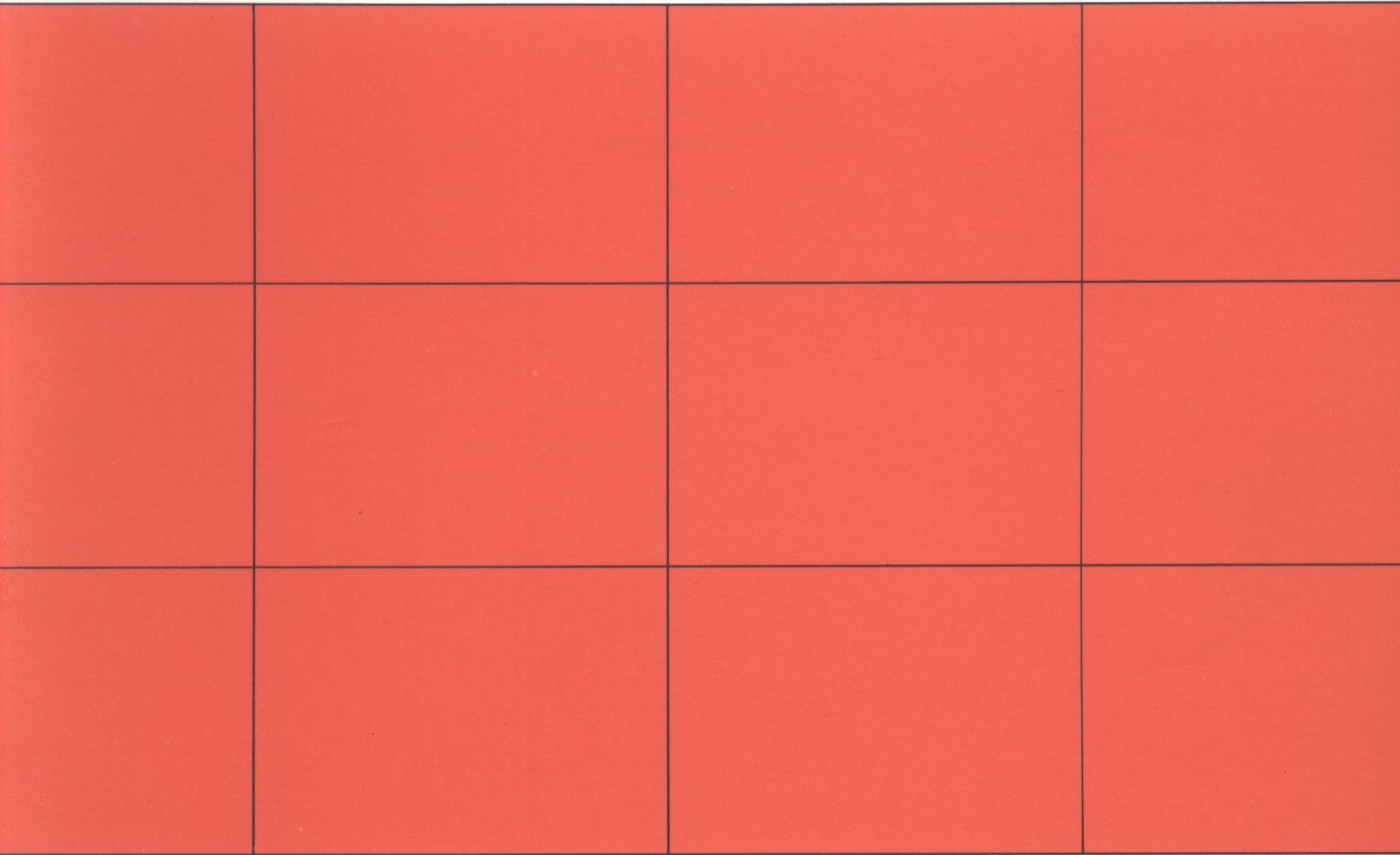


**The Impact of Asian Financial Crisis on  
The Southeast Asian Transitional Economies (SEATEs)  
Country Report: Thailand**

**Nattapong Thongpakde  
Srawooth Paitoonpong**



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Country Paper: Thailand**

by

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## Abstract

This paper investigates the impacts of Thailand's economic crisis on the Southeast Asian Transitional Economies (SEATEs). It found that the contraction of the Thai economy in 1998, the high inflation, the credit crunch, and a reduction in government revenues have some adverse implications on SEATEs in number of areas, especially, trade, investment, tourism, employment, and development cooperation.

After the crisis, Thailand's imports from Lao PDR has been most severely affected by the crisis, while Thailand's imports from Cambodia started to contract in the fourth quarter of 1997. However, a slowdown of imports of Thailand from worldwide is more than that from SEATEs. In addition, over-capacity in some industries and credit crunch in Thailand also restricts investment to be expanded both domestically and internationally. This in turn results in a reduction of Thailand's investment in SEATEs. Furthermore, a number of Thai tourists travel to these countries does not decline as much as the number of Thai tourists travel to other countries, such as, Singapore, Hong Kong, Europe, and USA. In contrast, the baht depreciation may in turn benefit Vietnam's, Cambodia's, and Lao PDR's tourism industry via spill over effect. Since Thailand is one of the major labor receiving countries for workers from SEATEs and other neighboring countries, an "unemployment alleviation action plan", which aimed at reducing the number of undocumented migrant, will more or less result in a reduction of employment of workers from SEATEs. Moreover, a reduction of the 1999 budget for the Department of Technical and Economic Cooperation (DTEC), which is the major organization responsible for coordinating the technical assistance to SEATEs, will certainly affect the technical assistance to receiving countries including mainly SEATEs.

It was noted that these adverse impacts on SEATEs are not only affected by the crisis situation in Thailand, but also from the domestic environment of each country, includes the political stability. For instance, the trend of value of foreign investment in SEATEs has been declining even before the crisis due to number of obstructive domestic rules and regulations.

The study indicates that the possibility for Thai economy to recover remains uncertain. As the external environment is not quite positive to Thailand exports and a lot of constraints are lying ahead, the prospective of Thai economy is hardly to predict. However, according to the sixth Letter of Intents, the recovery is expected to begin in 1999 and for any potential economic recovery to be viable and to sustain, the current credit crunch problems has to be solved quickly and get the financial system back in order.

There are few lessons learned from the crisis which are, firstly, domestic financial systems should have been liberalized before opening up to foreign capital and strict bank regulation and supervision are necessary for financial liberalization to prevent capital influx and investment in unproductive sectors. Moreover, the flexibility of exchange rate system is required as free capital movement and pegged exchange rate are dangerous combination. Furthermore, to rely on foreign capital, FDI is better than portfolio investment and loans since free capital movement, especially short-term, is difficult to control. Last but not least, good governance in both public and private sectors is important. The corruption in public sector and the irregularities in business practices lead to lack of foreign investors' confidence and create efficiency loss.

## I. Introduction

Thailand is the first in the row of the victims of the Asian financial crisis and an alleged carrier of a new epidemic called “*Tomyam Koong Disease*.” Until the crash, Thailand had experienced rapid economic growth from the mid-1980s to early-1990s, with average economic growth rates of 7.6 percent. The Thai economy rebounded strongly from the worldwide recession in the second half of the 1980s and the recovery began as early as the end of 1986 and continued until 1995 at least. Since July 1997 Thailand has been experiencing a severe economic meltdown. No doubt, the crisis of Thailand is worth studying with respect to its causes, impacts with a view to providing lessons for future policy making.

The primary objectives of the present study are to review origin or causes of the Thai crisis, to examine its socio-economic impacts domestically and its potential impacts on the Southeast Asian Transitional Economies (SEATEs) particularly, Cambodia, Lao PDR and Vietnam, and to delineate policy implications. The paper is structured into four sections. The first gives a brief introduction on the objectives and outline of the study. The second part deals with the causes of the crisis and its domestic impacts. The third part examines potential impacts on SEATEs and prospect of the Thai economy. The final section provides concluding remarks, lessons learned and some policy recommendations.

## II. A Review of the Thai Crisis

### 2.1 Causes

The crisis is not the result of a single, time-specific event: it is the result of a process related to weak policies, weak institutions and weak management. In other words, the crisis was caused by many factors, including volatile international financial markets, weak corporate governance and domestic policy failures. An ILO report puts on the list of the determining factors of the crisis “crony capitalism”—political interference in the market via corruption, relatives and cronies of the Government excessive and misallocated investment and a consequent lower rate of return to capital. (Lee, Eddy. 1998). Another school of thought divided causes into immediate and rooting causes of the crisis involving education, human capital etc. Indeed, professional opinion is seriously divided. This section will limit its discussion on the immediate causes with an emphasis on domestic economic factors.

#### *2.1.1 Foreign Exchange Liberalization with fixed exchange rate system*

Thailand’s high economic growth was the result of export growth and the massive inflows of foreign loans due to foreign exchange liberalization, with the establishment of Bangkok International Banking Facility (BIBF), and the Stock Exchange Commission (SEC) Act of 1992.

Foreign exchange liberalization, in short, is a relaxation of cumbersome rules and regulations governing the foreign exchange system of the country, which thwarted smooth international transactions. Since liberalization, there have been only a few restrictions, governing foreign transactions such as the prohibition of a Thai person or a Thai juristic person to invest in securities abroad. The liberalization unquestionably greatly facilitates international transactions including foreign borrowing.

BIBF was established in 1993 to facilitate international lending and borrowings. The aim was to establish Thailand as the financial center of the region. Under this scheme, Thai banks and representatives of foreign banks are allowed to act as intermediaries of foreign international currency transactions. Activities related to BIBF may be classified into three types; out-out, out-in, and in-out. Out-out activities involve lending abroad by borrowing abroad. Out-in activities are those related to lending in the domestic market by borrowings abroad. In-out activities include lending abroad by borrowing from the domestic market. As expected, among the three schemes, the out-in scheme has been the most successful. Initially, the minimum amount of lending was US\$ 500,000. Subsequently it rose to US\$ 2 million. The out-in scheme enabled small and medium size investors to have access to cheap funds abroad.

With the view of financial liberalization, the main objective of the SEC Act of 1992 was to develop the Thai capital market. It allows a limited company and a public company to issue debt instruments abroad as private placement without permission from the Security Exchange Commission. Since the issuing of debt instruments can be done only by large companies, the Act, therefore, permitted a large company to have an access to low interest foreign funds.

### *Influx of Foreign Borrowing*

With the basket system of foreign exchange, the Thai baht in effect was fixed with US dollar and as the exchange rate of the US dollar was quite stable, this eliminated exchange rate risk. In addition, domestic investors as well as arbitrageurs also took the advantage of the high interest rate differentials. As a result, the three schemes undoubtedly *had greatly promoted the massive foreign borrowings* through BIBF and the issue of long term debt instruments, which were mainly European Convertible Debentures. *The borrowings were often used to finance investment in various sectors, especially, property development and speculative activities.* Evidence of the sharp rise in investment may be found in the drastic increase in proportion of private investment spending in GDP and the high proportion of imported capital goods to total import during 1993 to 1996.

The government at that time also unintentionally stimulated foreign borrowings by drastically expanding expenditure. Although the budget was in surplus, government spending continued to increase. During the period 1993 to 1995, government spending increased at a rate of 17 percent on average. With the sharp increase in private and public spending, the Bank of Thailand maintained high interest rates in order to keep inflation under control. The high interest rates, stable exchange rates, and economic prosperity undoubtedly further induced more foreign borrowings.

The massive foreign borrowings and investment unfortunately later on caused the current severe economic downturn of the country. The massive borrowings led to an *enormous increase in the foreign debt burden*. Foreign debts outstanding increased from US\$ 43.6 billion in 1992 to US\$ 90.5 billion at the end of 1996. Foreign debts continued to increase in the first, the second and the third quarter of 1997 but then decreased through the fourth quarter of 1997, the first and the second quarter of 1998 to US\$ 88.2 billion (Table 2.1).

### **2.1.2 Weaken Financial Institutes due to High Non-performing Loans**

Furthermore, some foreign loans were not used productively, and there was *over investment* in many sectors, such as real estate and basic industries causing massive *excess supply*. The excess supply of housing in Bangkok and the metropolitan area is expected to exceed 300,000 units, and the occupancy rate of office space in Bangkok has dropped to only about 60 percent at the end of 1998. Due to the excess supply, some investors are unable to repay both foreign and local debts. As a result, *non-performing loans* proliferated creating problems for financial institutions. However, the problems were overshadowed by the illusion of the strong and never ending economic prosperity at the time.



Table 2.1 External Debt

(Billions of US\$)

	1992	1993	1994	1995	1996	1997 P	1997Q2p	1997Q3p	1997Q4p	1998Q1p	1998May.p
<b>Total Debt Stocks (End of Period)</b>											
<b>Public Sector</b>	<b>13.07</b>	<b>14.17</b>	<b>15.71</b>	<b>16.40</b>	<b>16.81</b>	<b>17.17</b>	<b>17.35</b>	<b>17.02</b>	<b>17.17</b>	<b>17.70</b>	<b>17.42</b>
Long-term	12.52	14.17	15.53	16.32	16.75	17.15	17.33	17.00	17.15	17.68	17.40
Short-term	0.55	-	0.18	0.09	0.05	0.02	0.02	0.02	0.02	0.02	0.02
<b>Private Sector</b>	<b>30.59</b>	<b>37.96</b>	<b>49.15</b>	<b>66.17</b>	<b>73.73</b>	<b>67.32</b>	<b>75.60</b>	<b>71.76</b>	<b>67.32</b>	<b>63.17</b>	<b>61.81</b>
Long-term	12.26	15.30	20.15	25.16	36.17	37.41	39.07	39.30	37.41	37.02	36.89
Short-term	18.33	22.66	29.00	41.01	37.56	29.91	36.54	32.46	29.91	26.15	24.92
Commercial Bank	6.30	5.30	9.87	14.44	10.68	8.16	11.76	9.89	8.16	8.92	9.03
Long-term	0.80	1.30	3.45	4.44	2.31	2.55	3.28	3.07	2.55	2.84	3.84
Short-term	5.50	4.00	6.42	9.99	8.37	5.62	8.49	6.82	5.62	6.09	5.19
BIBF	-	7.74	18.11	27.50	31.19	30.08	32.57	31.17	30.08	27.82	26.54
Long-term	-	1.34	2.97	3.80	10.70	10.32	11.40	11.41	10.32	9.82	8.47
Short-term	-	6.40	15.14	23.70	20.49	19.76	21.17	19.76	19.76	18.00	18.07
Non-Bank	24.29	24.92	21.18	24.23	31.86	29.08	31.27	30.71	29.08	26.43	26.24
Long-term	11.46	12.66	13.73	16.91	23.16	24.55	24.39	24.82	24.55	24.36	24.58
Short-term	12.83	12.26	7.44	7.31	8.70	4.53	6.88	5.89	4.53	2.06	1.66
<b>Monetary Authorities</b>	-	-	-	-	-	7.29	-	4.48	7.29	9.30	8.99
Use of IMF credit	-	-	-	-	-	2.43	-	1.62	2.43	2.70	2.67
Others	-	-	-	-	-	4.87	-	2.86	4.87	6.60	6.32
<b>Total</b>	<b>43.66</b>	<b>52.13</b>	<b>64.86</b>	<b>82.57</b>	<b>90.54</b>	<b>91.78</b>	<b>92.96</b>	<b>93.26</b>	<b>91.78</b>	<b>90.16</b>	<b>88.22</b>
Long-term	24.78	27.47	35.68	41.47	52.92	61.85	56.40	60.78	61.85	63.99	63.28
Short-term 1	18.88	22.66	29.18	41.10	37.61	29.93	36.56	32.48	29.93	26.17	24.94
<b>Debt Service Ratio</b>	<b>10.5</b>	<b>10.7</b>	<b>11.3</b>	<b>11.4</b>	<b>12.3</b>	<b>15.8</b>	<b>16.6</b>	<b>15.3</b>	<b>16.7</b>	<b>20.3</b>	<b>n.a.</b>
Public sector	3.7	3.7	3.4	2.8	2.5	2.6	2.0	3.3	2.2	3.1	n.a.
Private sector	6.8	7.0	7.9	8.6	9.8	13.2	14.6	12.0	14.5	17.2	n.a.

Short-term external debt is defined as debt that has an original maturity of one year or less.

BIBF's debt has been adjusted to original maturity basis since January, 1996, consistent with other external debt items.

Source: Bank of Thailand

Table 2.2 indicates a significant increase in the proportion of NPL to total loans of commercial banks during June 1997 to December 1997. Although total loans slightly increased during this period, the proportion of NPL to total loans drastically increased from 8.4 percent to 20.1 percent. The problem of bad debts of financial institutions is partly attributable to the supervision of the Bank of Thailand. Unlike most central banks, the bank of Thailand also supervises financial institutions. In addition, in case of troubled financial institutions, the Bank of Thailand also plays a supervisory role in the rehabilitation of those institutions. Since the Bank of Thailand is greatly independent from the Ministry of Finance and politics, it has almost absolute power to oversee activities related to financial institutions, and there is no other economic agent involved in the activities. Some information of financial institutions is classified as secret and cannot be disclosed to the public. Due to the system, the efficiency of the supervisory role of the Bank of Thailand has eroded overtime.

On 3rd March 1997, the Bank of Thailand ordered 10 financial companies which faced NPL and insolvency problems to recapitalize within 45 days and if they were not able to recapitalize, the Financial Institution Development Funds (FIDF) would then intervene. On 27th June, the Bank of Thailand made a decision to temporarily close down insolvent 16 financial companies and subsequently a further 42 companies on 5th August 1997.

### ***2.1.3 Weak Corporate Governance***

The question of how independent and transparent the management of the Bank of Thailand and other regulators in the financial sector, for example, the Stock Exchange of Thailand (SET) and the Securities and Exchange Commission (SEC) was brought into everyone's attention following the disclosure of the Bangkok Bank of Commerce Public Company Limited (BBC) problem. The BBC case has been described as the largest banking fraud in Thailand's history and one of the biggest in the world, cost Thailand more than 200 billion baht in bail out funds for BBC. The problem arose as more than 75 billion baht was borrowed by politicians and/or companies controlled by them of which about 5 percent have been repaid.

The similar situation also appeared in a number of financial companies as large sum of money were moved on the signatures of top executives and thus were recently under investigation of the Bank of Thailand. General Finance and Securities Public Company Limited executives were under investigation for allegedly having approved loans without sufficient collateral. Stica Investment Finance and Securities Public Company Limited executives were under investigation in relation to approximately 2 billion baht in money transfers to its leasing unit with little or no supporting documentation to legitimize such payments. Similarly, three of Finance One Public Company Limited top executives have been charged by the Bank of Thailand for approving loans exceeding 2.1 billion baht to two companies (located at the same address) which had a combined capitalization of 310 million baht and thus in turn combined negative net worth of 1.435 billion baht. In fact, such fraud transactions or connected party transactions appear consistently, not only in the financial sector and the one who benefit from such transactions are those who have the appropriate relationships with politicians, senior government officers and company executives.

Viverito (1998) suggested that a shortage of local accounting supervision brought on by a shortage of quality auditors, restrictions against foreign auditors and ineffective controls have contributed to the economic crisis in Thailand. The absence of corporate controls, the mingling of funds among listed and closely held companies of the same family, the use of multiple sets of accounting books and the highly paid rubber stamp directors are common characteristics of Thailand's private companies which is one of reasons that have brought Thai economy to the brink of collapse. Alphatec Electronics Public Company Limited is a good example in this story. Profits of the company had been overstated by at least 164 million US dollar during three-year period and at least 160 million US dollar had been transferred to other companies controlled by the founder without board approval. This recently generates great value of debt of 450 million US dollar to the company.

**Table 2.2 Loans and Non-Performance Loans of Commercial Banks**

	NPL		%Growth (Dec97/Jun97)	Total Loans*		NPL/Loans	
	Jun-97	Dec-97		Jun-97	Dec-97	Jun-97	Dec-97
Bangkok Bank	79,035	180,572	128.5	971,362	1,074,396	8.1	16.8
Krung Thai Bank	63,729	148,412	132.9	618,415	687,910	10.3	21.6
Thai Farmers Bank	41,434	105,379	154.3	563,272	609,494	7.4	17.3
First Bangkok City Bank	11,472	130,834	1040.5	237,299	287,915	4.8	45.4
Siam City Bank	14,233	70,401	394.6	198,378	233,634	7.2	30.1
The Siam Commercial Bank	27,836	66,403	138.6	468,250	568,160	5.9	11.7
Bangkok Metropolitan Bank	28,460	62,688	120.3	170,879	187,614	16.7	33.4
Bank of Ayudhaya	22,276	55,147	147.6	369,947	406,568	6.0	13.6
The Thai Military Bank	26,652	46,908	76.0	286,649	303,263	9.3	15.5
The Bangkok Bank of Commerce	27,225	45,417	66.8	150,531	148,799	18.1	30.5
The Laem Thong Bank	3,502	23,621	574.5	35,009	42,244	10.0	55.9
Bank of Asia	8,900	16,886	89.7	112,871	134,289	7.9	12.6
The Thai Dhanu Bank	5,563	16,534	197.2	105,725	115,814	5.3	14.3
The Union Bank of Bangkok	6,515	14,279	119.2	54,616	57,560	11.9	24.8
Nakornthon Bank	2,980	6,357	113.3	55,469	60,027	5.4	10.6
<b>Total</b>	<b>369,812</b>	<b>989,838</b>	<b>167.7</b>	<b>4,398,672</b>	<b>4,917,687</b>	<b>8.4</b>	<b>20.1</b>

\* Prior to deduction of provision for possible loan losses

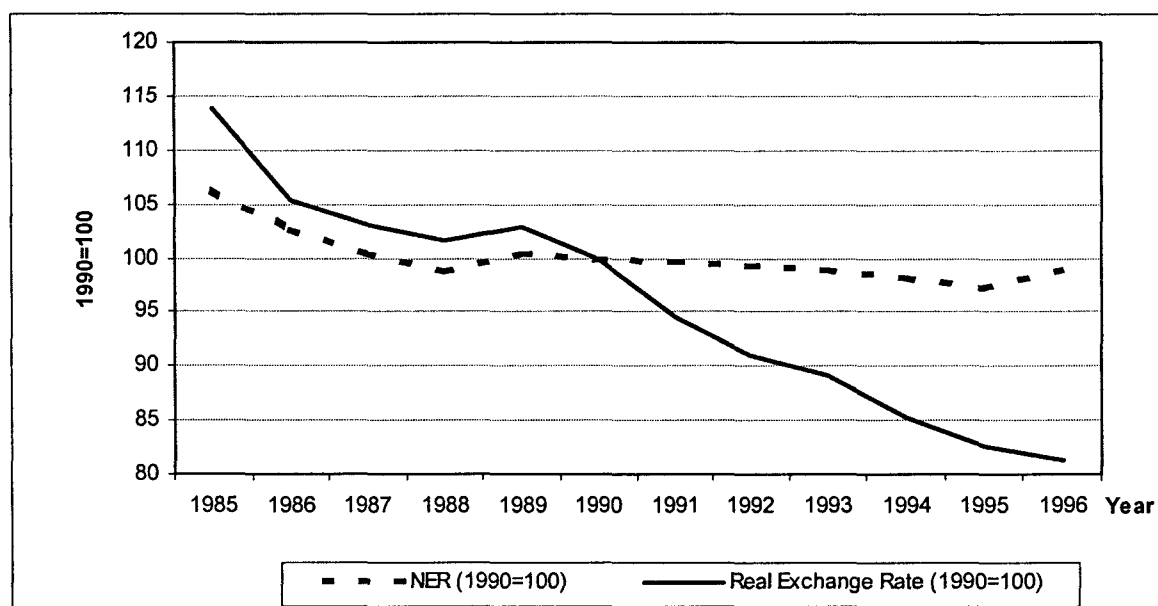
Source : Lewis (1998)

### 2.1.4 The Baht Appreciation and Export Slowdown

The economic prosperity came to an abrupt end in 1996. The US dollar after reaching its lowest level of about 79 Japanese yen per dollar at the end of 1995, rebounded strongly to a peak of about 127 yen per dollar in the mid 1996. As Thai baht was pegged against the dollar dominated basket system, it also appreciated against other currencies. Figure 2.1 shows changes in the nominal and real exchange rate of the baht and US dollar during 1985 to 1996. The nominal exchange rate of the baht was appreciated from 27.16 baht per US dollar in 1985 to its highest level at 24.92 baht per US dollar in 1995 but then slightly depreciated to 25.34 baht per US dollar in 1996. The real exchange rate of Thailand has also been continually and significantly appreciated since 1985 which has been mainly due to a continuous and higher increase of the price level in Thailand than those in her major trading partners. This in turn deteriorated Thailand's competitiveness and led to the slowdown of export, especially in labor-intensive products since the price of Thai exports, in term of dollar, was not competitive.

The problem was compounded by the inventory cycle in the US, and the inventory cycle of electronics worldwide. The export growth dropped sharply from about 23 percent in 1995 to 0.5 percent in 1996. In fact, most regional countries also experienced an export growth slowdown. Export growth of Malaysia and Singapore, in particular, exhibited a similar pattern to that of Thailand. Since exports contribute about 20 percent of GDP, a drop in export growth obviously had a strong adverse impact on economic growth, and GDP dropped from 8.6 percent in 1995 to about 6.7 percent in 1996.

**Figure 2.1**  
**Changes in Nominal and Real Exchange Rate (1990=100)**



**Data for Figure 2.1: Nominal and Real Exchange Rate of Thailand, compare with US dollar**

(1990=100)	1985	1986	1987	1988	1989	1990
NER	106.15	102.79	100.54	98.86	100.46	100
Real Exchange Rate	113.85	105.23	102.99	101.51	102.80	100
(1990=100)	1991	1992	1993	1994	1995	1996
NER	99.73	99.28	98.96	98.30	97.38	99.05
Real Exchange Rate	94.54	90.97	89.04	85.15	82.67	81.29

\* Weighted average of real exchange rate between Thailand and her 10 major trading partners which are USA, Japan, France, Germany, Netherlands, United Kingdom, China, Hong Kong, Malaysia, and Singapore.

Source: International Financial Statistics 1997. IMF.

### 2.1.5 High Current Account Deficit

Table 2.3 indicates a significant increase in current account deficit during 1987-1996. The current account deficit increased from 0.7 percent of GDP in 1987 to 8.5 percent of GDP in 1990 and continued to be high in a range between 5-8 percent until 1996. Theoretically, the rapid economic growth and high current account deficit indicated the imbalance between aggregate demand and aggregate supply. The excessive expansion of demand due to the surge of investment financed by foreign borrowing, is acceptable only if the investment project paid off, especially in terms of foreign currency earnings. However, as mentioned, most of foreign borrowing had been used in several unproductive activities, this in turn caused the economy to become more vulnerable to internal and external shocks. Moreover, since exports had stagnated and an over supply situation had developed in various sectors, confidence in the Thai economy and value of the baht eroded. Since the economic slowdown, the Thai economy has declined ever, and hidden problems began to emerge, which have greatly aggravated the severity of the economic downturn.

**Table 2.3**  
**Macroeconomic Indicators**

	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997
<b>Economic Growth (%)</b>	9.50	13.30	12.20	11.60	8.40	7.80	8.30	8.80	8.60	5.50	-0.40
<b>Inflation (%)</b>	2.50	3.80	5.40	6.00	5.70	4.10	3.40	5.20	5.70	5.90	5.60
<b>Current Account/GDP (%)</b>	-0.70	-2.70	-3.50	-8.50	-7.70	-5.70	-5.10	-5.60	-7.90	-7.90	-2.20
<b>Exchange Rates</b>	25.72	25.29	25.70	25.59	25.52	25.40	25.32	25.15	24.92	25.34	31.37
<b>Export Growth (%)*</b>	28.48	34.59	27.94	14.24	23.03	13.65	13.49	21.56	23.62	0.41	27.90
<b>Interest Rates (%)</b>	9.50	9.50	9.50	12.30	13.70	8.90	8.60	8.50	11.60	9.10	11.50

Note: \* Value of exports is calculated in terms of Baht.

Source: International Financial Statistics, 1997; World Economic Outlook, May 1998;  
Bank of Thailand's Key Economic Indicators, various issues.

### 2.1.6 Currency Attacks and Depletion of Foreign Exchange Reserve

The above discussion indicates the vulnerability of the Thai economy. The huge foreign debt outstanding accumulated during 1993 to 1996, high current account deficits for two consecutive years, an excess supply in property and other sectors leading to high and increasing non-performing loan of financial institutions, the unusually strong baht, and the slowdown of exports have made the baht unstable. As a result of these problems, the baht was under attacks by international hedge funds for almost two years and the Bank of Thailand adopted a strategy of defending the baht by keeping interest rates high. The inter-bank rate began to rise and the money market become more illiquid. As a result of the unstable baht and other economic problems, capital outflows has made credit tighter and interest rates have surged. The high interest rates and tight credit market caused a further slowdown in private investment and consumption spending. It is quite clear that the Thai economy currently is in a downturn of the current business cycle.

The severe baht attacks occurred in February and, subsequently in May 1997, as speculators staked on the fact that the Bank of Thailand would not able to endure the shaky situation. To defend the baht, the Bank of Thailand had to utilize foreign reserves to counter the attacks by buying in the both spot and forward markets. In May alone, foreign reserves fell by as much as US\$ 4 billion. The forward commitment of a long position on baht taken by the Bank of Thailand totaled an astonishingly high as US\$ 23.4 billion. In addition to the conventional scheme to defend the baht, The Bank of Thailand also adopted a two-tier foreign exchange market system, and the foreign exchange market was separated into on shore and off shore markets in May 1997. Under this scheme, financial institutions in Thailand were instructed not to transact baht in the off

shore market to limit the supply of baht to currency speculators. As a result, the speculators were unable to find baht to cover their short positions and were forced to settle with the Bank of Thailand. Apparently, the scheme worked at least in the short term as the gap between the off shore rate and on shore rate was rather substantial at the beginning of the scheme. Although the gap has become narrower, especially after the baht floatation, casted doubt on the effectiveness of the scheme and BOT abolished it in early 1998.

Since the attack in May, the financial situation has worsened. The money market has become tight which is reflected by the surge of inter bank rates which peak at almost 30 percent. Capital outflows rose and foreign reserves continued to dwindle. At the end of May, the minimum lending rate and minimum over draft rate rose sharply as liquidity was drained from the system. The situation deteriorated as the high interest rate slowed down the economy and non-performing loans rose, and rumors about financial difficulties spread. Consequently, panic ensued resulting in deposit runs at many financial companies producing a liquidity crunch in these companies. The problems in the financial sector finally began to permeate to the production sector due to the tight liquidity and high interest rates. Speculation about the baht devaluation became stronger causing capital outflows, which, in turn, caused a drain on liquidity in the financial market. The inter-bank rate has risen since the beginning of April and foreign reserves have dropped sharply due to the uncertainty of the economy and the defense of the baht.

Finally, the Bank of Thailand decided to abandon the old exchange rate regime of the basket system on July 2 and adopted the new managed float regime. Under this new regime, the value of the baht is determined by demand and supply of the baht. The former process whereby the mid-rate was quoted by the Exchange Equalization Fund each morning has been canceled. The reference rate which is the average closing rate of baht traded by the 15 commercial banks on the previous day is used under the regime, and the baht is expected to move according to economic fundamentals. The exchange rate will be closely monitored by the authorities who will intervene when necessary to stabilize the rate within an unspecified range.

The severity of the economic downturn and problem accumulated during the economic expansion reveal that the Thai economy and policy makers are not ready for the globalization of capital mobilization. There are weaknesses in various institutions including financial system and the supervision of financial system, policy making process and business community. For the Thai economy to have sustainable prosperity, these weaknesses must be seriously dealt with and structural adjustment in various sectors, financial sector, in particular are needed. Finally, the Thai government requested assistance from the International Monetary Fund (IMF) to alleviate the economic crisis.

## **2.2 Impacts of the Crisis**

### **2.2.1 Economic Impacts**

#### *a.) Exchange rates instability and increase in debt burden*

Unfortunately, similar to most countries whose currencies were floated, the baht has been volatile. As expected, the baht has depreciated because it had been considered overvalued. Since the change in the exchange rate regime, the baht has depreciated considerably from about 26 baht per US. dollar prior to the floatation to about 30 to 32 per US. dollar in the first two months after the floatation, and dropped to about 35 to 37 baht per US. dollar at the beginning of October. The baht continued to depreciate afterwards and hit its lowest point in January 1998 as it had been depreciated more than 100 percent to 56 baht per US. dollar. The baht has then appreciated and became stable in the range between 39 and 41 baht per US. dollar since the mid of March 1998 and further increased to 36 to 37 baht per US. dollar at the beginning of November.

Although, the baht floatation was considered as the first and necessary step to revive the ailing economy, it will have far reaching effects on the Thai economy in the short term. Since foreign debts were as high as US\$ 92.96 billion, at the end of the second quarter of 1997, the depreciation of the baht unquestionably causes a higher burdens for Thai debtors at immense size. Many corporations will go bankrupt as a result

*b.) Financial sector*

As mentioned above, many finance companies and commercial banks have experienced the problem of insolvency because an increasing share of their loans has become non-performing undermining profitability capacity. They also have faced liquidity problem since they have to pay back their foreign loans. Due to the economic situation, foreign lenders are unwilling to roll over the short-term debt. Furthermore, in the middle of 1997, there was the deposit run in finance companies and some small commercial banks because of the lack of confidence. These institutes had to borrow from the Bank of Thailand through Financial Institutes Development Fund (FIDF) which acts as the lender of the last resort. The excessive debt burden and undercapitalization of financial institutes caused the Bank of Thailand to intervene their operation.

On June 27 1997, the Bank of Thailand had temporarily closed down 16 financial companies, and then further closed down 42 financial companies on August 5th 1997. Since the economic situation was not improved during that period, the Bank of Thailand decided to permanently close 56 of 58 financial companies in December 1997. This closure reduced the liquidity in the financial system. There are a few more factors that cause illiquidity in the economy. Because of high non-performing loans, the existing finance companies and commercial banks need to increase their capital to satisfied BIS ratio. Furthermore, the Bank of Thailand initiates the new standard on provision of financial institutes' loans so these commercial banks are required to increase their reserves. There is no incentive for financial institutes to provide loans to business, with the exception of their old customers who have very good record, since they have to raise the provision and capital if the loans are bad ones.

These altogether cause the credit crunch and thus high interest rate. *Credit crunch* arose as banks were reluctant to lend to most corporations whose balance sheets have been significantly deteriorated as a result of the depreciation which in turn led to the contraction of the economy since the support of the domestic private companies by local financial institutions has been withdrawn. In addition, credit crunch could also be viewed as a result of a set of conditionalities stipulated by the IMF, along with its rescue package, for the purpose of financial reform. The tighter regulations and supervision of financial institutions were needed in order to restore both confidence in and stability of the financial system, the more difficult for investors to be approved to have an access to banks' loans. Without any doubts, the credit crunch directly affected in a fall in investment.

High interest rate was also one of obstacles to investment. Although high interest rate could be viewed as the mechanism to screen out bad borrowers, it discouraged investment. Interbank rates stayed in a range of 9-11 percent in 1995-1996, surged to 15-16 percent in 1997 and continued to increase to approximately 20 percent in the first four months of 1998 (Table 2.4). The minimum overdraft rate (MOR) and minimum lending rate (MLR) also shifted in a similar fashion in which MOR increased from 13.25-13.50 percent in June 1997 to 15.75-16.25 percent in April 1998 while MLR increased from 12.75 percent to 15.25-15.50 percent during the same period.

Vichyanond (1998) suggests that the primary reason for the escalation of interest rates is that money supply was drained out of the system to an increasing extent. The difference between the balance of payments (BOP) and the government cash surplus (GCS), which represents the net amount of money injected into the system, fell significantly from 53.3 billion baht in 1995 to 11.4 billion baht in 1996 and -308.3 billion baht in 1997, mostly attributed to worsening BOP. The drastic deterioration of BOP was mainly due to speculation on baht devaluation and repayments of

external debts in 1996-1997. However, in 1998, the improvement of the balance of payments, a further decrease in manufacturing production and private investment have not resulted in the reduction of interest rates. In contrast, interest rates have moved up slightly which in turn indicated that the credit crunch in 1998 was not caused by liquidity shortage, but rather due to a set of IMF requirements as mentioned above.

**Table 2.4**  
**Macroeconomic Monthly Data**

		Private Investment Index	Manu. Production (growth of 12 m. mov avg)	BOP (bln)	GCS (bln)	BOP-GCS (bln)	Interbank (%)	MOR (%)	MLR (%)
1995	1	115.6	8.8	-12.1	9.6	-21.7	12.43	11.75	11.75
	2	119.1	10	14	4.2	9.8	13.2	12.25-12.75	12.25
	3	121.4	10.3	-11.9	-1.4	-10.5	14.26	13.00-13.25	13
	4	122.9	10.8	32.9	9.5	23.4	13.08	13.50-13.75	13.5
	5	123	11.6	37.3	20.6	16.7	10.84	13.50-13.75	13.5
	6	125	11.8	43.3	30.7	12.6	9.5	13.50-13.75	13.5
	7	128.3	12.1	-8.6	22.5	-31.1	6.97	13.50-13.75	13.5
	8	124.2	12.1	21.8	-4.9	26.7	9.46	13.50-13.75	13.50-13.75
	9	124.1	12.2	28.6	17.3	11.3	11.3	13.50-13.75	13.50-13.75
	10	118.6	12	0.3	14.9	-14.6	8.65	13.75-14.00	13.50-13.75
	11	120	11.7	12.6	4.3	8.3	11.56	14	13.75
	12	118.9	11.9	21.3	-1.1	22.4	10.29	14.00-14.25	13.75
1996	1	118	11.7	24.8	15.4	9.4	7.06	14	13.75
	2	115.6	11.8	15.3	1.2	14.1	8.26	13.75-14.00	13.75
	3	113.4	10.8	9.9	-0.6	10.5	6.58	13.75-14.00	13.75
	4	111.4	10.3	-2	14.9	-16.9	6.12	13.75-14.00	13.75
	5	107.6	9.6	7.7	6	1.7	6.82	13.75-14.00	13.25-13.75
	6	104	8.9	20.5	36	-15.5	9.78	13.75-14.00	13.25-13.75
	7	101.3	8.3	-17.1	5.6	-22.7	10.54	13.25-13.75	13.25-13.50
	8	100.1	7.8	2.6	1.2	1.4	10.77	13.25-13.75	13.25-13.50
	9	100.9	7.7	8.4	6.4	2	12.94	13.25-13.75	13.25-13.50
	10	101.7	8	10	4.7	5.3	10.11	13.25-13.75	13.25-13.50
	11	98.8	7.6	-6.2	-17.2	11	10.7	13.25-13.75	13.25-13.50
	12	98.5	7.2	-19.2	-30.3	11.1	12.12	13.25-13.50	13.00-13.25
1997	1	96.3	7.4	24.7	2.9	21.8	10.65	13.25-13.50	13.00-13.25
	2	93.2	6.5	-26.6	-5	-21.6	14.94	13.25-13.50	13.00-13.25
	3	92	6.9	-0.7	0.6	-1.3	8.34	13.25-13.50	13.00-13.25
	4	91.1	6.7	-15.5	7.6	-23.1	8.75	13.25-13.50	12.75-13.00
	5	88.4	6.7	-112.3	-4.7	-107.6	12.13	13.25-13.50	12.75
	6	88.3	6.8	-24.6	29.5	-54.1	15.1	13.25-13.50	12.75
	7	88.2	6.7	-51.5	-18.7	-32.8	18.66	14.25-14.50	13.75
	8	83.5	5.6	-146.1	-21.9	-124.2	15.43	14.25-14.50	13.75
	9	80.2	4.3	133	21.5	111.5	23.87	14.75-15.00	14.25
	10	74.9	2.3	58.3	-17.4	75.7	18.72	15.25-15.50	14.75
	11	73.4	0.6	-185	11.9	-196.9	19.99	15.25-15.50	14.75
	12	69.7	-0.8	46.9	2.6	44.3	21.73	15.75-16.00	15.25
1998	1	61	-2.4	-19.5	3.5	-23	21.51	15.75-16.00	15.25
	2	55.8	-3.9	-26.7	0.4	-27.1	19.83	15.75-16.25	15.25-15.50
	3	49.5	-6.7	70.7	3.1	67.6	20.57	15.75-16.25	15.25-15.50
	4	40.5	-8.6	71.2	5	66.2	19.11	15.75-16.25	15.25-15.50
	5			-73.2					

Source: Bank of Thailand.



Although the government recently attempts to relax the monetary policy and to reduce interest rate in order to stimulate the economy, the commercial banks are still unwilling to lend due to the NPL problem.

*c.) Saving and investment*

The persistently high interest rates and economic downturn unquestionably have forced most entrepreneurs either to abolish or to postpone investment projects. There are two signs of a decline in investment spending; a slowdown in the investment index, and a decline in both the number of projects which have applied for investment promotion from the Board of Investment and the projects actually started. The number of projects that have applied for investment promotion from the Board of Investment decreased from 1,193 projects in 1996 to 993 projects in 1997 (Table 2.5). Such number is also expected to further decline in 1998 as only 735 projects have applied for investment promotion during January to October 1998. In addition, the number of projects actually started also decreased from 609 projects in 1996 to 480 projects in 1997. However, such number increased to 619 projects during January to October 1998.

The process whereby investment varies directly with GDP is known as the Acceleration Principle. Theoretically, during the business cycle, the accelerator works with a multiplier causing economic fluctuations. In case the of the current economic downturn, the theory fits rather well as investment spending is declining with the downturn. However, in this case, the decline in investment partly is the result of the tight money market and high interest rates, not from the economic downturn per se. Consequently, the downturn is more severe than a normal one

The economic situation has deteriorated rapidly mainly due to liquidity problem. Eventually, the Bank of Thailand decided to relax the monetary policy. The required reserve ratio was reduced 7 to 6 percent and the deposit rate of financial companies was tied to the deposit rate of banks as the rate offered by financial companies cannot exceed the average rate offered by large banks not more than 3 percent.

A reduction of capacity utilization was also leading to a fall in investment. According to Dollar and Driemeir (1998), capacity utilization on average fell in all five selected industries ; garments, textiles, electronics, food processing, and auto parts, from 1996 to the first half of 1997 and again in the second half of 1997. Half of firms reported cutting back their capacity in the second half of 1997, and 40 percent of firms still anticipate a further contraction in their rate of production in 1998.

While number of firms had cut back their capacity utilization, fifteen percent of firms reported the expansion. However, it should also be noted that 70 percent of them are exporters and 60 percent are large. In addition, the overall increase in capacity utilization is small (60 percent of firms reported increases of 10 percent or less). Moreover, more than 20 percent of firms had abandoned the path, which was planned before July 1997, to expand their capacity.

The withdrawal of foreign money was also expected to have effects on saving and investment. However, this was likely to reflect more in the decrease in investment rather than in saving which in turn reverse the trend of the current account deficit during the past couple of years.

*d.) Effects on Exports and Imports*

One positive result has emerged from the crisis, which is that export's growth of agricultural products rose since the prices of most agricultural products turn sharply upwards responding to the rise in exchange rates and increased demand arising from the impact of El Nino on other countries. Therefore, the volumes and value of export of such products are expected to increase.

Table 2.5 Promoted Direct Investment in Thailand

Unit : Million Baht

	Application				Application Approved				Promotion Certificates Issued				Start up			
	No.	Total Invest.	No.	Foreign Invest.	No.	Total Invest.	No.	Foreign Invest.	No.	Total Invest.	No.	Foreign Invest.	No.	Total Invest.	No.	Foreign Invest.
1996	1,193	833,818	648	417,685	970	531,198	519	332,593	939	426,401	512	236,281	609	229,790	401	150,443
1997	993	490,828	607	344,418	919	481,292	576	332,957	836	412,335	504	246,064	480	275,507	310	235,906
%change	-16.76	-41.13	-6.33	-17.54	-5.26	-9.39	10.98	0.11	-10.97	-3.30	-1.56	4.14	-21.18	19.90	-22.69	56.81
1998 (Jan.-Oct.)	735	211,421	554	190,495	620	268,863	478	240,068	513	212,795	386	187,799	619	246,627	373	178,377
Jan.	65	12,963	53	11,961	77	13,668	53	11,296	48	56,886	33	51,114	50	16,828	18	3,659
Feb.	75	14,779	52	12,447	69	77,133	54	73,964	57	19,681	34	13,624	48	23,533	31	21,039
Mar.	78	16,744	56	14,225	83	24,359	60	11,595	50	29,102	35	26,415	59	15,595	37	8,058
Apr.	78	67,395	65	66,606	44	7,300	37	6,756	46	13,147	40	10,096	52	11,239	31	7,450
May	63	13,727	48	9,194	55	9,736	38	8,420	52	16,742	36	15,071	45	11,130	29	5,804
June	75	27,975	56	26,207	75	17,996	64	16,724	54	12,925	42	11,817	72	23,733	45	10,993
July	82	23,014	65	21,113	45	6,760	34	5,589	70	13,208	56	11,173	80	36,226	47	30,195
Aug. & Sept.	153	25,391	108	20,620	108	32,423	85	30,383	96	38,777	74	36,514	145	78,979	92	63,760
Oct.	66	9,433	51	8,122	64	79,488	54	75,341	40	12,327	36	11,975	68	29,364	43	27,419

Source: The Board of Investment

However, considering the exports aside from agriculture, the benefit from the devaluation of baht has not had the effect on export volumes as much as expected. This is mainly due to the simultaneous collapse of other Asian currencies as mentioned above and also the shortage of working capital as a result of the credit contraction. Consequently, the total benefit from the depreciation is obviously lower than the baht depreciation in 1984 when most exports were mainly agricultural products and labor intensive products. Exports for the first three months after the baht floatation support this conclusion. In July and August; exports increased about 25 percent in baht terms and 8 percent in dollar terms. In September, exports unexpectedly surged to 54 percent growth rate in term of Thai baht and to 12 percent in term of dollar. This positive trend of exports continued throughout 1997 as total exports in 1997 significantly increased by 27.94 percent in baht terms and 10.09 percent in dollar terms. Orders have been received by many exporting companies showing signs of a strong recovery, however, problems of credit shortages may hinder the recovery. Many small and medium exporters, although in possession of orders, will be unable to fulfill their obligations due to a lack of credit and liquidity.

Exports in dollar terms in the first quarter of 1998 compare to those in the first quarter of 1997 fell by 1.55 percent even though exports in terms of the baht significantly increased by 79.35 percent. This in turn reflected a slight increase in volume of exports benefiting from a drastic devaluation of the baht. Although the exchange rate has become more stable in the second quarter of 1998, exports became worse since exports in dollar terms decreased by 6.74 percent which can be viewed as a result of intensifying competition among crisis-facing countries, fewer exporting markets and credit crunch.

Moreover, since other countries in Asia were also affected by the depreciation of their currencies against US dollar. During the period of 1 July 1997 to 13 July 1998, Yen and Taiwanese dollar depreciated approximately by 23 percent, while Singapore dollar and Malaysian ringgit also depreciated by 21 and 68 percent respectively. Indonesia was most severely affected by the crisis since the relative value of rupiah to US dollar on 13 July 1998 was 5 times less than it was on 1 July 1997. Since exports from Thailand to East Asian and Southeast Asian countries in 1996 was accounted for almost 50 percent of Thai total exports, such collapse of Asian currencies would more or less affect Thai exports. At least, it would affect the prospect to increase exports to these countries which is essential in this economic situation.

Considering the import side, Thailand's total imports significantly decreased from 72,318.62 millions US dollar in 1996 to 61,337.53 millions US dollar in 1997. In other words, the crisis as well as the depreciation of the baht adversely affected imports since the growth rate of imports in 1997 was negative at 15.18 percent. Imports continued to decrease in the first and the second quarter of 1998 as its growth rate was accounted for -37.32 and -38.11 percent respectively compared to those in the same period in the previous year.

#### *e) Severe decline in growth and high inflation*

As mentioned that Thailand had experienced rapid economic growth from the mid-1980s to early-1990s and this trend continued until 1995, averaging at 8 percent per annum. However, the growth rate had erupted to 5.5 percent in 1996. One of many factors causes a decline in economic growth is the slowdown of export while the economic crisis in 1997 also results in a further declining growth of the economy. This can be viewed as a result of the aggregate demand contraction and conditions set up by IMF.

A decline of Private Investment Index during 1996-1998 reflects a drastic fall of investment in Thailand (Table 2.4). The Private Investment Index was 118 in January 1996 and then continued to decrease, hitting the lowest point at 40.5 in April 1998. Similarly, the same trend can be seen in the growth rate of manufacturing production. While this growth rate was quite high in 1995 and also in the first half of 1996, it started to fall afterwards (Table 2.4). The negative growth rate of

manufacturing production at 8.6 percent in April 1998 indicates a severe contraction of the production in manufacturing sector.

Following the IMF conditions in the early stage of the crisis, however, generated a further contraction to the economy. Thai government had to adopt strict monetary and fiscal policy in order to meet the IMF condition on government budget surplus. A number of measures had been applied since the crisis, for example, decreasing government budget and maintaining high interest rate. This, in turn, seriously hurt real sectors as many businesses and industries were hit by credit crunch and thus went bankrupted.

Since major components of aggregate demand, namely, consumption and investment spending has been declined due to the economic situation, high interest rates, and steep budget cuts as a result of the revenue shortfall. Export growth, in term of baht, alone cannot counter the effect of the contraction of components of aggregated demand. Thus, the economic downturn caused by the aggregate demand contraction is almost unavoidable.

The growth rate of Thai economy in 1997 was negative at 0.4 percent. Moreover, according to the sixth letter of intents proposed to IMF (Table 2.6), Thai economy was estimated to further deteriorate in 1998. The real GDP growth rate at constant prices was expected to be in a range of -7 to -8 percent. The current account balance outcome in 1998 is expected to be positive at 13.5 billions US dollar or 11.5 percent of GDP. This surplus is expected to be mostly the contribution of a reduction of imports (in US dollar) of 25 to 30 percent rather than an increase in exports. Such high current account balance, which reflects weak domestic demand, carries over into higher projected reserves of approximately 28 billion US dollar by end year.

The baht depreciation could also increase import prices of finished goods, intermediate products, and raw materials including crude oil and petroleum products, and *inflation* is expected to surge. To alleviate the situation, the Department of Commerce has lunched many measures to counter inflation. The government also slowed down the increase in the price of public utilities such as electricity, telecommunications, and tap water for about six months. The rising oil prices, due to the baht depreciation was partly neutralized by the declining trend of world oil prices. Nevertheless, the increase in prices of imported goods, intermediate products, and raw materials, crude oil and petroleum products, in particular, will eventually be transmitted to a rise in consumer prices. When inventories of imported finished goods, intermediate products and raw materials have been depleted. Although the recent inflation rate is much higher than those in the last decade, it has not been severely high as anticipated since there are many deflationary factors such as the economic slowdown, budget cuts, consumption, and investment slowdown. The inflation rate for 1997 was 5.6 percent, slightly decreased from the previous year. In addition, according to the estimate in the sixth Letter of Intents, the inflation rate for 1998 is expected to be 8 percent.

**Table 2.6**  
**Macroeconomic Framework: 1998-1999 (the 6th Letter of Intent)**

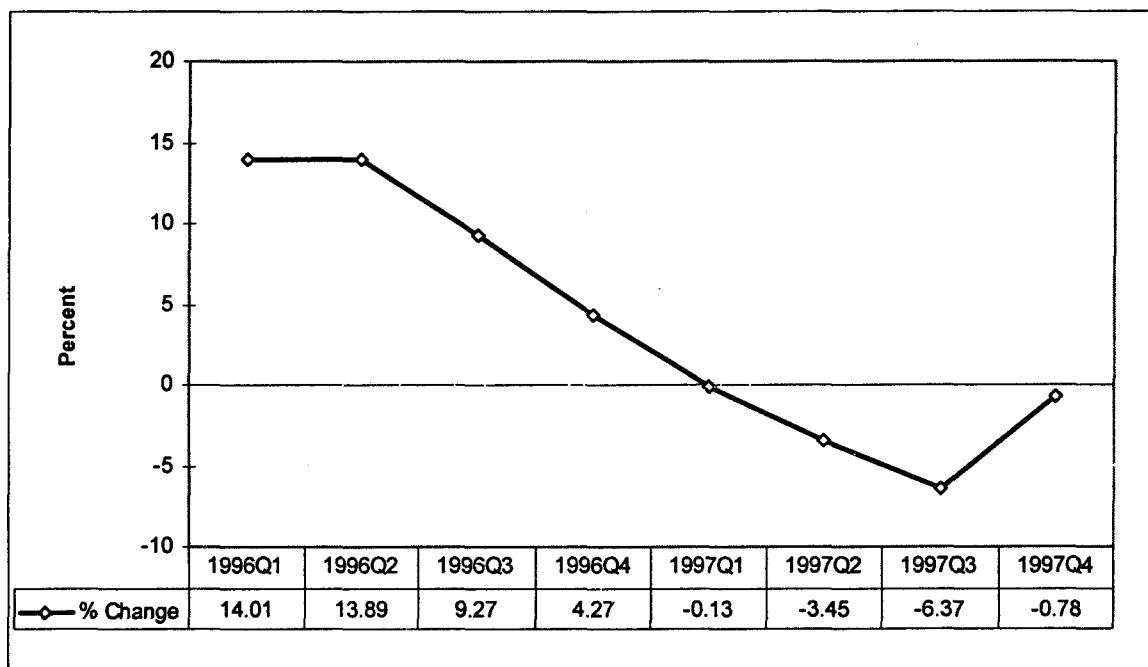
	1998		1999
	Lol 5	Lol 6	trend
	(In per cent)		
Real GDP growth at constant prices	-7	-7 to -8	1
CPI Inflation (period average)	9.2	8	2.5 to 3
	(In billions of US dollar)		
External current account balance	11 to 12	13.5	11
(In percent of GDP)	10	11.5	8.5
Gross official reserves (end-period)	26 to 28	28.5	32 to 34
(In months of imports)	7 to 7.5	8.25	8.5
(In percent of short-term debt)	77	113	178
Unwinding of swaps and forwards	9	10	3 to 4

Source: The sixth letter of intent, the Bank of Thailand.

### *f) Government revenue and expenditure*

Government revenues were also affected by the crisis. As shown in figure 2.2, government revenues began to deteriorate in the first quarter of 1997 and then significantly decreased in the third quarter. Although the improvement of government revenues could be seen in the fourth quarter, such improvement was likely to be the result of the policy by increasing the value added tax and gasoline and diesel excise tax rather than because of the recovery of the economy.

**Figure 2.2**  
**Changes in Government Revenues (percent relative to same quarter of the previous year)**



Source: Siamwalla and Sopchokchai 1998.

One can view government expenditure as the main factor to stabilize or to stimulate the economy, the reduction of the government revenues thus also affected the government expenditure in number of crucial areas for example ; expenditure for projects on human development (Health and Education), technology development, and those aimed to increase the domestic aggregate demand. Such reduction in government expenditures therefore affected both real economic and social sector.

The budget cuts resulting from the tight fiscal policy also affected government expenditure. Since the administrative expenditure; for example, salaries of officers, was difficult to be deducted, the government investment in number of projects mentioned above, includes those investments in physical and institutional infrastructure, had to be canceled or postponed. This in turn affected the future prospect of economic growth.

### **2.2.2 Social impacts**

The social impact of the Crisis covers a wide range of problems, including employment, education, health, crime and social security, drug abuse and trafficking, as well as family institution. In this section, only selected issues of social problems resulting from the crisis will be highlighted with an emphasis on unemployment.

### *a) Unemployment*

One of the major social impacts of the crisis in Thailand is the high and widespread unemployment. Unemployment reflects the social sufferings through losses of income, means of basic needs and the quality of life as well as social status,. A person's employment does not only indicate his/her utilization of time for productive purposes but also for social purposes. It also determines or is closely related to a person's social behavior. This section reviews the unemployment situation before and after the crash<sup>2</sup> under the presumption that the crisis is a major cause of the unemployment and other employment problems.

By and large, the credit crunch forced most of manufacturers to reduce production, and thus a fall in output. This in turn affected employment as many economic sectors have had to lay off workers or reduce their working hours at high and low ends of the market.

To understand more clearly the impact of the crisis on unemployment situation, a few observations should be made regarding employment statistics of Thailand. First, Thailand's employment is highly seasonal. As shown below (Table 2.7), employment varies seasonally according to the agricultural seasons which could be simply divided into dry or slack season (around February) and the wet or peak season (around August)<sup>3</sup>. Thus the comparison of employment data across a year should make a reference to the time of survey (For example, it is not correct to say that employment decreases from 33.2 millions in 1997 to 29.4 millions in 1998 because of the crisis as the decline is in fact due mainly to the seasonal reason). Second, the unemployment rate of Thailand is generally low for three major reasons – (a) there is no unemployment insurance system which will encourage workers to report their unemployment, (b) there is no registration system for the unemployed, and the measurement of unemployment is thus based on sample surveys which have limitations of coverage and definition of employment status, and (c) partly because of (a) and the nature of the Thai economy and society, the prospective unemployed, particularly the low income class, cannot afford unemployment and have to find employment in the agricultural or informal sectors. In addition, the impact of the crisis on employment does not always show up in the form of unemployment or lay-off. Reductions of wage/salary or working hours are also commonly practiced during the crisis.

Changes in unemployment during the crisis can be observed from the data in Table 2.8 *For the dry season*, the number of total unemployed persons<sup>4</sup> increased more than doubled from 0.70 millions in February 1997, to 1.48 millions surveyed in February. During this season, the number of the labor force waiting for farm season also increased from 1.04 millions in 1997 to 1.25 millions in 1998. In fact the size of the labor force (not counting those waiting for farm season) in February 1998 contracted from 30.96 millions to 30.89 millions. *For the wet season*, the number of the unemployed increased for almost four times from 0.29 millions in August 1997 to 1.134 millions in August 1998.

Additional information (Table 2.9) indicates that approximately 80 percent of the people unemployed were in rural areas, 0.874 millions in rural areas as compared to 0.26 millions in urban areas. However, the unemployment rate, the ratio of the unemployed to the labor force of the same area, is higher in the urban than in the rural areas, 3.84 compared to 3.34 percent in 1998.

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<sup>2</sup> Although the crisis is not the result of a single, time-specific event, we can say for the case of Thailand that the crisis became obvious around the third quarter of 1997 or after the 2<sup>nd</sup> July 1997 announcement of the managed floating exchange rate.

<sup>3</sup> The National Statistical Office (NSO) conducts periodic labor force surveys three rounds annually, Round 1 in February Round 2 in May, and Round 3 in August. NSO is planning a fourth round survey in December of every year.

<sup>4</sup> The number of unemployed is defined as those actively seeking work as well as those merely willing to work excluding the seasonally unemployed. The majority of the seasonally unemployed not caused by the crisis.

Table 2.7 Seasonal Change of Employment in Thailand, 1993-1998

(Million persons)

Year	Round 1 (Feb.)	Round3 (Aug.)	Change (%)
1993	29.21	32.15	10.07
1994	28.23	32.10	13.71
1995	29.06	32.58	12.11
1996	30.10	32.23	7.08
1997	30.27	33.16	9.55
1998	29.41	31.74	7.92

Source : National Statistical Office, Report of Labor Force Survey, Various years.

Table 2.8 Labor force and employment of Thailand, by work status 1996-1998

(Thousand)

Work status	1996			1997		1998		
	Round 1 Feb.	Round 2 May.	Round 3 Aug.	Round 1 Feb.	Round 3 Aug.	Round 1 Feb.	Round 2 May.	Round 3 Aug.
<b>Population</b>	<b>59,750.4</b>	<b>59,902.6</b>	<b>60,045.3</b>	<b>60,350.6</b>	<b>60,648.9</b>	<b>60,949.0</b>	<b>61,098.0</b>	<b>61,252.0</b>
<b>Labor force</b>	<b>31,898.4</b>	<b>32,504.1</b>	<b>32,750.2</b>	<b>32,000.2</b>	<b>33,560.7</b>	<b>32,143.1</b>	<b>32,169.8</b>	<b>32,937.0</b>
<b>1. Current labor force</b>	30,740.5	31,035.0	32,586.3	30,964.2	33,454.9	30,890.2	30,167.8	32,882.1
1.1 Employed	30,099.2	30,375.4	32,232.3	30,266.3	33,162.3	29,412.9	28,554.9	31,747.9
1) At work	28,088.3	28,567.4	31,760.4	28,308.9	32,714.5	26,958.5	25,765.3	31,070.3
2) Not at work	2,010.8	1,807.9	471.9	1,957.4	447.8	2,454.4	2,789.5	677.3
1.2 Unemployed	641.3	659.6	353.9	697.8	292.5	1,479.3	1,612.9	1,134.2
1) Looking for work	119.6	158.8	110.1	179.5	96.4	402.8	491.9	517.5
2) Not actively looking for work	521.6	500.8	243.7	518.3	196.1	1,076.5	1,120.9	616.6
<b>2. Waiting for farm season</b>	<b>1,157.8</b>	<b>1,469.0</b>	<b>163.7</b>	<b>1,035.9</b>	<b>105.7</b>	<b>1,250.8</b>	<b>2,002.0</b>	<b>55.8</b>
<b>3. Not in labor force (age 13+)</b>	<b>13,744.5</b>	<b>13,254.6</b>	<b>13,119.4</b>	<b>14,334.9</b>	<b>13,238.0</b>	<b>14,888.6</b>	<b>14,977.7</b>	<b>14,331.2</b>
1. Housework	4,007.4	3,829.9	3,539.3	4,195.0	3,450.1	4,341.2	4,270.0	3,575.8
2. Study	5,472.8	5,298.4	5,518.9	5,811.1	5,580.4	6,089.9	6,047.3	6,170.1
3. Too young or too old to work	3,379.0	3,398.5	3,377.4	3,463.0	3,517.1	3,660.6	3,838.4	3,650.7
4. Other	885.2	727.0	683.8	865.7	690.3	796.7	812.9	934.5
<b>4. Age less than 13</b>	<b>14,107.4</b>	<b>14,143.8</b>	<b>14,175.8</b>	<b>14,015.4</b>	<b>13,850.2</b>	<b>13,917.2</b>	<b>13,950.3</b>	<b>13,983.4</b>

Note: \* Estimated by National Statistical Office

Source : National Statistical Office, Report of the Labor Force Survey, various years.

**Table 2.9 Employment by rural-urban residence and work status, August 1997-1998**  
(thousand)

Work status	Municipal area	Non municipal area	Total
August 1998			
• Labor force	6,757.0	26,124.1	32,881.1
- Employed	6,497.9	25,249.9	31,747.8
- Unemployed	260.0	874.2	1,134.2
	(3.84)	(3.34)	
- Waiting for farm season	0	55.8	55.8
August 1997			
• Labor force	6,765.7	26,689.2	33,354.9
- Employed	6,696.2	26,466.1	33,162.3
- Unemployed	69.5	223.0	292.5
	(1.02)	(0.83)	
- Waiting for farm season	1.2	104.4	105.7

Source: National Statistical Office, Report of Labor Force Survey, Round 3, 1997-1998

**Table 2.10 Employment by industry, 1996-1998**

(thousand)

Industry	1996			1997		1998		
	Round 1 Feb.	Round 2 May.	Round 3 Aug.	Round 1 Feb.	Round 3 Aug.	Round 1 Feb.	Round 2 May.	Round 3 Aug.
<b>Total</b>	<b>30,099.2</b>	<b>30,375.4</b>	<b>32,232.3</b>	<b>30,266.3</b>	<b>33,162.3</b>	<b>29,412.9</b>	<b>28,554.9</b>	<b>31,747.9</b>
<b>1. Agriculture</b>	<b>12,146.2</b>	<b>12,765.4</b>	<b>16,127.1</b>	<b>11,938.0</b>	<b>16,691.2</b>	<b>11,640.0</b>	<b>11,125.4</b>	<b>15,373.2</b>
<b>2. Non-agriculture</b>	<b>17,953.0</b>	<b>17,610.0</b>	<b>16,105.2</b>	<b>18,328.3</b>	<b>16,471.1</b>	<b>17,772.9</b>	<b>17,429.5</b>	<b>16,374.7</b>
2.1 Mining and Quarrying.	60.0	56.7	47.1	58.1	46.9	58.1	42.3	37.7
2.2 Manufacturing	4,967.4	4,745.0	4,334.2	4,996.4	4,291.9	4,923.2	4,776.5	4,267.4
2.3 Construction, Repair, Demolition	3,125.3	2,689.7	2,171.9	2,983.5	2,020.7	2,042.3	1,921.8	1,310.7
2.4 Electricity, Gas, Water etc.								
2.5 Commerce	160.6	192.1	142.8	174.4	178.4	192.4	228.7	186.6
2.6 Transport, Storage, Communication	4,451.6	4,620.5	4,341.5	4,602.6	4,601.1	4,741.6	4,861.9	4,891.6
2.7 Services	1,036.6	1,045.9	953.7	1,098.5	980.3	1,074.1	964.7	986.5
2.8 Others								
	4,100.0	4,220.3	4,094.2	4,399.8	4,342.1	4,727.5	4,616.2	4,689.2
	51.0	394.	19.4	14.6	9.3	13.4	17.1	4.6

Source: Ibid.



The crisis seems to have caused a structural change in employment as well. The NSO data shown in Table 2.10 indicates obvious declines in the construction sector where employment decreased from 2.98 millions in February 1997 to 2.04 millions in February 1998 and from 2.02 millions in August 1997 to 1.31 millions in August 1998. The obvious gain in employment is found in Services sector and Commerce and Transport (dry season only). Surprisingly, in both dry and wet seasons, employment in the agricultural sector is found to have decreased rather than increased. This phenomenon suggests that during the time of the crisis, the agricultural sector did not absorb as many workers as might have been expected. The data in Table 2.8 supports this argument indicating the number of labor force waiting for farm season was unusually high in early 1998, 1.25 millions as compared to 1.04 millions in February 1997. On the other hand, the increased employment in Services and Commerce suggests that the informal sector has worked as a safety valve for unemployment during the time of the crisis.

If we assume roughly that employment in the formal sectors can be represented by the number of "employers" and "employees" and employment in the informal sector by the number of "self employed" and "unpaid family workers", it can be expected that there should be a decline in number or proportion of the employers/employees category while there should be an increase in number or proportion of those under the self-employed/unpaid family workers category. However, the data in Table 2.11 does not strongly support this conjecture. The proportion of the "self employed" and "unpaid family workers" in the rural areas increased from 56.9 in February 1997 to 58.6 in February 1998 whereas in the urban areas the proportions increased from 29.4 to 28.6 in 1998. The proportions of the "employers" and "employees", on the other hand, decreased slightly from 36.8 in February 1997 to 34.4 in February 1998 in the rural areas and from 56.3 to 55.1 in the urban areas. It should be noted, however, that the formal workers category does not include government employees under this circumstance as the increase in number of government employees is arbitrary by the government unemployment alleviation programmes that hired a large number of jobless workers.

**Table 2.11**  
**Number, Percentage and Percentage Change of Employed Persons, by Work Status and Area**

	1997	1998	%change
	(thousand)		
<b>Rural</b>	23,742.2 (100)	22,853.6 (100)	-3.74
Employers	505.8 (2.1)	496.9 (2.2)	-1.76
Government employees	1,490.1 (6.3)	1,601.7 (7.0)	7.49
Private employees	8,226.8 (34.7)	7,349.9 (32.2)	-10.66
Own-account workers	8,028.9 (33.8)	8,235.0 (36.0)	2.57
Unpaid family workers	5,490.4 (23.1)	5,169.8 (22.6)	-5.84
<b>Urban</b>	6,524.1 (100)	6,559.3 (100)	0.54
Employers	263.7 (4.0)	286.3 (4.4)	8.57
Government employees	925.5 (14.2)	1,066.2 (16.3)	15.20
Private employees	3,411.7 (52.3)	3,328.7 (50.7)	-2.43
Own-account workers	1,274.2 (19.5)	1,246.2 (19.0)	-2.20
Unpaid family workers	648.8 (9.9)	631.7 (9.6)	-2.64

Source: Labor Force Survey (Round 1) 1997, 1998, National Statistic Office, data tapes.

### *b) Layoff, underemployment and wage employment contraction*

The unemployment figure alone does not tell the whole story of the impacts of the crisis as there are a considerable number of workers whose employment is affected by the crisis in forms of layoff or reducing work hours or wage rate. Besides those who are laid off did not necessarily become unemployed.. Since there is no unemployment benefits to be collected or no substantial social insurance to cope with the unemployment, some of the laid off had to earn a living in the informal sector or return to their hometown for social safety. There is an evidence that the average number of working hours has declined during the crisis.

Between February 1997 and 1998, the number of people working less than 35 hours a week increased almost 2 millions from 2.43 million persons or 7.6 percent of the labor force in 1997 to 4.41 million persons or 13.7 percent in 1998 (Table 2.12). Out of this increase about 1.2 millions were "private employees." The 3 sectors with highest number of underemployment in early 1998 were Agriculture (1.86 millions), Manufacturing (1.1 millions) and commerce (0.7 millions). However, the largest increase of underemployment was found in manufacturing sector (Table 2.13). The increase was relatively more significant in urban areas as the number of people underemployed in urban areas increased from 100,000 persons in 1997 to 650,000 persons in 1998, while the number of people underemployed in rural areas increased from 450,000 persons to 820,000 persons during the same period. Among the underemployed in urban areas, almost half of the men and three quarters of the woman were in the industrial sector. The underemployment of a large number of industrial workers is a new phenomenon following the crisis (Siamwalla and Sopchokchai 1998).

Although manufacturing employment had slightly decreased from the previous year (as shown in Table 2.10), a significant decrease of manufacturing employment after February 1998 was expected as illiquidity and insolvency problems became more serious. The total number of labor which had been laid off estimated by the Ministry of Labour and Social Welfare accounted for almost 0.3 million persons. More than half of them were laid off while the establishment was still in operation, and the rest were laid off because the establishment was closed down.

According to the Department of Labor Protection and Welfare (Table 2.14) about 4,900 establishments went out of business laying off approximately 408,967 workers while in 1998, between January-August, about 2,600 establishments were closed down and laid off about 222,950 workers. The majority of the laid off were in Manufacturing factories, including automotive industry, Construction and Finance sector. It should be noted that the laid off figure is likely to be underestimated since it takes account of only the establishments that have gone out of business and does not includes the laid off workers from the downsized businesses. At the same time, it should also be noted that while there are businesses that were closed down there are also new born businesses hiring new workers. Looking at the number of the lay off only could exaggerate the unemployment situation.

From a different angle, the impact of the crisis on employment is manifested in drastic reductions of wage employment in the private sector, particularly during 1997-1998. As shown in Table 2.15, in the dry season (February) the number of private employees in 1998 decreased by 960,000 from 11.64 million in 1997 to 10.68 million in 1998. In the wet season, the number decreased by 1.03 million from 10.1 million in 1997 to 9.04 million in 1998.

### *c) Returned labor from abroad and new entrants*

Since the crisis has not affected only Thailand but rather most of the countries in Asia, there was an increase in the number of returned labor from abroad. A large number of Thai labor working abroad; for example in Taiwan and Brunei, were sent back to Thailand and this exacerbated the number of the unemployed. Although the government carried out a number of policies to support labor to work abroad in order to alleviate unemployment, the target has not yet been met. The return of workers from abroad could exacerbate the unemployment situation.

**Table 2.12 Underemployment (hours of work less than 35 hrs/week) by work status, 1995-1998 (February)**

Work status	Work less than 35 hrs/week				Change		
	1995	1996	1997	1998	1996	1997	1998
<b>Total</b>	<b>2,309,221</b>	<b>2,473,823</b>	<b>2,432,199</b>	<b>4,411,854</b>	<b>164,602</b>	<b>-41,624</b>	<b>1,979,655</b>
Private employee	504,513	570,450	502,644	1,769,155	65,937	-67,806	1,266,511
Government employee	36,166	32,611	35,673	94,436	-3,555	3,062	58,763
Employer	87,064	62,456	60,122	145,847	-24,608	-2,334	85,725
Self employed	933,188	969,105	970,955	1,258,670	35,917	1,850	287,715
Family workers	744,575	837,590	857,570	1,129,285	93,015	19,980	271,715
State enterprises	3,715	1,611	5,235	14,461	-2,104	3,624	9,226

Source: Working subcommittee on Estimate of Labor Force, Employment and Unemployment, Report of the Second meeting, 1998

**Table 2.13 Underemployment (hours of work less than 35 hrs/week) by industry, 1995-1998 (February)**

Industry	Work less than 35 hrs/week				Change		
	1995	1996	1997	1998	1996	1997	1998
<b>Total</b>	<b>2,309,221</b>	<b>2,473,826</b>	<b>2,432,199</b>	<b>4,411,854</b>	<b>164,602</b>	<b>-41,627</b>	<b>1,979,655</b>
Agriculture	1,374,592	1,615,880	1,590,470	1,861,536	241,288	-25,410	271,066
Mining & Quarrying	1,915	3,730	953	5,240	1,815	-2,777	4,287
Manufacturing	244,842	202,791	199,554	1,082,911	-42,051	-3,237	883,357
Construction	102,234	104,677	88,141	198,028	2,443	-16,536	109,887
Electricity, Gas, Water	3,887	2,170	3,554	10,577	-1,717	1,384	7,023
Commerce	294,605	286,947	285,563	706,512	-7,658	-1,384	420,949
Transport, storage, communication	64,108	67,791	58,969	113,005	3,683	-8,822	54,036
Services and other	223,038	189,840	204,995	434,045	-33,358	15,155	229,050

Source: Ibid.

Table 2.14 Number of laid off workers of establishments registered with the Office of Social Insurance, 1997- Aug. 1998

Year/Month	Establishment employing < 10 (Dep. of Social Welfare)		Establishment employing 10+ (Office of Social Insurance)		Total	
	No. of establishments	employees	No. of establishments	employees	No. of establishments	employees
1997	118	410	4,823	408,557	4,941	408,967
1998	128	393	2,468	222,561	2,596	222,954
Jan.	5	17	844	73,420	849	73,437
Feb.	23	84	251	21,607	274	21,691
Mar.	7	26	257	20,262	264	20,288
Apr.	16	37	225	28,045	241	28,082
May	10	16	236	24,785	246	24,801
Jun.	16	46	271	27,203	287	27,249
Jul.	35	125	224	22,093	259	22,218
Aug.	16	42	160	5,146	176	5,188
Total 1997-1998	246	803	7,291	631,118	7,537	631,921

Source: Working Subcommittee on Estimates of Labor Force, Employment and Unemployment, Ministry of Labor and Social Welfare 28 October 1998

Table 2.15 Change in wage employment, 1994-1998

	1994	1995	1996	1997	1998
	(thousand)				
February(First round survey)					
• Private employees	10,130.2	10,732.1	11,681.0	11,638.6	10,678.7
• Public employees	2,376.0	2,417.6	2,310.6	2,415.7	2,668.0
August(Third round survey)					
• Private employees	8,823.1	9,189.2	9,850.6	10,063.3	9,036.0
• Public employees	2,334.5	2,424.1	2,300.6	2,426.2	2,693.2

Source: National Statistical Office, Labor Force Surveys, various years.

The unemployment situation has been and will be hampered by the influx of new entrants to the labor market. Thailand Development Research Institute Foundation (1998) indicated that the number of graduated students in all levels of education to enter the labor market during 1997-2001 was averaged at 525,823 persons per annum. While more than half of the new entrants would graduate at university level, the demand for this group of labor accounted for only 20 percent of its supply. This over supply reflected that more labor would be unemployed. Moreover, considering demand and supply of labor during 1997-2001, TDRI maintained that there will be an excess demand for labor with lower than primary and primary education accounting for 219,220 persons. In contrast, the excess supply of labor attained secondary and university education accounted for more than 0.26 million persons. In the case that the excess supply of labor is not able to adjust themselves to work in the agricultural sector in which there is an excess demand, unemployment among educated labor will become more serious. Although there is an excess demand for labor with lower than primary and primary education, it can be substituted by alien labor which recently account for more than 0.7 million persons. *Therefore, the policy to send this labor back to their countries is necessary, otherwise unemployment among uneducated labor will become more severe. Whether this policy will have an impact on SEATEs will be discussed later in this report.*

#### *d) Migration*

It is evident that a large-scale reverse migration is taking place which reflects in the increasing number of unemployed people in rural areas. This in turn raises the concern whether the Thai rural economy, especially the farm sector, is able to accommodate all the returned migrants after it has been neglected for years. The poor quality of public services (health and education), the natural resources and environment which are already fragile and the expected severe and long drought in rural areas can altogether be viewed as obstacles for the expansion of the rural economy.

Before the crisis, most of families living in rural areas consisted of elderly people and children, while youngsters and parents of the children were away to work in Bangkok, big cities and abroad. Although the return of migrants would benefit the society in the sense of the increasing family values, this in turn increased the burden of women and the old to feed all members of the family, sometimes by using their saving. This happened especially when there is no other occupation; for example, handicraft and small-scale livestock, to accommodate the returnees. As shown earlier, although there has been a tendency of returning urban-rural migration, the employment in the agricultural sector does not increase.

#### *e) Decreased social services*

Another major concern concentrates on the social impact caused by a fall in the government expenditure, occasioned by a fall in government revenues. While there is increasing demand for public services, especially health and education, the budget constraints have forced the government to curtail some social programmes. In cutting expenditures, the government acted under the advice of the IMF. Following the criteria set by the IMF, a number of programmes, for example, programmes which have low priority in the Eighth National Economic and Social Development Programme, construction projects which are not urgent, and programmes which are no longer appropriate because of changing economic conditions, were eligible for cuts. In contrast, programmes that are aimed at improving the Thai competitiveness, lessening the social impact of the crisis, and at improving the economy of the provinces would not be affected by the budget cuts.

Although there was an attempt to follow those criteria, it was not consistently done. The sharpest cuts were in transport and communications, but balanced against that were equally severe cuts in environment and in *social services* (Siamwalla and Sopchokchai 1998).

According to the 1998 budget which had been revised several times to accommodate the IMF conditionalities, more than 18 percent of the firstly submitted budget, accounted for 182,000

million baht, was cut from the budget bill. The budget cut had been carried out three times, the first cut was accounted for 59,000 million baht while the second and third cuts were accounted for 100,000 and 23,000 million baht, respectively. This section will mainly consider the budget cuts of the Ministry of Education, the Ministry of Public Health, the Ministry of Labour and Social Welfare and Ministry of Interior, since these budget cuts directly affect the number of programmes related to social development.

The 1998 budget for the Ministry of Education reflects a 10.7 percent reduction from the budget bill with a cut of 17,731.8 million baht, leaving 148,577.15 million baht available for all the departments of the Ministry (Table 2.16). While more than 80 percent of the budget was distributed to the Office of National Primary Education Commission, the Department of General Education and the Department of Vocational Education, only 25,686.86 million baht was available to other 9 departments, including the Department of Non-Formal Education and the Office of the Teacher Civil Service Commission.

**Table 2.16**  
**Budget of Ministry of Education, 1998**

	FY 1998	cut	balance
Unit: Million Baht			
<b>Ministry of Education</b>	<b>166,308.91</b>	<b>17,731.76</b>	<b>148,577.15</b>
Office of Permanent Secretary	4,330.24	382.13	3,948.11
The Religious Affairs Department	2,487.60	130.82	2,356.78
The Office of Rajabhat Institutes Council Education Ministry	5,669.52	891.99	477.52
Department of Physical Education	2,519.47	551.26	1,968.21
The Fine Arts Department	1,852.16	298.03	1,554.12
Department of General Education	35,199.31	3,998.85	31,200.46
Department of Non-Formal Education	3,029.80	316.99	2,712.82
Department of Vocational Education	13,864.87	2,900.09	10,964.78
Office of the National Culture Commission	366.45	45.87	320.58
Rajamangala Institute of Technology Office of the President	3,949.09	722.99	3,226.10
Office of the National Primary Education Commission	87,991.95	7,266.91	80,725.05
Office of the Teacher Civil Service Commission (TCSC)	133.96	10.18	123.78

Source: The Bureau of the Budget.

This decline in budget raises concerns on the human resources development problem of the country, as it is evident that the number of students dropped out from schools and universities has significantly increased over time since the crisis started. Such an increase can be viewed as a result of the loss or reduction of income of their parents, causing their children to drop out from schools and universities to look for jobs. A survey by the Ministry of Education indicates that more than 45,000 students have been affected because their parents have lost their jobs (UNDP 1998). Although the government provided loans for drop-out students for 1,000 million baht, only 10 percent of the amount have been made.

The crisis has not only affected students, both public and private schools also face the problem of decreasing budget and increasing costs. While private schools all over the country recorded 923 million baht overdue tuition for the second semester of the 1997 academic year, public schools experienced a decreasing budget expenditure for stationary, tuition fee, and food.

The impact of the budget cut on the government scholarships should also be taken into consideration since this is an important means to develop human resources in the government sector. Table 2.17 presents the number of scholarships subsidized by the government. The total

number of scholarship provided by the Office of the Civil Service Commission in 1998 increases from those provided in 1997, partly because of the introduction of the government project aimed at increasing manpower in the government sector. Under this project, 500 scholarships are proposed each year from 1998 to 2002. With the budget constraints, even though expenditure on scholarships was untouched and protected from cuts, it became insufficient due to the baht depreciation. The budget constraints also affected the ongoing scholarships in the form of a 10% reduction on allowance, and reduction in other expenses, such as funds supporting for computer appliance, learning materials, trips or seminars.

**Table 2.17**  
**Number of Scholarship**

	Total Scholarship	Candidate	Scholar Student
<b>Scholarship in 1997</b>			
King's Scholarship	9	258	9
Post-secondary education level	13	1,263	12
Under and Post Graduate level	44	250	32
<b>Total</b>	<b>66</b>	<b>1,771</b>	<b>53</b>
<b>Scholarship in 1998</b>			
King's Scholarship	9	295	8
Post-secondary education level	125	1,905	98
Under and Post Graduate level	228	1,806	136
<b>Total</b>	<b>362</b>	<b>4,006</b>	<b>242</b>

Source: Office of the Civil Service Commission.

Although parts of the scholarship budget for this fiscal year was transferred to support the ongoing scholarships, some programmes under this project were suspended. These suspended programmes consist of the scholarships for the first and second class honor students, domestic training by foreign experts, and short-course training for prospective executive officers. For this fiscal year, 106 from 242 scholarships; eight of the King's scholarships, ninety eight of post-secondary education scholarships, get the full support from government budget, while others which are for students at university level are partly supported by government agencies and international organizations through the Department of Technical and Economic Cooperation and the Ministry of Foreign Affairs. The rest of the scholarships are in the process of seeking supporters since the Thai government is unable to subsidize all the scholarships in the current economic situation.

The Ministry of Public Health's budget also suffered a 14.57 percent cut resulting in 14.62 percent reduction from the 1997 budget (Table 2.18). While more than 75 percent of the 1998 budget accounted for 45,245.39 million baht was earmarked for the Office of Permanent Secretary, only 13,258.23 million baht or 22 percent of the 1998 budget was for the Department of Medical Services, Department of Communicable Disease Control (CDC), Department of Mental Health, and Department of Health.

The insufficiency of public health services now become more severe as public hospitals are now facing problems of being overloaded with fewer budgets, higher cost of imported medical supplies, and an increasing number of patients who can no longer afford private hospitals and clinics even though private hospitals have lowered their charges in order to attract more patients.

**Table 2.18**  
**Budget of Ministry of Public Health, 1998**

	Unit: Million Baht		
	FY 1998	cut	balance
Ministry of Public Health	70,145.50	10,224.61	59,920.90
Office of Permanent Secretary	53,509.21	8,263.81	45,245.39
Department of Medical Services	3,769.48	462.10	3,307.38
Department of Communicable Disease Control (CDC)	4,193.58	480.06	3,713.51
Department of Medical Sciences	1,004.54	127.49	877.05
Department of Mental Health	1,663.70	225.59	1,438.10
Department of Health	5,355.05	555.81	4,799.24
The Food and Drug Administration	576.94	96.73	480.21
Institute of Research on Public Health System	73.00	13.00	60.00

Source: The Bureau of the Budget.

*f) Other social problems*

Apart from the social impacts mentioned above, other social problems ; for example drug abuse, crime, and prostitution, were also expected to increase due to the crisis. Since laying off a large number of workers has the immediate impact on the loss of income, the contracted economy also makes it more difficult for laid off workers to find new jobs, and the drastic rise in cost of living severely hurt this group of people. These altogether may pressure or induce the unemployed to engage in crimes. More and more criminal acts have been reported in newspapers everyday, especially the selling of amphetamine and ecstasy, robbery and car theft. Furthermore, such pressure and tension may also worsen the problem of drug abuse as a number of frustrated people may turn themselves to drugs.

Prostitution has long been a problem in Thailand. Although the survey by Thailand Development Research Institute Foundation in 1998 suggested a decrease in total number of bawdy houses and massages in Chiang Mai as a result of the crisis, a number of private or self-employed prostitutes was expected to increase.

Mr. Montree Sinthawichai, the secretary of the Children Protection Foundation, suggested that the number of prostitution has significantly increased as a result of the crisis in which some of them are voluntary while some are lured into the business. Therefore it is essential for the police to beware and put their attention on these problems, especially on the latter case (*Matichon Daily*, 5 August 1998).

Another group of people affected by the crisis were those who needed social welfare. Although the expenditure on social welfare were protected from cuts according to IMF conditionalities, the amount of such expenditure in real term was lessened as a result of the significant increase in the cost of living. Moreover, the increasing number of people unemployed and the reduction of income of a number of workers severely worsen the problem since the demand for social welfare has significantly increased, while the supply has been unchanged.



### III. Potential Impact on the SEATEs

#### 3.1 Impact on Trade

The crisis causes a contraction in the Thai economy that in turn excessively reduces her demand for import. One can observe that the current account surplus resulted mainly from declining import, not by an increase in export. Thailand is a market for SEATEs' export, so to investigate impacts of the crisis on trade; this section examines the changes in import from SEATEs before and after the crisis. The impact of the reduction of Thailand's imports on each SEATEs country depends on how important of Thailand is as a trading partner, i.e., magnitude of trade and how sluggish the growth of import has been.

With regard to the magnitude of import, among the three countries, value of imports from Cambodia to Thailand was the highest during 1993-1995 as shown in Table 3.1. However, the value reduced to only \$47 million in 1996 and \$70 million in 1997. The import value from Lao PDR came in second until 1997 when the import from Vietnam rose almost triple of the value in 1996 and surpassed that of Lao PDR.

Although the value of import from Lao PDR to Thailand was small due to the size of her economy, Thailand was the second largest destination of Laotian export next to Vietnam, with the share of 20% in 1996 (Table 3.2). Thailand was also the second largest market for Cambodia's. However, export markets of Vietnam has been more diversified than those of the two countries, and Thailand was not in the top 15 of Vietnam largest export destination. From this aspect, Lao PDR and Cambodia would be affected from the Thai crisis greater than Vietnam.

Considering the growth rates of imports from SEATEs to Thailand from 1994 to 1997, data from Table 3.1 show that they are highly fluctuated especially in the case of Cambodia that the growth rate in 1994 was 31%, then in 1996 the growth dropped to minus 70% from the previous year. The imports from Vietnam experienced an uprising trend even in 1997 and the first half, the period after the crisis. However, after the crisis, Lao PDR has been most severely affected by the crisis. Thailand's imports from Lao PDR grew at a negative rate of 19.21 percent in 1997, and further deteriorated in the first and the second quarters of 1998 at the rates of 55.31 and 60.06 percent respectively. In contrast, imports from Cambodia and Vietnam grew by 47.09 and 178.23 percent respectively in 1997 even though Thailand's imports from Cambodia started to contract in the fourth quarter of 1997.

Diversification of export products lessened the impact of the crisis. Vietnam's major export products to Thailand include crude oil, frozen seafood, gem, hide, chemical, and electronics. Trade in electronics products indicates linkages between Thai and Vietnamese electronics firms that produce for the international network not for domestic demand. For some products that are relatively cheap raw materials, Thai firms utilize them for exports that still exhibit positive growth in the world market. In addition, the magnitude of Vietnam and Thailand before 1997 was small compared to the size of her economy (the value of import from Vietnam was less than that of from Lao PDR to Thailand in 1996); thus there is potential of trade expansion between these two countries, and the growth rates of import in 1997 and 1998 were positive. Wood, wood products and electricity are only major exports from Lao PDR. Wood and wood products depend on the growth rates of Thai production in real estate and furniture sectors that severely affected by the crisis. Demand for electricity in Thailand also slows down significantly and there is excess reserve of the generation system. The slow down in export from Cambodia resulted from both the unstable security and political situation, which disrupt the trade flow between these two countries and the contraction of the Thai economy.

Table 3.1 Thailand's Trade with SEATEs

Millions of US dollar											
	1993	1994	1995	1996	1997	1997				1998	
						Q1	Q2	Q3	Q4	Q1	Q2
a.Exports to											
Cambodia	179.27	260.16	334.09	362.61	306.61	93.65	82.51	62.95	73.24	72.29	77.62
Laos	175.00	291.29	354.48	362.97	376.64	95.00	99.62	96.33	88.39	84.62	82.88
Vietnam	115.76	253.68	467.75	578.60	543.22	143.26	119.42	128.78	147.19	155.13	159.53
Total export to SEATes	470.03	805.14	1,156.33	1,304.18	1,226.48	331.91	301.55	288.06	308.83	312.05	320.02
Total export to Thailand	36,961.81	45,232.96	56,444.12	55,717.98	57,589.54	14,129.24	14,025.57	14,575.09	14,773.47	13,734.73	13,079.94
b.Imports from											
Cambodia	96.41	126.32	160.02	47.78	70.29	36.46	23.20	14.69	4.32	5.69	7.56
Laos	63.15	69.11	69.76	68.42	55.27	19.91	21.24	12.06	6.66	8.89	8.48
Vietnam	84.76	39.17	43.11	65.66	182.68	33.52	35.52	52.89	53.99	55.18	48.53
Total import from SEATes	244.32	234.59	272.89	181.86	308.24	89.90	79.96	79.64	64.96	69.77	64.58
Total import from Thailand	46,074.60	54,435.30	70,783.86	72,318.62	61,337.53	17,483.74	17,206.07	15,166.75	12,914.38	10,950.85	10,648.55

Source: Bank of Thailand

**Table 3.2**  
**Ranking of SEATEs' Major Export Destination 1996**

Countries	Cambodia	Lao PDR	Vietnam
Vietnam	5 (6.9277)	1 (40.8410)	- -
Thailand	1 (12.9520)	2 (18.6190)	(0.8654)
Malaysia	9 (2.1084)	...	13 (1.9761)
Indonesia	10 (1.8072)	...	15 (1.3414)
Singapore	1 (12.9520)	10 (0.9010)	3 (5.7262)
France	8 (3.3133)	4 (6.006)	4 (4.8464)
Germany	2 (12.6510)	5 (4.8048)	2 (8.1206)
USA	12 (1.2048)	5 (4.8048)	5 (4.4858)
UK	3 (9.3373)	7 (3.003)	9 (3.2742)
Japan	10 (1.8072)	3 (6.6066)	1 (26.3810)

Note: The figures in parenthesis are percentage of export value in total export.

Source: Direction of Trade Statistics Yearbook 1997.

It should be mentioned that a slowdown of imports of Thailand from worldwide is more than that from SEATEs, i.e., the Thai economic crisis has had less effect on imports from SEATEs compared to the rest of the world. Thailand's major imports from the rest of the world are machinery and parts, and raw materials for production; these items are used for exports and for production of capital-intensive industries such as petrochemical, steel, automobile, and cement. Since the export growth has been slow especially for labor intensive-products while domestic demand for import substitution capital-intensive industries decline excessively. The demand for imports from these industries declined significantly.

The trade growth of SEATEs is not only affected by the crisis situation in Thailand, but also from the domestic environment of each country. The liberalization policies in these countries have increased trade and investment flow enormously especially in Vietnam after the abolishment of The US embargo. On the other hand, the political instability and insecurity in Cambodia cause the fluctuation of trade, both exports and imports, during the period of the study. Consequently, if the situation in Thailand is improved, internal factors in each country are still the major constraints on how much trade can be enhanced.

The above discussion focuses on impact of the crisis on import and economic growth of SEATEs. There is another aspect of impact on trade to Lao PDR, which is an impact on inflation. Lao PDR imports 80% of total import value from Thailand. The higher inflation in Thailand can transmit to Lao PDR via higher import prices and baht depreciation does not offset the inflation since and transaction border trade is conducted in baht.

There is also some concern that Vietnam will loss competitiveness to Thailand due to baht depreciation. However, the baht at 36 baht/\$ is about the same depreciation rate with Vietnamese dong. Furthermore major export markets of Vietnam are Japan, Germany, Singapore, and France while the major markets for Thailand are ASEAN, Japan and the US. Japan seems to be a major market that Thailand competes with Vietnam. However, the export products of Thailand are semi-high-technology intensive while Vietnam are processing products and labor-intensive. Thus, the argument that the crisis intensified competition between these two countries is not conclusive.

### 3.2 Impact on Investment

Foreign Direct Investment (FDI) has long been regarded as one of major factors in the development process in developing countries. Each country may benefit from technology transfer, export generation, employment generation, and industrial linkages as a result of FDI. Therefore, a number of developing countries include SEATEs, have pursued policy measures, which attracts FDI for years. For transitional economies FDI is the most important for integration with the world trade system since these countries still lack entrepreneurs and international market channels after the long period under central planning economies.

Thailand is one of the major investors in all these three countries. The value of Thailand's investment in Lao PDR from the year 1988 until March 1998 is \$2.657 billion, which is the highest among foreign investors in the country (Table 3.3). Thai investors invested in various activities for examples, hotels, electricity, garment, banking, telecommunication, and wood products. While a number of projects invested in Lao PDR by Thai investors significantly increased during 1991-1994, the investment started to rise at a slower pace since 1995. Thai investors invested 55 projects in 1993 while the number dropped to 13 projects in 1997. (Table 3.4)

**Table 3.3**  
**Stocks of Foreign Direct Investment in Lao PDR**

Country	1988-1996		1988-March 1998	
	Total Projects	Project Value	Total Projects	Project Value
<i>Thailand</i>	<b>232</b>	<b>2,592</b>	<b>244</b>	<b>2,657</b>
USA	36	1,482	39	1,483
South Korea	20	455	25	463
France	72	318	78	319
Malaysia	11	202	17	278
Australia	41	135	44	139
Taiwan	32	71	35	71
China	62	40	67	44
UK	16	35	18	36
Hong Kong	22	28	22	28
Singapore	15	14	20	17

Source: The Board of Investment.

**Table 3.4**  
**Thailand's Foreign Direct Investment in Lao PDR**

Unit: Million US\$

Year	No. of Projects	Project Value*	Total Investment**
1988	4	0.69	0.89
1989	21	11.08	61.42
1990	10	4.22	5.17
1991	23	92.93	112.78
1992	35	34.95	39.27
1993	55	56.55	88.39
1994	46	1,571.98	2,528.57
1995	19	161.53	760.50
1996	18	646.57	1,034.77
1997	13	5.68	7.27
<i>Jan-June 1998</i>	<i>11</i>	<i>NA</i>	<i>81.623***</i>
<b>Total</b>	<b>255</b>	<b>2,586.20 (until 1997)</b>	<b>4,639.02</b>

Notes : \* Value of FDI for the whole project, include share of other countries' investment.

\*\* include share of Laos' investors.

\*\*\* Laos Railway Transportation project accounts for 75,000 billion US\$.

Source: The Board of Investment.

Thailand is the eighth and the tenth biggest foreign investor in Vietnam and Cambodia respectively. Until 1997, Thailand had invested 109 projects in Vietnam with total value of \$1.038 billion, while Thailand's investment in Cambodia accounted for 44.6 million US dollar during the same period. (Table 3.5 – Table 3.7)

There are three reasons motivating direct foreign investment: one is to utilize host countries resource endowment; the second is to produce for domestic demand; and the third is to use the host countries as an export base taking advantage of strategic factors such as location or low-wage labor. As mentioned above, Thailand has invested in number of activities in SEATEs, covering agriculture, manufacturing, and services sectors. Most activities are aimed at using host country resources to serve regional demand or utilizing domestic demand rather than to produce for export. The rate of natural resource deterioration in Thailand has increased overtime; the utilization of natural resources in SEATEs has still been one of major motivation of the investment from Thailand.

The economic crisis has discouraged outward investment in Thailand. Overcapacity in some industries such as cement and automobile reduce incentive to invest in SEATEs. Over capacity in Thailand does not only result in no expansion of capacity in Thailand, but also affect the investment expansion in SEATEs as well. Credit crunch also restricts investment not only abroad but also in Thailand. Credit crunch arose as banks were reluctant to lend to most corporations whose balance sheets have been significantly deteriorated as a result of the depreciation and thus drastic increase in foreign debts. Moreover, the unwillingness of foreign creditors to lend to banks also worsened the problem. Since they became much less willing to lend to their customers, it is unlikely that the investment of Thailand can be expanded both domestically and internationally.

While the economic crisis directly results in a decline in investment in Thailand and thus an expected decrease in Thailand's investment in SEATEs, the internal factors of host country also have strong effect on a decline of the investment. The slow growth and excess supply, such as in the case of hotel and real estates in SEATEs make the investment in these countries unattractive.

In addition, number of rules and regulations in SEATEs can also be viewed as obstacles of foreign direct investment, even before the crisis. For example, the underutilization of the Mekong Bridge from Nong Khai to Vientiane because regulation does not permit entry of cars from Thailand and visa entry requirement for travel in the region within limited time which obstruct the movement of people. Consequently, the elimination of rules and regulations that obstruct flow of border trade and movement of people will likely to attract more FDI and thus benefit SEATEs. The data indicate that trend of value of foreign investment has been declining even before the crisis reflecting other factors such as absorptive capacity of the host countries and obstacle regulations.

### **3.3 Impact on Tourism**

One of the factors worsening current account deficits was the foreign exchange outflow due to large number of outward Thai tourists whom are notorious as big spenders. With baht depreciation, travel abroad becomes more expensive, coupling with the slow down of economic growth; thus, it is anticipated that the number of outward Thai tourists will be declining. The data confirm this hypothesis. In 1996, a number of outward Thai travelers were 1,823,676 persons. This number, however, significantly dropped by 10.2 percent to 1,637,595 persons in 1997 and then further decreased by 25.86 percent during January to July 1998 compared with the figure in the same period in 1997 (Table 3.8).

**Table 3.5**  
**Foreign Direct Investment in Cambodia**

Unit: Million US\$

Country	Aug 94-Dec 95		1996		1997		Total	
	No. of Projects	Project Value	No. of Projects	Project Value	No. of Projects	Project Value	No. of Projects	Project Value
Malaysia	25	1,495.6	24	25.6	16	52.9	65	1,574.1
Cambodia	13	467.5	106	129.3	92	73.8	211	670.6
Singapore	27	124.8	18	35.1	16	12.5	61	172.4
China	21	72.8	28	21.4	30	21.8	79	116.0
Canada	1	80.0	2	7.6	7	1.8	10	89.4
United Kingdom	11	50.7	6	50.3	13	5.8	30	106.8
Taiwan	22	42.8	33	124.7	63	48.3	118	215.8
Indonesia	2	43.0	5	1.5	4	2.2	11	46.7
USA	16	29.7	6	6.7	9	13.8	31	50.2
<b>Thailand</b>	<b>16</b>	<b>25.4</b>	<b>10</b>	<b>11.8</b>	<b>10</b>	<b>7.4</b>	<b>36</b>	<b>44.6</b>
Others	45	44.1	50	41.7	63	132.3	158	218.1
Total	199	2,476.4	288	455.7	323	372.6	810	3,304.7

Source: Cambodia Investment Board.

**Table 3.6**  
**Foreign Direct Investment Projects in Vietnam**

Year	Number of Projects	Registered Capital (Mil. US\$)	Of which: Legal Capital (Mil. US\$)
1988	37	371.8	288.4
1989	68	582.5	311.5
1990	108	839	407.5
1991	151	1322.3	663.6
1992	197	2165	1418
1993	269	2900	1468.5
1994	343	3765.6	1729.9
1995	370	6530.8	2986.6
1996	325	8497.3	2940.8
1997	340	4462.5	2148.8
<b>Total</b>	<b>2208</b>	<b>31436.8</b>	<b>14363.6</b>

Note: Excluded the projects of VIETSOVPETRO and the licensed projects in export processing zones.

Source: Vietnam Statistical Yearbook 1997.

**Table 3.7**  
**Foreign Direct Investment to Vietnam 1988-1997 by Countries**

Country	Number of Projects	Registered Capital (Mil. US\$)	Of which: Legal Capital (Mil. US\$)
UK	27	569.1	427.2
Belgium	10	20.4	7.7
Canada	23	168.5	157.6
F. R. Germany	29	205.1	77.4
Taiwan	354	4,168.5	1,845.8
Netherlands	32	565.4	461.9
Korea Rep. of	223	2,960.7	1,126.6
Hong Kong	264	3,364	1,414.9
USA	74	1,095.4	452.2
Indonesia	18	318.3	103.5
Italy	11	70.4	25.2
Fed. Russian	56	191.3	137.2
Malaysia	68	943.9	437.8
Japan	236	3,037.5	1,574.3
Australia	72	1,080.8	436.3
France	119	1,705.1	981.8
Philippines	24	221.8	109.2
British Virgin Islands	66	1,667.4	664.2
Thailand	109	1,037.5	452.4
Switzerland	25	618.6	244.7
China	56	88	49.8
Singapore	185	4,845.7	1,722.6
Others	127	2,493.4	1,453.3
<b>Total</b>	<b>2,208</b>	<b>31,436.8</b>	<b>14,363.6</b>

Source: Vietnam Statistical Yearbook 1997.

**Table 3.8**  
**Outward Thai Tourists**

Unit : Persons

Destination	1996	1997	1997(Jan.-Jul.)	1998 (Jan.-Jul.)
Laos	141,078	153,231	76,118*	105,811*
Cambodia	14,834	14,137	9,918	6,694
Vietnam	16,458	16,716	10,215	8,599
Myanmar	25,774	26,572	15,192*	12,729*
Singapore	268,560	211,114	132,753	95,516
Hong Kong	273,448	201,368	132,838	62,899
Europe	174,241	155,661	95,710	45,646
USA	65,362	53,935	33,449	17,096
<b>Total</b>	<b>979,755</b>	<b>832,734</b>	<b>414,883</b>	<b>236,450</b>
<b>Others</b>	<b>843,921</b>	<b>804,861</b>	<b>660,127</b>	<b>560,527</b>
<b>Grand Total</b>	<b>1,823,676</b>	<b>1,637,595</b>	<b>1,075,010</b>	<b>796,977</b>

Note: \* Jan.-Jun.

Sources: The Tourism Authority of Thailand;  
Immigration Bureau, Police Department

Likewise, Vietnam, Cambodia and Lao PDR tourist industries should be adversely affected by the baht depreciation. However, Table 3.8 shows that a number of Thai tourists travel to these countries does not decline as much as the number of Thai tourists travel to other countries, such as, Singapore, Hong Kong, Europe, and USA. In 1997, the number of Thai tourists travel to Vietnam increased by 1.57 percent from 16,458 persons in 1996 to 16,716 persons in 1997, while the number of Thai tourists travel to Cambodia and Lao PDR (using Visa entry) dropped by 4.7 and 6.04 percent respectively. During January to July 1998, a reverse trend can be noticed in the case of Vietnam and Lao PDR in which the number of Thai tourists travel to Vietnam decreased by 15.82 percent while the number of Thai tourists travel to Lao PDR increased by 1.68 percent. In addition, the number of Thai tourists' travel to Cambodia significantly declined at a rate of 32.51 percent during the same period. A significant declining in the number of Thai tourist's travel to Cambodia also resulted from the political instability and security problem in the country.

While the number of Thai tourists travel to Lao PDR using visa entry tends to decrease or increase at low rate. The number of Thai tourists travel to Lao PDR using border passes has significantly increased by 17.83 percent in 1997 and further increased by 61.62 percent during January to July 1998. Therefore, the total number of tourist from Thailand to Lao PDR rose by 8.6 % in 1997 and 39% in the first half of 1998. From January to July 1998, the number of Thai tourists travel by car, coach and train increased by 18.4 percent while the number of Thai tourists travel by airplane and ship dropped by 37.34 and 5.66 percent respectively.

The crisis does not have a strong negative impact on tourism in SEATEs. The baht depreciation, however, benefit Thailand's tourist industry as the number of tourists arrival to Thailand has continually increased by 3.46, 1.42, and 6.44 percent in 1996, 1997, and January to September 1998 (Table 3.9). This in turn may benefit Vietnam, Cambodia, and Lao PDR from spill over effect, since there is a possibility that those tourists may continue their journey to these countries. However, the information of the number of tourists arrival to Thailand and continue their journey to Vietnam, Cambodia, and Lao PDR is not available, leaving this comment inconclusive. Nevertheless, cooperation in tourism between SEATEs and Thailand will provide mutual benefit for the region.

**Table 3.9**  
**International Tourist Arrivals to Thailand**

	1995	1996	%change	1997	%change	1998 (Jan.-Sep.)	% change**
<b>Total</b>	<b>6,951,566</b>	<b>7,192,145</b>	<b>3.46</b>	<b>7,293,957</b>	<b>1.42</b>	<b>5,669,028*</b>	<b>6.44</b>
Jan.	—	608,953	—	624,972	2.63	710,350	13.66
Feb.	—	681,342	—	713,950	4.79	663,253	-7.10
March	—	649,765	—	671,572	3.36	689,907	2.73
April	—	581,979	—	576,589	-0.93	637,909	10.63
May	—	499,179	—	533,420	6.86	536,527	0.58
June	—	510,114	—	500,300	-1.92	558,724	11.68
July	—	584,918	—	577,895	-1.20	630,354	9.08
Aug.	—	624,529	—	625,643	0.18	670,179	7.12
Sept.	—	483,251	—	501,878	3.85	571,825	13.94
Oct.	—	565,909	—	540,628	-4.47	—	—
Nov.	—	669,425	—	653,430	-2.39	—	—
Dec.	—	732,771	—	773,680	5.58	—	—

Notes: \* (Jan.-Sept. 1998).

\*\* growth of tourist arrivals year-on-year.

Sources: The Tourism Authority of Thailand;  
Immigration Bureau, Police Department.



### 3.4 Employment: SEATEs migrant workers

The potential impact of the Thai economic crisis on employment of the SEATEs workers may be divided into *direct impact* where the crisis directly affects the employment of SEATEs workers and *indirect impact* where the crisis indirectly affects the SEATEs economies in general and in turn induces change in the SEATEs labor market. This section limits its discussion on the first issue particularly with regard to the employment of SEATEs workers in Thailand.

Thailand is one of the major labor receiving countries for workers from SEATEs and other neighboring countries. Given the serious employment problems encountered by Thailand, there is expected an impact on the SEATEs migrant workers to some extent. The natural tendency for Thailand or other countries in this position was to repatriate foreign workers, especially undocumented workers, to save jobs for the locals in view of strong political pressures in the wake of rising domestic unemployment.

#### *SEATEs migrant workers in Thailand*

To begin with, we need to know the extent of the presence of SEATEs workers in Thailand. Indeed, the number of migrant workers from SEATEs is not that many as compared to those from Myanmar or Bangladesh.

Migrant workers in Thailand can be divided into two major groups, *legal immigrants* and *illegal immigrants or undocumented migrant workers*. According to Yongyuth and Chalongphop (1996, p16) the total number of legal aliens in Thailand reached 316,174 in 1996, a sizable increase from 180,022 in 1994. The increase is due to an increase in the number of *temporary work permits* which resulted from cabinet resolutions in mid-1996 to give amnesty to illegal migrant workers. However the majority of the legal migrant workers are from non-SEATEs countries such as Japan, Hong Kong, the Republic of China (Taiwan) and Western countries.

The number of illegal migrants workers was estimated at 943,745 in 1997 compared to 750,000 in the previous year (Ibid, p17). The movement of undocumented unskilled workers entering the border from Indochina and South Asia has grown since World War II. The *push* factors include civil wars in neighboring countries that have made Thailand an asylum for Indochinese refugees. The *pull* factors include Thailand's increasing affluence during the bubble economics. Yongyuth and Chalongphop indicate that the major reasons for the increasing number of illegal migrants in Thailand are, *first*, an enormous wage differential between Thailand and her neighbors, 10 times compared to Myanmar and 5 times with Lao PDR or Cambodia. It was estimated that these migrant workers sent at least US\$ 1 billion back home each year while the Thai employers saved at least US\$ 3 billion on their wage bills; *second*, the lack of job opportunities in their own countries, in addition to unfavorable living conditions; *third*, informally organized networks of private placement agencies with cooperation from both officials and business people helped facilitate or speed up the influx of illegal migrants; *fourth*, the long border and too many channels making enforcement very difficult and: *fifth*, bribery, corruption and inefficiency of immigration law enforcement encouraging employers to opt for cheap migrant workers.

How many of the illegal migrants are from SEATEs? Because of its underground nature, there is not clear data on illegal migrants. According to the National Security Council, there were 525,000 illegal migrants in Thailand in September 1994, nearly two thirds of them were from Myanmar. By the end of 1994, the number of Myanmar migrants increased by at least 10 percent. As mentioned earlier, the number of illegal migrants workers was estimated at 943,745 in 1997

compared to 750,000 in 1996<sup>5</sup>. The number of undocumented migrants is given in Table 3.10. Out of the 943,745, only 293,652 or about 39 percent became registered when the Government allowed in 1995. While it is not known how many of the unregistered migrant workers are from SEATEs, the official data indicates that out of 269,948 *registered* migrant workers only 10,874 are from Lao PDR, 23,439 from Cambodia and none from Vietnam. It is difficult to tell how many of the remaining 673,797 undocumented migrants not registered are from SEATEs. (At the risk of over simplifying, if the same proportion of registered migrant workers is applied, the number of *unregistered* migrant workers from Lao PDR may be around 26,952 that from Cambodia around 58,620. As a result of this simple estimate, the total number of undocumented migrant workers is around 37,826 from Lao PDR and 82,020 from Cambodia.)

**Table 3.10**  
**Number of Undocumented Migrants in Thailand by Major Areas, 1997**

Areas	Number	%	Number	%	Number	%
Border	256,146	27.1	79,195	29.3	176,951	26.3
Coastal	313,896	33.3	117,549	43.5	196,347	29.1
Others						
– Bangkok	223,288	23.7	38,412	14.2	184,876	27.4
– Non-BKK	150,415	15.9	34,792	12.9	115,623	17.2
Total	943,745	100.0	269,948	100.0	673,797	100.0
Percent	100.0		28.6		71.4	

Source: Department of Employment, Ministry of Labor and Social Welfare, 1997.

### *The crisis, unemployment and policy to replace migrant workers*

In response to the crisis, and under the IMF conditionalities, in December 1997 the Thai Government adopted a resolution to establish an “unemployment alleviation action plan” consisting of 7 policy measures, among which is “Immigrant Workers Replacement”. The measure is aimed at reducing the number of undocumented migrant workers working in factories by 300,000 to provide employment for local workers.

The measure, however, was not implemented without a resistance from local employers who are used to cheap and not-demanding workers. Their argument was that local workers were not willing to go into the jobs involving arduous and risky work with low pay, usually one third to one half of wages paid to Thai workers. The industries that are in demand for these workers are particularly rice milling and fishing industry. In response to the pressure from the employers, the Government has appointed a working committee to study the problem and to recommend appropriate measures. At present the relaxation is underway to allow workers from Lao PDR, Cambodia and Myanmar to work in specified border provinces and only in marine fishing and milling industry.

As of July 1998, the Department of employment reported that 230,000 illegal migrant workers have been pushed off. However, only 80,000 of their jobs have been replaced by Thai workers (Sontisakyothin 2000).

<sup>5</sup> According to an ILO estimate the number of migrant workers was 1.26 million in 1997 and 0.8 million in mid 1998 (Wickramsekara, Table 18). The figure, however, may include all migrant workers both documented and undocumented.

### *Impact of the Thai crisis on the SEATEs migrants*

By a rough assessment, it seems that the Thai crisis affects the SEATEs migrants a little and for a short time when the policy to replace foreign workers was newly implemented. The measure has been relaxed after a pressure from local employers who have shown that certain types of work (3Ds: dangerous, dirty and demanding) cannot find Thai workers. Depending on how long the crisis will last and how long the Thai laborers can stand the tightened job markets, there is still a demand for foreign workers. The following observations could be made.

- The total size of the migrant workers to be affected is about 37,826 from Lao PDR and 82,020 from Cambodia, a total of 119,846. Out of this number, not all of them will be defected.
- For the time being, it may be more difficult for them not only to work openly but also to find employment. It is clear that certain industry in Thailand particularly Construction is in deep trouble, thus there will be no demand from this sector. At present, only work in the marine fishing and milling industry in given provinces are permit. According to an ILO estimate about one thirds of work for migrant workers has gone (Wickramasekara 1998, Table 18).
- Although virtually the labor market of the SEATEs migrants is different from the local workers, if the crisis lasts longer there will be more pressure to replace the foreign workers.

### **3.5 Development cooperation with SEATEs (HRD)**

Thailand's economic crisis does not only put her into a bad position financially but also reveal many other problems reflecting her structural weaknesses. Her confidence as the fifth Tiger of Asia has probably gone and her active role in development cooperation in the Greater Mekong Sub-region is subject to question. In the context of SEATEs which include Cambodia, Lao PDR, and Vietnam, this section reviews and discusses the potential role of Thailand in providing technical assistance to these countries with an emphasis on human resource development.

#### **3.5.1 Background**

Thailand's development cooperation dated from 1954, when the government organized education and training programmes for fellows or trainees from developing countries who received fellowships from international organization or donor countries. However, the cooperation was rather informal as a neighboring country. The events of the mid-1970s, when Communism and Socialism assumed power in Indochina countries, played down Thailand's role in cooperation with these countries. With the end of Cold War, Thailand's cooperation was resumed. The obvious and formal resumption occurred in 1988 when Thailand's Prime Minister announced his policy of turning the Indochina battlefield into a marketplace.

Thailand's development cooperation is presently under the responsibility of four major government agencies: the Ministry of Foreign Affairs, the National Security Council, the Department of Technical and Economic Cooperation (DTEC), and the Committee for the Coordination of Economic Cooperation with Neighboring Countries (CCEC).<sup>6</sup> Under DTEC, the Division of External Cooperation established in March 1992 is responsible for the administration

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<sup>6</sup> Formerly established on 20 August 1993 as the National Committee for the Coordination of Economic Cooperation in the Greater Mekong Subregion. The present Committee was established on 23 June 1995. The Committee is chaired by the Prime Minister and has a secretariat office attached to the Office of the National Economic and Social and Development Board.

and coordination of technical and economic cooperation provided by the Thai Government to other countries. The CCEC, on the other hand, is responsible for the coordination of economic cooperation between Thailand and neighboring countries in the Greater Mekong Subregion, particularly those under the frameworks of ADB's Greater Mekong Subregional Economic Cooperation Programme (ADB-GMS), the Mekong River Commission (MRC), the Forum for the Comprehensive Development of Indochina (FCDI), the Working Group on Economic Cooperation in Indochina and Myanmar (WGEC-CLM or AEM-MITI), the ASEAN-Mekong Basin Development Cooperation and the Quadripartite Economic Cooperation (QEC).

Generally, there are three broad types of development cooperation—bilateral, trilateral and multilateral. Bilateral cooperation is the cooperation between Thailand and another country with funding from Thailand and possible partly counter funding from the partner country. The trilateral cooperation involves three parties—Thailand, donor countries/organization and recipient developing countries. The multilateral cooperation is basically the cooperation that Thailand cooperates with international organizations to provide assistance to developing countries. Operationally, however, Thai International Cooperation Programme (TICP), especially the cooperation under the responsibility of DTEC is classified into four types as follows:

- (1) Bilateral Programme,
- (2) Annual International Training Courses (AITC) or Thai International Training Programme (TITP),
- (3) Technical Cooperation among Developing Countries (TCDC),
- (4) Third Countries Training Programme (TCTP), and
- (5) Multilateral Cooperation Programme.

The Bilateral Programme consists of two types of programmes (a) Country programme and individual requests and (b) Sino-Thai Cooperation. The first programme focuses on human resources development in the field of education, health and agriculture by assisting other developing countries in identifying and designing special courses which could serve their specific needs, and which the courses are not offered under the group training option. The second type was created in 1978 when the People's Republic of China and Thailand began its scientific and technical cooperation under the bilateral discussion on a basis of the UNDP/TCDC modality arrangements in exchanging experts.

The Annual International Training Courses provides a wide range of courses of development concerns such as agriculture, rural and community development, industry, energy, health care, telecommunications etc. Fellowships to support participation are also available.

The TCDC was an adoption of the UNDP/TCDC modality under the Bueno Aires Plan of Action. The responsibility of the cost involved is shared between both countries who make exchange of participants—the participating country is responsible for international costs while the host country absorbs all local costs.

The Third Country Training Programme (TCTP) organizes training programmes or study tour in Thailand for participants from other countries whom are sponsored by international organizations or donor countries. The Department of Technical and Economic Cooperation is responsible for the coordination and programme arrangements as well as the administrative costs.

The Multilateral Cooperation Programme could be arranged in a number of ways. The first alternative is under the TCTP. The second alternative is based on cost-sharing between the Thai Government and donor countries or international organizations to provide assistance to recipient developing countries. Such assistance include—group training courses, sub-regional cooperation programme, partnership programme, and technical cooperation among developing countries (TCDC).

### 3.5.2 Assistance to SEATEs

In 1997 the Thai development assistance to SEATEs was 282.89 million baht, 56.7 million for Cambodia, 177.7 million for Lao PDR and 48.5 for Vietnam (Table 3.11), compared to 205 million baht in 1995 reflecting an increase of about 19 percent per annum. (In 1995 Thailand's development assistance was 20.2 million baht for Cambodia, 157 million for Lao PDR and 27.9 for Vietnam. (Srawooth et.al.1996, 20)) About 63 percent of this assistance went to Lao PDR whereas 20 percent and 17 percent went to Cambodia and Vietnam respectively. Approximately 90 percent of the development assistance in 1995 was under the Bilateral Programme, mostly in the form of assistance on requests. Group Training was second on demand from Indochina (accounting for 8.5 percent) whereas TCDC accounted very little in the cooperation (1.17 percent).

**Table 3.11**  
**Total Value of Thai International Cooperation Program According to Program (FY 1997)**

						Value in Thousand Baht
Country	Bilateral	AITC	TCDC	ILP	TCTP	Total (Percentage)
Cambodia	48,414	6,970	375	430	527	56,716 (20.04)
Lao PDR	168,709	6,349	49	1,496	1,062	177,665 (62.81)
Vietnam	37,505	5,428	49	4,802	728	48,512 (17.14)
Total	254,628	18,747	473	6,728	2,317	282,893
(Percentage)	(90.00)	(6.63)	(0.17)	(2.38)	(0.82)	(100.00)

Note: Types of Thai International Cooperation Program (TICP)

1. Bilateral Program
2. Annual International Training Courses Program
3. Technical Cooperation among Developing Countries Program
4. Institutional Linkage Program
5. Other TICP Activities
6. Third Country Training Program

Source: Department of Technical and Economic Cooperation 1997.

In 1997 the majority of the assistance (67.3 million baht or 70%) was for Equipment and Construction while the assistance for HRD came down to 18 million (19%) compared to 114 million in 1995. (Table 3.12).

**Table 3.12**  
**Development Projects (FY 1997)**

					Value in Thousand Baht
Country	Training	Expert/Mission Mission	Equipment/ Construction	Others	Total
Cambodia	3,104	277	32,567	–	35,948
Lao PDR	7,731	2,338	20,157	2,962	33,188
Vietnam	723	3,571	14,603	1,166	26,571
Total	18,066	6,186	67,327	4,128	95,707
(Percentage)	(18.9)	(6.50)	(70.30)	(4.30)	(100.00)

Source: Department of Technical and Economic Cooperation 1997.

**Table 3.13**  
**Total Value of TICP by Sector (FY 1997)**

	Value in Thousand Baht		
	Cambodia	Lao PDR	Vietnam
Agriculture	4,412	20,198	15,541
Communications	195	2,633	492
Economic Development	2,064	22,917	3,848
Education	1,763	43,519	16,332
Industry	413	1,928	1,337
Infra. & Utilities	98	5,030	144
Public Adm. & Legislation	2,833	19,038	1,088
Public Health	24,231	47,518	5,353
Sci. & Tech. & Env.	523	5,650	1,906
Social Development	18,540	4,495	1,831
Trade & Service	1,427	4,739	-
<b>Total</b>	<b>56,549</b>	<b>177,665</b>	<b>47,872</b>

Source: Department of Technical and Economic Cooperation 1997.

### ***3.5.3 Potential impact on SEATEs***

The potential impact of the crisis on Thailand's technical assistance to SEATEs depends almost solely on the Government budget allocated to the responsible agencies, namely, the Ministry of Foreign Affairs, the National Security Council, the Department of Technical and Economic Cooperation (DTEC), and the Committee for the Coordination of Economic Cooperation with Neighboring Countries (CCEC).<sup>7</sup> In this connection, DTEC's budget deserves attention as it is the major organization responsible for coordinating the technical assistance to SEATEs.

According to the 1998 budget which have been revised a number of times to accommodate the IMF conditionalities, more than 18 percent of the initially proposed budget (of 182,000 million baht) would be cut. At the end, the 1999 budget for DTEC was reduced to 133 million baht as compared to about 300 million allocated in the 1998 Fiscal Year. This heavy cut will certainly affect the technical assistance to receiving countries including mainly SEATEs. In an informal consultation DTEC authority, we learned that the government's policy in connection with the subregional technical assistance is to pursue the commitment on the ongoing projects and refrain from giving new assistance. The policy will be reconsidered in the year 2000 depending on the crisis situation.

## **3.6 Prospect of the Thai Economy**

To foresee how the country's prospect will be, one should monitor what we have done to rectify the problem and other measures which are in the process of implementation. Moreover, it is also necessary to explore the external environment that is likely to contribute positively or negatively towards recovery in the Thai economy.

<sup>7</sup> Formerly established on 20 August 1993 as the National Committee for the Coordination of Economic Cooperation in the Greater Mekong Subregion. The present Committee was established on 23 June 1995. The Committee is chaired by the Prime Minister and has a secretariat office attached to the Office of the National Economic and Social and Development Board.

### ***3.6.1 Government measures in response to the crisis***

Abundant government measures have been employed since the start of the crisis. Weak macroeconomic conditions led to the baht attack in early 1997. Accordingly, exchange rate system has been changed from basket of currency system to managed float scheme. In the meantime, financial institutions were also in trouble due to excessive foreign debt burden, mounting bad debt and the economic slowdown. Both currency and financial crises led to severe economic meltdown. When the crisis is unlikely to be controlled by the sole government, IMF was called in August 1997. The rescue package was formulated under the standby credit arrangement scheme. Under the scheme, IMF together with member countries collectively lent 17.2 billion US dollar to Thailand. The policy measures are the results of the consultation and negotiation between Thai government officials and IMF. The policy measures and targets are described in the Letter of Intent (LOI). In this section, we discuss major policy measures on macroeconomic management, financial system restructuring and structural reform. However, not only economic policy measures, the government also launched various measures to alleviate the social impacts from the crisis, although we do not discuss in this paper (Thongpakde et al. 1998: 28-47).

#### ***a) Macroeconomic management***

When the IMF were called in, the standard IMF dose of medicine was to be initiated. The main objectives of the IMF rescue plan were to stabilize the currency and eliminate excess demand. Hence, tight monetary policy and fiscal discipline were placed on as the country macroeconomic policies. A cut in government budget, an increase in tax to reduce consumption, both public and private, and high interest rates to reduce investment and to stabilize exchange rate. The improvement in the current account and baht stability were our main policy objections during that time.

The contractionary policy during LOI 1 to 4 resulted in more than expected slowdown in the Thai economy. In addition the contagion effect in the Asia region which discouraged Thai export demand that further shrunk aggregate demand of the economy. Domestic output fell sharply, unemployment grew up and many business firms have gone under. Accordingly, due to severe economic recession, the macroeconomic policy has been shifted from contractionary to expansionary in the fifth LOI. The fiscal policy was eased from budget surplus to a deficit of 3% to GDP. The expanded government spending is aimed to stimulate domestic demand as well as to alleviate social impacts from the crisis. The monetary policy is also reversed from tightening to relaxation. More liquidity had been injected in to the market and provides credit for important sectors such as exports and manufacturing. As a result, an interest rate has been declined since October 1998. In addition, the government also put more emphasis on improving broader agricultural production, industrial restructuring and the market opening of Thailand's economy.

In the recent LOI (the sixth one), the Thai government has extended its role to boost up the economy, which is resulted in greater budget deficit from 3% to 5% of GDP. Most expenditure is planned to spend for community and social services. Monetary policy is further eased. The government has also put more pressure on commercial banks to lower lending rates. As a result, interest rates tend to further move downward.

#### ***b) Financial System Restructuring***

Financial liberalization without adequate prudential regulation and supervision allowed local financial institutes and corporations to spoil foreign borrowing at low cost. Mismatching of capital usage and unhedged foreign borrowing positions because of the stable baht under the basket of exchange rate scheme let the local borrowers to be vulnerable to sudden currency fluctuation. Over-lending to unproductive sectors, skyrocket of debts due to baht depreciation, excess capacity in various sectors and slow down of economic growth were the major factors driving the local

financial institutions into trouble situation due to the jump in non-performing loans. As a consequent, loss of public confidence to the financial system had been widespread. Financial Institutions Development Fund (FIDF) at the time was the only instrument of central bank to deal with the liquidity problem of financial institutions as a lender of last resort.

Basic idea of the policy is to restructure and rehabilitate the whole financial system. Government produces a number of measures, which are aimed to:

Restore and maintain the solvency and credibility of the Thai financial system,

- strengthen the capital position of the financial institutions,
- impose the international standard to the financial institution system,
- intervene the finance institutes which failed to raise capital and consolidate them,
- enable the financial institutions to perform effectively their role in supporting economic growth, and
- give incentives to facilitate corporate recovery.

The government measures to restructure and alleviate ailing financial system are demonstrated below;

#### 1) Closure of failed financial institutions

The first stage of the financial crisis was developed from currency crisis started in early 1997. Loss of public confidence to the local financial system caused runs in certain finance companies. As a consequent, the government decided to suspend operation of those troubled finance companies. To restore confidence, it also required all financial institutions to recapitalize in order to strengthen their capital base. Finally, the financial institutions that failed to raise capital had been permanently shut down. Together with the closure of finance companies, the government announced that all depositors and creditors are guaranteed to protect the exposure of financial system. In addition, the government established new organizations namely Financial Restructuring Agency (FRA) and Asset Management Company (AMC) to manage and liquidate asset seized from the closed companies. It also set up a new bank, Radhanasin Bank to be a good bank at the time.

#### 2) Intervening in troubled companies

Non-performing loans had kept on rising and problems deteriorated overtime. The closure of the troubled finance companies had been proved to be improper. Thus, the government applied intervention and consolidation method instead. The failed financial institutions were ordered to write down its shareholders' equity to cover the losses in bad debts, and existing management had been replaced. The FIDF stepped in and converted debt into equity in the effort to recapitalize them, which maenad to nationalize them. They would at a certain time be sold or no longer exist.

#### 3) Capital support facilities (CSFs) for the solvency institutions

The package is based on the idea that the shareholders must be responsible for the losses incurred from existing bad debts through the losses in their equity. Then, the government will support new investors in the ailing banks, providing new liquidity and absorbing the rest of the loss through Tier 1 and Tier 2 Capital Support Facilities (CSFs). It is prepared to ease the Basle standards through the regulatory changes in the Capital Adequacy Ratio (CAR) between Tier 1 and Tier 2 capital.



#### 4) Additional measures

- Loan classification and provisioning rules had been tightening to meet international standard (Table 3.14).

- The government also liberalized foreign shareholding limit in financial institutions in order to encourage foreign investment. Foreign investors are allowed to hold share of financial institutions unlimited up to 10 years. After the tenth year, they will be able to hold majority stake but they are not able to get the newly issued shares.

- The financial institutions are encouraged to set up private Asset Management Companies (AMCs). The private AMCs are able to manage the distress loans that are separated from the banks and finance companies. This will enable the financial institutions to solve NPLs more quickly.

- Financial Restructuring Advisory Committee (FRAC) has been established to oversee all implementation relating to financial restructuring and rehabilitation as well as corporate debt restructuring.

- Corporate Debt Restructuring Advisory Committee (CDRAC) has been established by the Bank of Thailand to facilitate and oversee debt restructuring of corporate. The incentive package supporting restructuring, comprising a series of tax incentives developed over the last several months is currently fully completed.

- Institutional frameworks for supervision of financial institutions has been reviewed and reformed to avoid past mistake. The Bank of Thailand is in the process of strengthening its supervisory capacity with help from a Steering Committee of international bankers and World Bank.

- Deposit insurance scheme would be established to replace the current general guarantee that created problem of moral hazard. Private credit bureau is planned to be established by the Thai Bankers' Association with some guidance from the Bank of Thailand. The preliminary strategy calls for development in two phases: a negative list (NPLs, reorganizations, foreclosures), and then an expansion to all firms.

#### *c) Privatization*

Liberalization to increase competition and efficiency is one of the main targets for IMF rescue package. Cabinet had approved the Master Plan for State Enterprise Reform on September 1, 1998. The first batch of reform should be state enterprises relating to water, transportation, telecommunications and energy.

#### *d) Legal Reform*

Amendment of legislation related to foreclosure and bankruptcy reform (Civil Procedure Act and Civil & Commercial Code) and foreign ownership (the Alien Business law, Land Code, Condominium Act) has been carried out. These laws support debt restructuring, speeding up the process of foreclosing on collateral and increased foreign investment. They also increase capacity in the juridical system for the resolution of commercial disputes. A bankruptcy court will be established too.

Table 3.14: Provisioning requirements

Loan classification	Provisioning required
Pass	1%
Special mention	2%
Substandard	20%
Doubtful	50%
Loss	100% or write off

Source: Bank of Thailand

Note: Became effective on December 31, 1997

Table 3.15: Summary of IMF rescue package

LOI 1-4	LOI-5	LOI-6
<i>Contractionary scheme</i>	<i>Expansionary scheme</i>	<i>Focus on debt restructuring</i>
<ul style="list-style-type: none"> <li>Budget surplus (LOI 1-2)</li> <li>Tight monetary policy</li> <li>Closure of 56 financial institutes and setting 3 special units to manage and liquidate seized asset.</li> <li>New provisioning rules for loans and NPLs</li> <li>Guarantee to depositors and creditors</li> <li>Enactment of 4 laws to rehabilitate financial system</li> </ul>	<ul style="list-style-type: none"> <li>Budget deficit of 3% of GDP (FY 99)</li> <li>Relaxed monetary policy</li> <li>Emphasis on financial and corporate debt restructuring</li> <li>Foreclosure law to be passed by October 1998</li> <li>Better social safety net to improve broader agricultural production and industrial restructuring and the market opening of Thailand's economy</li> </ul>	<ul style="list-style-type: none"> <li>Budget deficit of 5% of GDP (FY 99)</li> <li>Encouraging credit extension</li> <li>Balance of incentives, penalties and arbitration among creditors in debt restructuring</li> <li>Urge the recapitalization of financial institutions</li> <li>Social safety net program to support priority areas in rural and urban sectors to relieve impact on economic recession</li> <li>Foreclosure laws and others passage by first quarter of 1999</li> </ul>

Source: Compiled from Thailand Letter of Intent to the IMF No. 1-6

### **3.6.2 Assessment for Economic Outlook**

#### *a) Anticipated impacts of government measures*

Increased fiscal stimulation with a planned deficit of 5% of GDP in fiscal year 1999 should boost consumption and investment to some extent. However, it is not expected to have a significant impact in driving up local demand. This is due to 1) government expenditure accounts only 20% to GDP 2) more than half of the expenses will go for general governmental services and community & social services (20% and 42% respectively).

The supportive monetary policy will further lower interest rate, however, low interest rates may not boost credit growth substantially, in view of mounting non-performing loans and massive recapitalization need. NPLs currently are not estimated to reach their peak level, which is believed to be at 50%. Banks are over sensitive to the NPLs problems.

The Capital Support Facilities announced in mid August 1998 has yet to produce fruitful results. Most banks, especially those big ones are hesitate to apply for capital injection from the programme. Main concern is that the existing shareholder's funds will probably be wiped out or substantially reduced before new capital from private investors or from the government is injected into the financial institutions. This results from one of the conditions imposed by the government that any interest financial institutions have to adopt up-front the year-end 2000 loan classification and provisioning rules. This means the financial institutions have to set aside full provisioning and up-front write-off, which results in the existing shareholders absorbing all the loan losses.

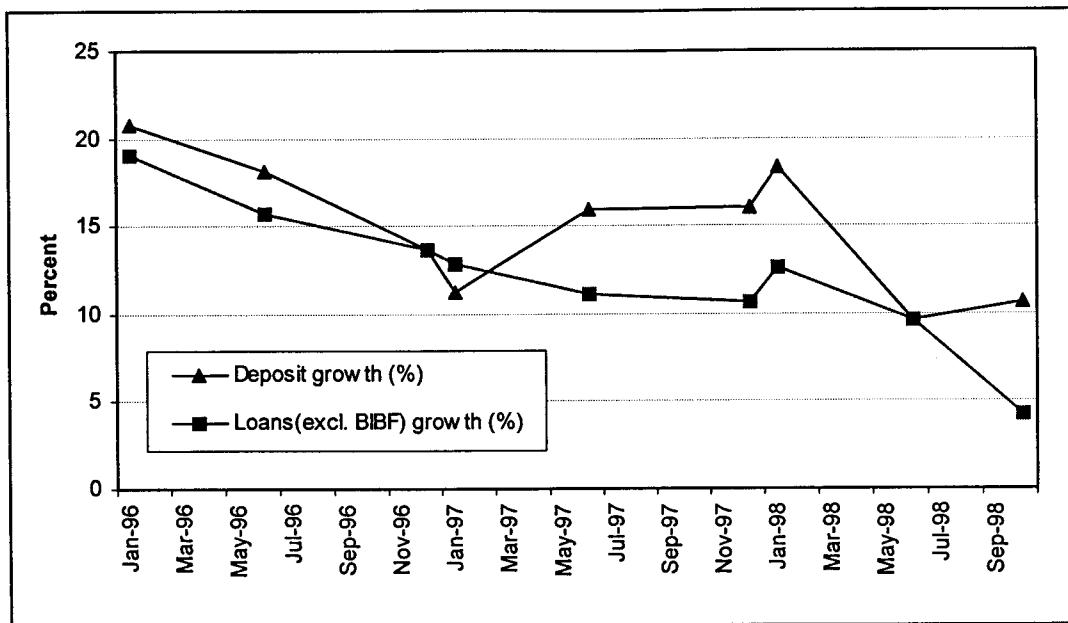
The establishment of private AMC's will be beneficial to the financial institutions in which the spinning off NPLs recovery unit will alleviate the bank stock's problem. Additionally, it is expected that private AMC's be in an advantage position to attract new capital from specific investors specialized in management of distress loans. However, some concerns should be pointed out. A transfer of sale of the NPLs to private AMC's should mark to market, which means at a discount to the loan face value. To offset the discounts, the financial institutions should write down their equities by the same amount. This will lead to discouragement to set up their private AMC's.

In sum, both CSFs and establishment private AMC's may not result in loan growth. Hence, if the credit crunch persists. It will hurt the production sector and the domestic demand. The latest data showed banking loans growth has been dropped overtime (Figure 3.1). It means that the financial institutions remain cautious to extend loans due to the rising NPLs and huge recapitalization required.

Corporate debt restructuring moves slowly. Among the 200 large cases monitored by the Bank of Thailand Corporate Debt Restructuring Advisory Committee (CDRAC), only 0.7% of total NPLs or 16.7 billion baht (\$463.9 million) were completely restructured as of September 30, 1998. Corporate debt of 437.7 billion baht (12.2 billion dollars) is yet to be restructured, with more than half in the manufacturing sector. The debt restructuring is another hope to stimulate production activities. However, the result is quite far from satisfaction (Table 3.16).

On the structural reform side, the process will take quite long time. So it will not have a significant impact for economic recovery in the near future. However, many expected that the sooner passage of legislation reform involving foreclosure and bankruptcy could bring the economic activities back to life. But, the outcome of the reform is still uncertain.

**Figure 3.1**  
**Banking Loans and Deposits Growth**



**Data for Figure 3.1 on Banking Loans and Deposits Growth**

	1996		1997		1998	
	Deposit growth (%)	Loans (excl. BIBF) growth (%)	Deposit growth (%)	Loans (excl. BIBF) growth (%)	Deposit growth (%)	Loans (excl. BIBF) growth (%)
January	20.8	19.0	11.2	12.8	18.4	12.6
February	21.3	19.0	11.0	12.7	17.5	10.9
March	23.3	19.4	12.3	12.3	14.2	11.1
April	22.8	16.9	12.8	12.8	12.8	10.3
May	20.2	16.0	11.8	12.8	13.0	8.5
June	18.1	15.7	15.9	11.1	9.6	9.6
July	16.8	14.8	18.2	11.5	9.8	8.4
August	15.0	15.0	16.9	11.3	11.4	7.3
September	14.9	15.8	16.5	10.9	12.7	6.1
October	12.4	14.5	18.9	11.0	10.7	4.2
November	14.1	14.1	16.7	10.0		
December	13.7	13.7	16.0	10.7		

Source: Bank of Thailand.

**Table 3.16: Progress in restructuring the 200 firms selected by the CDRAC (totaling debt worth 300 billion baht, BOT estimate)**

Billion baht					
	Total debt	In-process (debt being negotiated)		Completed restructuring	
		June	Sept	June	Sept
Manufacturing		131	228	2	6
Construction		6	14		1
Real Estate		29	61	0	1
Exports		6	8		
Other		45	133	1	8
Total	530	217	438	4	17

Source: Bank of Thailand

**Table 3.17: Overview of the World Economic Outlook Projection**  
(Annual percent change unless otherwise noted)

	Current projections		Differences from May'98 projections	
	1998	1999	1998	1999
World Output	2.0	2.5	-1.1	-1.2
Advanced economies	2.0	1.9	-0.4	-0.6
Major industrial countries	2.1	1.9	-0.2	-0.3
United States	3.5	2.0	0.6	-0.2
Japan	-2.5	0.5	-2.5	-0.8
Germany	2.6	2.5	0.1	-0.3
France	3.1	2.8	0.2	-0.2
Italy	2.1	2.5	-0.2	-0.2
United Kingdom	2.3	1.2	0.0	-0.9
Canada	3.0	2.5	-0.2	-0.3
Other advanced economies	1.4	2.3	-1.5	-1.3
<i>Memorandum</i>				
Industrial countries	2.3	2.0	-0.1	-0.4
European Union	2.9	2.5	0.1	-0.3
Euro Area	3.0	2.8	0.1	-0.2
Newly industrialized Asian economies	-2.9	0.7	-4.7	-3.8
Developing countries	2.3	3.6	-1.8	-1.7
Africa	3.7	4.7	-0.9	-0.2
Asia	1.8	3.9	-2.6	-2.0
Asean-4	-10.4	-0.1	-7.7	-2.6
Middle East and Europe	2.3	2.7	-1.0	-1.3
Western Hemisphere	2.8	2.7	-0.6	-1.6
Countries in Transition	-0.2	-0.2	-3.1	-3.6
Central and eastern Europe	3.4	3.6	-0.5	-0.6
Excluding Belarus and Ukraine	3.7	4.1	-0.7	-0.5
Russia	-6.0	-6.0	-7.0	-7.9
Transcaucasus	4.1	3.8	-0.4	-1.3
World trade volume(goods & services)	3.7	4.6	-2.7	-1.5

Source: World Economic Outlook, September 1998

### *b) International environment*

- International collaboration

From Asian crisis to Russia and Latin America, and from short-term shock to long-term recession, it is unlikely for solely small country as Thailand to be recover without international assistance. It could be said that the major developed countries, such as the US, Japan, the UK and German had well responded to this crisis but too slow. However, it is better late than never. For Thailand, the way to get back to its normal growth path needs both regional and international co-operation. Recently, several international conferences had been arranged in according to search for the solution preventing the world economy from the depression. Those included G-7, G-22, IMF, World Bank and APEC. Thus, it sounds to be good to Thailand and other troubled countries in Asia. The meetings had resulted in interest rate cut in major industrialized countries, more money contribution to the IMF, economic propping up in Japan and most important the set up of Asian fund via Miyazawa plan. The fund worth of \$ 30 billion has been set up through initiation of Mr. Miyazawa, Japan Finance Minister to assist the Asian countries. Thailand is currently preparing to request for the financial aid from this scheme to increase its foreign reserve and restructure the economy.

- World economy

Contagion effect had caused severe impact to the world economy beyond expectation. We were told that the current recession is the worst since the 1930s, but so far it had not generated austerity in other parts of the world in that scale. Share of the developed countries' GDP is around half of the entire world. So a sluggish in the economy of the US, and Europe, while Japan is still in a slump, and at the same time the rest of Asia is still in deep trouble will bring the world economy to the recession unavoidably.

As the Asia crisis persists as well as Russia and Latin America, major economic institutions have revised downward their growth projection for 1999. World GDP growth was on average 4% in 1996 and 1997, but JP Morgan revised the growth for 1998 and 1999 to around 1.5% and 1.7% respectively. IMF in its latest World Economic Outlook, September 1998 revised the numbers down to 2.0% and 2.5% in 1998 and 1999. However, most institutions still perceive next year to be a slightly better year than 1998 (Table 3.17). The implication for prospective Asian recovery is therefore possible. Nevertheless, how magnitude of the Asian recovery depends on the growth of demand for imports from those developed countries as well. Thailand also is not exempt.

To consider in more details of the major Thailand's trading partners is necessary.

- The US is the biggest economy in the world and having a crucial role for Thai economic recovery as it contributes to around 22% of Thai exports (Table 3.18). From the current projection, the US economic growth will slowly decline from 3.5% in 1998 to 2.0% in 1999.

- The continued slowdown in its economy, which has been going on for the past 8 years partly, contributed to the worsening of the current crisis. Japan exports around 40% of its merchandise exports and around 37% of its service to the Asian region. So it is an important player whose direction in its economy could contribute intensely to the region. Japan has been urged by fellow developed countries to play a more active role in the region. First by putting its own house in order by cleaning up its financial system. Second it should provide market for Asian exports in order to pulling Asian economy out of the current recession. To do so, Japan has launched a lot of measures to clean up its financial system, and boost up its local consumption. Furthermore, a fund has been set up to give financial aid to other Asian Countries.

With its long sluggish economy, it is unlikely for Japanese economy to pick up soon enough to pull other countries out of the recession.

- The new Euro will take place as a new common currency for the Euro-11 on January 1, 1999. The EU members, particularly, the Euro-11 will be rather restrictive on their monetary and fiscal policies towards 1999. The current crisis in Asia affects the EU only marginally. However, the contagion that spread to Russia and other emerging countries in Eastern Europe could adversely affect Europe. First through its financial institutions and then a reduction in demand for its exports. EU was ranked the third for Thailand exports, thus closely monitor is required.

- ASEAN is the second rank for Thailand exports. With the same problem, it is not expected other ASEAN countries to recover from their own deep recession in the near term. So, this will not considerably contribute to the Thai exports.

In all, the world economic situations will not greatly bring Thailand getting back to normal. Hopefully, it may not worsen the current situation.

### *c) Appraise various forecast of the Thai Economy*

Various forecasts show that Thailand would be slightly better in 1999 (Table 3.19). SCB Research Institute is the most optimistic forecaster, while other institutes look difference. However, the same issue mentioned is that exports will not be a major economic driven due to the world sluggish trade and less competitiveness of Thai products. Government spending will play an important role to boost domestic consumption. Furthermore, debt restructuring process and financial restructuring are also the main topics for recovery next year.

In sum, possibility for Thai economy to be back in track remains cloudy. A number of measures to revive the financial system remain fruitless. The increased government spending could have a minimal impact to stimulate economic activities. While bank lending that dries up constitute a much bigger part of liquidity and demand. A 5% budget deficit of GDP amounts to around Bt 250 billion per year, while banks had been lending at around 3t. 50-60 billion per month prior to crisis. Therefore, the credit crunch problem has to be tackled and get the financial system back in order. This will generate the necessary demand in consumption and investment.

A return in the foreign capital inflows and the stop in the outflows are certainly a big help and constitute a positive sign. However, a part from the Baht that has been improving due to the depreciation of US dollar and the inflows, despite the drop in local interest rates, there have been hardly any signs of consistent improvement in other key indicators. Growth of the Manufacture Production Index and the Private Investment Index remain negative through out of past 20 months, without significant sign of improvement. The current account may be in surplus, but export growth has been plunging in dollars term.

Other hindered factor to Thai economy is declining prices of agricultural products. This would worsen the local consumption in some extent.

Given the slow growth in world economy, especially major Thailand trading partners, the collapse of intra-Asian trade, the strengthening of Baht, and slow improvement in export competitiveness, Thai exports should not immediately recover next year. Accordingly, the country economy would depend on how fast the local demand would be boosted. In this case, local consumption and investment will play a dominant role, particularly in government side. Exports would not benefit from baht appreciation, and restructuring to increase competitiveness will take long period.

Table 3.18: Thailand Exports Market

Country	1997		1998*	
	Growth	% Share	Growth	% Share
The US	12.7	19.6	9.9	22.3
ASEAN	3.5	18.8	-23.3	17.7
EU	3.7	16.1	7.7	17.6
Japan	-7.9	14.9	-17.3	13.6
Others	3.4	30.6	-9.6	28.7
Total	3.3	100.0	-5.6	100

Note: \* (Jan-Sept)

Source: Bank of Thailand

Table 3.19: Comparison of Economic Forecasts for Thailand

	1998					
	IMF	TDRI	IDE	SCB	SG	Merrill
Real GDP growth (%)	-7 to -8	-5.5	-7.7	-7.4	-8.3	-9.6
Inflation (%)	8.0	9.4	8.2	8.1	8.0	8.3
	1999					
	IMF	TDRI	IDE	SCB	SG	Merrill
Real GDP growth (%)	1.0	1.0	-0.2	5.2	1.3	-2.4
Inflation (%)	2.5-3.0	4.0	3.6	0.0	2.5	4.4

Sources:

IMF: International Monetary Fund

TDRI: Thailand Development Research Institute

IDE: Institute of Developing Economies, Japan External Trade Organization

SCB: Siam Commercial Bank Research Institute

SG: SG Securities Research Limited, 1998

Merrill: Merrill Lynch, Pierce, Fenner &amp; Smith Inc.



As the external environment is not quite positive to Thailand exports and a lot of constraints are lying ahead, the prospective of Thai economy is hardly to predict. For any potential economic recovery to be viable and to sustain, the current credit crunch problems has to be solved quickly and get the financial system back in order.

#### IV. Concluding Remarks

One should bear in mind that recovery process could not be accomplished in the short term because the crisis problem has been accumulated for a long time. Excessive foreign debt exposure, excess capacity, over-spending and high current account deficit, highly leverage company, over valued baht in the fixed exchange rate regime, weak financial system and bubble economy were the main causes of the current crisis. Thus to restore from the current deep recession, a lot of measures are required. Effectiveness and efficiency of the policy implementation are important factor contributing to get out from the bottom. Actually, it is not easy task for the coalition government comprising a number of political parties with difference view. Eventually, IMF is not only a doctor for the current syndrome. Some fine-tuning between government and IMF over the policy measures may be necessary.

To conclude the study, a few lessons learned could be mentioned.

##### *a) What should be done before liberalization?*

1) Domestic financial systems should have been liberalized before opening up to foreign capital. But, Thailand failed to do this. Interest rate ceilings, limited competition, government-directed lending and insider relationships between banks and borrowers or patronage system have all served to inefficiently channel credit without regard for rates of return. Foreign money was employed in the same directions, leading to excessive and unproductive investment.

2) Strict bank regulation and supervision are necessary for financial liberalization to prevent a reversal in capital flows. This includes placing ceiling on bank's foreign-currency exposure.

3) Flexibility of exchange rate system is required. Free capital movement and pegged exchange rate are dangerous combination. A fix rate encouraged too much foreign-currency borrowings when foreign interest rates are lower than local ones. In addition, it did not encourage local borrower to hedge the foreign borrowings, leading to vulnerability to currency fluctuation.

4) Not only reliable information is required, but also its accession. If lenders had had better information about the reserves of Thai banks and they would have pulled back sooner or lesser lend. Then the eventual problems would have been less severe.

Result of the 4 mistakes resulted in high foreign debt, excess capacity, rising NPLs, and instability of financial system. Evidently, the government permanently shut down 56 finance companies out of its 91 units, and 18 finance companies and commercial banks had been nationalized.

##### *b) Dealing with financial institution problems*

1) Closure of weak financial institutions could not stop public from confidential panic. As a consequent, this measure caused the government to bear huge financial burden.

2) Strengthen capital base and stricter loan provision rules alone can not bring back confidence to the financial system. To the contrary, the measures severely cripple financial system. Due to the implementation of the measures, massive required capital and rising NPLs could have negative impact to credit extension. Tight credit policy further impeded corporate revival, resulting in mounting problem loans. Thus, it will further deepen recession.

3) Finally, the public has to bear the burden of the financial damage via the budgetary system. The philosophy that financial institutions can not be gone under is proved to generate huge loss.

*c) Other issues*

1) The experience points out to the need for a number of restructuring such as sound macroeconomic management, structural adjustment, social safety net to cope with the sudden external shock, and public administration reform.

2) To rely on foreign capital, FDI is better than portfolio investment and loans. Free capital movement, especially short-term is difficult to control, thus it causes instability. Foreign financial institutes can make mistake in project appraisal so we cannot be sure that they will provide loans to good and productive projects.

3) When the financial regulation, supervision, monitoring and rehabilitation functions are in the same organization, it requires a proper check and balance system to overview the whole working process.

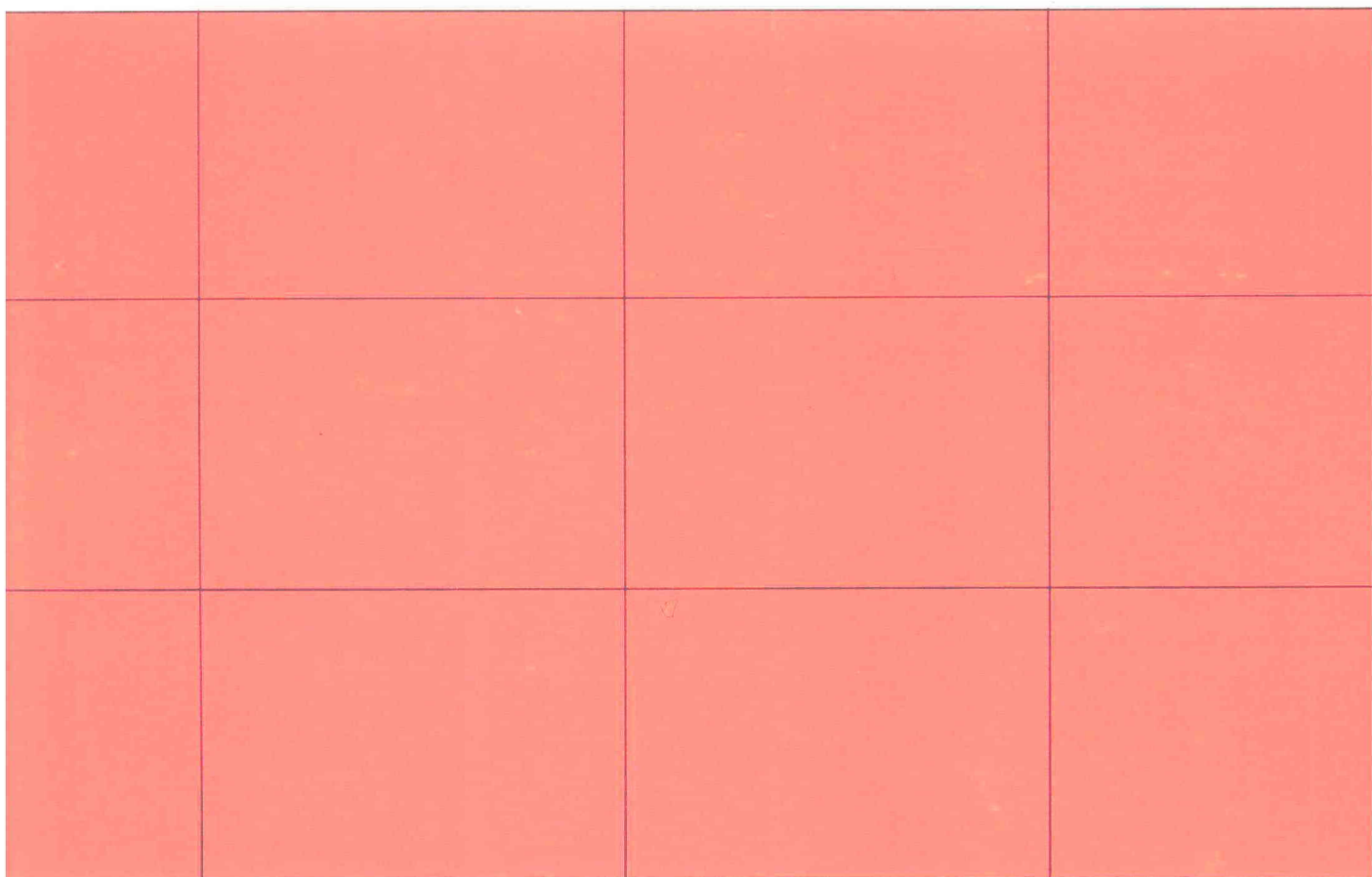
4) During the crisis, flexibility in management of the policy measures is important due to the dynamics of the problems. For instance, strict to tight monetary and fiscal policies in the initial stage of the crisis was appropriate since it raised investors' confidence. However, when the economy has been excessively contracted, the promptly adjustment to expansionary policy is necessary. Some may argue that due to IMF conditionally, the adjustment in the case of Thailand was too slow.

5) Good governance in both public and private sectors is important. The corruption in public sector in developing countries is well recognized that it increases transaction costs of business and causes mismanagement of policy measures. The crisis in Thailand shows that the irregularities in business practices is also quite common, and this leads to lack of foreign investors' confidence. For examples, management of some financial institutes provide loans without proper project appraisal but based on personal benefits. Accounting system provides inadequate, or sometime false, information on status of companies. There are financial institutes engaged in stock price manipulation. Therefore, transparency, accountability, and reliable information disclosures are crucial to establish good corporate governance in order to get out of the crisis.

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