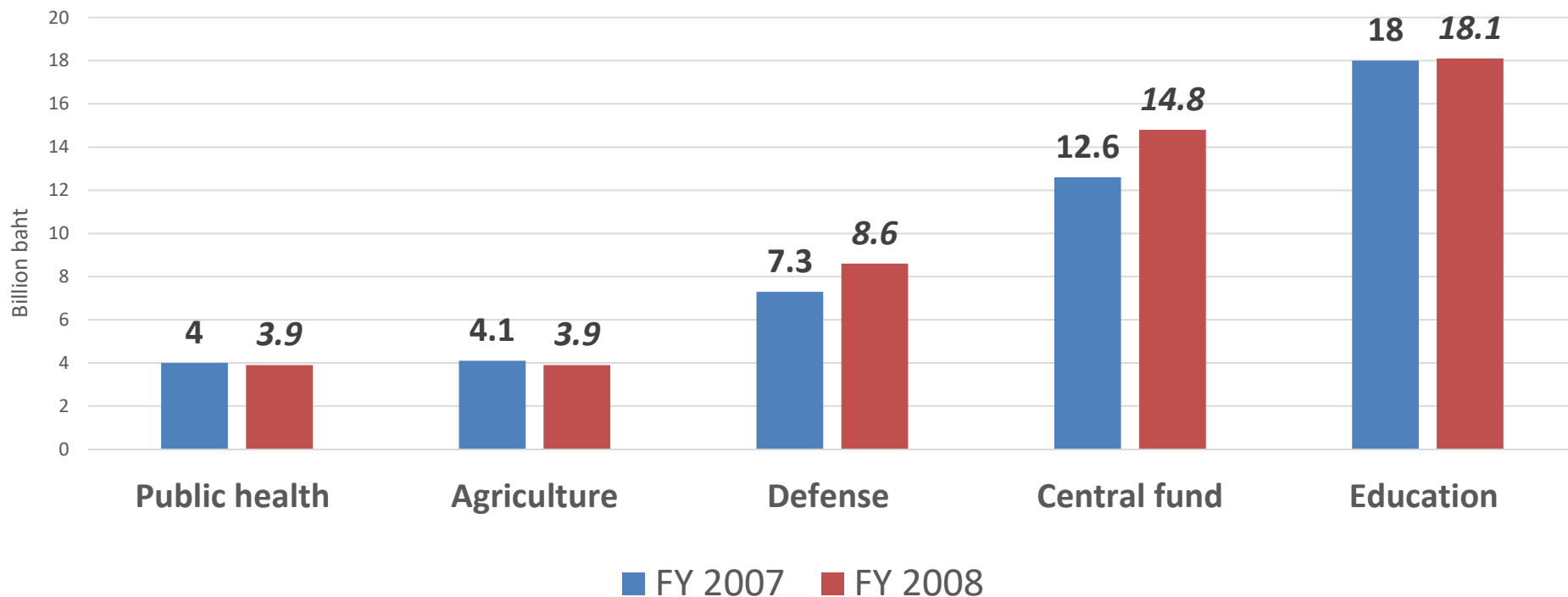
The high cost of the 2006 coup

Comparison of Growth in 2007

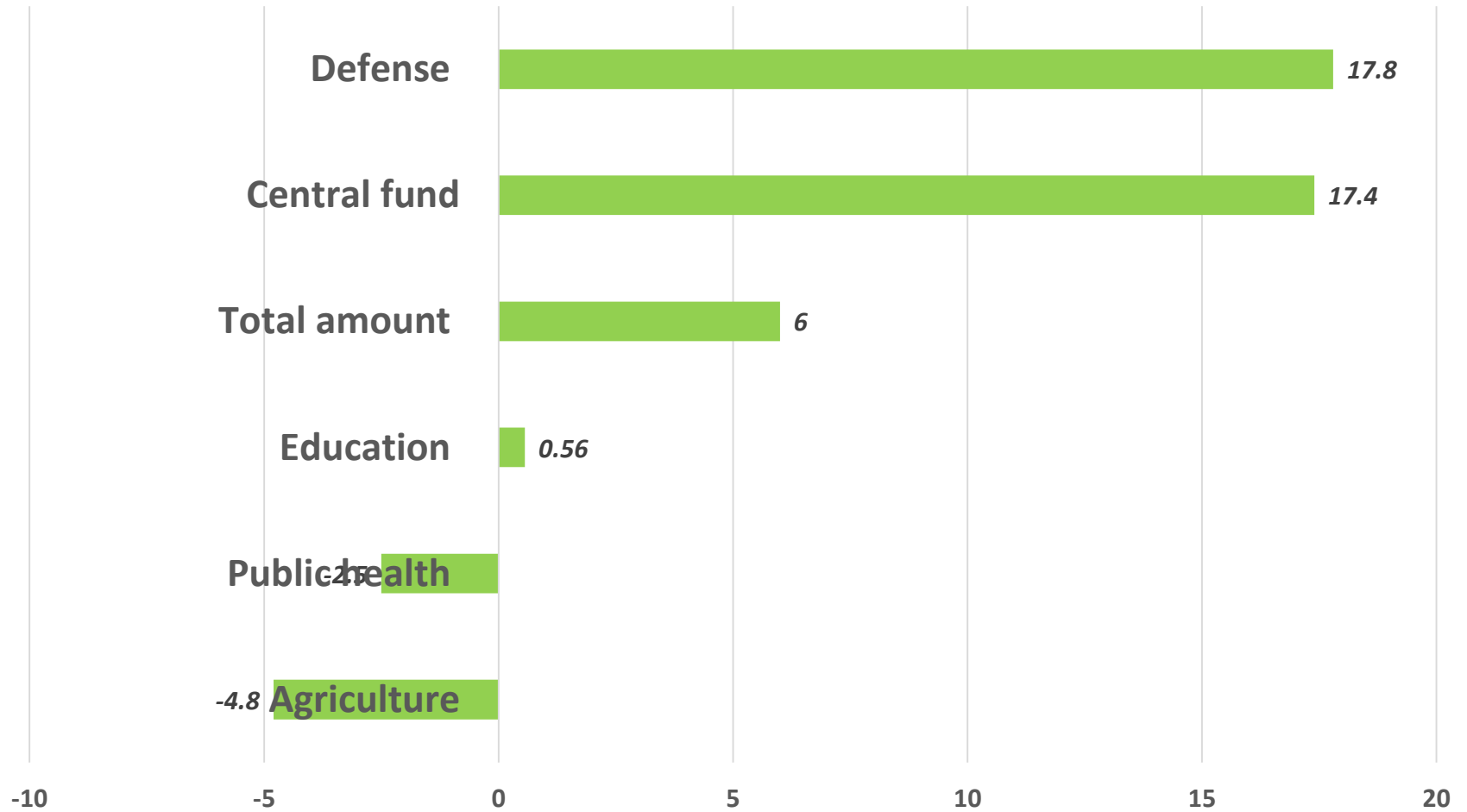


PM General Surayud

Fiscal budget under the military-backed government



Percentage change : 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.
- Cross-country evidence shows a **negative** impact of military spending on economic performance.

Michael Grossman

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

Journal of Political Economy (1972)

- **Health capital stock produces an output of healthy time.**
- Individual inherits an initial stock of health that **depreciates with age** and can be increased by investment.
- **The shadow price falls** with **education** as more educated people are more efficient producers of health.

Michael Grossman
The Shadow Price of health

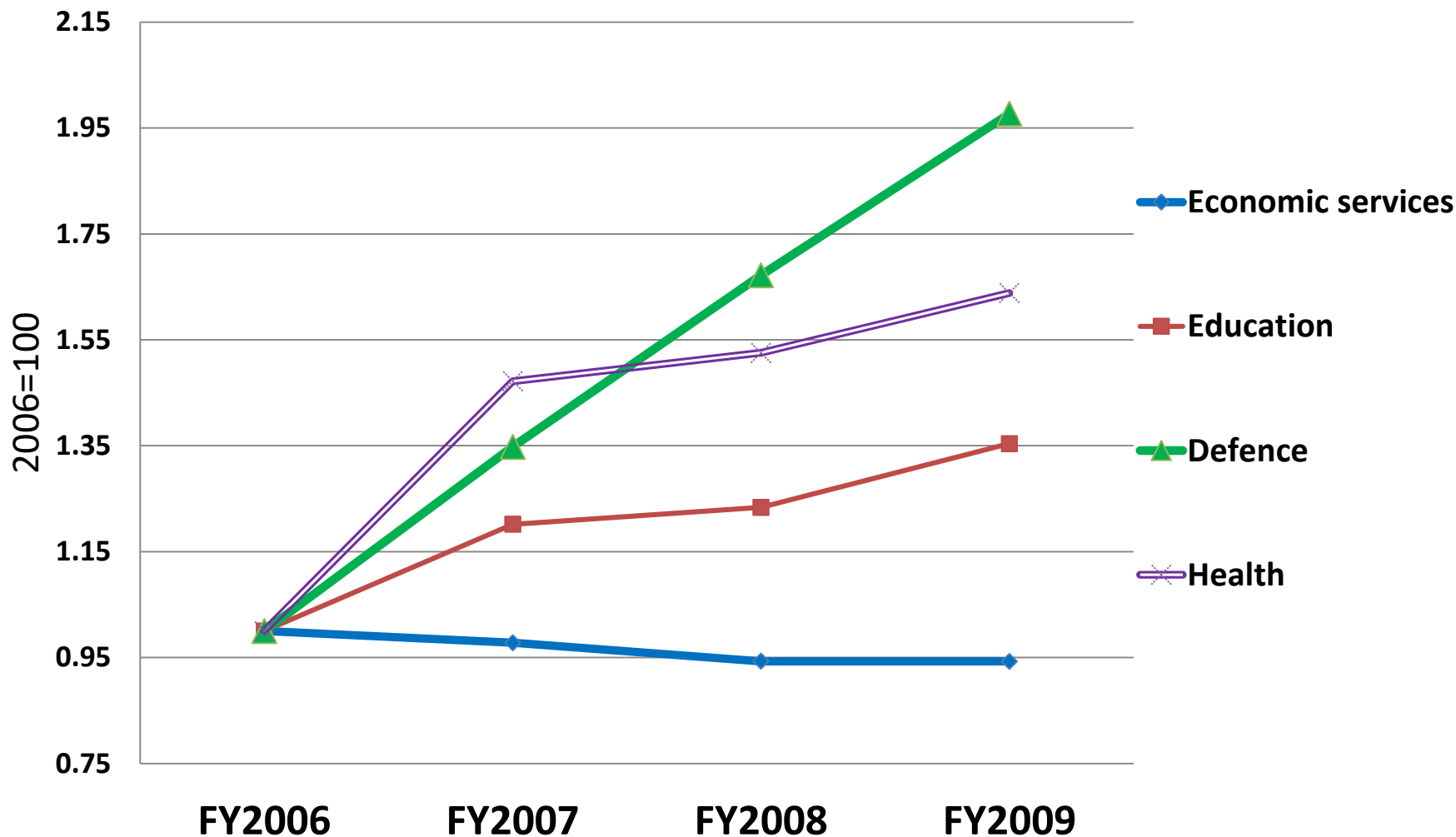
- The “shadow price” of health *reflects the cost of medical care.*
- The shadow price rises with age when health deteriorates over time, due to ageing (higher depreciation of health capital stock).
- There are *eight people* die every hour in Thailand because of creeping cancer.

Probability of having cancer rises with ages

- Liver: men 30 years old plus (3- 6 months to live)
- Lung: men 65+ (recall instant gratification)
- Breast: female 40+
- Colon: 50+ (require colonoscopy)
- Prostate: 50+ 60% probability for 60 years old
90% probability for 90 years old
- Health budget must rise *pari-passu* with ageing society, but

Government Budget appropriation after the 2006 military coup

Source: BOB

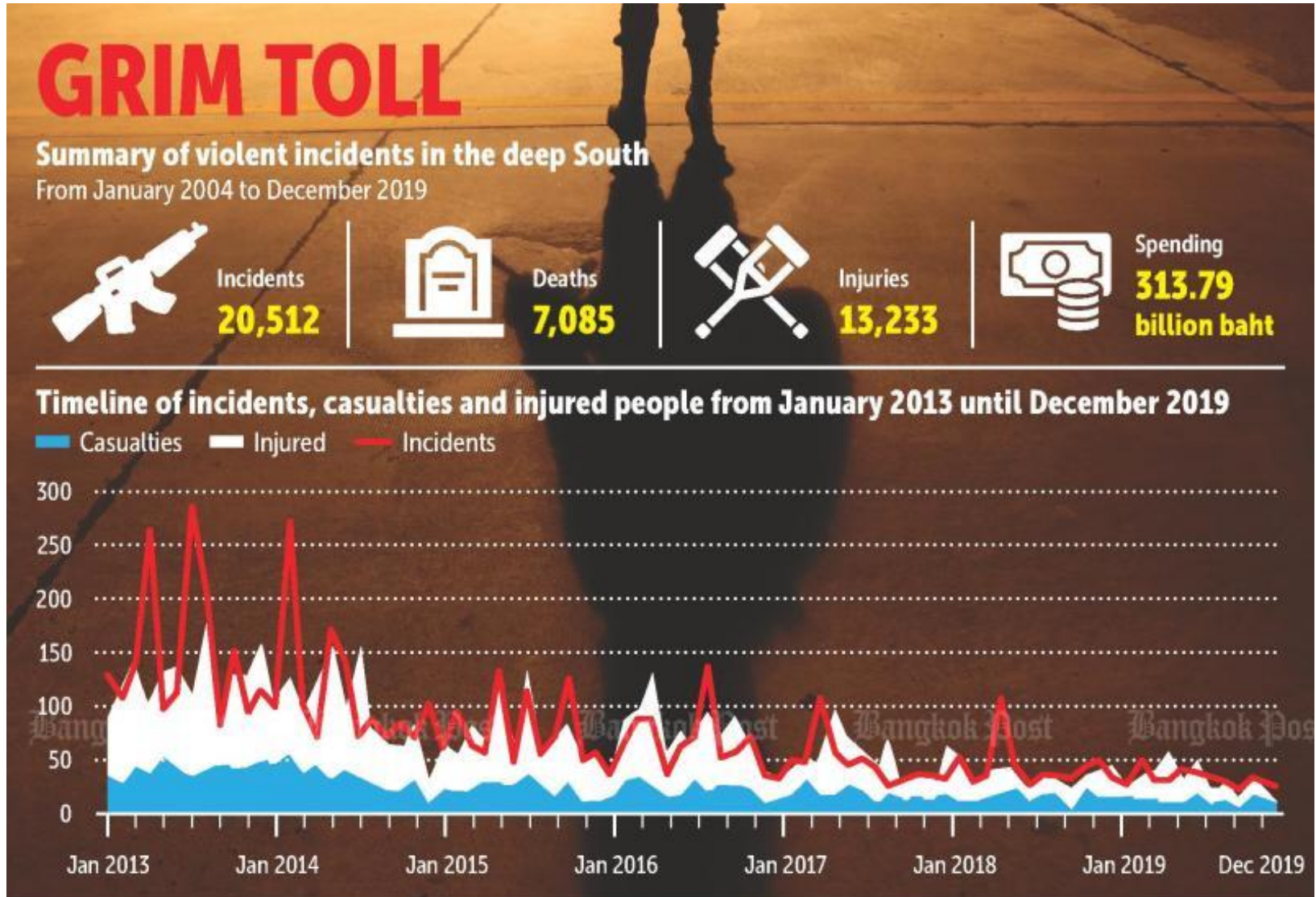


Thailand's perennial problems

- Exchange rate risks: too weak or too strong
- Fluctuations of the world economy: Business cycle synchronization
- Absence of the rule of law: poor quality institutions
- Military coups and judicial threat (a TV cooking show can lead to sacking the PM).
- Political division and disturbances
- *Southern violence: an explosion gives rise to higher defense budget—the marginal cost violence*



7,085 Deaths from Jan 2004 to Dec 2019



Physical capital formation

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

Why growth is good for the poor

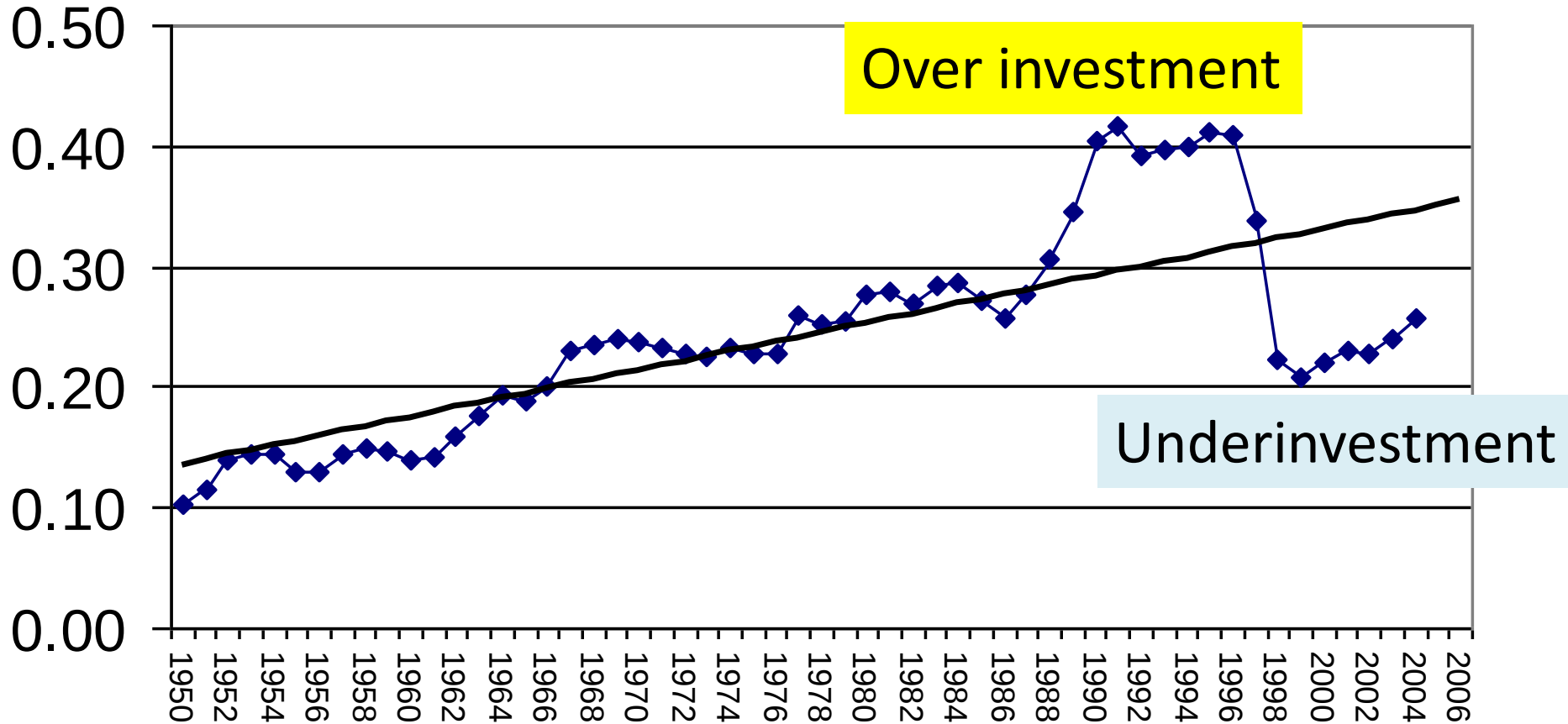
- Growth increases the *ability* to redistribute income among people and reduce unemployment.

- 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).

Share of investment in GDP



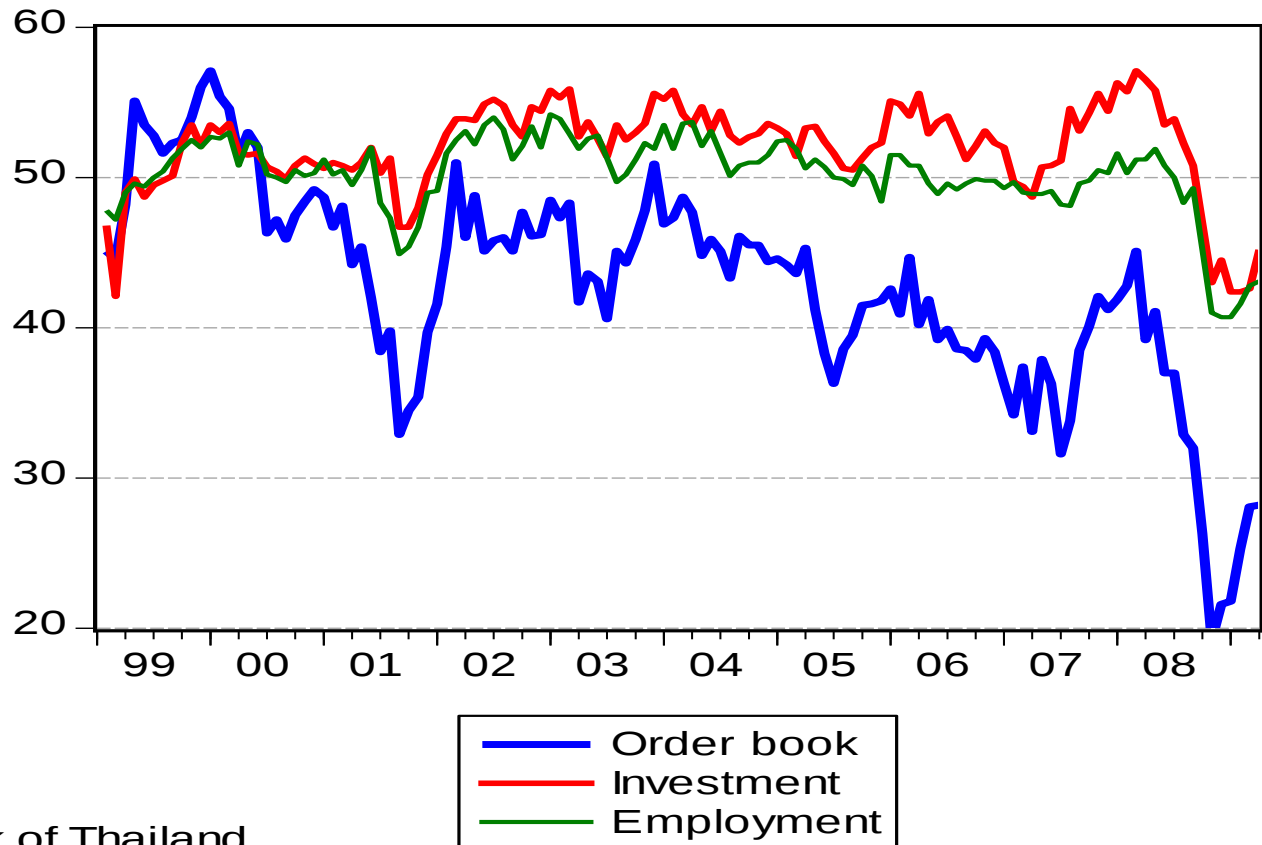
Animal spirits

(An extension from Keynes investor confidence)

- **Akerlof and Shiller** (2009) extend Keynes' animal spirits from investor confidence to include the followings:
- **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 decision.**
- ***To rekindle Thailand's animal spirits, we must uphold fairness and social justice and say no to double standards***
- ***MNE: Cases of double standards***

Business sentiment Index

How can we rekindle favorable investment climate?



Source: Bank of Thailand



The 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 (e.g. Akara mining), appropriate regulatory structures, the quality and *independence of the judiciary and bureaucratic capacity (Red bull)*.
- Low quality Institutions cannot manage conflict, maintain law and order. They are destroying 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.
- *How do we estimate the cost of the coups?*
- 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 two recent coups

- The Thai 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.

Thailand's coup was just a 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 of 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).

Thai coup in 2014

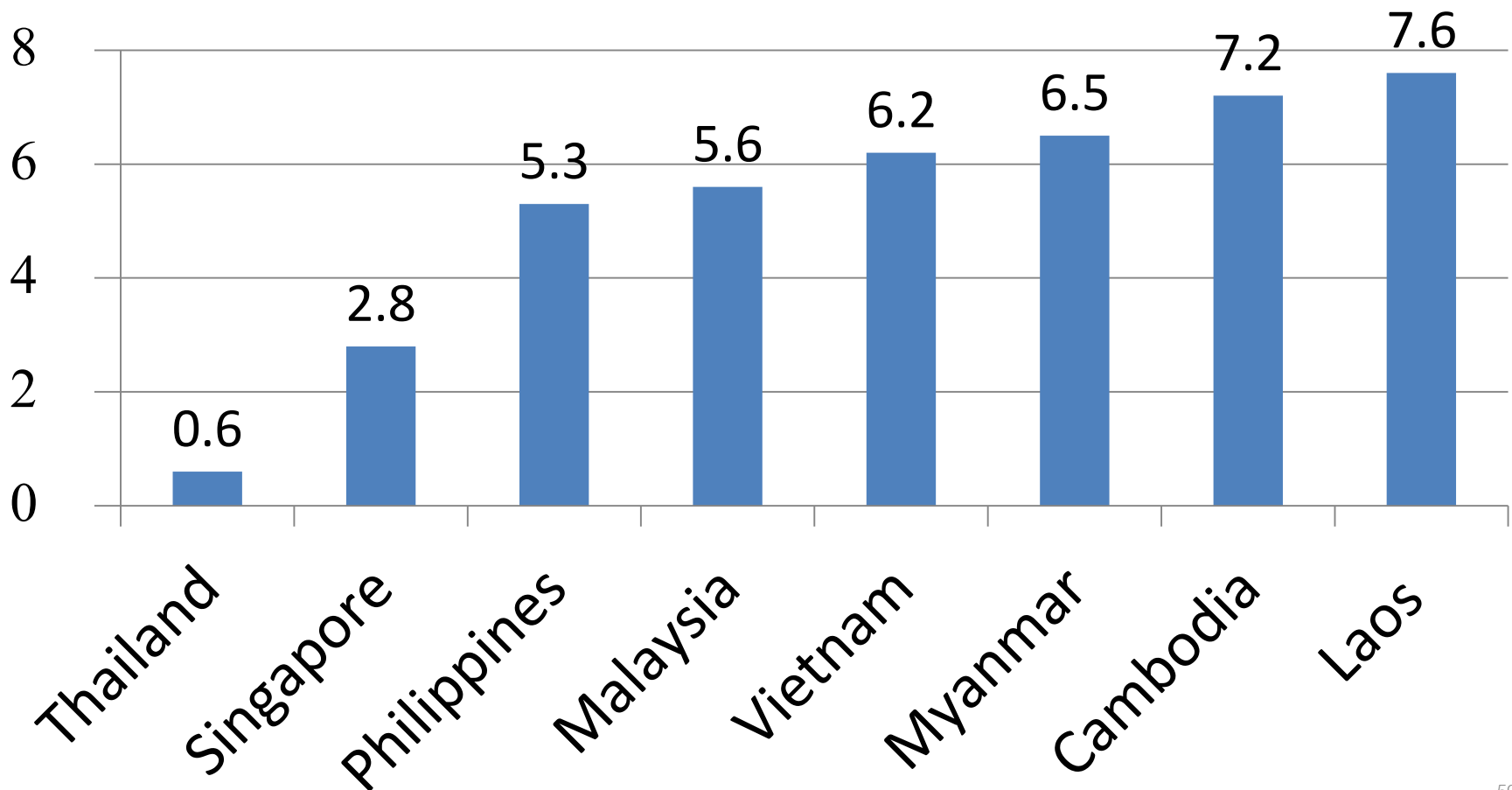
- Thailand's economy was already struggling before the country's military seized power in a bloodless coup on 24 May 2014, saying it needed to restore order after six months of protests aimed at ousting the elected government.
- *“Please give me a bit longer time” That is the name of the forgotten song after the coup*
- The military takeover in 2014 could ensure stability in the short term.

More challenges for economy after the coup

- The army's intervention results in sharper **political divide**, holding back the economy and depressing living standards in the longer run.

The high price of the May 2014 coup

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



FINISH

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มาสวนดุสิต



Run to oppose the PM

Jan 12, 2020



Thailand remains divided after the coup



Royalists rally to support monarchy

Bangkok Post, August 30, 2020



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.

Key words

- Okun gap
- Harberger triangle
- Health capital
- The shadow price of health
- Animal spirits (Alkerlof and Shiller)