

ASIAN DEVELOPMENT BANK

INTERIM

COUNTRY OPERATIONAL STRATEGY STUDY

THAILAND

May 1999

CURRENCY EQUIVALENTS

(1 May 1999)

Currency Unit	—	Baht (B)
B1.00	=	\$0.026878107
\$1.00	=	B37.205

Since 1984 the baht had been linked to a trade-weighted basket of major currencies, with the US dollar having the dominant weight. On 2 July 1997 it was delinked from the basket and allowed to float.

ABBREVIATIONS

AIDS	-	Acquired Immune Deficiency Syndrome
BMR	-	Bangkok Metropolitan Region
EXIMT	-	Export-Import Bank of Thailand
GDP	-	Gross Domestic Product
GMS	-	Greater Mekong Subregion
HIV	-	Human Immunodeficiency Virus
IMF	-	International Monetary Fund
IMT-GT	-	Indonesia-Malaysia-Thailand Growth Triangle
OECF	-	Overseas Economic Cooperation Fund
TA	-	Technical Assistance
UN	-	United Nations
UNDP	-	United Nations Development Programme

NOTES

- (i) The fiscal year (FY) of the Government ends on 30 September. FY before a calendar year denotes the year in which a fiscal year ends, e.g., FY1997 ends on 30 September 1997. Data presented in this Report refer to calendar years unless otherwise stated.
- (ii) In this Report, "\$" refers to US dollars.

CONTENTS

	Page
EXECUTIVE SUMMARY	ii
MAP	vi
I. BACKGROUND	1
A. Economic Performance	1
B. Socioenvironmental Performance	2
II. SUMMARY OF DEVELOPMENT ISSUES AND OUTLOOK	3
A. Development Policies and Challenges	3
B. Reform and Restructuring of the Financial Sector	4
C. Industrial Restructuring and Competitiveness	5
D. Agricultural Productivity and Rural Development	5
E. Human Resource Development	6
F. Infrastructure Investment	6
G. Governance: Sound Development Management	7
H. The Outlook: Risks and Uncertainties	8
III. DEVELOPMENT ASSISTANCE EXPERIENCE AND OUTLOOK	9
A. Previous Strategy	9
B. Lending Operations and Portfolio Performance	9
C. Technical Assistance	11
D. Bank Assistance for Improved Governance and Private Sector Development	11
E. External Assistance and Aid Coordination	12
F. The Impact of External Assistance: An Assessment	13
G. Cofinancing and Catalyzing External Resources	14
IV. THE BANK'S FUTURE ROLE IN THAILAND	15
A. Strategic Objectives	15
B. The Interim Strategy	16
C. Sector Strategies	17
D. Cross-Cutting Concerns of Bank Operations	20
E. Resources, Lending Modalities and Cofinancing	22
F. Technical Assistance and Economic and Sector Work	22
G. Conclusion	23
APPENDIXES	25

EXECUTIVE SUMMARY

This interim country operational strategy for Thailand has been prepared to provide a strategic framework for Bank operations against the background of a severe economic crisis that has affected several major economies in the Asian region, and continuing uncertainties resulting from the crisis. The interim strategy will be followed by a new strategy after normal economic conditions are restored. When the crisis first emerged in Thailand in early 1997, the immediate challenge was to deal with the external financing gap and stabilize the economy. In response to the request of the Government, funding agencies responded with a \$17.2 billion assistance package, linked to an International Monetary Fund Stand By Arrangement. On its part the Government introduced a comprehensive package of stabilization measures. These measures turned out to be very effective in closing the external financing gap. Imports fell sharply and the current account deficit was reduced from almost 8 percent in 1996 to only 2 percent in 1997. It is estimated that 1998 will close with a current account surplus equivalent to over 9 percent of gross domestic product. Gross foreign exchange reserves now exceed \$28 billion or about eight months of imports. However, this closure of the external financing gap has been achieved at a high cost in terms of unemployment and underutilization of capacity in the real sector. The aggregate demand compression measures, combined with the contagion effect of adverse trends in other crisis-affected countries in the region, have set off a severe recession. GDP is now estimated to have declined by 7-8 percent this year and total unemployment is estimated at 1.8 million persons, including the seasonally inactive labor force. The main challenge of economic policy now is to arrest recession.

To address this challenge, the Government has reversed its contractionary macroeconomic policy stance. The earlier fiscal surplus target of 1 percent of GDP for FY 1998 has been replaced by a deficit target of 5 percent in FY1999, excluding the fiscal cost of bank recapitalization. In addition, interest rates are being brought down. Steps are also being taken to revive the flow of liquidity, which has been severely drained in the past few months. However, success in reviving the Thai economy will depend on effective structural reforms in the financial sector, successful restructuring and recapitalization of banks, and the restoration of investor confidence. From a longer term perspective, the main development challenges facing Thailand include the restoration of competitiveness and high growth, consistent with protection of the environment, and the containment of disparities across income groups, regions, and gender. These long-term goals will require major investments and policy and institutional reforms in industry, agriculture, human resource development, and infrastructure.

Development Assistance Experience and Outlook

By 31 October 1998 the Bank had approved a total of 77 loan projects for \$4,249 million to the public sector in Thailand. Of these, 57 are complete and the loans closed. To date, \$3,217 million has been disbursed including disbursements on ongoing projects. In addition, the Bank has approved loans and equity of \$58.3 million for 8 private sector projects; all are complete. There are 16 ongoing projects at present with a total net loan amount of \$2,208 million; \$1,261 million have been disbursed, leaving a disbursable amount of \$947 million. During 1995 and 1996 the net resource transfer to Thailand was negative. However, in 1997 and 1998 there was a net resource transfer of about \$457 million and \$440 million, respectively.

The Bank's previous country operational strategy had two main objectives: to assist the country in developing the basis for long-term competitiveness and sustained economic growth; and to assist the country in achieving more equitable development, with emphasis on decentralization and dispersal of economic activities. To achieve these objectives, the Bank's

past programs for Thailand gave priority to improvement of infrastructure, especially in lagging regions. This was in line with the Government's own priorities. These are also the sectors that were prominent in assistance programs of other major funding agencies like the Overseas Economic Cooperation Fund and World Bank. The projects in themselves have on the whole been quite successful, and Thailand now has a fairly well-developed infrastructure base. However, the financial sector, social services, and agriculture were relatively neglected. Weakness of these sectors is an important contributory factor in the present crisis, and it is also a major constraint facing Thailand's recovery toward sustainable growth.

The Interim Strategy

This interim country operational strategy is based on the strategic objectives and thematic priorities spelt out in the Bank's Medium Term Strategic Framework (1995-1998). In applying this framework to the specific context of Thailand, four key considerations have been kept in view. First, the Bank is in the process of its own transformation from a project-financing institution to a broad-based development institution, which is increasingly concerned with the overall policy and investment environment. Second, as a leading development institution in the region, the Bank needs to play a major role in assisting Thailand cope with the current economic crisis. Third, the Bank's operational strategy in Thailand has to blend the Bank's medium-term strategic priorities with those identified in Thailand's Eighth Plan (1997-2001), which was itself revised to address the economic crisis. Fourth, the interim strategy should address the relative neglect of the social, agriculture, and financial sectors in past assistance programs, as these are key sectors for Thailand's recovery and future growth.

Based on these considerations the interim strategy is designed to address three country-specific objectives:

Structural adjustment. The country now has a large current account surplus and comfortable foreign exchange reserves. However, this was achieved at the cost of a severe recession. Tackling the recession and reviving the growth process are the most urgent tasks now. These, in turn, depend on structural adjustment, especially in the financial sector. It is the weakness of this sector that largely accounts for the current economic crisis. The sector has also been neglected in external assistance programs in the past, including those of the Bank. The Government is firmly committed to reform and restructuring of the financial sector as the centerpiece of its adjustment program. It has also sought the assistance of the Bank and other external assistance agencies in implementing its structural adjustment program.

Strengthening competitiveness to promote efficient, regionally balanced, and sustainable growth. Once the economy is stabilized and repositioned for growth, sustaining this growth over the long term will be the next challenge. Without greater efficiency, and enhanced competitiveness, the country will find it difficult to return to a high growth path. Moreover, the quality of growth matters. A special effort will be required to ensure that growth is better balanced across regions than in the past, and less damaging to the environment. Assisting the Government to move in this direction should be a major priority of the Bank's operational strategy, in line with its own strategic objectives.

Poverty reduction and improving the quality of life. Growth is the most powerful vehicle for eliminating poverty. However, international experience indicates that the growth-mediated strategy of human development can be considerably enhanced by programs that directly target poverty reduction, education, health, gender equity, and protection of the environment, among other quality of life goals. This perspective is incorporated in the Bank's

strategic objectives. It is particularly appropriate in Thailand at present because of the setback to human development that has resulted from the crisis. It is a major theme of the Government's present development strategy.

To optimize the impact of Bank operations on these objectives, subject to the constraint of limited resources, the interim strategy gives priority to interventions that have a maximum impact on these objectives; particularly those interventions that simultaneously promote more than one objective. The strategy includes the following five elements:

- (i) The financial, social, and rural/agriculture sectors will be given priority as the key sectors for promoting competitiveness and efficient, sustainable, long-term growth. The social and rural/agriculture sectors are also important for their direct impact on poverty reduction and improving the quality of life, in addition to their indirect impact on poverty reduction via growth.
- (ii) All modalities of Bank assistance such as loan and technical assistance projects, cofinancing, private sector operations, and economic and sector work will primarily focus on the financial and social sectors, and agriculture and rural development. The strategy aims to concentrate Bank operations in these three key areas to maximize the impact of Bank operations despite resource constraints.
- (iii) Spatially, all projects except those related to national systems will be concentrated in the north, northeast, and southern regions of the country, which are relatively less developed, and account for the bulk of Thailand's population, particularly target groups living below the poverty line. This will help to contain growing regional disparity and maximize the poverty-reducing impact of the program, in addition to other primary or secondary objectives of individual projects.
- (iv) The strategy will attempt to mainstream cross-cutting concerns such as poverty reduction, enhancing the role of women in development, improvements in governance, private sector development, and protection of the environment. Growth-oriented projects that address these concerns will be given priority as they will enhance quality of life, as well as other project-specific objectives. Cross-cutting concerns will also be addressed through loans with primary social/environmental objectives, technical assistance, and the Bank's Private Sector Group where appropriate.
- (v) Finally, emphasis will be given to both official and commercial cofinancing, to maximize the leverage of Bank assistance to Thailand, and hence the impact of Bank operations.

The Outlook: Risks and Uncertainties

Although the balance of payment crisis has been tackled, Thailand is yet to recover from the recession. In the immediate future this will depend on the urgent and determined implementation of financial sector reforms, especially the restructuring and recapitalization of banks. This is essential for the recovery of investor confidence and the consequent resumption of growth. In the longer term, sustaining the growth process will entail restoration of competitiveness of the Thai economy. This in turn will require reforms in industry and agriculture, investment in human resource development, and improvements in governance. Such reforms and investments will not only contribute to poverty reduction via growth, but they will also have a strong direct

impact on poverty reduction. These priorities are recognized by the Government. They are reflected in the development priorities of the revised Eighth Plan and in the reforms currently under way.

The strategy being pursued by the Government for recovery and future development is sound. The Bank considers this to be a feasible approach, consistent with its own approach to development and its assessment of priorities. The Government has also demonstrated its willingness to recognize problems and adjust policies where needed, as evidenced by the recent reversal of its contractionary macroeconomic policy stance. Nevertheless, there are risks involved. In the short run, there is the risk of moral hazard¹ in the bank restructuring process, and a risk of inadequate recapitalization, that could jeopardize the whole process of recovery. In the longer term, there is a risk that cross-cutting concerns such as regionally balanced development, strengthening the role of women in development, protection of the environment, and a more participatory approach to development may get neglected, despite stated intentions to the contrary, if these are not integrated into mainstream development programs.

The Bank's future lending will have to be directed at supporting policies and programs that meet the stated priorities, and are calibrated in relation to actual achievements. Close monitoring of the impact of development programs is therefore an integral component of the Bank's interim operational strategy. A performance assessment and monitoring system based on identified impact indicators and monitoring instruments has been specified to facilitate the monitoring process.

¹ Moral hazard is a situation in which one party in a transaction affects the costs or benefits to the other party after the transaction is completed. It frequently occurs in banking when borrowers take more financial risks than they would have with their own money.

I. BACKGROUND

A. Economic Performance

1. Thailand's impressive record of high growth and low inflation, sustained over a period of about three decades, masked the accumulation of some major structural imbalances that finally surfaced in early 1997. These imbalances are traceable to weak and poorly regulated financial markets, combined with a fixed exchange rate policy, and premature liberalization of the external capital account. An exchange rate policy that linked the baht to the dollar through a basket of currencies served Thailand well and helped to promote exports, until the dollar began strengthening against the yen and the currencies of Thailand's other major trading partners from 1995 onward. The appreciation of the baht and weak demand conditions abroad squeezed Thai exports out of several Asian and European markets, resulting in a sharp downturn in exports. The dollar value of exports declined by 1.9 percent in 1996. The export slump delivered a major shock to industry and other sectors of the Thai economy, leading to a slowdown in growth (Appendix 1).

2. Meanwhile, the protection against exchange risk provided by a fixed exchange rate, combined with differences in interest rates at home and abroad, offered large arbitrage opportunities, especially following the introduction of the Bangkok International Banking Facility. This facility allowed financial intermediaries to raise foreign currency loans abroad for onlending to domestic borrowers at higher interest rates. There was a huge increase in external capital flows, which rose from about \$10 billion-12 billion in 1993 and 1994 to \$21.9 billion in 1995. Much of this was short-term debt, which was imprudently directed to real estate and other asset investments, resulting in rapid asset inflation. The slump in real growth in 1996 reversed the process and resulted in rapid deterioration of asset quality for banks, and especially private nonbank finance companies. It also resulted in loss of investor confidence and outflows of foreign exchange. After a period of costly but ineffective attempts to shore up the finance companies and the baht, the central bank of Thailand finally allowed the baht to float on 2 July 1997. Thailand subsequently adopted an adjustment program under an International Monetary Fund Stand By Arrangement, supported by a \$17.2 billion assistance package from several multilateral and bilateral funding sources, including the Bank.

3. The adjustment program includes macroeconomic stabilization measures as well as structural adjustment measures, especially in the financial sector. The initial stabilization program entailed very strong fiscal compression on top of a tight monetary policy. While this helped to quickly turn around the external deficit, it also exacerbated recessionary trends. Real gross domestic product (GDP) fell by 0.4 percent in 1997 and is now expected to decline by 7-8 percent in 1998. In response, the fiscal stance has been altered and made more expansionary since the third review of the Stand By Arrangement, undertaken in May 1998. The fifth review was completed in December 1998. The combination of macroeconomic policies and structural adjustment measures being implemented under the Arrangement is broadly appropriate. The Government has taken bold measures to restructure the financial sector, culminating in a comprehensive package of measures for restructuring and recapitalizing commercial banks, which was announced on 14 August 1998. However, progress on the actual recapitalization of private and public sector financial institutions has been limited. This is the main challenge facing economic management in Thailand today. Without adequate recapitalization, it will not be possible to ease the liquidity squeeze or turn around the decline in economic activity. Thailand deserves urgent external assistance in this area, because there is a severe recession despite determined and swift action by the Government to implement stabilization and structural

adjustment measures recommended under the IMF Stand By Arrangement.

B. Socioenvironmental Performance

4. Rapid economic growth over a period of three decades reduced overall poverty levels from an estimated 30 percent in the early 1980s to about 12 percent by 1996. Unfortunately, this trend may have been reversed because of rising unemployment and shrinking incomes in the wake of the ongoing economic crisis. This retrogression apart, there are also significant inequalities in Thailand. Between 1988 and 1992, the share of total income accounted for by the top 20 percent of households rose from 54 to 59 percent. Over the same period, the bottom 20 percent of households experienced a decline in their share from 4.6 to 3.9 percent. The Gini coefficient rose from around 0.45 in the late 1980s to 0.52 in 1992, giving Thailand a relatively high level of inequality by Asian standards. Key underlying factors include the slow growth of agricultural incomes and widening gaps between skilled and unskilled workers. Regional income disparities have also increased, due largely to the concentration of industrial and commercial development in the Bangkok Metropolitan Region (BMR). In the northeast, where 35 percent of the population lives, average per capita income is only 35 percent of that in BMR. In the north and south, which account for 20 and 13 percent of Thailand's population, respectively, average incomes are 40-50 percent less than in BMR. Bangkok and its surrounding environs account for more than 50 percent of Thailand's GDP, generating per capita incomes above \$8,000. Here, less than 1 percent of the population is poor. Such wide regional and rural-urban income disparities lead to large urban migration, urban congestion, and pollution. Although only 30 percent of the population lives in urban centers at present, this is expected to increase to 50 percent by 2010, implying that some 12-14 million additional people will have to be accommodated in urban centers over the next 15 years. Appendix 2 includes a detailed analysis of the poverty situation in Thailand and the Bank's strategy for poverty reduction.

5. Thailand ranks high on the gender-related development index, one of the highest among developing countries; 40th of 163 countries worldwide.¹ This is testimony to the importance attached to the role of women in development. Maternal mortality rates have fallen from 270 to 200 per 100,000 live births from 1985-1996. Legislation provides for equal rights for men and women, including equal pay for work of equal value. Notwithstanding this broadly encouraging picture in Thailand, women do face serious obstacles to optimizing their economic participation and in their access to development benefits. Despite equitable education enrolment rates at most levels, women are still somewhat underrepresented in the adult workforce (47 percent female, 53 percent male). Women employees account for only 35 percent in Government service, and 20 percent of employers and 40 percent of employees in the private sector. In broad terms, women are concentrated in lower paid, unskilled work or unpaid family work. There is also large-scale exploitation of women in commercial sex. Women's share of the national income is estimated to be only 37 percent, which is well below their share of population.² The Bank's gender strategy in Thailand is discussed in Appendix 3.

6. Recent retrogression, inequality, and pockets of significant poverty notwithstanding, the last three decades of rapid economic growth have seen substantial improvements in the well-being of the Thai people. Infant mortality rates have been reduced from 103 per 1,000 births in 1960 to 31 per 1,000 in 1996, and life expectancy has risen from 52 to 70

¹ United Nations Development Programme. 1998. *Human Development Report 1998*. New York: Oxford University Press.

² The status of women in Thailand is discussed in greater detail in Asian Development Bank. 1998. *Country Briefing Paper: Women in Thailand*. Manila.

years during the same period. The incidence of malnutrition fell from 24 to 13 percent over the period 1987-1996. Adult literacy rates increased from 78 percent in 1970 to 94 percent in 1995. Access to safe water as a percentage of the population also increased from 64 percent from 1985-1987 to 89 percent from 1990-1996, and access to sanitation rose from 53 to 96 percent. Thailand ranks 59th among 174 countries on the Human Development Index of the United Nations Development Programme (UNDP) and is classified as a high human development country.¹

7. Thailand's environmental problems in rural areas include excessive deforestation, destruction of critical watersheds, flooding and soil erosion, sedimentation of irrigation reservoirs, cultivation of fragile lands, overuse of pesticides, overfishing, and loss of genetic and biological resources. During the past several decades there has been underinvestment in rehabilitation, regeneration, and conservation of valuable natural resources; and the environment has been significantly degraded to the point where it may impede further economic development. Shifting cultivation, urban expansion, and limited effectiveness of control over logging continue to result in deforestation and forest degradation. Governance issues of accountability and transparency remain important as the Government struggles to control illegal logging, protect forests, and limit area encroachment. Meanwhile, the rapid growth of industrial and agro-industrial production has transformed Thailand from a mainly agriculture-based economy into an economy dominated by the manufacturing and service industries. This has resulted in serious air, surface, and groundwater pollution in urban areas, especially in BMR, where about 16 percent of the population and 75 percent of Thai manufacturing output are located. The passage in 1992 of a revised and strengthened Enhancement and Conservation of National Environmental Quality Act, and the establishment of the Environment Fund, indicated the resolve of the Government to restore and protect Thailand's environment and natural resources. The Policy and Perspective Plan for Enhancement and Conservation of National Environmental Quality: 1997-2016 was adopted by the Government in late 1996 to meet this goal.

II. SUMMARY OF DEVELOPMENT ISSUES AND OUTLOOK

A. Development Policies and Challenges

8. Past national development strategies, policies, and programs were articulated through a system of five-year plans. During the 1960s, the emphasis was on industrialization through import substitution. Agriculture development was another key component. Subsequently, the emphasis shifted toward industrial exports, although high rates of protection were still maintained. During the 1970s, the Government invested heavily in infrastructure. Beginning with the Fifth Plan (1982-1986), the Government has emphasized improved regional distribution of the country's wealth. However, this goal has only met with limited success. An economic crisis in the mid-1980s forced a sea change in Thailand's development strategy, from an emphasis on agricultural expansion and import substitution to a manufacturing-export-led strategy. By the end of the 1980s, Thailand was on the path to becoming a newly industrialized country. The Seventh Plan (1992-1996) continued the focus on economic growth, targeting real GDP expansion at 8.2 percent annually. The plan also sought to reduce income inequalities and improve the environment. While the growth target was reached during the first four years of the plan, and

¹ United Nations Development Programme. 1998. *Human Development Report 1998*. New York: Oxford University Press. See also Appendix 1, page 2.

poverty continued to fall, little progress was made on regional disparities and the environment.

9. The Eighth National Economic and Social Development Plan (1997-2001), which was launched in October 1997, shifts the emphasis of development away from growth to quality of life, distribution issues, the environment, and governance concerns. The latter is to be addressed through decentralization of planning and a more participatory approach to development. However, soon after the plan was adopted, it had to be revised to address the new challenges emerging from the economic crisis. The immediate challenge was to address the balance of payments crisis, i.e., deal with the external financing gap and stabilize the economy. In response to the request of the Government, aid sources responded with a \$17.2 billion assistance package, linked to an IMF Stand By Arrangement. On its part the Government introduced a comprehensive package of stabilization measures. The baht was floated on 2 July and allowed to depreciate, thereby shifting the relative price of tradeables in favor of exports rather than imports. This expenditure-switching policy was backed up by very strong aggregate expenditure reduction measures. A tight monetary policy and high interest rates were combined with fiscal compression. These measures turned out to be very effective in closing the external financing gap. Imports fell sharply, and the current account deficit was reduced from almost 8 percent in 1996 to only 2 percent in 1997. On a monthly basis, a current account surplus has been reported since September 1997. It is estimated that 1998 will close with a current account surplus equivalent to over 9 percent of GDP. Gross foreign exchange resources are now estimated to exceed \$28 billion or about eight months of imports.

10. However, this closure of the external financing gap has been achieved at a high cost in terms of unemployment and underutilization of capacity in the real sector.¹ The aggregate demand compression measures, combined with the contagion effect of adverse trends in other crisis-affected countries in the region, have set off a severe recession. GDP is now expected to decline by 7-8 percent. Total unemployment, including the seasonally inactive labor force, rose to about 1.8 million persons, over 5.3 percent of the workforce by August 1998.

11. The main challenge of economic policy now is to arrest recession. The contractionary macroeconomic policy stance has been reversed. The earlier 1 percent of GDP fiscal surplus target was replaced by a deficit target of 3 percent of GDP for FY1998. The deficit target for FY1999 has been set at 5 percent, excluding the fiscal cost of bank recapitalization. Interest rates are also being brought down. Steps are being taken to revive the flow of liquidity, which was severely drained in the past few months. This is in turn linked to effective structural reforms in the financial sector, restructuring and recapitalization of banks, and restoration of investor confidence. From a long-term perspective, the main development challenges facing Thailand include the restoration of competitiveness and high growth, consistent with protection of the environment, and the containment of disparities across income groups, regions, and genders. These long-term goals will require major investments and policy and institutional reforms in industry, agriculture, human resource development, and infrastructure. A discussion of the key issues in each of these sectors follows.

B. Reform and Restructuring of the Financial Sector

12. The centerpiece of the Government's structural adjustment program is reform and restructuring of the financial sector. The process began with the suspension of 58 finance companies around the middle of 1997, of which 56 were subsequently closed in December. This

¹ The real sector refers to the production of goods and services excluding financial and monetary activities.

was followed by a tightening of prudential norms for capital adequacy, income recognition, and loan loss provisioning; reform of the capital market; improved supervision of the financial sector; and further intervention in several banks and nonbank financial companies that had heavily impaired assets. Finally, on 14 August 1998 the Government announced comprehensive measures for the restructuring of all commercial banks, that failed to meet the capital adequacy requirements, along with a two-tier public recapitalization scheme that will enable banks to reschedule debt and resume the flow of new credit (Appendix 4).

13. In undertaking this exercise the Government has been motivated by the need to avoid a systemic collapse of the entire banking sector, which would further exacerbate a deep economic recession. At the same time the Government has been attempting to minimize the fiscal cost and risk of moral hazard, by ensuring that the cost of restructuring is first borne by the shareholders and owners of subordinated debt.

C. Industrial Restructuring and Competitiveness

14. Thailand needs to restructure the industry sector so as to strengthen its competitiveness. Real wages in Thailand are now quite high relative to several of its neighbors and competitors.¹ Hence, it can no longer rely on cheap labor and abundant natural resources as the basis for its exports. A progressive shift to a higher value-added production structure is necessary, requiring more efficient resource utilization, increased skills, and higher levels of technology in both traditional and emerging industries.

15. Continued competitiveness of Thailand's exports—especially manufactured exports—is dependent on product diversification and improvements in product quality. Thailand's industrial restructuring will have to move along two dimensions. One dimension involves intraindustry restructuring, that is, shifts within existing industries to more efficient, often higher technology and more skill intensive, production processes, and higher value-added outputs. Process and product innovation in existing industries such as textiles and food processing are two examples. The other dimension involves interindustry restructuring, that is, the transition from low-productivity, labor intensive, light industries, to high productivity, technology- and skill-intensive industries such as information technology.

16. Such industrial restructuring and competitiveness will require human resource development to improve labor productivity, upgrading the technology of existing industries, and development of new technology-based industries. It will also require development of managerial skills to cope with more competitive environments, including effective cost control, logistics management, and new market development; financial sector development to improve access to capital, especially for small- and medium-size enterprises; development of infrastructure services to support increased competitiveness, including improvement of industrial infrastructure in the more remote regions; and policy, regulatory, and institutional reforms.

D. Agricultural Productivity and Rural Development

17. Improved agricultural practices are critical for restoring export competitiveness and export-led growth, as well as for poverty reduction and reducing regional disparities. Three systems characterize Thailand's agriculture sector: the first system, concentrated in the central

¹ CER: THA 97031: *Country Economic Review, Thailand*, November 1997.

plains, is commercially oriented rice production; the second, concentrated in the south, involves high-value plantation crops such as rubber and oil palm, and upland crops such as pineapples, cassava, and tropical tree fruits; and the third, concentrated in the north, northeast, and (to a lesser extent) the south, consists of upland subsistence farming. This latter system has low productivity and gives rise to low incomes, poverty, social alienation, outward migration, and environmental degradation. Typically, farmers with no legal title produce low-value crops such as rainfed rice, cassava, maize, soybean, and a variety of minor crops. Their farming practices are generally unsustainable. The portion of the population engaged in this type of production may be as much as 20 percent, and includes almost all of the 12 percent of the country's total population living below the poverty line. The scarcity of water resources is a particularly severe constraint for this system of agriculture, despite investments in several large irrigation projects in the north, northeast, and south.

18. In terms of policy, rural development in Thailand will require substantial investments in the management of water resources, especially small irrigation projects. It will also require institutional and policy reforms to create an enabling environment for growth and transformation of the agriculture sector, as well as stimulating alternative income sources. The Government recognizes the strategic importance of this sector, particularly in the context of the current crisis, for promoting export-led growth, as well as for containing the adverse social impact of the crisis. However, the Government is also aware of the numerous structural weaknesses in the sector including distortions in the product market, the input supply systems, and the land market; technological stagnation; the inadequate flow of credit, especially for small farmers; and inadequate investment. The Government therefore proposes to introduce wide-ranging reforms to revive the sector.

E. Human Resource Development

19. The quality of the labor force is among the most important determinants of Thailand's long-term growth prospects. It will take a sustained commitment to rectify current weaknesses. For example, 80 percent of Thailand's labor force has only primary education or less, as compared with 60 and 50 percent in the case of Malaysia and the Republic of Korea, respectively. Although the Government has made considerable efforts to expand education opportunities, primary education completion rates have actually fallen in recent years (to 69 percent in 1996). Some 5.5 million persons in the 6-19 year-old age group are not in school or some form of training. For rural persons, participation in education or skill development is strikingly low. For those who do participate, the standards are poor. Low quality and low enrollment appear to be strongly correlated. With regard to training, only 1 percent of the labor force participates in formal, institution-based programs. In-house and on-the-job training schemes have been increasing, but skill shortages have been one of the main factors impeding Thailand's transition to higher value-added industry.

20. The important question is why Thailand has lagged behind other countries in the region in human resource development. Assistance must be directed to rectifying the causes of resource misallocation in this area. The predominately supply-driven, government-dominated system must be transformed to a more market-responsive system. Decentralization is part of the answer. Further, the potential of the nonformal sector must be more effectively developed.

F. Infrastructure Investment

21. Infrastructure investment has played a key role in Thailand's rapid economic and

industrial growth. The recent slowdown in economic activity has eased the pressure on infrastructure. Nevertheless, improvements in both sector efficiency and capacity augmentation remain important. While the condition of the major highway network is good, the secondary road system linking villages is in need of extensive improvement and better maintenance. Telecommunications services are much more varied, with urban areas generally well served. Private sector investment has been a major factor in tripling the number of direct exchange lines over the past five years. However, some 43,000 of Thailand's 64,000 villages do not have ready access to telecommunications services. Water supply and sanitation services in provincial urban centers and villages also need to be expanded, as between 30-40 percent of this population is without such services. Pollution from wastewater is reaching extreme levels in parts of BMR and other urban centers. In contrast, the power supply situation is now comfortable. Thailand's energy requirements more than doubled from 1989-1995, but the slowdown in economic growth and recent successes in demand management have led to significant downward revisions of projected future demand. Further, electrification now extends to 98 percent of the population.

22. The economic crisis and fiscal restraint have intensified the need for more effective public policies to encourage private capital in infrastructure investment. The Government has substantially privatized or commercialized public investment in energy and telecommunications. Private sector infrastructure projects in urban mass transit, water supply, and wastewater management are also being promoted. Four mass-transit systems are being planned for BMR, of which one is already under construction. However, lack of transparency and weaknesses in the legal and administrative framework, among other factors, are serious impediments to private sector participation in infrastructure investment. These impediments need to be resolved, so as to mobilize commercial funds.

G. Governance: Sound Development Management

23. The financial crisis in Thailand is partly attributable to lack of transparency, corruption, and poor Government supervision of the financial sector. The Government is widely considered to have proven capabilities in economic management, the management of development, and project implementation. The brain drain from the public sector to the private sector in recent years notwithstanding, Thai civil servants at senior levels are well trained and competent. Structural reform and economic liberalization have also led to streamlining of Government procedures in recent years, and a reduced role for Government agencies in economic management. Despite this, there have been significant failures in governance. A consensus-building approach to decision making has led to slow implementation of some economic reform measures. Corruption and rent-seeking activities have also impeded efficiency, transparency, and predictability in Governmental transactions, particularly in the financial sector.

24. However, significant gains have been recorded during the past year. The new constitution, which came into effect following its approval by the King on 11 October, marks a major development in the recent history of governance in Thailand. The participatory process through which the constitution was drafted is itself unprecedented in the country. The 99-person Constitutional Drafting Assembly included former prime ministers, politicians, academics, lawyers, and a cross section of representatives from all sections of the population. It also held wide-ranging public discussions. This participatory approach is reflected in the new balance of power between the State and civil society, a high level of public accountability, and protection of civil rights in the new constitution. It features a constitutional court, an election commission, a parliament ombudsman, and a human rights commission. The new constitution also enshrines

rules governing disclosure of government records, protection of detainees against police brutality, the right to resist coups, etc. Under the new constitution the election commission will replace the Interior Ministry in organizing elections. Legislators will be elected from two streams, direct election in single-seat constituencies and proportional representation in larger constituencies. These elected legislators will be required to resign if they join the cabinet. Investigation against legislators and considerations of new legislation will be compulsory if such a demand is backed by 50,000 signatures. Investigation of corruption charges will be conducted by the National Counter Corruption Commission and a political court attached to the Supreme Court. These new institutional arrangements are expected to significantly improve the electoral process and raise standards of accountability and probity in public life.

25. Another important governance issue relates to regional imbalances, represented by substantial income disparities. To contain these disparities, the decentralization of decision making in public services needs to be pursued further, along with greater beneficiary participation in the development process. The Eighth Plan is designed to address these issues. In the preparation process of the plan, the Government held numerous town meetings and invited public participation. The plan states that development priority will be given to improving the quality of life of the people, rather than an emphasis on higher economic growth as in the past. The Government is undertaking a major review of relationships, both administrative and financial, between Bangkok and the provinces, with a view to introducing a substantial delegation of powers and greater public participation in development at provincial, municipal, and village levels. The committees that are engaged in this exercise comprise the principal political and civil service authorities in the country. Their deliberations may bring about fundamental changes in the currently centralized structure of Thai governance. However, this will also require a major effort in capacity building for local governments.

H. The Outlook: Risks and Uncertainties

26. The foregoing analysis has indicated that although the balance of payment crisis has been tackled, Thailand is yet to recover from the recession. In the immediate future this will depend on the urgent and determined implementation of financial sector reforms, especially the restructuring and recapitalization of banks. This is essential for the recovery of investor confidence and the consequent resumption of growth. In the longer term, sustaining the growth process will entail restoration of competitiveness of the Thai economy. This in turn will require reforms in industry and agriculture, investment in human resource development, and improvements in governance. Such reforms and investments will not only contribute to poverty reduction via growth, but they will also have a strong direct impact on poverty reduction.

27. These priorities are recognized by the Government. They are reflected in the short-term adjustment program under the IMF Stand By Arrangement, as well as reforms being undertaken with assistance from the Bank and the World Bank. They are also reflected in the development priorities of the revised Eighth Plan. Apart from facilitating the recovery toward growth, the emphasis on reforms in agriculture and the social sector are also appropriate for addressing cross-cutting concerns such as poverty reduction, balanced regional growth, strengthening the role of women in development, protection of the environment, and a more participatory approach to development. The Bank considers this a feasible approach, consistent with its own approach to development and its assessment of priorities.

28. The strategy being pursued by the Government for recovery and future development is sound. The Government has also demonstrated its willingness to recognize

problems and adjust policies where this is needed, as evidenced by the recent reversal of its contractionary macroeconomic policy stance. Nevertheless there are risks involved. In the short run, there is the risk of moral hazard¹ in the bank restructuring process and a risk of inadequate recapitalization, which could jeopardize the whole process of recovery. In the longer term, there is a risk that cross-cutting concerns such as regionally balanced development, strengthening the role of women in development, protection of the environment, and a more participatory approach to development may get neglected, despite stated intentions to the contrary, if these are not integrated into mainstream development programs. The Bank's future lending will have to be directed at supporting policies and programs that meet the stated priorities, and also calibrated in relation to actual achievements.

III. DEVELOPMENT ASSISTANCE EXPERIENCE AND OUTLOOK

A. Previous Strategy

29. The Bank's previous country operational strategy had two main objectives: to assist the country in developing the basis for long-term competitiveness and sustained economic growth, and to assist the country in achieving more equitable development with an emphasis on decentralization and dispersal of economic activities. To achieve these objectives, the Bank's past programs for Thailand gave priority to improving physical infrastructure, especially in lagging regions, in partnership with the private sector where possible. However, the achievements of this strategy have been mixed, as explained here in the assessment of development assistance experience.

B. Lending Operations and Portfolio Performance

30. Bank lending to Thailand has grown from about \$10 million per annum in the late 1960s to about \$150 million-200 million in the 1970s and 1980s, and further to \$300 million-400 million in the 1990s, finally rising to \$550 million in 1997 in response to the economic crisis. Altogether, the Bank has approved a total of 77 loan projects for the public sector in Thailand (as of 31 October 1998), amounting to \$4,249 million. Of these, 61 projects have been completed and the loans closed. A total of \$3,217 million has been disbursed to date, including disbursements on ongoing projects. In addition, the Bank has approved loans and equity for 8 private sector projects, amounting to \$58.3 million, all of which are complete. There are 16 ongoing projects at present with a total net loan amount of \$2,208 million, \$1,261 million have been disbursed, leaving a disbursable amount of \$947 million.

31. The current Bank portfolio in Thailand comprises 14 projects and two program loans. All of the projects are classified as AAA, implying generally satisfactory performance in terms of compliance with loan covenants, implementation schedule, and project cost (Appendix 5, page 2). The program loans are also given an A rating. In the early 1990s, the disbursement ratio for loans to Thailand was around 20 percent (Table 1). Subsequently, after declining quite sharply to 12 percent in 1996, the disbursement ratio rose to a record 38.3 percent in 1997, and has remained high at 35.6 percent up to October of 1998. The disbursement ratios have been

¹ Moral hazard is a situation in which one party in a transaction affects the costs or benefits to the other party after the transaction is completed. It frequently occurs in banking when borrowers take more financial risks than they would have with their own money.

much higher for Thailand than the Bankwide ratio in 1997 and 1998. This is partly attributable to two large fast-disbursing program loans and line of credit loans. It also reflects the maturity of the Thai portfolio, as disbursements pick up toward the later stages of a project. However, the disbursement ratio excluding program loans is 23.04, still much higher than the Bankwide average of 14.77 percent.

Table 1: Disbursement Performance (1993-1998)

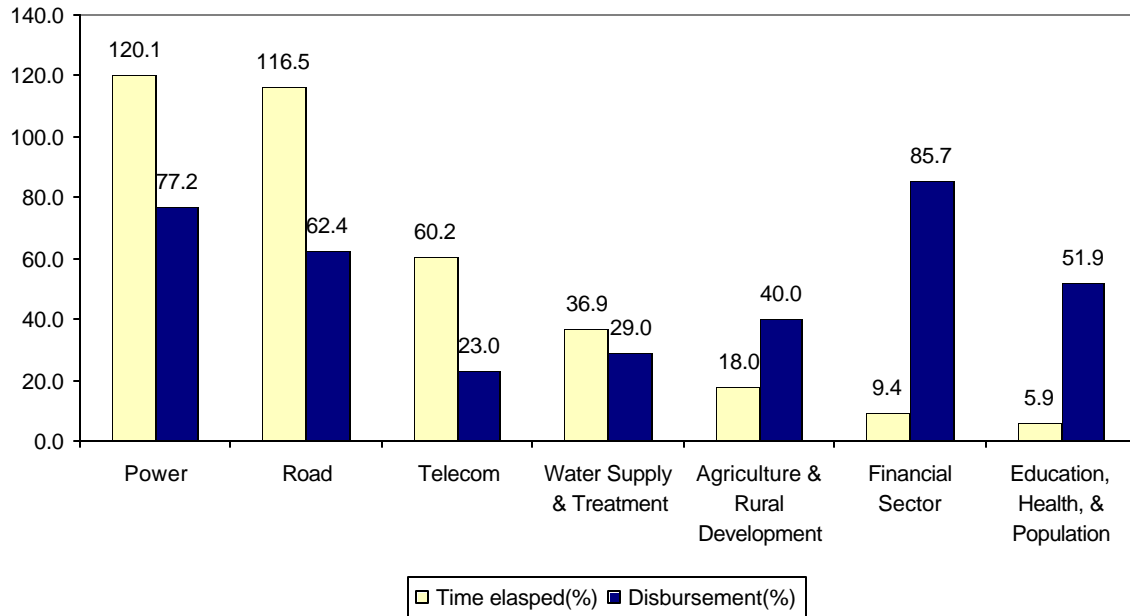
Item	1993	1994	1995	1996	1997	1998 (Jan-Oct)
Annual Disbursements (\$ million)	138.5	186.7	162.4	123.3	592.9	523.7
Disbursement Ratio (%) ^a	19.8	19.6	20.3	12.0	38.3	35.6
Bankwide Disbursement Ratio (%) ^a	15.7	18.8	18.4	17.8	25.2	21.2
Disbursement Ratio without Program Loans (%)	19.8	19.6	20.3	12.0	23.5	23.0
Bank-wide Disbursement Ratio without Program Loans (%)	15.3	17.3	17.8	17.4	18.6	14.8

^a Ratio of disbursement during the year over the undisbursed net loan balance less cancellations at the beginning of the period/year

32. A comparison of sectoral disbursement ratios with the age of the sectoral portfolio reveal large variations in disbursement performance across sectors. In agriculture and rural development, 40 percent of the net loan amount has been disbursed although the average elapsed project time is only 18 percent (Figure 1).¹ In the financial sector, over 85 percent of the net loan amount has been disbursed, although only 9.4 percent of project time has elapsed. In the education, health, and population sector, again, nearly 52 percent of the net loan amount has been disbursed although less than 6 percent of project time has elapsed. The high level of disbursement performance reflects the predominance of fast-disbursing line of credit or program loans in these sectors. At the other end of the spectrum, in sectors like power and roads the average elapsed time is well over 100 percent of the original closing date, yet the disbursement ratios are only 77 and 62 percent respectively. In telecommunications, the average elapsed time is 60 percent while the disbursement ratio is only 23 percent. This imbalance points to implementation constraints that need to be urgently addressed.

¹ The average elapsed project time in a sector is the average of individual projects weighted by loan size.

Figure 1: Elapsed Project Time and Disbursement Ratios by Sectors



C. Technical Assistance

33. The Bank has provided a total of \$40.2 million in technical assistance (TA) to Thailand for 80 advisory TAs and 47 project preparatory TAs since 1969 (Appendix 5 page 3). TA for policy support has mainly emphasized reforms, improved governance, and private sector development. Capacity-building support has involved four areas: poverty reduction and income redistribution, human development, environmental regulation, and subregional cooperation. The Bank's TA in Thailand is consistent with the previous country operational strategy. It has contributed to the accomplishment of both strategic and specific objectives. It may be noted, however, that Bank involvement in natural resource management has been narrow. To date, Bank involvement in environmental management in Thailand has included 17 TAs, 12 of which were advisory and 5 were for project preparation. Environmental projects have been largely concerned with "brown" pollution.¹ The Government requires that borrowing under ordinary capital resources terms be restricted to those projects with high financial returns. This has been reflected in the emphasis on brown projects even in the TA program, as the latter is linked to lending projects. However, Thailand has recently borrowed from the World Bank for some "green" projects², indicating growing flexibility.

D. Bank Assistance for Improved Governance and Private Sector Development

34. The Bank's assistance for improved governance and private sector development through institutional and policy reforms has been an important part of its program in Thailand.

¹ Brown refers to waste management, both liquid and solid, primarily from domestic, municipal, and industrial sources.

² Green refers to the preservation of the natural environment and especially living natural resources.

The Bank's policy support program has focused on (i) policy reforms in the financial and social sectors for improved governance, (ii) decentralization, and (iii) privatization and greater private sector involvement in the process of physical and social infrastructure development. Apart from the reforms built into the policy matrices of program loans in the financial and social sectors, and associated TAs, the Bank has also provided several advisory TAs to support the Government's efforts in these areas. Furthermore, policy issues, such as rationalization of prices, establishment of cost-recovery principles, and private sector participation, have been addressed in various loan projects. In the field of decentralization, the Bank provided TAs to develop a policy framework for a national decentralization strategy.

35. The Bank's operational strategy for Thailand includes greater private sector participation in the provision of services previously supplied by the public sector. Operationally, the emphasis has been on private sector involvement in physical infrastructure investments, environment and natural resources management, and human resource development. Further, the Bank supports strengthening the financial and capital markets. The Bank has provided (as of October 1998) \$85.3 million in direct support to eight private sector projects in Thailand; \$26.8 million of this was provided in equity and \$31.5 million was in the form of loans without a Government guarantee. The Bank also maintains an effective partnership with the private sector in several investments. Earlier this year a \$1 billion commercial cofinancing was arranged in partnership with a syndicate of 68 international commercial banks for an export financing facility at the Export-Import Bank of Thailand (EXIMT). The Bank's Private Sector Group is also exploring possibilities for expanded private sector operations, starting with possible support for private investment in the banking sector, wastewater treatment, and solid waste management. Meanwhile, the Bank has provided substantial TA for privatization, starting with a TA for preparation of a database on Government decision making on privatization. It was followed by several TAs to prepare corporatization and privatization strategies for selected government enterprises, including Provincial Waterworks Authority, Electricity Generating Authority of Thailand, Metropolitan Electricity Authority, and Petroleum Authority of Thailand.

E. External Assistance and Aid Coordination

36. Up to 1997, the major sources of loans to Thailand from official sources were the Overseas Economic Cooperation Fund (OECF), World Bank, and ADB. Since then, the economic crisis has necessitated a very large additional infusion of external assistance from multiple sources under the IMF-led structural adjustment assistance program, which was endorsed by the Government on 21 August 1997. The assistance program provides for \$17.2 billion to finance the balance-of-payments gap and rebuild international reserves, and envisages major economic and financial reforms to stabilize the economy and reestablish conditions for growth. Japan is taking a leading role, contributing \$4 billion from the Exim Bank, followed by IMF at \$3.9 billion (SDR 2.9 billion) in standby credit. Australia; People's Republic of China; Hong Kong, China; Malaysia, and Singapore will provide \$1 billion each, while Brunei, Canada, and the Republic of Korea will provide \$500 million each.¹ The monetary authorities of the G-10 countries² agreed to provide up to \$3.3 billion in bridging finance through the Bank for International Settlements. The credit lines for the these loans will come due in three to five years, and will generally be in line with market rates. The Bank agreed to provide \$1.2 billion during

¹ Canada has agreed to provide the \$500 million pledged in August 1997 by Indonesia, which Indonesia will be unable to provide.

² The G-10 countries include Belgium, Canada, France, Germany, Italy, Japan, Netherlands, Sweden, United Kingdom, United States.

1997-1999, which has been subsequently raised to about \$1.5 billion. In addition, the Bank has provided a partial credit guarantee for a syndicated commercial loan of \$950 million for an export financing facility at the Export-Import Bank of Thailand. The World Bank pledged to contribute \$1.5 billion, which has now been increased to \$2.9 billion.

37. IMF, World Bank, and ADB are working closely together to address the crisis in Thailand. Within the comprehensive financial sector restructuring program, IMF and World Bank have paid special attention to issues related to strengthening the central bank, restructuring the private nonbank finance companies, and strengthening the supervisory and regulatory framework for commercial banks; while the Bank has focused on capital markets reforms. IMF (and the World Bank) have both also supported the policy conditionalities of the Bank's financial markets reform loan¹ and social sector program loan² through cross conditionalities in their own policy-based loans. The World Bank approved a \$350 million finance companies restructuring loan in December 1997 to support Thailand's comprehensive program to restructure the finance companies and increase the overall soundness, efficiency, and competitiveness of the financial sector. In addition, the World Bank has provided TA totaling \$30 million for (i) financial sector reform, especially restructuring of finance companies suspended during Thailand's economic crisis; and (ii) upgrading macroeconomic management and public administration, public enterprise reform, and strengthening the competitiveness of Thailand's industry sector. Recently, the World Bank also developed a large social investment project, which is being closely coordinated with the Bank's Social Sector Program loan. It is now processing a series of economic and financial adjustment loans, each valued at \$400 million.

38. United Nations (UN) agencies are key development partners with Thailand and the Bank. UNDP has focused on improving public administration and governance, and its efforts on grassroots development span a wide range of people-centered development activities. Bilateral funding sources also play an important role in the development dialogue in Thailand, particularly regional partners including Australia, Canada, the European Union, Germany and Japan. The Bank maintains a dialogue with a number of UN agencies and major bilateral funding bodies. Total grant assistance from 1992-1997 was \$602 million, of which \$223 million was provided by the Government of Japan, \$77 million by various UN agencies, \$65 million by nongovernment organizations, \$45 million by the Government of Australia, \$39 million by the Government of Germany, and \$22 million by the Government of Denmark. Further details on concessional loans and TA is given in Appendix 6.

F. The Impact of External Assistance: An Assessment

39. The overall development impact of Bank assistance to Thailand cannot be easily segregated from the impact of investments made by other funding sources and, more importantly, domestic public and private investment. Development outcomes reflect the aggregate impact of all these investments, along with Bank assistance. In the past, the Bank's portfolio in Thailand was dominated by physical infrastructure projects such as energy, roads, and communications, which were also the main areas of assistance from the World Bank and OECF, the other two major funding sources in Thailand (excluding the temporary support from IMF). This is presumably because these were the priority sectors in the Government's own investment program. These are also the sectors where Thailand's progress during the past

¹ Loan No. 1600-THA: *Financial Markets Reform Program*, for \$300 million, approved on 19 December 1997.

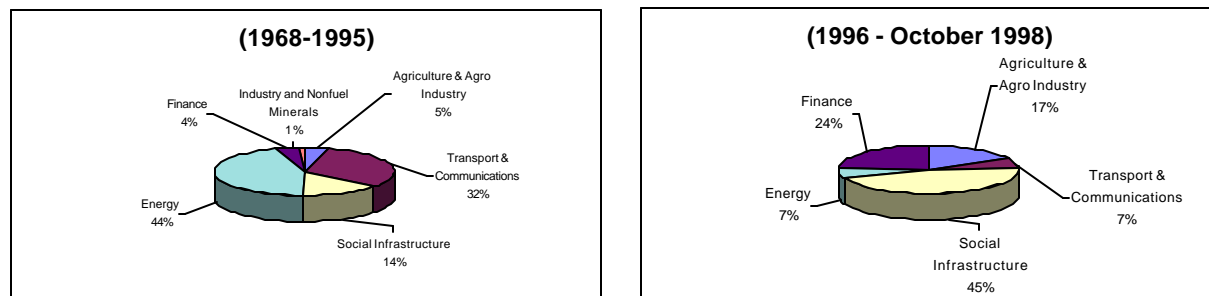
² Loan No. 1611-THA: *Social Sector Program*, for \$500 million, approved on 12 March 1998.

three decades has been excellent, supporting a very high rate of growth until the recent crisis. In that sense, the Bank's past assistance to Thailand, along with that of other funding sources, must be deemed successful. This conclusion is supported by internal postevaluation reports that indicate that 90 percent of postevaluated projects in Thailand have been generally successful, as compared with a Bankwide average of 57.2 percent (Appendix 5).

40. However, the successful investment in physical infrastructure by the Bank, as well as the Government and other funding bodies, was achieved at the cost of relative neglect of the financial and social sectors. The Bank also withdrew from the agriculture sector from around the mid-1980s, in tune with Government policy. The World Bank and, especially, OECF continued to support agriculture, but with limited results. These lapses have now cost the country dearly. A weak and neglected financial sector is the root cause of the current crisis. Stagnant productivity in agriculture has led to the loss of Thailand's competitive edge in this sector. On the other hand, low skill levels of the workforce, deriving from low education attainment, have made it difficult for Thailand to establish a new comparative advantage in skill intensive, high technology industries that would be better suited to its relatively high wage economy.

41. Quite appropriately, all the major funding sources are now restructuring their loan portfolios in favor of the neglected sectors. In the case of the Bank, the energy sector, which accounted for 44 percent of Bank lending up to 1995, is now down to a share of only 7 percent (Figure 2). The share of transport and communications has declined from 32 to 7 percent. The share of the social infrastructure sector has meanwhile risen from 14 to 45 percent, and that of the financial sector from 4 to 24 percent. The share of agriculture has risen from only 5 to 17 percent. This restructuring of the Bank's portfolio is in line with the new interim strategy (para. 47 and 48), and will be further reinforced by it.

**Figure 2: Thailand Lending Program (Loans)
Sectoral Distribution by Amount**



G. Cofinancing and Catalyzing External Resources

42. Since 1987 the Bank has provided \$1.4 billion to support 16 cofinanced projects in Thailand, with cofinancing totaling \$2.9 billion. Following the onset of the economic crisis, as the Bank's actual operational strategy in Thailand shifted from project lending to fast-disbursing program loans, the cofinancing strategy was also adjusted to match this new thrust in Bank operations. The Bank's cofinancing operations in Thailand gained momentum during 1998 after the Board approved support for the \$1 billion Export Financing Facility for Thailand. In this project

the Bank mobilized \$950 million commercial cofinancing in conjunction with the Bank's direct lending of \$50 million, yielding a leverage ratio of 19:1. This was the first term financing for Thailand since the onset of the economic crisis. The Export Financing Facility is funding pre- and postshipment financing of exports, the import of raw material needs of exporters, and export-related plant and machinery requirements. It consists of a \$50 million anchor loan by the Bank to EXIMT, and \$950 million equivalent in cofinancing from 68 international banks (from Asia, Australia, Europe, Middle East, and North and South America) to EXIMT in the form of a syndicated five-year term loan. The Bank is providing a partial credit guarantee to the commercial cofinanciers of the syndicated loan, with a counter guarantee from the Government to the Bank. A portion of the Bank's loan and the commercial cofinancing is being relented by EXIMT to subborrowers, and the balance is being relented by EXIMT to various participating credit institutions for onlending to subborrowers. The drawdown from this facility has been adversely affected by the rising share of nonperforming loans, and tightened provisioning requirements in these participating credit institutions. Future cofinancing operations in the sector need to be protected from the rapid deterioration that has severely damaged the whole financial sector.

IV. THE BANK'S FUTURE ROLE IN THAILAND

A Strategic Objectives

43. This interim country operational strategy is based on the strategic objectives and thematic priorities that serve as the basic strategic framework for all Bank operations.¹ The five strategic objectives are (i) promoting economic growth, (ii) reducing poverty, (iii) supporting human development (including population plans), (iv) improving the status of women, and (v) protecting the environment.

44. The thematic priorities that support these objectives include encouragement of private sector development, strengthening public sector management capacity, human resource development, and natural resource management.

45. In applying this strategic framework to the specific context of Thailand, four key considerations have been kept in view. First, the Bank is in the process of its own transformation from a project-financing institution to a broad-based development institution. It is recognized that sound project investments cannot be dissociated from the overall policy and investment environment. Second, as a leading development institution in the region, the Bank needs to play a major role in assisting Thailand to cope with the current economic crisis. Third, the Bank's operational strategy in Thailand has to blend the Bank's medium-term strategic priority with those identified in Thailand's Eighth Plan (1997-2001), which was itself revised to address the economic crisis. Fourth, the interim strategy should reflect the assessment of past external assistance, in particular the relative neglect of the agriculture, social, and financial sectors.

46. Based on these considerations, the interim strategy has been designed to address three country-specific objectives.

1. Structural Adjustment

¹ For a discussion of this strategic framework see Asian Development Bank. 1995. *The Bank's Medium-Term Strategic Framework (1995-1998)*. Manila.

47. The balance of payments situation has been stabilized. There is now a large current account surplus and comfortable foreign exchange reserves. However, this was achieved at the cost of a severe recession. Tackling the recession and restoring investor confidence are the most urgent tasks now for stabilizing the economy and reviving the growth process. These, in turn, depend on structural adjustment, especially in the financial sector, which has remained a weak link in Thailand's past development experience. It is the weakness of this sector that largely accounts for the current economic crisis. The sector has also been neglected in past external assistance programs, including those of the Bank. The Government is firmly committed to reforming and restructuring the financial sector as the centerpiece of its adjustment program. It has also sought the assistance of the Bank and other funding sources in implementing its structural adjustment program.

2. Strengthening Competitiveness to Promote Efficient, Regionally Balanced, and Sustainable Growth

48. Once the economy is stabilized and repositioned for growth, the next challenge will be sustaining this growth over the long term. Compared with some of its neighbors and competitors, Thailand is losing its comparative cost advantage. Without greater efficiency and enhanced competitiveness, the country will find it difficult to return to a high growth path. Moreover, the quality of growth matters. A special effort will also be required to ensure that growth is better balanced across regions than in the past and less damaging to the environment. Assisting the Government to move in this direction should be a major priority of the Bank's operational strategy, in line with its own strategic objective.

3. Poverty Reduction and Improving the Quality of Life

49. Growth is the most powerful vehicle for eliminating poverty and improving the quality of life, e.g., levels of material consumption, education and health, and social conditions. However, the fruits of growth are not distributed evenly across society, and the trickle-down process works slowly. International experience indicates that the growth-mediated strategy of human development can be considerably enhanced by programs that directly target poverty reduction, education status, health status, gender equity, and protection of the environment, among other quality of life goals. This perspective is incorporated in the Bank's strategic objectives. It is particularly appropriate in Thailand at present because of the setback to human development that resulted from the crisis. Hence it is a major theme of the Government's present development strategy, as reflected in the revised Eighth Plan.

B. The Interim Strategy

50. To optimize the impact of Bank operations on these objectives, subject to the constraint of limited resources, the interim strategy gives priority to interventions that will have maximum impact, particularly those interventions that simultaneously promote more than one objective. For the same purpose, the interim strategy also emphasizes keeping country operations sharply focused both spatially and sectorally. The interim strategy includes the following five elements:

- (i) The financial, rural/agriculture, and social sectors will be given priority as the key sectors for promoting competitiveness and efficient, sustainable, long-term growth. The social and rural/agriculture sectors are also important for their direct

impact on poverty reduction and improving the quality of life, in addition to their indirect impact on poverty reduction via growth.

- (ii) All modalities of Bank assistance such as loan and TA projects, cofinancing, private sector operations, and economic and sector work will primarily focus on the financial and social sectors, and agriculture and rural development. The strategy aims to concentrate Bank operations in these three key areas to maximize the impact of Bank operations despite resource constraints.
- (iii) Spatially, all projects except those related to national systems will be concentrated in the north, northeast, and southern regions of the country, which are relatively less developed, and account for the bulk of Thailand's population, particularly target groups living below the poverty line. This will help to contain growing regional disparity, and maximize the poverty-reducing impact of the program, in addition to other primary or secondary objectives of individual projects.
- (iv) The strategy will attempt to mainstream cross-cutting concerns such as poverty reduction, enhancing the role of women in development, improvements in governance, private sector development, and protection of the environment. Growth-oriented projects that address these concerns will be given priority as they will enhance quality of life, as well as other project-specific objectives. Cross-cutting concerns will also be addressed through loans with primary social/environmental objectives, TA and investments by the Bank's Private Sector Group where appropriate.
- (v) Finally, emphasis will be given to cofinancing through both official and commercial sources, to maximize the leverage of Bank assistance to Thailand, and hence the impact of Bank assistance.

C. Sector Strategies

51. The interim country operational strategy has identified three key sectors as the focus of Bank operations over the next three to four years, i.e., the financial, social, and agriculture/rural sectors.

1. Financial Sector

52. The ongoing financial crisis was set off by the erosion of investor confidence in Thailand's financial institutions, particularly the commercial banks and private nonbank financial institutions. Imprudent lending by poorly regulated institutions, that ignored prudential norms lies at the root of the problem. Reforming the financial sector is therefore the single most important strategic measure necessary for restoring investor confidence and reviving the process of growth. The interim strategy accordingly identifies the financial sector as a major priority for Bank operations in Thailand over the medium term.

53. ADB has been working very closely with IMF and the World Bank on financial sector reforms in Thailand. IMF has undertaken responsibility for reforming and strengthening the central bank, while the World Bank has led the effort to reform and rationalize the nonbank

financial institutions subsector. IMF and the World Bank are also assisting the Government in reforming the regulatory framework for banks and other private financial companies. The Bank has focused on assisting the Government in reforming and developing the capital market as an alternative channel of resource mobilization. This assistance should be sustained.

54. Restructuring and recapitalizing the financial institutions is now the most urgent requirement in the sector. The Government has requested the Bank to provide assistance for recapitalizing some of the State-owned commercial banks and specialized financial institutions. However, recapitalization can only be the final outcome of a three-stage process starting with a review of the identified institutions, i.e., international standard financial and management audit; preparation of restructuring plans; and finally recapitalization. This will be necessary to ensure that intervention does not create any moral hazard. The Bank will support the Government through technical assistance for the first two stages. The question of support for recapitalization can be reviewed at a later stage, following the outcome of the technical assistance.

2. Agriculture and Rural Development

55. The rural/agriculture sector is a key sector for restoring the growth process in Thailand, as it is a major source of exports. The sector is also critical for poverty reduction and improving quality of life, as a large proportion of the population, and the bulk of the poor, live in rural areas. Poverty is closely associated with landlessness. The Government recognizes the strategic importance of the sector, particularly in the context of the current economic crisis, but it is also aware of the many structural weaknesses in the sector. Hence the Government plans to initiate a wide-ranging program of reform. The Bank will resume operations in this sector after a gap of several years, starting with assistance to the Government for comprehensive institutional and policy reform, combined with key investments in public goods like agricultural research and dissemination of methodologies to improve agricultural practices.

56. Development of the sector faces several constraints, including pressure on the competitiveness of exports. Low productivity, high production costs, difficulties for the poor in accessing credit, and an overly interventionist role of the Government are some of the main issues that need to be addressed over the medium term. Research and development in the sector has been ad hoc and farmers have not extensively adopted the results. Agriculture research needs to be strengthened and extension services made more effective. Land and water management also require attention. Watershed management and comprehensive water resource development needs to be undertaken. Simultaneously, tenancy reforms and land-titling processes need to be accelerated. This will allow the consolidation of agricultural lands, development of land banks, and easier access to rural credit. Government policy also needs to support shifts in cropping patterns in response to market signals. Crop diversification is expected to lead to a better balanced agriculture sector. Market reforms are also necessary in the context of agricultural prices and subsidies, the import-export regime, and resource mobilization from within the sector. Thus, there is scope for intervention over a broad front. However, to ensure that the Bank's intervention has a tangible impact, Bank assistance will have to be carefully prioritized (Appendix 7).

3. Social Sector

a. Education and Training

57. Thailand's earlier success in making primary education universal has not been replicated in the quality of secondary and higher levels of education. The transition rate from primary to secondary level has improved from less than 50 percent in the 1980s to about 90 percent in 1996. However, the enrollment rate has remained very low at 34 percent of the population aged 15-17 years. Also, there has been little improvement of quality in secondary education, especially in science and mathematics. Mainly due to the historical predominance of course offerings in the humanities and arts, and the tendency for teachers to marginalize difficult subjects, recent monitoring tests in mathematics and science have shown broad stagnation and decline. Vocational and skills training programs have also largely been implemented without the active participation of the private sector in the planning, design and execution of training programs. As a consequence, there is growing concern regarding the mismatch between education and training systems and the evolving demands of the labor market, brought about by structural changes in the Thai economy, in particular the need to move away from labor-intensive production in which Thailand is no longer competitive. In line with the Bank's strategic objective of assisting Thailand to develop a strong foundation for long-term competitiveness, and equitable economic growth, Bank lending and TA operations will support the development of human resources to overcome skill shortages and upgrade the technology base.

b. Health

58. As a consequence of the Thai Government's political and economic commitment to improve Thailand's health status, health care services now reach virtually all communities through an extensive primary health care system. Health indicators are very favorable compared with other developing nations; and some indicators are at or are quickly approaching the levels observed in developed nations. Life expectancy at birth is now 67 years for males and 72 for females. Thailand has also experienced impressive reductions in infant and under-five mortality and maternal mortality. These are now 31 per 1,000, 38 per 1,000, and 2.0 per 1,000, respectively. Malnutrition levels fell from 24 to 13 percent from 1987-1996. However, the trend may have been reversed during the past year of economic crisis. Also, health risks due to environmental pollution, drug abuse, and HIV/AIDS¹ remain major public health challenges. Moreover, although infant and child mortality has been reduced significantly, high rates still exist in pockets of the extreme south, the northeast, among hill tribes in the north, and among the urban poor, especially in Bangkok. The country is now beginning to experience a transition from communicable diseases to chronic and degenerative diseases due to its aging population. This epidemiological transition is also accompanied by a weakening of the traditional family-based support system. Consequently, strengthening of the public health system in combination with insurance and social security schemes has become urgent.

59. The economic crisis has intensified these challenges in the health sector. First, the crisis has resulted in large numbers of workers losing their jobs, and along with that, medical cover for themselves and their families. Second, the tight fiscal situation has restricted budgetary resources for programs that provide medical and public health services. While resources have shrunk, the pressure on medical and public health services has increased. This has particularly affected the working of the low-income card scheme for health services and the welfare of the poor and the disadvantaged. Finally, the crisis has increased prices of almost all health inputs, especially imported pharmaceuticals. The health sector will need to improve its allocative and technical efficiency to take on the new challenges. This will be the guiding principle for health-

¹ HIV/AIDS is Human Immunodeficiency Virus/Acquired Immune Deficiency Syndrome.

related Bank operations.

c. Waste Management and Water Supply

60. Urbanization and industrialization have led to an acute water supply scarcity and water quality problems in Thailand. During the last decade the coverage of the piped water supply was expanded in BMR and other urban areas, achieving 80-90 percent coverage. However, in provincial urban centers and villages, about 60 percent of the population remains unserved. Although sanitation in most provincial centers is reasonably good, as evidenced by the low incidence of illness caused by waterborne diseases, wastewater is inadequately treated and polluted wastes are often discharged untreated into the natural environment. Pollution of water bodies from domestic, commercial, and industrial sources is rapidly reaching extreme levels in most urban centers, and there is an urgent need for major increases in investment to meet both municipal and industrial water supply and sanitation development requirements. To address these challenges Bank financial and TA for waste management and water supply development in provincial towns and cities will remain significant in the medium term (Appendix 8).

D. Cross-Cutting Concerns of Bank Operations

1. Poverty Reduction in Bank Operations

61. Rapid growth has contributed to a significant reduction of poverty in Thailand in the past. This trend has probably been reversed during the past year of crisis because of declining income and employment. In the medium/long term, the recovery of growth will help to resume the past trend of poverty reduction. In the short term, safety net measures need to be used in the labor market (without distorting incentives), and in education and health services to contain the adverse social impact of the crisis. The country-specific strategic objectives outlined in para. 50 directly address these requirements. Hence all Bank operations guided by this strategic framework will contribute to poverty reduction. A more detailed treatment of this issue is presented in Appendix 2.

2. Gender Dimensions of Bank Operations

62. A great deal of importance is attached to the role of women in development, as reflected in Thailand's high rank in the gender-inclusive Human Development Index: 40th out of 163 countries. Indicators such as the sharp drop in maternal mortality from 2.7 to 2.0 per 1,000 live births from 1985-1996, equitable education rates at all levels, and legislation to ensure equal rights for men and women, including equal pay for equal work, also bear testimony to this. Nevertheless, women are still slightly underrepresented in the workforce (47 percent), and more so in Government service (35 percent), or as employers (20 percent). The gender strategy in Thailand needs to address this concern. Legislation for equal rights and opportunities is already in place. Hence, the best means of reducing the gender gap in employment profiles is through measures to improve the competitiveness of women in the job market, particularly in Government service or managerial positions, and as entrepreneurs/employers. In the Bank's operations in Thailand this can best be achieved by bringing gender equity concerns into the mainstream. Social sector programs will remain a major focus of operations. In all these operations, components will be built in to ensure that adequate priority is attached to developing the skill profile of women in the workforce, and to better match this with the requirements of Government service, managerial jobs, and entrepreneurship. To track the progress in improving the status of women in development, and the gender gap in employment profiles, economic and

sector work on Thailand will continue to prepare periodic Women in Development profiles (Appendix 3).

3. Governance Dimensions of Bank Operations

63. Improvement of governance and the promotion of policies and institutions that reduce opportunities for corruption constitute a central element of the Bank's operational program in Thailand. This is especially important in the financial sector as the failure of governance in this sector is an important factor underlying the present financial crisis. However, governance-related operations will have a much wider coverage. The major challenge of improving governance in Thailand is systemic and not so much a constraint of technical capability. Consequently, the major focus of governance dimensions in Bank operations will be improvement of systems, although improvement of technical capacity will also be addressed.

64. The strategy adopted to improve governance and reduce the opportunity for corruption is to introduce policy and institutional reforms through policy loans that will help to replace discretionary resource allocation by market-based allocation, promote greater transparency, improve supervision by regulatory authorities, and reduce opportunities for corruption. The governance dimension of loan activities will also be supported by a series of governance-related TA projects, and a governance briefing paper that is currently under preparation.

4. Environment and Natural Resource Management

65. The pressure on Government financial resources because of the economic crisis has raised new challenges in management of the environment. The Bank will therefore continue to actively support the Government in meeting environmental objectives. The Bank's strategy in the near term will focus on capacity building and institutional strengthening of environment management agencies, but the focus will subsequently shift from central agencies to regional and local agencies, and to enhanced participation of local residents and the nonformal sector. The Bank will also continue to assist the Government in institutionalizing environmental concerns by ensuring that they are incorporated in development programs and project designs. At present waste management is the focus of environmentally oriented projects in the Bank's program, and these will remain important. However, the Bank will now also begin to support the green sector, particularly water resources management, watershed protection and rehabilitation, and biodiversity maintenance. The Bank is also beginning to assist with demand-side management, promotion of market-based instruments in environment management, and activating the private sector for improved management of natural resources (Appendix 9).

5. Private Sector Operations

66. The Thai economy is largely market based, and the private sector is already well developed. Hence, private sector development is not as urgent a priority as it is in some other countries of the region that are less private sector oriented. The main thrust of the Bank's strategy for further private sector development is to reform and strengthen the financial sector, which is the main driving force of a market economy. This will be supplemented by private sector development initiatives in rural areas and the social sector. Moreover, there is room for further expansion of private enterprise in selected preserves of the public sector. The Bank's strategy for Thailand includes greater private sector participation in the provision of public sector services. Accordingly, the Bank will continue to support privatization and commercialization

initiatives, including contracting out public sector functions to the private sector, and the use of private intermediaries to channel public sector assistance. The Bank has already played a key role in improving the environment for the private sector in the energy and telecommunications sectors. During the next few years Bank initiatives for private sector development are likely to focus on the financial sector, as well as agriculture, urban water supply and sanitation, and the social sector, in line with the Bank's strategic priorities in Thailand. A paper on the Bank's Private Sector development strategy will be prepared to give greater cohesiveness to these activities and identify possible synergies among them.

6. Subregional Economic Cooperation

67. The interim strategy will continue emphasizing subregional economic cooperation. Thailand has played a leading role in the Bank's initiative to promote subregional economic cooperation in Southeast Asia. At present, it is a participant in two Bank-facilitated subregional cooperation programs: the Program of Economic Cooperation in the Greater Mekong Subregion (GMS) and the Indonesia-Malaysia-Thailand Growth Triangle (IMT-GT). As the economic powerhouse in the GMS subregion, Thailand has been able to establish a strong mutuality of interests with its neighbors. It is emerging both as a market for their produce and as a source of technology and capital. Thai investment in power production in the Lao People's Democratic Republic for import into Thailand is an example of this potential. With Bank assistance, Thailand has adopted a policy of actively promoting and improving GMS transport and power links both in Thailand and to neighboring countries. This will serve as a useful foundation for the new GMS strategy of developing cross-border economic corridors. Subregional projects also contribute to balanced growth in Thailand's lagging regions (northeast Thailand for the GMS and the south for the IMT-GT). Physical infrastructure projects, which used to dominate the Thailand program earlier, are now being gradually phased out because of changed conditions. However, infrastructure projects in energy, transportation, etc., that help to develop the remote and less-developed areas of Thailand through cross-border economic activities will be retained.

E. Resources, Lending Modalities, and Cofinancing

68. The need for external assistance to Thailand from the Bank and other external sources increased significantly following the economic crisis. This need also increased enormously in other crisis-affected countries. However, there has been no commensurate increase in the Bank's own resources. Moreover, while addressing challenges in the crisis-affected countries, the Bank cannot neglect the equally urgent and important need for assistance in other developing member countries. Hence, assistance to Thailand will have to be provided under severe resource constraints within the Bank. To maximize the impact of Bank assistance, these limited resources will have to be significantly leveraged. Cofinancing operations will therefore play an increasingly significant role in Bank operations in Thailand.

69. In the past, cofinancing mainly focused on other multilateral and bilateral aid assistance. These sources will now have to be combined with other instruments like commercial cofinancing, and the use of the Bank's guarantee operations. A specific strategy for mobilizing commercial resources through guarantee operations will have to be crafted following the Bank's new guarantee policy, which is currently under preparation.

F. Technical Assistance and Economic and Sector Work

70. In the interim strategy the objective of TA and economic and sector work is

threefold:

- (i) sound preparation for lending operations;
- (ii) addressing cross-cutting concerns, especially determining specific steps for mainstreaming these concerns; and
- (iii) capacity building.

To meet these objectives the annual country assistance plans will have to develop TA pipelines that adequately support the lending program through project preparatory, advisory, and capacity-building TAs related to loan operations. Additionally, a consolidated program of advisory TAs, capacity-building TAs, and economic and sector work will be developed to address cross-cutting concerns, based on a series of preliminary papers that are now being finalized, i.e., Women in Development briefing paper, environment profile, governance issues paper, and social sector issues paper.

71. Finally, a special advisory TA is planned to review the economic and social impact of the crisis, and assist the Government in revisiting its medium term development strategy, based on this assessment. The new TA will build on an existing TA, that is developing the framework and monitoring system for tracking living standards and the quality of life at the national level as well as a disaggregated provincial level, and other ongoing exercises to monitor the economic and social impact of the crisis. These assessments will be supplemented by annual country profiles, country economic reviews, short economic updates, and political reviews from time to time as appropriate. Figure 3 presents a stylized representation of the total monitoring and assessment system. The proposed advisory TA will draw on these assessments and additional exercises to evaluate the achievements of the whole structural adjustment program that was initiated in 1997, including the policy and institutional reforms introduced under adjustment programs of IMF, World Bank and ADB. The proposed TA will also evaluate the effectiveness of aid-assisted investment programs. This evaluation of the impact of external assistance, including Bank operations, will provide the basis for preparing a regular country operational strategy that will follow this interim strategy after normalcy has been restored in the Thai economy.

G. Conclusion

72. The assumption underlying this interim country operational strategy is that the recent setback that Thailand has experienced is temporary. The country-specific strategic objectives, the corresponding strategic priorities, and the choice of sectors and operational instruments are all guided by an assumption that the Thai economy can and will be turned around within the next couple of years. Should that happen, this interim strategy will have served its purpose and become irrelevant. This is the most desirable outcome. Indeed, it will be the best measure of success of the strategy as its whole purpose is to guide a program of Bank assistance to help Thailand overcome the very conditions that have necessitated this interim strategy.

Figure 3: Performance Assessment and Monitoring System

Impact	Indicators	Monitoring Instruments
A. Financial Sector		
??Improvement of the legal and regulatory framework	?? Tightening of capital adequacy provisioning norms	??Bank of Thailand bulletins ??Bank CER and economic updates
??Restructuring of the financial sector	?? Improvement in NPL ratios ?? Enhanced flow of liquidity	??IMF/World Bank/staff reviews ??EFF monitoring system
??Recapitalization	?? Growth recovery	??Relevant IWFI TAs ??PW3 Crisis Impact Review TA and Structural Adjustment Assessment TA
B. Agricultural, Natural Resources and Rural Development		
??Policy reforms	?? Growth of production	??National accounts statistics
??Institutional reforms	?? Growth of exports	??Production, export, and productivity data
??Improved productivity	?? Rise in yields	??Forestry and irrigation statistics
??Improved management of natural, human, and financial resources	?? Increase in forest cover ?? Increase in irrigation cover, reduced flooding	??Wage and employment data ??Rural credit data ??Bank CER and economic updates
??Improved management of inputs	?? Rising rural wages, lower unemployment	??IMF/UN/World Bank reviews
??Development of research and extension systems	?? Greater flow of rural credit ?? Improved flow of research and extension services	??Relevant AWARD/AFW TAs ??PW3 Crisis Impact Review TA and Structural Adjustment Assessment TA
C. Social Sector Development		
??Expansion of secondary education	?? Higher enrolment rates in secondary education	??Poverty and well-being indicators from PW3 TA No. 2744
??Higher enrolment in science/math courses, foreign languages at secondary and higher levels	?? Higher share of science/math/foreign language courses in core syllabus and student enrolment in secondary and higher levels of education	??Official education statistics ??Official health statistics ??National accounts, wage and employment data
??Greater private sector involvement in education, especially at secondary, vocational and higher levels	?? Higher share of private sector services in student enrolment in vocational and higher education	??IMF/UN/World Bank reviews ??Bank social sector profile ??Relevant AWEH TAs
??Improved access to health care services for disadvantaged groups	?? Improved nutrition and health indicators for disadvantaged groups ?? Reduced per student cost in education services	??PW3 Crisis Impact Review TA and Structural Adjustment Assessment TA
??Improving the cost effectiveness of publicly provided education and health services	?? Reduced per patient cost in health services	
D. Cross-Cutting Concerns: Poverty, Gender, Environment, Governance, and Private Sector		
??Reduction of poverty	?? Poverty estimates	??Official reports on cross-cutting concerns
??Improvement of the status of women in development	?? Well-being indicators ?? Gender-specific wage and employment estimates	??Data on poverty, wage, employment, status of women
??Improvement of the quality of environment	?? Indicators of social and political status of women	??Forestry and environment statistics
??Greater accountability, transparency, and efficiency in governance	?? Air and water quality indicators ?? Forestry cover indicators	??Poverty and well-being indicators from PW3 TA No. 2744 ??Bank social sector profile, environment profile, WID briefing paper, governance strategy paper and private sector development strategy paper
??Recovery and growth of private enterprise, reduced Government role in the market	?? Polls and commentaries on quality of governance ?? Human rights and crime indicators	??IMF/UN/World Bank reports on cross-cutting concerns ??Relevant AWD TAs ??PW3 Crisis Impact Review TA and

Structural Adjustment Assessment TA

AWAR = Agriculture and Rural Development Division West; AWD = Agriculture and Social Sectors Department; AWEH = Education, Health and Population Division West; AWFN = Forestry and natural Resources Division West; CER = Country Economic Review; EFF = Export Financing Facility; IMF = International Monetary Fund; IWF1 = Financial Sector and Industry Division West; PW3 = Programs Department West Division 3; UN = United Nations; WID = Women in Development.

APPENDIXES

Number	Title	Page	Cited on (page, para.)
1	Country Performance Indicators	26	1, 1
2	Poverty Profile for Thailand	28	2, 4
3	Strategic Direction for Enhancing the Role of Women in Development	32	2, 5
4	Strategic Priorities for Financial Sector Reform and Bank Restructuring	35	5, 12
5	Portfolio Performance	41	9, 31
6	Overall External Assistance	47	13, 38
7	Strategic Directions for Reform in Agriculture and Rural Development	48	18, 57
8	Strategic Directions for Social Sectors	51	20, 61
9	Strategic Directions for Environment Related Operations in Thailand	55	21, 66

COUNTRY PERFORMANCE INDICATORS

Item	1994	1995	1996 ^a	1997 ^a	1998 ^a
A. Income and Growth					
1. GDP per capita (current price, \$)	2,461	2,833	3,027	2,543	1,902
2. GDP Growth (constant 1988 prices,%)	8.9	8.8	5.5	-0.4	-8.0
Agriculture	5.3	2.5	3.8	1.4	2.1
Industry	10.1	10.5	7.0	-0.1	-12.1
Services	8.9	9.0	4.6	-1.1	-6.8
B. Saving and Investment (current prices, % of GDP)					
1. Gross Saving	34.7	33.6	33.7	32.9	35.9
2. Gross Domestic Investment	40.3	41.6	41.7	35.0	24.4
C. Money and Inflation (annual % change)					
1. Consumer Prices	5.1	5.8	5.9	5.6	8.1
2. Money Supply (M2)	12.9	17.0	12.6	16.4	9.6
D. Government Finance (% of GDP)^b					
1. Revenue and Grants	19.1	19.3	19.5	18.3	15.0
2. Expenditure and Net Lending	17.2	16.3	17.1	19.2	17.7
3. Fiscal Balance	1.9	3.0	2.4	-0.9	-2.5
E. Balance of Payments					
1. Trade Balance (% of GDP)	-6.0	-8.7	-8.9	-3.0	9.8
2. Current Account Balance (% of GDP) ^c	-5.4	-7.9	-7.9	-2.0	11.5
3. Exports (growth rate, %)	22.1	24.8	-1.9	3.8	-6.6
4. Imports (growth rate, %)	18.4	31.9	0.6	-13.4	-32.3
F. External Payments Indicators					
1. Gross Official Reserves (\$ billion)	30.3	37.0	38.7	27.0	29.5
(months of imports of goods)	6.8	6.3	6.6	5.3	8.5
2. External Debt Service (% of exports of goods and services)	11.7	11.4	12.3	15.6	21.3
3. External Debt (% of GDP)	44.9	49.1	49.9	60.6	72.9
Memorandum Items:					
GDP (current prices, B billion)	3,630.8	4,188.9	4,598.3	4,827.2	4,839.4
Average Exchange rate (B/\$)	25.13	24.89	25.32	31.32	41.31
Population (million)	58.713	59.401	60.003	60.602	61.602

^a Preliminary estimates.

^b On a fiscal year basis. Covers Central Government budgetary and nonbudgetary accounts, and social security funds only and does not include interest costs of financial sector restructuring.

^c Excluding official transfers.

Sources: National Economic and Social Development Board (NESDB). 1997. *National Income of Thailand 1996 Edition*; NESDB. 1995. *Population Projections for Thailand 1990-2020*; Bank of Thailand (BOT). 1998. *Quarterly Bulletins, Monthly Bulletins*; BOT. 1998. *Monthly Statistical Releases*; International Monetary Fund reports; Economic Research Department, BOT; Fiscal Policy Office, Ministry of Finance; Bureau of the Budget; and staff estimates.

POVERTY PROFILE FOR THAILAND¹

1. Until recently the incidence of poverty in Thailand had been declining rapidly. The recent economic crisis has changed this situation. The Government needs to have new policies to deal with the new situation. However, the crisis is still ongoing and the full impact of the crisis is as yet unknown.

A. Poverty at the Aggregate Level

2. The most popular measure of poverty is the head-count ratio: the percentage of population that is living below the poverty line. This measure does not reflect the depth or severity of poverty suffered by the poor. The problem is, how poor are the poor? They may have incomes that approximate the poverty line or they may have incomes of almost zero. If the deviation of a poor person's income from the poverty line is proportional to the degree of misery suffered by the person, the sum total of these deviations divided by the total population may be considered a desirable measure of poverty. This index, called the poverty gap ratio, measures the depth of poverty. The main drawback of this measure is that it is completely insensitive to any income (or welfare) transfer among the poor. To overcome this drawback we use the Foster-Greer-Thorbecke index (FGT), which is sensitive to income transfers among the poor. This index adequately measures the severity of poverty.

3. Table 1 presents the poverty estimates for the whole country. In 1988, 32.6 percent of Thailand's population was identified as poor. This figure declined to 27.2 percent in 1990, 23.3 percent in 1992, 16.3 percent in 1994, and 11.4 percent in 1996. This dramatic reduction in poverty is indicated by all the poverty indicators presented in Table 1. This suggests that the high economic growth in the 1990s (until 1996) has been trickling down to the poor. The absolute number of poor also declined sharply from 17.9 million in 1988 to only 6.8 million in 1996. Unfortunately, this pattern of rapid poverty reduction has been reversed since the crisis. By 1998 all the poverty incidence measures had increased and the number of poor had increased over 1 million compared to 1996 (Table 1).

Table 1: Aggregate Poverty in Thailand

Item	1988	1990	1992	1994	1996	1998
Percentage of poor	32.6	27.2	23.2	16.3	11.4	12.9
Poverty depth (%)	10.4	8.0	6.8	4.3	2.8	3.2
Severity of poverty (%)	4.6	3.3	2.8	1.7	1.1	1.2
Number of poor (Million Persons)	17.9	15.3	13.5	9.7	6.8	7.9

Source: National Economic and Social Development Board. *Indicators of Well-being and Policy Analysis*, Bangkok, Vol. 2 No. 3, May 1998, and Vol. 3 No. 1, January 1999 (forthcoming).

¹ This note is based on the results of an ongoing Technical Assistance to Development Evaluation Division, NESDB. (TA No. 2744-THA) which has developed the conceptual framework and monitoring system for indicators of well-being in Thailand, including indicators of poverty. For a more detailed discussion please see Development Evaluation Division, NESDB. *Indicators of Well-Being and Policy Analysis*, Vol. 2 No. 3, May 1998, and Vol. 3 No. 1, January 1999 (forthcoming).

B. Poverty Incidence by Region and Area

4. It is noted from Table 2 that the incidence of poverty varies widely across regions. The Northeastern Region has the highest incidence of poverty. In 1998, the percentage of poor in the region was 23.2 percent as compared with 12.9 percent for the whole country. The most striking result is that poverty reduction during the past decade has also been the greatest in the Northeastern Region—where poverty incidence declined by over 25 percentage points compared with 19.7 percentage points for the whole country.

5. The Northern Region enjoyed an impressive reduction in poverty from 1992-1994. The percentage of poor declined from 22.6 percent in 1992 to 13.2 percent in 1994. This progress in poverty reduction has slowed down since then.

Table 2: Percentage of Poor by Region

Period	Central	Northern	Northeast	Southern	Bangkok & vicinity	Thailand
1988	26.6	32.0	48.4	32.5	6.1	32.6
1990	22.3	23.2	43.1	27.6	3.5	27.2
1992	13.3	22.6	39.9	19.7	1.9	23.2
1994	9.2	13.2	28.6	17.3	0.9	16.3
1996	6.3	11.2	19.4	11.5	0.6	11.4
1998	7.7	9.0	23.2	14.8	0.6	12.9

Source: National Economic and Social Development Board. *Indicators of Well-being and Policy Analysis*, Bangkok, Vol. 2 No. 3, May 1998, and Vol. 3 No. 1, January 1999 (forthcoming).

6. Villages in rural areas have experienced a very large reduction in poverty (Table 3). The percentage of the poor in the entire village population of Thailand declined by 8.5 percentage points from 1992-1994, and by another 6.3 percentage points from 1994-1996. This is indeed good for Thailand because the incidence of poverty has always been extremely high in rural areas. Unfortunately, the decline was reversed from 1996-1998 because of the crisis.

Table 3: Percentage of Poor by Community Type

Community	1988	1990	1992	1994	1996	1998
Municipal areas	8.0	6.9	3.6	2.4	1.6	1.5
Sanitary districts	21.8	18.2	12.7	9.6	5.8	7.2
Villages	40.3	33.8	29.7	21.2	14.9	14.9
Thailand	32.6	27.2	23.2	16.3	11.4	12.9

Source: National Economic and Social Development Board. *Indicators of Well-being and Policy Analysis*, Bangkok, Vol. 2 No. 3, May 1998, and Vol. 3 No. 1, January 1999 (forthcoming).

C. Factors Associated with the Incidence of Poverty

7. Among other features of poverty incidence it is to be noted that children in Thailand are suffering from a higher degree of poverty than adults. Hence, the Government needs to devise policies that help children directly. It is also widely recognized that education has a strong impact on poverty. Heads of the poor households have a much lower level of education than those of the nonpoor households. On average, the poor household heads complete only 3.6 years of schooling, whereas the nonpoor household heads complete 5.5 years of schooling. This shows that education of household heads is closely related to poverty. The household head is generally the main earner in the household. Therefore, education of household heads should be an important factor in determining household welfare and poverty. The average educational level varies widely across the communities. The educational level in villages is very low. The average index value in villages among the nonpoor households is only 4.5 compared with a value of 8.3 in municipal areas. Among the poor households also, the municipal areas and sanitary districts have a higher educational level than in villages. A general conclusion that emerges from this result is that the average educational level in rural Thailand is very low and it is not showing any sign of significant improvement.

8. The poverty estimates also reveal that poverty is the highest among household in which the heads are agriculturalists. In 1988, 45.6 percent of the population in these households was poor. This figure declined to 38.6 percent in 1990 and 35.7 percent in 1992. From 1992 onward, the rate of poverty reduction among these households accelerated, with the percentage of poor declining to 26.6 in 1994 and to 18.8 in 1996. Still, the agriculturalist households account for the bulk of poverty in Thailand. This observation strongly supports the traditional view that poverty in Thailand is mainly a rural phenomenon. The good news is that rural poverty was also declining rapidly until 1997. However, this trend has been reversed by the current economic crisis since 1997.

D. Poverty and Land Size

9. Since the incidence of poverty was found to be the highest among agriculturalist households, the incidence of poverty among farm households with different landholdings has been investigated. Table 4 presents the poverty estimates among farmers with different land holdings separately for farm owners and farm renters.

10. In 1988 and 1990, the incidence of poverty was highest among the farm households having landholdings of less than 5 rai¹. This is what we would naturally expect. This situation changed from 1992-1994. The incidence of poverty remained the lowest among the large farmers with a landholding of 20 rai or more. However, the poverty ranking between the smallholders (with a landholding of less than 5 rai) and the medium-size holders (with a landholding between 5 to 19 rai) reversed from 1992-1994. However, in 1996 and 1998 households with less than 5 rai again revealed the highest incidence of poverty. From these observations, it is difficult to infer whether or not smallholders have become more efficient compared to medium-size landholders. It is possible that the smallholders tend to obtain income from other sources, whereas the medium-size holders derive their incomes mainly from their farms and are more sensitive to farm production trends. It also needs to be ascertained whether there were any peculiar features of the 1994 survey which yielded sharply out of trend features.

¹ 1 rai = 0.16 hectare.

**Table 4: Percentage of Poor Among Farm Households
by Size of Land Holding**

Period	Less than 5 rai	5 to 19 rai	20 rai or more
1988	67.7	52.9	41.2
1990	67.7	52.9	41.2
1992	56.2	52.1	46.3
1994	32.9	26.9	31.2
1996	67.7	52.9	41.2
1998	67.4	60.0	30.3

1 rai = 0.16 hectare.

Source: National Economic and Social Development Board. *Indicators of Well-being and Policy Analysis*. Bangkok, Vol. 2 No. 3, May 1998, and Vol. 3 No. 1, January 1999 (forthcoming).

11. What is important to note is that poverty among farm households with a landholding of less than 5 rai and those with landholdings of 5-19 rai has increased substantially in 1998 compared to either 1992 or 1994. Thus, the large reduction in poverty among farm households since 1992 is mainly attributed to the large reductions in poverty among households with relatively large landholdings, while there has been greater impoverishment among the landless and near landless.

E. Bank Strategy for Poverty Reduction

12. Growth is the only long-term vehicle for poverty reduction, hence the Bank will pursue a growth-mediated strategy of poverty reduction in Thailand. The foregoing analysis shows that although rural poverty was declining rapidly, at least prior to the onset of the economic crisis, poverty is nevertheless largely a rural phenomenon—closely associated with landlessness. Consequently, the thrust of a poverty reduction strategy will have to be centered around agriculture and rural development. The Bank will therefore return to operations in the agriculture sector after a gap of several years, starting with a program loan to eliminate policy and institutional distortions in the sector, and promote improvements in productivity and export competitiveness. Although the agriculture sector program loan will have a primary growth objective, it will also simultaneously be directed at poverty reduction through growth. The importance of landlessness as a determinant of poverty also suggests that poverty reduction will require increasing rural employment opportunities outside agriculture, i.e., rural development through growth of rural non-agricultural enterprise. Bank operations should therefore target support for integrated area development programs, especially diversification to off-farm activities, in high poverty incidence regions like the Northeast.

13. This strategy of poverty reduction through growth is a long-term process. Hence, it needs to be supplemented by relief measures in the short run to contain the immediate adverse effects of the economic crisis. Consequently, the second plank of the Bank's poverty reduction strategy in Thailand is direct support to vulnerable groups through social sector projects. This has already been addressed partly in the ongoing Social Sector Program Loan. However, it can be followed through in subsequent education or health projects and a proposed social sector development loan scheduled for 2001. Since women and children are revealed to be the most deprived among the poor, education and health sector projects/program components should specifically target these groups.

STRATEGIC DIRECTION FOR ENHANCING THE ROLE OF WOMEN IN DEVELOPMENT

A Introduction

1. The economic crisis in Thailand has had a very severe impact on women. Products produced mostly by female labor, including textiles and ready-made garments, integrated circuits, gems and jewelry, shoes and leather goods, artificial flowers, toys, and electrical goods were some of the hardest hit. It is therefore important to ensure that programs introduced to mitigate the adverse social and economic impact of the crisis are designed to extend adequate relief to women and that the benefits of the recovery measures are also equitably shared by women and men.

B. The Bank's Gender Strategy¹

1. The Bank's Operational Strategy

2. The Bank's operational strategy in Thailand has three strategic objectives:
- (i) stabilization and adjustment to restore the process of growth;
 - (ii) strengthening competitiveness to promote efficient, regionally balanced and sustainable long term growth; and
 - (iii) improving the quality of life.
3. Within this framework, it is possible to mainstream a gender equity strategy by including activities that would directly and indirectly enhance women's economic and social position. In this period of economic crisis, the Bank can assist both in defending the gains made to date by women and in correcting the remaining imbalances.

2. Human Resource Development

4. With manufacturing production processes shifting toward higher value-added activities, there is an urgent need to produce better-trained workers at all levels. This also applies to tertiary sector jobs. Bank assistance in improving the quality of the Thai workforce will contain targeted components designed to reduce women's disadvantageous position in the labor market through upgrading women's managerial as well as technical and vocational skills. Resources will be allocated to increasing enrollment and retention rates of girls and, especially, to encourage female entry into secondary and higher levels of education, as well as vocational specialization. Affirmative action policies will be adopted to facilitate participation of women in areas where they are currently underrepresented.

5. Future Bank assistance to this sector is likely to focus on strengthening postgraduate education and research in medicine, law, finance, management, science, and technology to enhance Thailand's economic competitiveness. Given women's low representation in these fields, the Bank will make efforts to devise mechanisms and strategies to promote increased female participation in these fields, especially in postgraduate courses. Since

¹ The Gender Strategy was prepared on the basis of a detailed analysis of the status of women in Thailand with regard to work and employment, health, education and literacy, their social status, legal rights, and political status. This analysis is reported in Asian Development Bank. 1998. *Country Briefing Paper: Women in Thailand*. Manila.

there are large numbers of women completing tertiary education in Thailand, albeit in traditional female fields, some of these women could be redirected at the postgraduate level into medicine, law, finance, management, science, and technology. Incentives such as scholarships, stipends, and exchange programs will be provided to encourage women to pursue studies in these fields. Research fellowships for women in these fields will also be included.

6. Another important challenge in the education sector is to devise mechanisms and strategies to increase female participation and retention rates in secondary education, especially in the poorer regions. In any future assistance to this sector, the Bank will develop measures such as programs for parental awareness, scholarships, and stipends to encourage parents to keep their daughters at school. To meet both the changing skills requirements in Thailand and enable women to benefit from the shortage of labor in certain areas, the Bank will also promote nontraditional skills training (e.g. plumbers, electricians, mechanics, carpenters) for women through its nonformal education projects. Efforts will also be made to offer the nontraditional skills training courses to women recently retrenched as a result of the economic crises. To date, in preliminary training programs in these areas women have performed very well. The Bank will also explore opportunities to assist the Ministry of Labor and Social Welfare to find innovative training schemes that focus on building confidence and communication skills, and schemes that provide information on employment opportunities, skills requirements, and training opportunities.

3. Agriculture/Rural Development

7. The new Bank operational strategy gives high priority to agriculture and rural development. Future Bank assistance to this sector will explore the possibility of targeting women and devising measures to enhance women's income-earning capacity. Efforts will also be made to explore the potential for including land-titling components in Bank projects, where feasible, to support and promote women's land ownership rights and reduce the barriers women face in the access to credit.

8. Within the strategy to upgrade agriculture technology, the Bank will promote and facilitate the participation of rural women in training for new agricultural technology. Appropriate design features will be built into projects to encourage the participation and training of women. Evidence suggests that women are normally excluded when new agricultural technology is introduced, due to their secondary family status, low education, and sometimes, the selection process. Women's lower literacy rate poses another major obstacle for rural women causing them to have more problems than men in understanding written instructions in agricultural training programs. In the case of scientific and technical information, the problems become even more serious. Audiovisual materials have been proven to increase women's understanding of technical matters and thus will be more widely used. Nontraditional methods of instruction such as the use of performing arts will also be considered.

9. Small-scale enterprises are more likely to employ women workers than the large- or medium-scale enterprises. The food industry has the potential to increase incomes through greater exports and create employment at a time when traditional exports are being squeezed by regional competition. This sector is a large employer of women. Dairy farming is another new area of women's work in which science and technology can play an important role. New areas such as artificial insemination and processing of dairy products now enjoy a rapidly expanding market. The Bank's rural credit initiatives and technical assistance should be used to promote these activities where feasible. Also, the probability of women benefiting from the Bank's Small Farmer Credit and Rural Enterprise Credit projects are high. However, credit components in

future policy lending for agriculture/rural development will build in features to ensure that women borrowers are provided access and not excluded from the program as a result of their official status as unpaid family workers and not farmers.

4. Partnership with Nongovernment Organizations

10. Nongovernment organizations (NGOs) in Thailand have contributed toward improvements in women's status both through their advocacy and service delivery roles. The increasing recognition of NGOs in the development process is gaining widespread recognition, as evident in the regular advice they provide to governments. In Thailand, many NGOs are now routinely invited by the Government to assist in the preparation and implementation of projects and programs. The Bank will investigate mechanisms through which NGO activities that address women's needs can be supported and promoted within the framework of agriculture sector program lending and social sector development. Opportunities to assist women's NGOs will also be explored.

5. Strengthening Institutional Capacity of the National Women's Machinery

11. As part of its capacity-building support, the Bank will investigate the potential to assist the National Commission on Women's Affairs (NCWA) undertake its revised and broader mandate as a coordinating and monitoring agency. Over the next year, NCWA is to be upgraded to departmental status. Capacity building through the modality of technical assistance could focus on developing the modified terms of reference for the upgraded department, preparing an institutional framework, and building the capacity of the staff to perform the revised functions and duties. As the Government's focal point on women, the NCWA's terms of reference need careful assessment and revision to meet their new mandate, as well as the current needs of women in Thailand. Development of a framework to monitor the implementation of Government commitments to the Beijing Platform for Action could be included as an integral part of the capacity-building assistance.

STRATEGIC PRIORITIES FOR FINANCIAL SECTOR REFORM AND BANK RESTRUCTURING

1. The ongoing financial crisis was set off by the erosion of investor confidence in Thailand's financial institutions, particularly the commercial banks and private nonbank financial institutions. Imprudent lending by poorly regulated institutions that ignored prudential norms lies at the root of the problem. Reforming the financial sector is therefore the single most important strategic measure necessary for restoring investor confidence and reviving the process of growth. The new interim country operational strategy accordingly identifies the financial sector as the first priority for Bank operations in Thailand over the medium term.

2. The Bank has been working very closely with the International Monetary Fund (IMF) and the World Bank on financial sector reforms in Thailand. IMF has undertaken responsibility for reforming and strengthening the central bank, while the World Bank has led the effort to reform and rationalize the nonbank financial institutions subsector. IMF and the World Bank are also assisting the Government in reforming the regulatory framework for banks and other private financial companies. The Bank has focused on assisting the Government in reforming and developing the capital market as an alternative channel of resource mobilization, i.e., the stock exchange, the bond market, and the Securities and Exchange Commission, through a Financial Markets Reform Program loan of \$300 million in the first phase. To provide urgently required liquidity for exporters, the Bank also arranged a \$1 billion syndicated loan from 68 international commercial banks, based on a \$50 million anchor loan and partial credit guarantee from the Bank.

3. Recapitalization of commercial banks is now the most urgent requirement in the sector. The Government has requested the Bank to provide assistance for restructuring and recapitalization of some of the State-owned commercial banks and specialized financial institutions. The Bank is in the process of determining its role in this context, not only in Thailand but all the crisis-affected countries. Recapitalization can only be the final outcome of a three stage process starting with a review of the identified institutions (i.e., international standard financial and management audit), preparation and implementation of restructuring plans, and finally recapitalization. This will be necessary to ensure that intervention does not create any moral hazard. Bank operations in this area in Thailand, if any, will be programmed following the enunciation of a Bank policy on the subject.

A. Steps Taken for Bank Restructuring in Thailand

4. In August 1998 the Thai Government announced a comprehensive range of measures covering restructuring and consolidation of the nonbank finance companies sector, restructuring plans for domestic commercial banks, restructuring and privatization strategy for Krung Thai Bank, the largest public sector commercial bank, a financing plan for recapitalization of private financial institutions, and measures for the legal/regulatory framework. This marks the latest stage in a sequence of significant steps the Government has undertaken since the emergence of the economic crisis in June last year, to restructure the country's financial sector.¹

¹

It should be pointed out that in the early 1980s, Thailand had already faced a crisis in its finance company sector. As part of the earlier response, the Financial Institutions Development Fund (FIDF) was created. The FIDF is designed to provide liquidity support to financial institutions at penal rates as a lender of last resort. As of February 1998, the FIDF had extended about B716.1 (about \$17.9 billion) to various financial institutions.

The complete set of financial sector reform measures taken so far, culminating in the 14 August policy announcement, is outlined here.

1. Diagnostic Review and Restructuring of Private Nonbank Finance Companies

5. The Government first suspended the operations of 58 finance companies, requiring these companies to submit rehabilitation plans, and created the Financial Sector Restructuring Authority (FRA) to consider the rehabilitation plans. Subsequently, the Government closed 56 finance companies based on FRA's evaluation of the rehabilitation plans, and approved the rehabilitation plans of the remaining two suspended finance companies, allowing them to reopen operations.

6. Depositors and creditors of the closed finance companies have been given the option of exchanging their claims for notes issued by Krung Thai Thanakit and Krung Thai Bank. The Financial Institutions Development Fund will service payments of interest and principal on these notes.

7. FRA was tasked with maintaining and disposing of the nonperforming assets of the closed finance companies.¹ The Government created the Asset Management Corporation (AMC) as the bidder of last resort, to bid for assets that fail to be liquidated after the initial auction. Except for the finalization of regulatory safeguards to ensure that AMC functions only as the bidder of last resort, the organization and procedures of AMC are largely in place. An increase in its capital to B10 billion has also been authorized. The Government has also established the Radanasin Bank, which is intended to bid for the high quality assets to be auctioned off by FRA, though it will subsequently function as a normal commercial bank. The rules, guidelines, and procedures for valuation and bidding for the Radanasin Bank are in place. Radanasin Bank is currently holding discussions to identify a strategic partner.

8. The first auction of core assets by FRA was held in June 1998 for hire-purchase contracts with an aggregate principal balance of B52 billion (about \$1.3 billion). The winning bids totaled B24.9 billion, about 48 percent of the outstanding principal balance. There were a fairly large number of bidders comprising both local and foreign investors. The earlier sale of noncore assets, comprising vehicles, furniture, and bonds was well received and netted B40 billion. FRA has a target to complete the sale of all core assets by the end of 1998. However, legal obstacles to the smooth operation of FRA still remain. The Government is addressing these problems. Among other things, these problems include the interruption of auctions when the creditor of a finance company initiates bankruptcy proceedings, guarantee of good title, and the need to secure borrowers consent to the assignment of loans.

9. In the meantime, the Government has intervened in another 12 finance companies (up to 14 August 1998) that are to be consolidated with Krung Thai Thanakit, a State-controlled finance company. Of the remaining 23 finance companies, some have found market niches. Others, particularly smaller ones, are also likely to be consolidated if they are unable to comply with the more stringent prudential regulations that are now in place, and the consequent larger recapitalization requirements.

1

To deal with problematic real estate projects, the Government also set up the Property Loan Management Organization (PLMO). However, the scheme was not well received as it restricted purchases by PLMO to good assets, and placed an additional requirement for selling companies to provide additional loans to its borrowers.

2. Strengthening the Market Infrastructure

10. In parallel, the Government has prepared the groundwork for strengthening the regulatory and supervisory framework applicable to both finance companies and banks with IMF/World Bank assistance. The Bank of Thailand has tightened prudential regulations covering asset classification, income recognition, collateral valuation, and provisioning, which have become effective from 1 July 1998. The provisioning requirements are now being further tightened, under the 14 August proposals, to meet international standards for those financial institutions that propose to draw on the public recapitalization scheme announced in the same proposals.

11. Furthermore, the Government has amended the Bankruptcy Act, which provides an opportunity for financially strapped companies to have their businesses reorganized through court-supervised procedures and allows an equitable treatment for creditors in the recovery process. Foreclosure procedures are also being improved. Amendments of existing laws are expected to be accomplished by the fourth quarter of 1998. Removal of the disincentives for debt write-offs and exemption of asset transfers from value-added tax payments are also being initiated.

3. Banking Sector Review, Restructuring, and Recapitalization

12. In the private banking sector, the Government initially adopted, in consultation with IMF, a market-based strategy, i.e., to create an enabling environment and allow the private sector to work out its own restructuring. Some banks were able to raise fresh capital from the market, including the Bangkok Bank (over \$1.0 billion) and Thai Farmers Bank (approximately \$825 million). Lesser amounts have been raised by the Bank of Asia (\$187.5 million) and Thai Danu Bank (\$150 million). Of the 6 public sector commercial banks, Krung Thai Bank was able to raise B20 billion (\$500 million) from Government funds, and the Thai Military Bank about B5 billion (\$125 million) from local sources connected with the military. However, such recapitalization efforts have been piecemeal. Consequently, the Government has had to intervene in five commercial banks that were unable to meet capital adequacy norms, in addition to the Bangkok Bank of Commerce, that was taken over earlier in 1997. In the 14 August proposals the Government presented restructuring proposals for all these intervened banks, including mergers, acquisition, and privatization. The Government, at the same time, announced a two-tier public recapitalization scheme for remaining private sector banks and nonbank finance companies. These proposals have also announced a restructuring and privatization plan for Krung Thai Bank, the main public sector commercial bank (Box).

13. For the State-owned specialized financial institutions¹ the Government has completed a preliminary review with the help of the World Bank. It is also preparing a global bond issue of \$5 billion (Yankee bonds) to help replenish their capital base, especially for Industrial Finance Corporation of Thailand (IFCT) and Thai Exim Bank. The role of the State-owned financial institutions needs to be thought through. The Government intends to utilize these institutions to funnel credit into the economy. This carries the risk of perpetuating directed lending practices. It is therefore essential that they operate within a clear-cut policy and regulatory framework and with appropriate supervision. The World Bank is providing technical assistance. However, there is no direct intervention in this area indicated so far by either IMF or the World Bank in their policy reform agenda.

¹

These include Krung Thai Bank, Bank for Agriculture and Agricultural Cooperatives, Radanasin Bank, Exim Bank, Industrial Finance Corporation of Thailand, the Government Housing Bank, the National Housing Authority, the Government Savings Bank, and the recently organized Secondary Mortgage Corporation.

Thailand: Implementation of the August 14 Announcement For Comprehensive Financial Restructuring	
Measure	Date
A. Intervened Banks: Liquidation, Merger, and Sale Timetables	
<p>BMB and SCIB privatized</p> <ul style="list-style-type: none"> /// After full provisioning, recapitalization up to 8.5 percent of risk-weighted assets. /// Selection of financial advisers for privatization. /// Announcement of divestiture modalities for the privatization process. /// Acceptance of bids and transfer to new investors. 	<p>31 August 1998 15 September 1998 30 September 1998 31 December 1998</p>
<p>BBC transformed into Nonbank Financial Institution (AMC) and wound down</p> <ul style="list-style-type: none"> /// BBC's banking license to be restricted from accepting new deposits, extending new credit, entering new foreign exchange operations, and assuming contingent liabilities. /// MOF/BOT to announce the modalities for KTB's absorption of performing assets, deposits and other liabilities. /// Terminate management contract with IFCT in line with existing contractual arrangements. /// Transfer of performing assets, deposits, and other liabilities to KTB. /// Banking license revoked and BBC turned into a private AMC. /// Adoption of plan for effective closure of BBC by 31 December 1999, including with regard to the rationalization of staff and branches, and the disposition of nonperforming assets. 	<p>17 August 1998 17 August 1998 31 August 1998 30 September 1998 31 October 1998 31 October 1998</p>
<p>FBCB integrated with KTB</p> <ul style="list-style-type: none"> /// KTB management to take charge of all FBCB operations. /// After full provisioning, recapitalization up to 8.5 percent of risk-weighted assets. /// MOF/BOT to announce modalities for the integration with KTB. /// FBCB to be fully integrated with KTB and revocation of license. 	<p>17 August 1998 30 September 1998 30 September 1998 31 December 1999</p>
<p>UBB integrated with KTT</p> <ul style="list-style-type: none"> /// After full provisioning, recapitalization of UBB up to 8.5 percent of risk-weighted assets. /// Adopt plan for completing UBB's integration with KTT by 31 December 1998. 	<p>31 August 1998 31 October 1998</p>
<p>LTB integrated with Radhanasin Bank (RAB)</p> <ul style="list-style-type: none"> /// After full provisioning, recapitalization of LTB up to 8.5 percent of risk-weighted assets. /// Adopt plan for completing LTB's integration with RAB by December 31, 1998. /// After full provisioning, recapitalization upon BOT's approval of operational plan. 	<p>31 August 1998 31 October 1998 15 November 1998</p>

Box, continued	
B. Restructuring of KTB	
<ul style="list-style-type: none"> /// Appointment of new Board. /// Completion of plan for operational restructuring of the combined bank in consultation with outside experts. This plan should include rationalization of branch network, internal control and risk management systems, and analysis of staffing needs and training, in preparation of KTB's privatization within two years. /// After full provisioning, recapitalization upon BOT's approval of operational plan. 	<p>31 August 1998</p> <p>30 November 1998</p> <p>15 December 1998</p>
C. Consolidation of Finance Company Sector	
<ul style="list-style-type: none"> /// BOT to issue guidelines regarding finance companies' entitlement to a banking license. /// Adopt plan for completing KTT's integration with finance companies and UBB. /// After full provisioning, recapitalization of the combined KTT/UBB upon BOT's approval of operational plan. 	<p>30 September 1998</p> <p>31 October 1998</p> <p>15 November 1998</p>
D. Implementation of Tier 1 and Tier 2 Capital Support Facilities	
<ul style="list-style-type: none"> /// Appointment of Financial Restructuring Advisory Committee (FRAC) to monitor Tier 1 and Tier 2 capital support schemes and other aspects of financial sector restructuring. /// Issuance of detailed guidelines for participating in the recapitalization schemes by FRAC. 	<p>31 August 1998</p> <p>30 September 1998</p>
E. Associated Legal Measures	
<ul style="list-style-type: none"> /// Amend by emergency decree the Commercial Banking Law to facilitate merger of banks and transfer of assets. /// Obtain, by emergency decree, authority to issue up to B 300 billion of bonds for capital support schemes. /// Approve by emergency decree enabling legislation for establishment of private AMCs. /// BOT to amend CAR regulations. /// BOT to amend LCP/TDR regulations. 	<p>21 August 1998</p> <p>21 August 1998</p> <p>21 August 1998</p> <p>7 September 1998</p> <p>7 September 1998</p>

AMC = Asset Management Company; BBC = Bangkok Bank of Commerce; BMB = Bangkok Metropolitan Bank; BOT = Bank of Thailand; CAR = capital adequacy ratio; FBCB = First Bangkok City Bank; FRAC = Financial Restructuring Advisory Committee; IFCT = Industrial Finance Corporation of Thailand; KTB = Krung Thai Bank; KTT = Krungthai Thanakit; LCP = loan classification and provisioning rules; LTB = Laem Thong Bank; MOF = Ministry of Finance; RAB = Radhanasin Bank; SCIB = Siam City Bank; UBB = Union Bank of Thailand.

4. Private Debt Restructuring

14. With regard to private debt restructuring also, the Government initially adopted a market-based approach, encouraging the formation of credit committees and debt workout units on a voluntary basis. The Government's role was to be confined to eliminating institutional and

tax barriers to corporate restructuring and facilitating negotiations between debtors and creditors. However, it soon became clear that a more interventionist public sector role was necessary initially to facilitate a market response. Consequently, the 14 August proposals have linked tier 2 of the public recapitalization scheme for financial institutions to corporate debt restructuring. This should facilitate the process of corporate debt restructuring significantly. Some legal impediments are also slowing down the process. These include gaps in the Bankruptcy Act, deficiencies in foreclosure procedures, disincentives in the tax regime, and the slow process of liberalizing foreign investment limits under the Alien Business Law, a condition of the Bank's Financial Markets Reform Program loan for listed companies and securities firms. These legal constraints now need to be dealt with expeditiously.

B. The Bank's Role in Financial Reforms and Bank Restructuring

15. To a large extent the Bank's involvement will be shaped by the nature of the Government's request and requirement; the Government's commitment, capacity, and available resources for pursuing the announced restructuring measures; the Bank's own willingness and capacity to commit staff, time, and resources to undertake the restructuring tasks; and the allocation of roles in this area by IMF, World Bank, and bilaterals as requested by the Government.

16. In the first phase of financial sector reforms the Bank has assisted the Government with developing the capital market. The Bank should continue its assistance for capital market development, focusing on pension/provident fund schemes, and insurance services that were not included in the first phase of capital market reforms. The Government has also requested the Bank on different occasions to provide assistance for the recapitalization of different State-owned banks and financial institutions. These institutions are a very important segment of the financial sector in Thailand, particularly in the context of constraints that the commercial banks are facing in performing their normal intermediation role. Their recapitalization can only be the final outcome of a three-stage process starting with a review of the identified institutions, i.e., international standard financial and management audit; preparation of restructuring plans; and finally recapitalization. This will be necessary to ensure that intervention does not create any moral hazard. The Bank can support the first two stages through technical assistance. The issue of support for recapitalization can be reviewed at a later date, following the outcome of the technical assistance.

STRATEGIC DIRECTIONS FOR REFORM IN AGRICULTURE AND RURAL DEVELOPMENT

A. Introduction

1. Although Thailand's agriculture sector accounts for only 11 percent of the country's gross domestic product, it contributes significantly to export earnings (17 percent of total value in 1997). Also, a large proportion of the population still live in rural communities and are directly or indirectly dependent on agriculture. Hence, improved agricultural practices are critical for restoring export competitiveness and export-led growth, as well as for poverty reduction and reducing regional disparities. Three systems characterize Thailand's agriculture sector: the first system, concentrated in the central plains, is commercially oriented rice production; the second system, concentrated in the south, is high-value plantation crops such as rubber and oil palm, and upland crops such as pineapples, cassava, and tropical tree fruits; the third system, concentrated in the north, northeast, and (to a lesser extent) the south, consists of upland subsistence farming. This latter system has low productivity and gives rise to low incomes, poverty, social alienation, outward migration, and environmental degradation. Typically, farmers with no legal title produce low-value crops such as rainfed rice, cassava, maize, soybean, and a variety of minor crops. Their farming practices are generally unsustainable. The portion of the population engaged in this type of production may be as much as 20 percent but certainly includes almost all of the 12 percent of the country's total population living below the poverty line.

2. In terms of policy, rural development in Thailand entails putting in place an enabling environment for growth and transformation of the agriculture sector, as well as stimulating alternative income sources. The Government recognizes the strategic importance of this sector, particularly in the context of the current crisis, for promoting export led growth as well as for containing the adverse social impact of the crisis. However, the Government is also aware of the numerous structural weaknesses in the sector including distortions in the product market, the input supply systems and the land market; technological stagnation; the inadequate flow of credit and inadequate investment. The Government therefore proposes to introduce wide-ranging reforms to revive the agriculture sector.

B. The Bank's Operational Strategy in Agriculture

3. The Government has requested the Bank's assistance in reviewing the status of the sector and helping the Government to develop a broad-based program of institutional change and policy reform as part of a program loan. In line with its strategic objectives in the country, the Bank should respond positively, and assist the Government with comprehensive agriculture sector reforms. The priority areas of reform include the following:

1. Product Markets, Exports, and Import Substitution

4. Reforms should include the following:

- (i) Address the structure, conduct, and performance of major agricultural product markets, to eliminate distortions and improve the efficiency of markets.
- (ii) For all tradeable outputs and inputs of the agriculture sector, eliminate quantitative trade restrictions (QRs) and inefficient tariff/subsidy/pricing policies.

- (iii) Establish a timetable for tariff reduction and QR removal for Association of Southeast Asian Nations Free Trade Area-World Trade Organization compliance,
- (iv) Institute policy or institutional reforms and public investments that may be necessary in various subsectors to consolidate Thailand's cost competitiveness and dynamic comparative advantage in agricultural export markets, consistent with AFTA-WTO requirements.

2. Irrigation and Water Management

5. Activities should include the following:

- (i) Reform Government policies on irrigation and public and private irrigation systems to optimize the comparative strengths and weaknesses of each system.
- (ii) Introduce policy changes needed for integrated river basin development, as advocated in the Bank's water sector policy, to improve the efficiency of water use. Eliminate water shortages, keeping in view the nature of competition for water among industry, agriculture, and household sectors, and its impact on production and cropping patterns. Initiate measures for groundwater development and the conjunctive use of water, where appropriate.
- (iii) Initiate measures to improve the extent of cost recovery in public irrigation systems, taking into account its impact on agricultural prices as well as on conservation of water, possibly phasing in a system of irrigation water charges or alternative cost-recovery arrangements.

3. Land and Natural Resource Management

6. Activities should include the following:

- (i) Based on an assessment of the current systems of land holding, land use and land administration, and reforms under way for tenancy and land titling, introduce further land reform measures as necessary.
- (ii) To promote the consolidation of land holdings, and take advantage of economies of scale and mechanization, develop land banks, if appropriate.
- (iii) Introduce a policy agenda with milestones and responsibility centers, for improved natural resource management, specifically those that govern the management of watersheds, river basins, forest areas, and coastal zones, specifically focusing on policies related to conservation and rehabilitation of degraded ecosystems, including forests and coastal area environments.

4. Rural Credit and Savings Mobilization

7. Reforms should include the following:

- (i) Reform incentive systems and policies for the promotion of rural savings, together with institutional and other arrangements (including the Government Savings Bank). Evaluate the role of farmer organizations in administering the

funds, and review policies for utilization and recovery. Introduce policy measures to strengthen rural savings through volume expansion, better targeting of schemes for low-income groups, increase user participation particularly by farmers organizations, and improve recovery of funds.

- (ii) Reform present policies concerning rural credit keeping in view constraints on the availability of credit and its delivery in the context of current and forecast demand, and linkages between nonfarm rural activities that do not as yet qualify for credit from the Bank for Agriculture and Agricultural Cooperatives, and rural development.
- (iii) Eliminate barriers faced by target groups like women and the poor in accessing credit, possibly including the relationship between access to credit and the ownership of a regular title to land.
- (iv) Introduce measures for making long-term loans to leverage investments for new forms of farming with long-gestation crops.

5. Rural Labor Market and Employment

8. Introduce institutional or policy reforms, including the role of nongovernment organizations, to improve the functioning of the labor market, especially rural labor legislation, relief employment programs, and social monitoring systems.

6. Input Markets

9. Reforms should include the following:

- (i) Initiate reform of policies or institutions to improve the supply, quality, and price efficiency of inputs markets, including input production and distribution systems. This would entail the elimination of QRs as well as inefficient tariff/subsidy/pricing policies.
- (ii) Introduce measures to promote private investment in improved input supply or input quality.

7. Agricultural Research and Extension

10. Introduce appropriate policies or public investments to improve key institutional agencies engaged in agricultural research and development, and measures to promote private sector research and extension services.

8. Role of the Government

11. Introduce reforms and capacity-building measures in the Ministry of Agriculture and Cooperatives, and develop an effective regulatory framework that optimizes the development potential of the sector.

STRATEGIC DIRECTIONS FOR THE SOCIAL SECTOR

1. Bank operations in the social sector constitute the third key component of the Bank's operational strategy in Thailand. Interventions will simultaneously address two strategic objectives:

- (i) strengthening competitiveness to promote efficient, regionally balanced, and sustainable long-term growth; and
- (ii) improving the quality of life.

A. Education and Training

2. Thailand's earlier success in making primary education universal has not been replicated in the quality of secondary and higher levels of education. The transition rate from primary to secondary level has improved from less than 50 percent in the 1980s to about 90 percent in 1996. However, the enrollment rate has remained very low at 34 percent of the population aged 15-17 years. Also, there has been little improvement of quality in secondary education, especially in science and mathematics. Mainly due to the historical predominance of course offerings in the humanities and arts, and the tendency for teachers to marginalize difficult subjects, recent monitoring tests in mathematics and science have shown broad stagnation and decline. Enrollment in higher education remains heavily weighted toward the social sciences and humanities, with science and technology accounting for about 22 percent of total enrollment. The budgetary allocation for the education sector was increased to 21 percent of the national budget in FY1997. This is a welcome development. However, budgetary support for research and development activities at the university level has been piecemeal and inadequate. Vocational and skills-training programs have also largely been implemented without the active participation of the private sector in the planning, design, and execution of training programs. A placement rate (defined as the ratio of graduates who find jobs requiring the skills obtained) of 40 percent indicates the lack of relevance of training programs for the labor market.

3. As a consequence, there is growing concern regarding the mismatch between education and training systems and the evolving demands of the labor market, brought about by structural changes in the Thai economy, in particular the need to move away from labor-intensive production in which Thailand is no longer competitive. In addition to these long-standing issues, the present economic crisis has also given rise to various problems that could further weaken the education sector and labor market if remedial measures are not immediately put in place. The fallout from current financial difficulties will inevitably include (i) an increase in the incidence of school dropouts from all levels of education; (ii) reduced budgetary support for university research, and teacher development and training programs, including those in the private sector; and (iii) weakening of the financial viability of private institutions.

4. Recognizing the need to strengthen its human capital base, made more compelling by the current economic crisis, the Government has adopted a number of policy initiatives to address the underlying weaknesses of the Thai educational and training system. The new Thai constitution, approved in 1997, lays renewed emphasis on the importance of basic education by making education compulsory up to 12 years. A broad package of educational reforms is being pursued during the Eighth Plan (1997-2001), focusing on such key areas as (i) improvement of the quality and relevance of education, (ii) improvement of administration and management through decentralization and increased community participation, (iii) development of the teacher education system, (iv) expansion of science and technology education and improvement of the vocational training program through greater

private sector involvement, (v) restructuring of higher education by enhancing the autonomous status of universities, and (vi) increased private sector participation in the provision of educational services. Specific targets under the Eighth Plan include raising by 2001 (i) the share of the workforce with at least lower secondary education from the current 20 percent to at least 50 percent, (ii) increasing the share of science and technology enrollment to 40 percent, and (iii) raising the share of research and development investments from 0.2 percent to 0.75 percent of gross domestic product. To address the short- and long-term impacts of the financial crisis on the education sector and labor market, the Government has adopted several policy initiatives within the framework of a social sector program loan and two technical assistance (TA) grants provided by the Bank.¹

5. In line with the Bank's strategic objective to help Thailand develop a strong foundation for long-term competitiveness to ensure sustained and equitable economic growth, Bank lending and TA operations will support the development of human resources to overcome skill shortages and upgrade the technology base. Essentially, the Bank will assist the Government to (i) upgrade the skills of the country's labor force through the expansion of market-responsive vocational education and skills development programs; (ii) strengthen the role of higher education in promoting technical courses such as engineering, management, and the sciences; and (iii) expand and enhance the quality and relevance of secondary education. In all these areas, improving the skill profile of women in the workforce will be given particular emphasis. The Bank's agenda for policy discussions on increased private sector involvement in education and training, institutional and management reforms, and women-in-development have been facilitated through the Social Sector Program loan. Other short- and long-term structural issues of the education sector will be addressed through the accompanying TA (TA No.2996-THA). This TA will (i) improve the efficiency and equitable functioning of the student loan scheme, (ii) improve the efficiency of budgetary allocation, (iii) develop a more effective teaching personnel strategy, and (iv) develop an implementation strategy for the decentralization of managerial responsibilities to local government bodies in the education sector. The proposed higher education development project (1999) and nonformal secondary education project (2000) will enable the Bank to reinforce its role in enhancing the quality and relevance of Thailand's education and training sector, following the Skills Development Project that was approved in 1997. A second social sector program is also envisaged in 2001. It will be prepared on the basis of the ongoing accompanying TA, a project preparatory TA, and an advisory TA in 1999 that will review the economic and social impact of the financial crisis. A capacity-building TA is also proposed in 2000 to strengthen the role of the National Education Commission as the principal policymaking, planning, and coordinating arm of the Government for all levels of education.

B. Health

6. As a consequence of the Thai Government's political and economic commitment to improve the population's health status, health care services now reach virtually all communities through an extensive primary health care system. Health indicators are very favorable compared with other developing nations; and some indicators are at or are quickly approaching the levels observed in developed nations. Life expectancy at birth is now 67 and 72 for males and females respectively. Thailand has also experienced impressive reductions in infant and under-five mortality and maternal mortality. These are now 29 per 1,000, 32 per

¹ Loan No.1611-THA: *Social Sector Program*, for \$500 million, approved on 12 March 1998; TA No. 2995-THA: *Capacity-Building for Social Sector Reform*, for \$700,000, approved on 12 March 1998; and TA No. 2996-THA: *Education Management and Financing Study*, for \$700,000, approved on 12 March 1998.

1,000, and 1.6 per 1,000 respectively. Malnutrition levels fell from 51 to 25 percent from 1979-1986. They are likely to have fallen further during the past decade, although the trend may have been reversed during the past year of economic crisis. Also, health risks due to environmental pollution, drug abuse, and HIV/AIDS¹ remain major public health challenges. Moreover, although infant and child mortality has been reduced significantly, high rates still exist in pockets of the extreme south, the northeast, among hill tribes in the north, and among the urban poor, especially in Bangkok. The country is now beginning to experience a transition from communicable diseases to chronic and degenerative diseases due to its aging population. This epidemiological transition is also accompanied by the weakening of the traditional family-based support system. Consequently, strengthening of the public health system in combination with insurance and social security schemes has become urgent.

7. The economic crisis will increase the challenges in the health sector. First, the crisis will result in large numbers of workers losing their jobs, and along with that, medical cover for themselves and their families. Second, the tightening fiscal situation will restrict budgetary resources for programs that provide medical and public health services. While resources are likely to shrink, the pressure on medical and public health services is expected to increase in the coming months because people will substitute publicly provided services for more expensive private services. This will particularly influence the working of the low-income card scheme for health services and will adversely affect the welfare of the poor and disadvantaged. Finally, the crisis will increase prices of almost all health inputs, especially imported pharmaceuticals. Consequently, the ability to acquire paid health services will decline, particularly among low income groups. The health sector will need to improve its allocative and technical efficiency to take on the new challenges. A major component of the recently approved Social Sector Program loan is designed to address these challenges. The ongoing TA on health management and financing² will support the Government in undertaking health sector reforms that will rationalize various health financing schemes, reduce rural-urban disparities in the deployment of personnel, and improve efficiency of the health system. It is proposed that a second phase of lending for health sector reforms will be initiated in 2001, based on this accompanying TA, a project preparatory TA, and the results of an advisory TA, scheduled for 1999, which will assess the economic and social impact of the economic crisis.

C. Waste Management and Water Supply

8. Urbanization and industrialization have led to acute water supply and quality problems in Thailand. The piped water supply sector has expanded its coverage during the last decade in the Bangkok Metropolitan Region and other urban areas, achieving 80-90 percent coverage, but in provincial urban centers and villages, about 60 percent of the population remains unserved. Although environmental sanitation in most provincial centers is reasonably good, as evidenced by the low incidence of illness caused by waterborne diseases, wastewater is inadequately treated and polluted wastes are often discharged untreated into the natural environment. Pollution of water bodies from domestic, commercial, and industrial sources is rapidly reaching extreme levels in most urban centers, and there is an urgent need for major increases in investment to meet both municipal and industrial water supply and sanitation development requirements.

9. The level of Bank financial and TA for waste management and water supply development in provincial towns and cities will remain significant in the medium term. Consistent

¹ HIV/AIDS is Human Immunodeficiency Virus/Acquired Immune Deficiency Syndrome.

² TA No. 2997-THA: *Health Management and Financing Study*, for \$700,000, approved on 12 March 1998.

with this approach, a solid waste management project is included in the loan pipeline for 1999-2001, in addition to a supplementary loan for the Samut Prakarn Wastewater Management Project in 1998. A solid waste management project is programmed for selected urban growth centers in the north, northeast, and southern regions of the country in 2001. A border towns project (2001) is intended to improve urban management, infrastructure, and services in several tertiary cities. The pipeline also includes a TA for locally administered water supply in 2001.

STRATEGIC DIRECTIONS FOR ENVIRONMENT-RELATED OPERATIONS IN THAILAND

A Introduction and Key Environmental Problems

1. Thailand is a country in transition from an agrarian to an industrial economy and, due to inadequate allocations of effort and resources to the rational management of environmental resources and urban growth, is currently facing a variety of environmental problems common to both developing and industrialized nations.¹ A number of key environmental problems are readily identified, and virtually all are derived from a basic set of underlying issues. The major current environmental problems in Thailand include the following:

- (i) Water pollution: this is a significant problem throughout Thailand from agricultural, industrial, municipal, and household wastes, resulting in reduced clean water supplies, and reduced aquatic productivity and depleted fisheries.
- (ii) Water use conflicts: formerly plentiful and free, clean water is now a scarce resource for which demand exceeds supply, resulting in conflicts especially between agricultural use and urban and industrial use, which could have significant environmental implications.
- (iii) Air pollution: this is a serious problem in Bangkok due to heavy traffic and construction, and can be a problem also in the vicinity of fossil fuel power plants and industrial zones.
- (iv) Urban and industrial wastes: Thailand does not yet have adequate incineration and other treatment facilities to handle locally produced solid wastes, including hazardous and toxic wastes, nor sufficient safe landfills and other long-term disposal options for solid wastes.
- (v) Deforestation: Thailand's forest cover, including all classes, is roughly estimated at about 25 percent of the total land area, less than 13 million hectares (ha), and is still slowly declining (estimated at 160,000 ha/yr) despite a logging ban since 1988; this is resulting in climate change, watershed degradation, biodiversity losses, and other disbenefits.
- (vi) Degradation of coastal resources: mangrove forests especially have been decimated due primarily to recent extensive prawn farm development, resulting in deforestation, fish stock depletions, increasing coastal erosion, and other problems.

¹ Environmental problems and projects are often subdivided into three color-coded classes: (i) *brown* - dealing with waste management, both liquid and solid, primarily from domestic, municipal, and industrial sources; (ii) *green* - focusing on the preservation of the natural environment and especially living natural resources; and (iii) *blue* - water supply and water resources management. Some environmental projects may span two or even all three of the classes; while some focus on other issues that may not fit easily into any of the three classes, such as capacity building (environmental training) or institutional strengthening (the development of environmental laws and regulations).

- (vii) Degradation of land and soil: in some parts of the country, and especially in deforested mountainous areas in the north and areas planted to cassava in the northeast, land has become unproductive due to soil erosion, salinization, and other problems.

B. Basic Issues and Strategies to Address Key Environmental Problems

2. There is a fundamental set of issues that has contributed to the development of the environmental problems facing Thailand (and other developing countries). To help solve these and to prevent their recurrence, the underlying facilitating conditions or issues also need to be addressed. Some of the more important issues are

- (i) population management, including both the rate of growth of the population, and its spatial distribution (urbanization);
- (ii) poverty reduction, to enable the poor to choose more environmentally benign ways of life;
- (iii) the need to develop greater environmental understanding and a stronger environmental ethic among the public;
- (iv) the insufficient supply of trained environmental professionals in both the public and private sectors;
- (v) the need to sustainably manage traditionally open access or common property resources, and to stop the mining (permanent depletion) of renewable resources;
- (vi) the need for a strong legal basis and institutional framework in the environment sector, backed up by enforcement; and
- (vii) how to develop cost-recovery and funding mechanisms for environmental programs.

These fundamental issues are of common concern to the Bank's developing member countries, but to varying degrees. And all are cross-sectoral issues that normally are not addressed by environment agencies, but that call for strong support from the environment sector to stress the urgent need for attention.

C. Bank's Strategic Approach

3. In assisting the Government to address some of these key environmental issues a two-track strategy will be pursued. First, wherever appropriate, environmental goals will be included as secondary objectives, and environment components will be built into loan projects that are not primarily environment projects. This is the only route to mainstream environmental concerns as Thailand is unlikely to borrow at ordinary capital resources rates for purely environmental loan projects. The proposed agriculture sector program loan may be appropriate for this approach. The second track of the strategy will include a series of capacity-building TAs to strengthen the regulatory framework and enhance the capability of the environment management authorities in Thailand.

Thailand
Table 2: Technical Assistance Pipeline, 1998-2001

Sector	Type	Title	Project Division	\$'000
1998 (IPF: \$2 million)				
Agriculture	ADTA	Agriculture Sector Needs Assessment Study	AWFN	150
Environment	ADTA	Promotion of Market-based Instruments for Environment Management	ENVD	605
Social Infra	ADTA	Health Management and Financing Study (piggy-backed)	AWEH	700
Social Infra	ADTA	Capacity Building for Social Sector Program (piggy-backed)	AWEH	700
Social Infra	ADTA	Education Management and Financing Study (piggy-backed)	AWEH	700
Finance	ADTA	Banking Sector Restructuring	IWFI	1,000
Total				3,855
1999 (IPF: \$2 million)				
Transport	PPTA	Northeast Region Area Development	IWTC	850
Agriculture	ADTA	Institutional Strengthening for Water Sector Management	AWFN	600
Agriculture	ADTA	National Forestry Management Review	AWFN	500
Energy	ADTA	PEA Corporate Planning for Privatization	IWEN	400
Multisector	ADTA	Assessment of Economic and Social Impact of the Financial Crisis	PW3	900
Others	ADTA	Capacity Building in Loan Policy and Management Division	PW3	400
Total				3,650
2000 (IPF: \$2 million)				
Agriculture	PPTA	Watershed Management in North, Northeast and South Regions	AWFN	1,000
Social Infra	ADTA	Strengthening National Education Commission and Sector	AWEH	500
Environment	ADTA	Capacity Building for Regional Environment Offices	ENVD	900
Others	ADTA	Capacity Building of Local Governments in Resource Mobilization	PW3	400
Total				2,800
2001				
Others	ADTA	Civil Service Reform: Phase 1	PW3	450
Social Infra	PPTA	Locally Administered Water Supply	AWWU	600
Multisector	ADTA	Review of the Thailand Adjustment Program	PW3	900
Total				1,950

Note: Shaded portion shows approved TA projects.

THAILAND
1998-2001 Lending Program
Sectoral Distribution

Loans (Scenario 1)

Sector	No. of Loans	Loan Amount	%
		(\$ million)	
Agriculture/Agro Industry	1	300	18
Social Infrastructure	6	640	39
Transport and Communications	1	100	6
Finance	2	600	37
Total	10	1,640	100

THAILAND
1998-2001 Lending Program
Strategic Development Objective

Loans (Scenario 1)

Sector	No. of Loans	Loan Amount	%
		(\$ million)	
ECONOMIC GROWTH	2	600	37
SOCIAL/ENV CONCERNS	8	1,040	63
Total	10	1,640	100

Figure 3: Performance Assessment and Monitoring System

Impact	Indicators	Monitoring Instruments
A. Financial Sector		
* Improvement of the legal and regulatory framework	* Tightening of capital adequacy and provisioning norms	* Bank of Thailand bulletins
* Restructuring of the financial sector	* Improvement in NPL ratios	* IMF/World Bank staff reviews
* Recapitalization	* Enhanced flow of liquidity	* Bank CER and economic updates
	* Growth recovery	* EFF monitoring system
		* IWFI TAs
		* PW3 Crisis Impact Review TA and Structural Adjustment Assessment TA
B. Agricultural, Natural Resources and Rural Development		
* Policy reforms	* Growth of production	* National accounts statistics
* Institutional reforms	* Growth of exports	* Production, export, and productivity data
* Improved productivity	* Rise in yields	* Forestry and irrigation statistics
* Improved management of natural, human, and financial resources	* Increase in forest cover	* Wage and employment data
* Improved management of inputs	* Increase in irrigation cover, reduced flooding	* Rural credit data
* Development of research and extension systems	* Rising rural wages, lower unemployment	* IMF/UN/World Bank reviews
	* Greater flow of rural credit	* Bank CER and economic updates
	* Improved flow of research and extension services	* AWAR/AWFN TAs
		* PW3 Crisis Impact Review TA and Structural Adjustment Assessment TA
C. Social Sector Development		
* Improvement of regulatory framework for education and health services	* Improved literacy and education status	* Poverty and well-being indicators from PW3 TA No. 2744
* Better delivery of public sector education and health services	* Improved employment and wage indicators	* Official education statistics
* Better private sector delivery of education and health services	* Improved demographic indicators	* Official health statistics
	* Improved nutrition and health indicators	* National accounts, wage and employment data
	* Reduced incidence of infectious and life-threatening diseases	* IMF/UN/World Bank reviews
		* Bank social sector profile
		* AWEH TAs
		* PW3 Crisis Impact Review TA and Structural Adjustment Assessment TA
D. Cross-Cutting Concerns: Poverty, Gender, Environment, Governance, & Private Sector		
* Reduction of poverty	* Poverty estimates	* Official reports on cross-cutting concerns
* Improvement of the status of women in development	* Well-being indicators	* Data on poverty, wage, employment, status of women
* Improved quality of the environment	* Gender-specific wage and employment estimates	* Forestry and environment statistics
* Greater accountability, transparency, and efficiency in governance	* Indicators of social and political status of women	* Poverty and well-being indicators from Programs Department West Division 3 TA No. 2744
* Recovery and growth of private enterprise, reduced Government role in	* Air and water quality indicators	* IMF/UN/World Bank reports on cross-cutting concerns
	* Forestry cover indicators	* Bank social sector profile, environment profile, WID briefing
	* Polls and commentaries on quality of governance	* Relevant AWD TAs
	* Human rights and crime indicators	* PW3 Crisis Impact Review TA and Structural Adjustment Assessment TA
	* Private enterprise size indicators	

AWAR = Agriculture and Rural Development Division West; AWD = Agriculture and Social Sectors Department; AWEH = Education, Health and Population Division West; AWFN = Forestry and Natural Resources Division West; CER = Country Economic Review; EFF = Export Financing Facility; IMF = International Monetary Fund; IWFI = Financial Sector and Industry Division West; PW3 = Programs Department West Division 3; UN = United Nations.