

Buffeting by the unholy trinity

Adjustment to external shocks

Bhanupong

Lecture 7

Asian Economic Papers 5(2), 2006

outline

- The Avian Influenza
- The 2006 Asian tsunami
- The oil price shock in 2005
- The oil fund
- A positive oil price 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.

Bird flu

- 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

The spread of AI caused heavy damage to the industry because of massive culling and a temporary decline in domestic consumption.

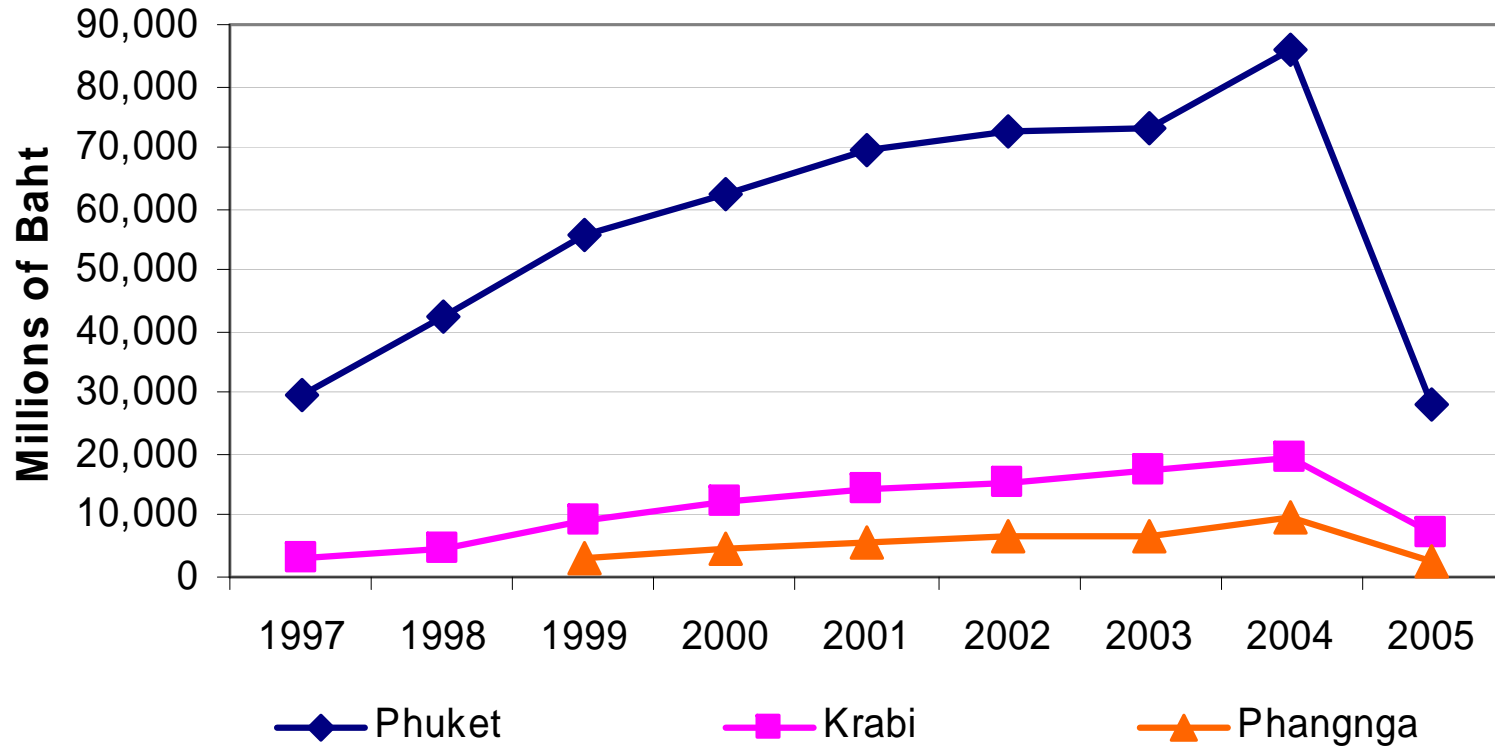
The fear subsided by October 2004, and domestic chicken consumption returned to its rising trend.

The Ministry of Finance estimated that AI reduced GDP growth by 0.1 percentage points in 2004

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.²
- 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

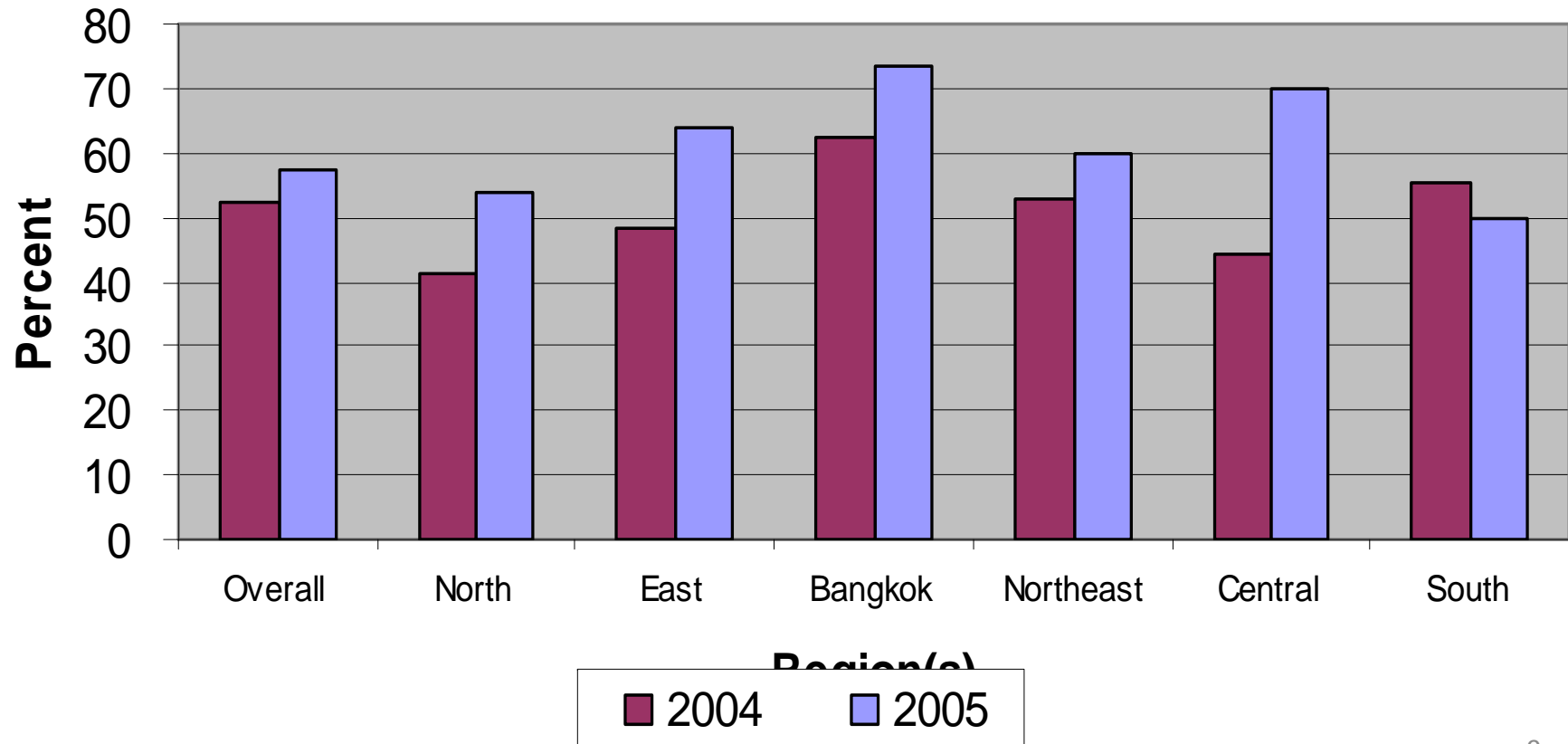
Tourism Revenue from Visitors in Three Provinces



Source: Tourism Authority of Thailand

Substitution is the key

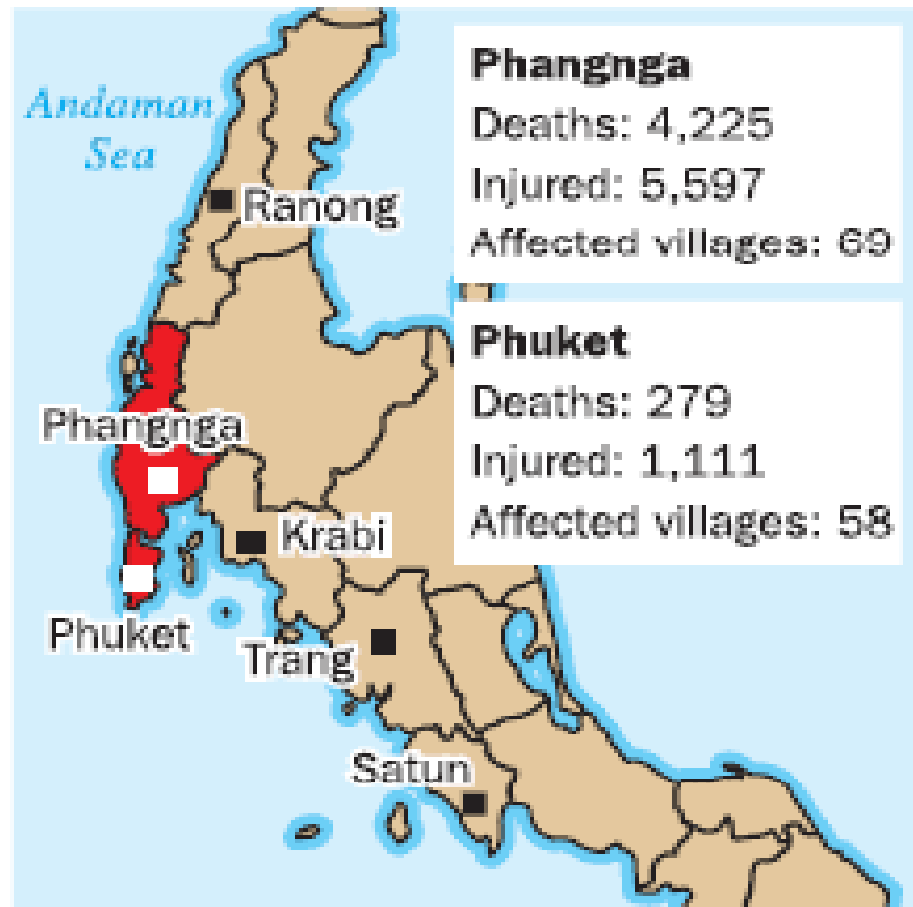
Hotel Occupancy Rate by Region January - August



Shock after shock

- 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)

TSUNAMI RECORD

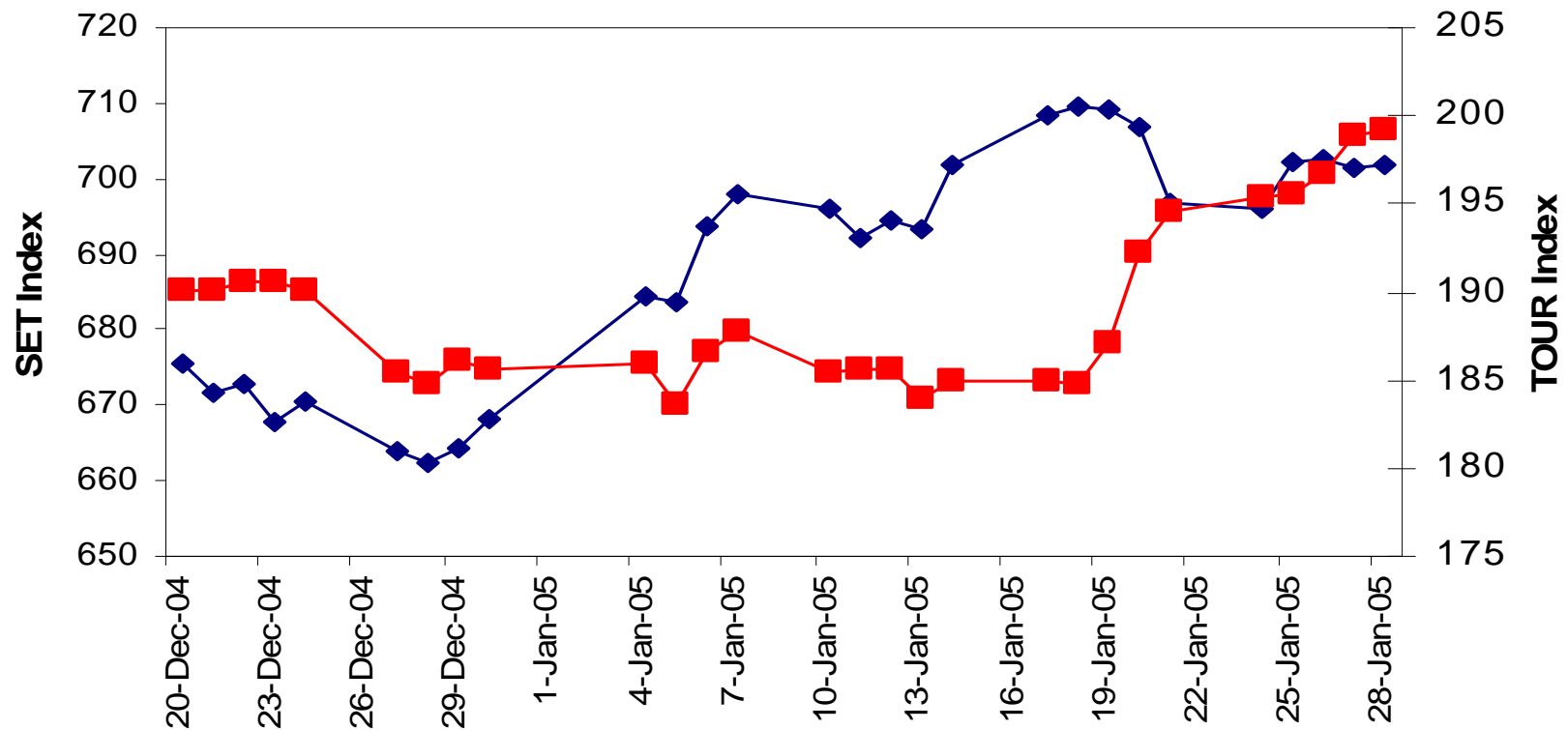


Source: Disaster Prevention and Mitigation Department

POSTgraphics

A temporary shock: Less than a month

Tsunami Impact effect on the Thai Stock Market



Source: Stock Exchange of Thailand

—◆— SET —■— TOUR

Six More Shocks (still counting)

- Bangkok bombing (Jan 2007)
- PAD uprising and airport shutdowns (2008)
- Global (Great) recession (2009)
- Type-A(H1N1) (2009)
- Red shirts (UDD) uprising (April 2009, March 2010, April and May 2010)
- Japan quake (March 2011)

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 recent 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

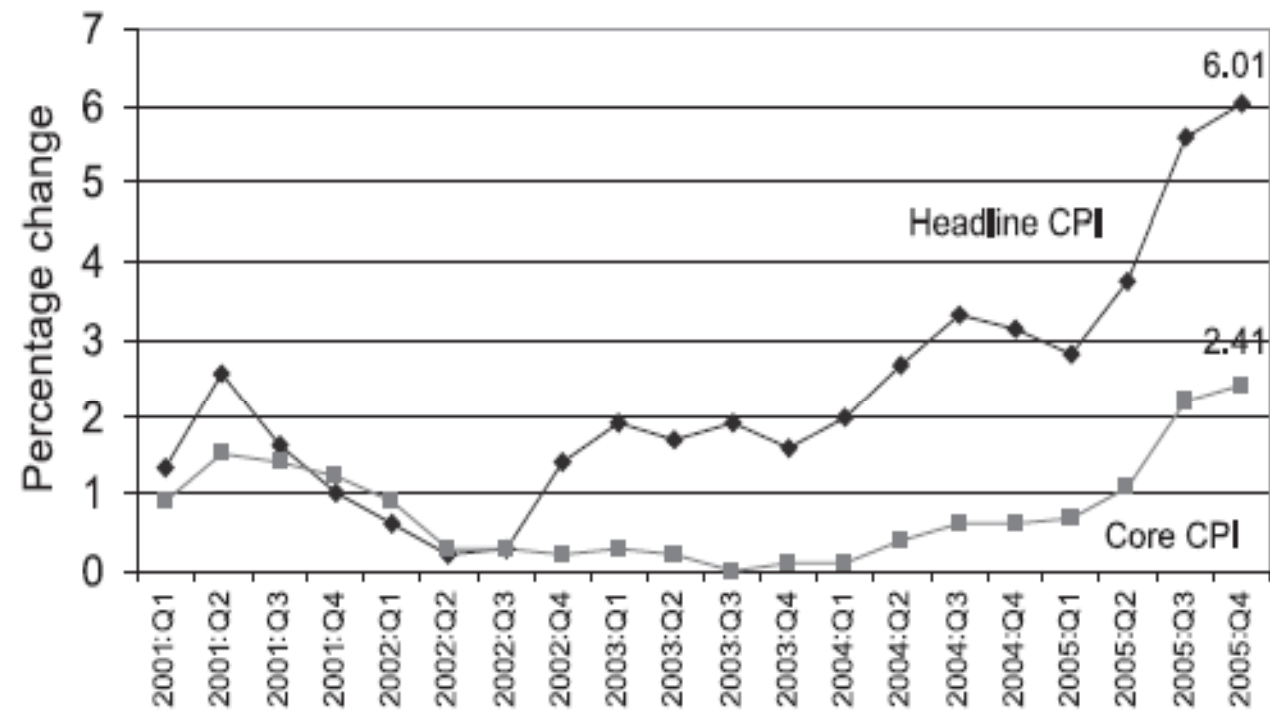
Buffeting of Thailand

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.

Figure 4. Inflationary impact of the third oil price shock



Source: Bank of Thailand.

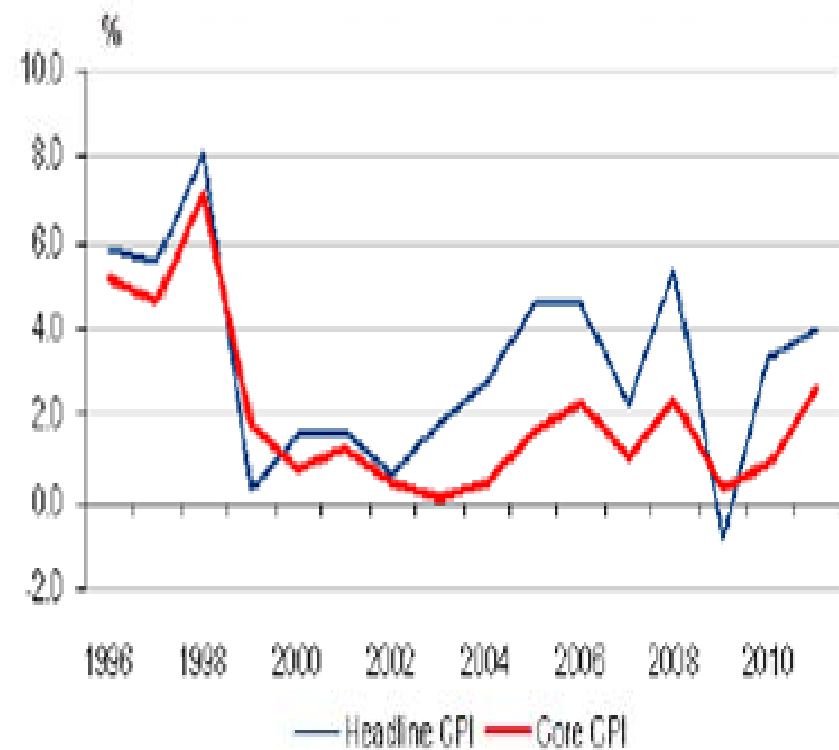
Fiscal space and inflationary pressure

Chart 2: Public debt



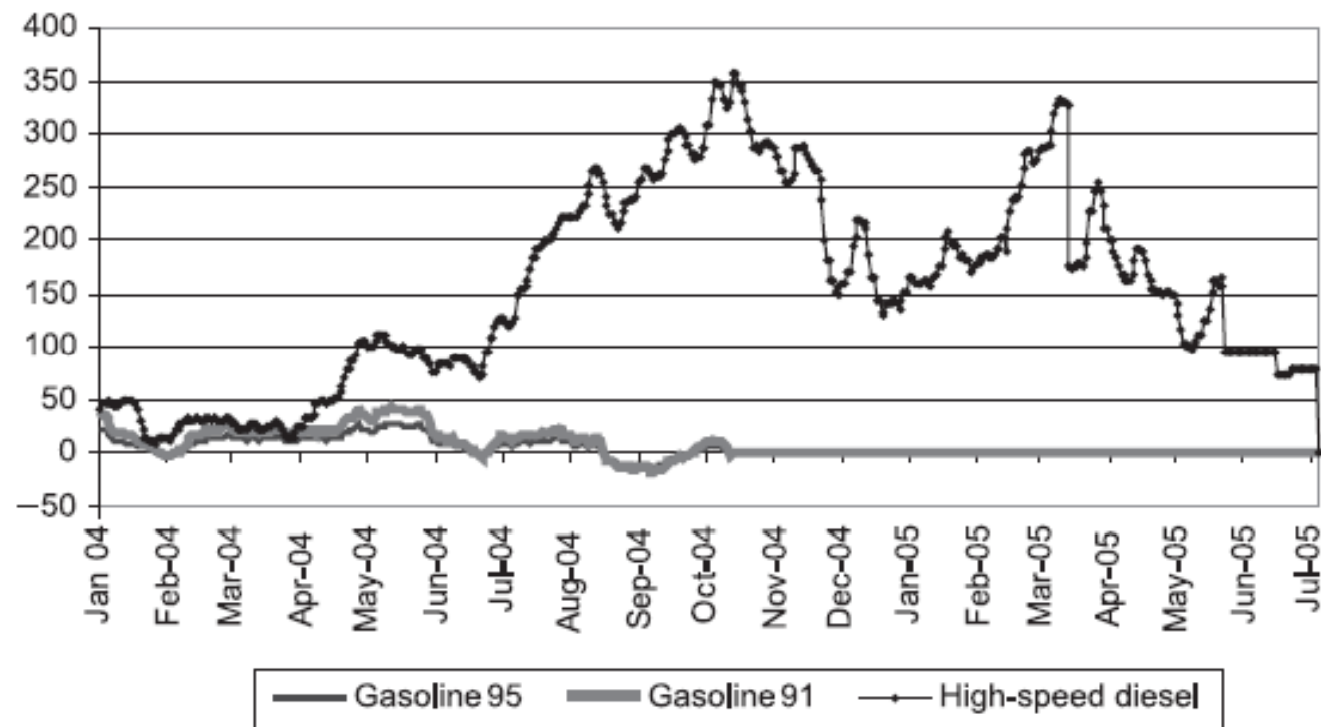
Source: MoF

Chart 3: Inflation rate



Source: MoF

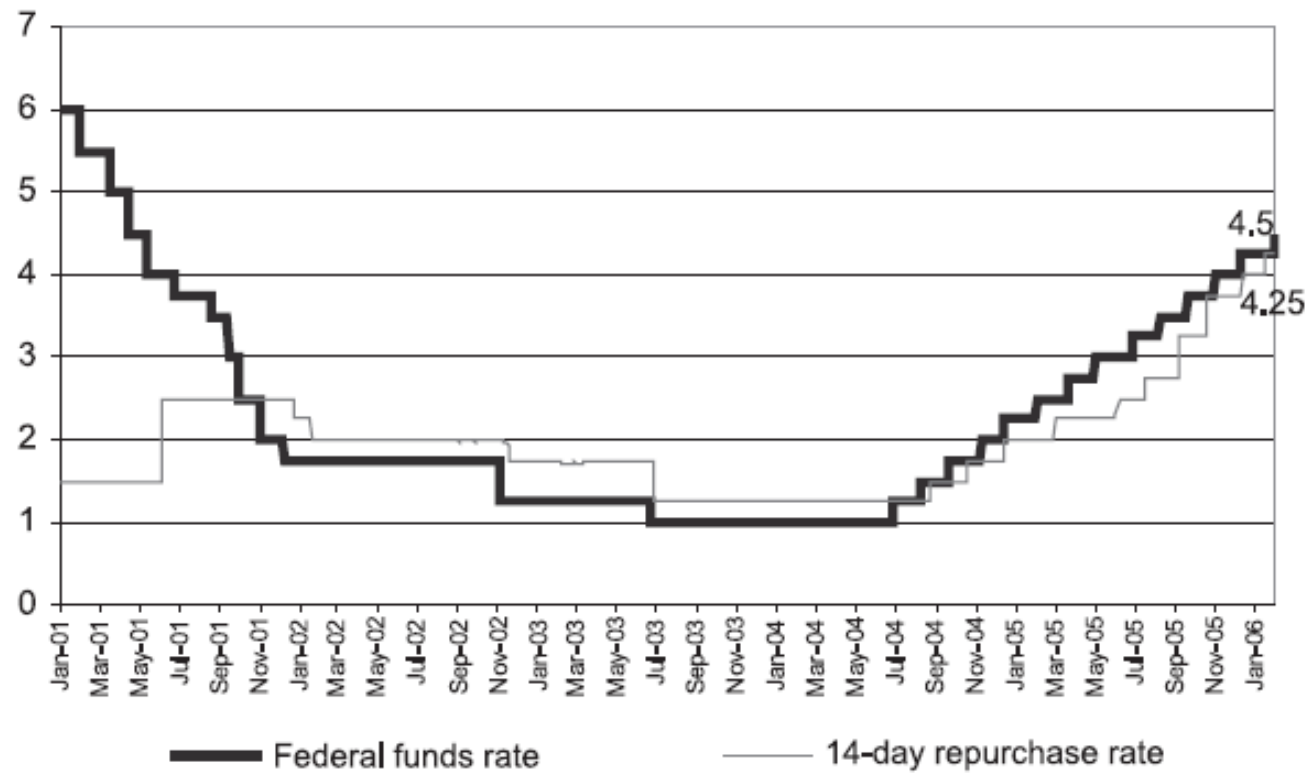
Figure 5. Oil subsidies per day (million baht)



Source: Energy Policy and Planning Office.

Buffeting of Thailand

Figure 6. Federal funds and repurchase rates



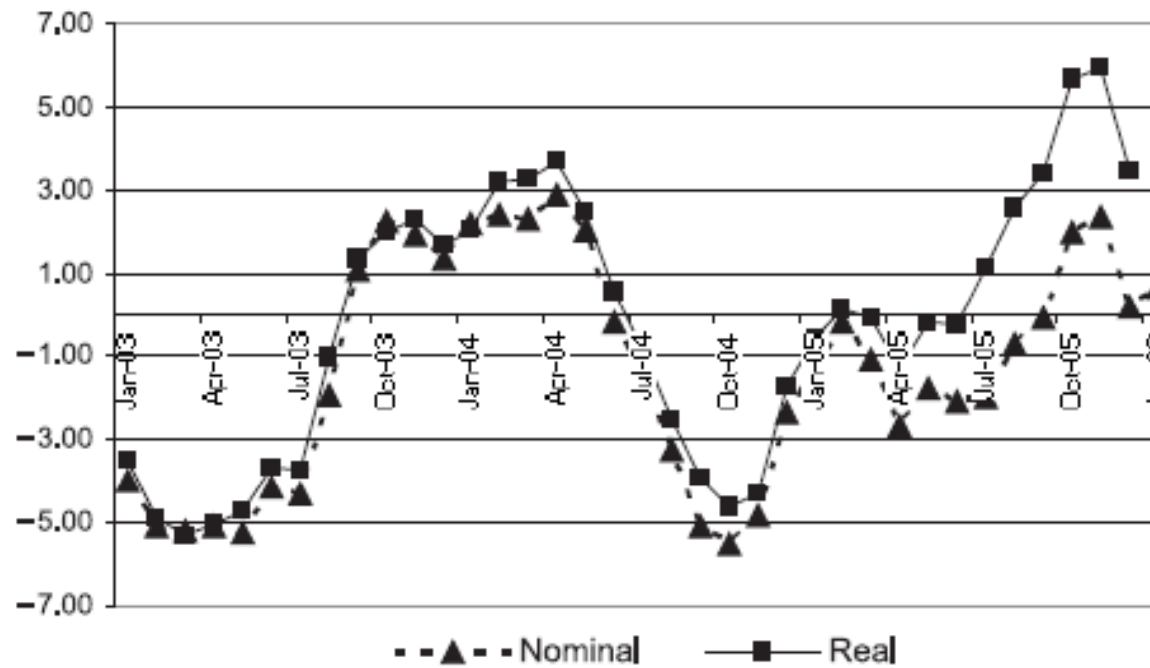
Sources: Bank of Thailand, Federal Reserve.

Bank of Thailand: 3.5%

- Indonesia's policy rate is now 6.75%; India's is 8%.
- That gives central bankers some room to cut if the world economy sags.
- The big exceptions are Taiwan, where the discount rate is less than 1.9%, and Singapore, which carries out monetary policy by setting a path for the exchange rate, not the interest rate.

Buffeting of Thailand

Figure 7. Real and nominal effective exchange rate (% change year-on-year)



Source: Bank of Thailand.

Appropriate policy responses to various economic shocks are very important.

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.

August 28, 2011

- Energy Minister Pichai Nariphaphan said contributions and value-added tax have been cut by 3 baht a litre for diesel, 7.17 baht for 91 octane petrol and 8.02 baht for 95 octane petrol.
- Overall, 10 million motorcycle drivers, 7 million diesel consumers and one million premium petrol users would benefit from the policy.

A temporary policy

- He insisted the measure would be only temporary.
- The Oil Fund is expected to lose 6.16 billion baht in income a month from the measure.
- "The government will monitor oil prices and other economic factors, as well as progress in our policies to raise the incomes of lower-income workers," Mr Pichai said.

According to Mr. Korn

- The reductions in contributions to the State Oil Fund would reduce incentives for commuters to use alternative fuels, affecting long-term energy security, conservation efforts and ethanol producers.
- Mr Korn, the former finance minister, said the government would also face a challenge in raising funds to support cooking gas subsidies.
- Without subsidies from the Oil Fund, local prices for a 15-kilogramme tank of cooking gas would more than double to 570 baht, in line with market prices, he said.
- "The government has two choices _ float gas prices, which will affect lower-income users, or use taxpayer funds to subsidise cooking gas,"

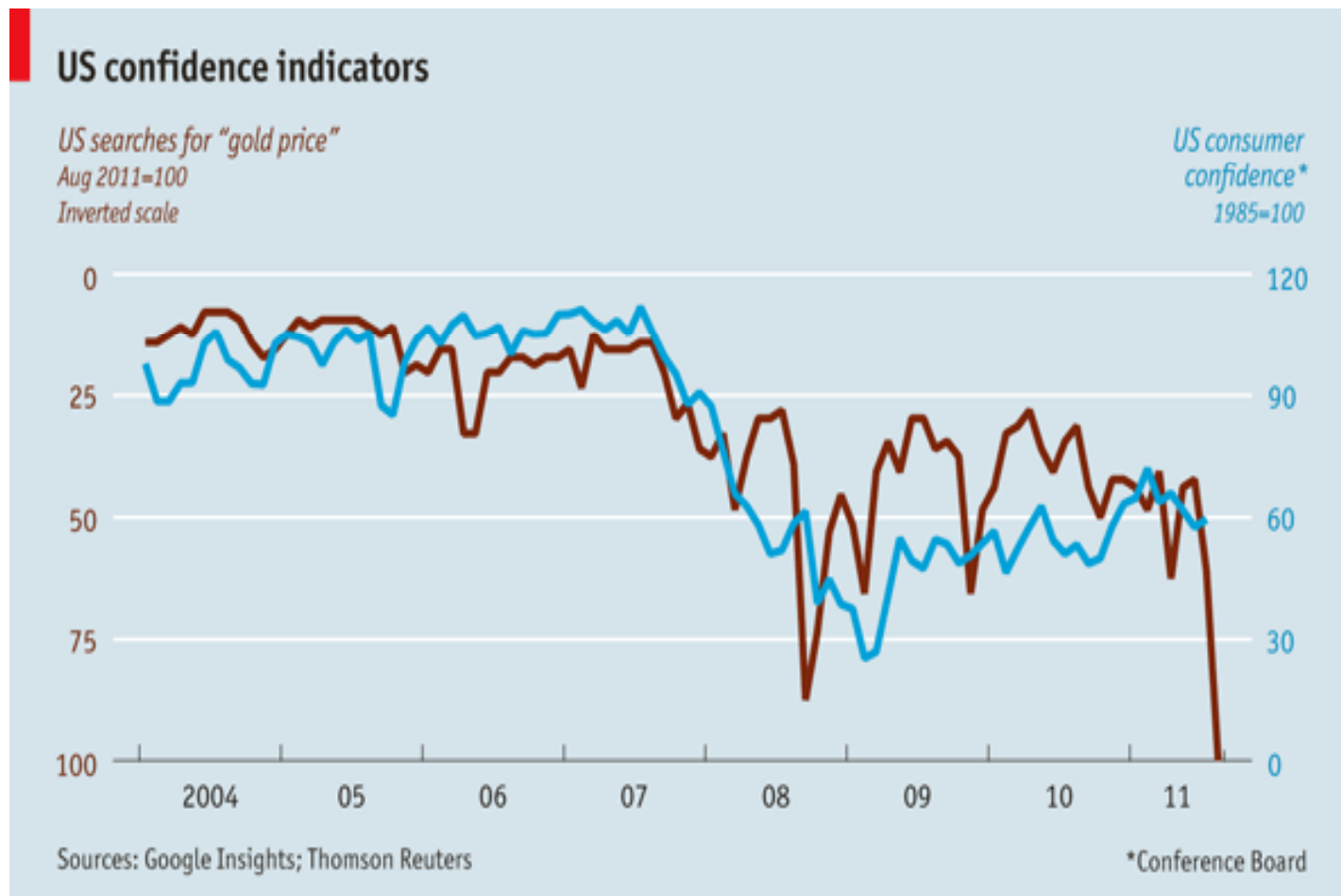
Excise taxes

- The energy policy committee had yet to consider any changes on excise taxes charged for fuel or whether to extend the tax cut measure taken by the last government that is due to expire next month.
- The government collects **7** baht a litre in excise tax for 95 and 91 petrol, **6.3** baht for 95 and 91 gasohol and **0.005** baht for diesel.
- Unleaded 91 petrol prices have risen by 8.5% this year to 41.94 baht a litre while diesel has been capped at 29.99 baht.

Suggested indicators of economic activity

- A vet claims that his business leads the economic cycle by six months, because when times get tough pet owners are quick to cut back on vaccinations and non-essential surgery.
- A reader from the pharmaceutical industry recommends tracking suppositories.
- “Financial worries and austerity changes in diet cause intestinal disorders,” he says, and sales of suppositories therefore rise as the economy goes down the pan.

Gold price as an indicator of the lack of consumer confidence

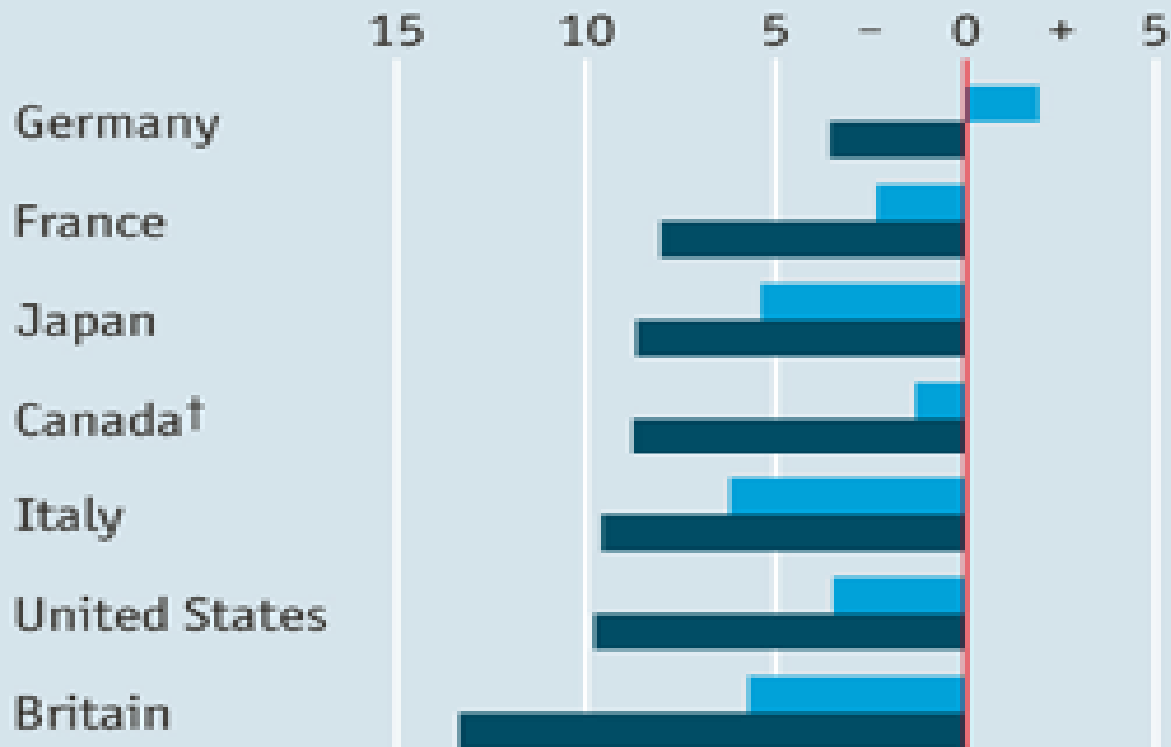


The cost of the crisis

Real GDP per person, Q2 2011

■ % change since Q4 2007

■ % change relative to trend*



*Assumes growth continued at average pace 1997-2007

Sources: Haver Analytics; IMF; JPMorgan; *The Economist*

†Q2 2011 estimate

Inflation threat

- The Thai economy, like many in Asia, sprang free from the great recession surprisingly quickly.
- This year the bigger threat has been the widening jaws of inflation.
- With that in mind, the Bank of Thailand raised interest rates on August 24th for the ninth time since mid-2010. But it was a split decision.
- The economic woes of America and Europe have darkened Asia's mood.

A Policy dilemma?

- Thailand's headline consumer-price inflation (4.1% in the year to July) was too high for the central bank's comfort, but lower than in many of its neighbours, such as China (6.5%), India, where wholesale prices rose by 9.2%, or Vietnam, where consumer prices rose by an alarming 23% in the year to August.