Thailand

Fractious politics aggravated the impact of the global recession on this economy, which contracted steeply in 2009 despite expansionary fiscal and monetary stances. Consumer prices fell over the year. The pace of recovery is expected to be moderate in 2010, in light of political tensions that will likely cause some delays in a government infrastructure program. Inflation will quicken and the current account is likely to record a surplus. Economic growth is forecast to pick up in 2011, based on stronger exports and investment.

Economic performance

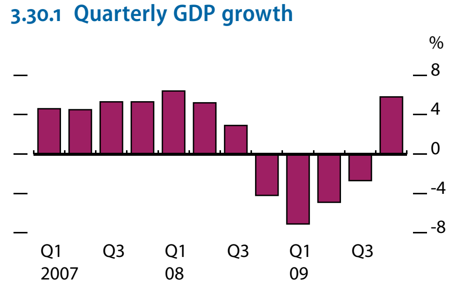
The impact of the global recession, coupled with a fractious domestic political setting, caused this economy to contract by 2.3% in 2009, the deepest decline in Southeast Asia last year. A steep slide in exports led to cutbacks in manufacturing and in investment. Then, antigovernment street protests in April 2009, coming after a long period of rising political tensions, eroded consumer sentiment and aggravated a decline in tourism prompted by recession in industrial countries. GDP contracted for 4 consecutive quarters year on year, then sprang back in the fourth quarter of 2009 (Figure 3.30.1).

Manufacturing production fell by 5.1% in 2009, a result of the slide in export demand. Worst-hit industries were those making capital goods and higher-technology products such as automobiles and electrical appliances. These industries led the recovery in the fourth quarter, when export demand rebounded. Construction activity started to pick up in the second quarter as the government accelerated public works under two fiscal stimulus packages aimed at cushioning the impact of the global forces on the economy. For the full year, though, construction output was flat. Total industrial output fell by 4.3% (Figure 3.30.2).

Weak consumer confidence and declining tourist arrivals contributed to a 0.4% fall in services output last year. Tourist arrivals fell for most of the year, then rebounded in the fourth quarter, but still showed a full-year decline of about 3%. The services subsectors of hotels and restaurants and transport and communications fell particularly sharply from the fourth quarter of 2008 through the third quarter of 2009. Even agriculture had a bad year in 2009, with production down by 0.6% owing, on the one hand, to price declines, notably for paddy, cassava, maize, and natural rubber, and, on the other, to pest infestations.

Private consumption contracted by 1.1% in 2009, crimped, particularly in the first half, by the weaker labor market, declines in farm incomes, and the political strife. Consumer sentiment improved in the second half, when the government rolled out fiscal stimulus measures, employment started to pick up, and prices for farm products bottomed. In contrast

3.30.1 Quarterly GDP growth



Source: CEIC Data Company (accessed 23 February 2010).
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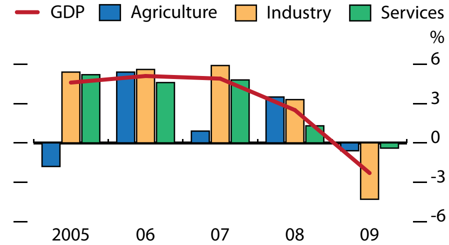
3.30.2 GDP growth by sector



Source: CEIC Data Company (accessed 23 February 2010).
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This chapter was written by Luxmon Attapich of the Thailand Resident Mission, ADB, Bangkok.

to private consumption, public consumption spending rose by 5.8% in 2009, as the government ratcheted up its outlays, including the stimulus measures.

Investment was a major drag on GDP in 2009. Fixed capital investment fell by 9.0%, and the private sector segment dropped even more sharply, by nearly 13% (government fixed investment rose by about 3%). Fixed investment in construction was virtually flat, but that in equipment fell by 13.4% as companies cut back on expansion and reequipment plans. The contraction in private fixed investment slowed in the fourth quarter (Figure 3.30.3).

Net exports were positive in 2009 because real imports fell much more sharply than exports.

An expansionary fiscal policy played an important role in moderating the recession. The first stimulus package of B116 billion ($3.4 billion) was implemented from March 2009. It included monthly cash payments of B2,000 a person for about 9 million low-income earners, assistance for the aged, and extra spending on skills training and public health programs. Businesses received tax breaks for small and medium-sized firms and the property and tourism industries, and certain businesses were given access to concessional loans. Altogether, this package was valued at the equivalent of 1.3% of GDP.

A second stimulus package that could cost as much as B1.43 trillion ($42 billion) is being implemented over 3 fiscal years starting from October 2009. This program, named Thai Khem Kaeng, or Strong Thailand, covers public investment mainly in infrastructure such as transportation, water, and energy, as well as extra funding for health, education, and tourism. The planned outlays represent about 5% of GDP for each of the 3 years.

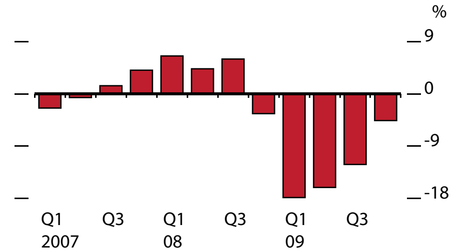
State enterprises are responsible for driving around one-third of the infrastructure program over the 3 years. Most of the funding for the infrastructure will be off budget, sought from domestic debt markets and public–private partnerships, supplemented by budget funds. However, disbursement of the Thai Khem Kaeng program got off to a slow start in the fourth quarter of 2009.

Additional government spending in FY2009 (ended 30 September 2009), at a time of subdued growth in revenue, widened the budget deficit to the equivalent of 4.3% of GDP, from just 0.4% in FY2008.

Lower prices for imported oil and commodities, and weak domestic demand, brought down inflation in 2009 from high levels in the prior year. Government concessions introduced in 2008 to help those on low incomes (such as free electricity, water supply, and public transportation) contributed to downward pressure on prices. The consumer price index fell for much of the year, then turned up late in the year (Figure 3.30.4) when oil prices rose.

Fading inflation and the weak economy prompted the Bank of Thailand to cut its policy interest rate by 250 basis points, to 1.25%, between early December 2008 and April 2009. Credit growth was sluggish, though—private credit rose by only 3% in 2009, and most of that was for households. The government directed state-owned financial institutions to step up their lending, particularly to small businesses facing a credit squeeze.

3.30.3 Private fixed investment growth



Source: CEIC Data Company (accessed 23 February 2010).

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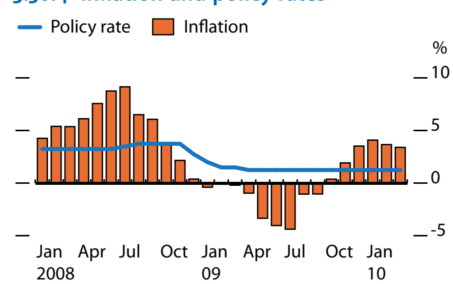
3.30.4 Inflation and policy rates



Source: CEIC Data Company (accessed 8 April 2010).

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Merchandise exports fell by 13.9% in US dollar terms last year, reflecting the slump in external demand (Figure 3.30.5), especially in industrial countries (exports to the People's Republic of China and India were little changed from 2008). Sharp falls were recorded in both manufactured and agricultural exports. The slide hit bottom in the first half, and by November exports had rebounded on a year-on-year basis. Imports tumbled by nearly 25% in 2009, a result of the slump in manufactured exports (which require imported raw materials), weak domestic demand, and lower prices for oil and commodities.

Partly as a consequence of the steep drop in imports, the trade balance showed a record surplus of $19.4 billion. With balances in services, income, and transfers close to 2008 levels, the trade surplus pushed up the current account surplus to the equivalent of 7.7% of GDP. Net outflows in the capital account slowed last year from 2008 to $1.3 billion. By year-end, foreign reserves were up by nearly 25% to $138.4 billion, or 10.6 months of import cover (Figure 3.30.6).

Large current account surpluses during the year contributed to a 4.1% appreciation of the baht against the US dollar in 2009 (Figure 3.30.7), and a rise of about 0.4% in its nominal effective exchange rate. The Bank of Thailand in August eased regulations on Thai investment in foreign securities to facilitate capital outflows and ease upward pressure on the baht. The Thai stock market hit its nadir in March 2009 and rallied strongly (up by 63% over the year), in line with other Asian markets.

Nevertheless, Standard & Poor's lowered Thailand's local currency debt rating from A to A- in April 2009, while Fitch downgraded the long-term foreign currency rating to BBB that month, on the ground that political uncertainty undermined the ability of the government to implement policies.

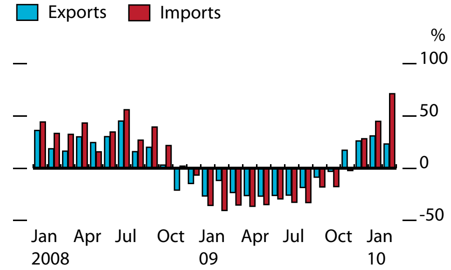
Economic prospects

The forecasts assume that there will be no severe political disruptions in the next 2 years, and that national elections to be held later in 2010 will go smoothly.

It is also assumed that a serious legal wrangle, which led to the suspension of $12 billion of projects at the Map Ta Phut industrial estate on Thailand's eastern seaboard, and has created uncertainty about environmental regulations, will be resolved soon. The new Thai constitution that came into effect in 2007 requires that certain industries conduct health impact assessments on new projects. But laws to implement this provision were not put in place and the assessments not done. In a case backed by residents and environmental activists, a Thai court ruling in September 2009 suspended the projects, which are mainly in petrochemicals, steel, and power plants. Some were later allowed to proceed, but most remained suspended in March 2010. The government is working to resolve the problem so the projects can proceed this year, and so new investors face a more certain regulatory environment.

On this basis, the economy is expected to recover this year, but probably at the mild pace of about 4.0% (Figure 3.30.8), even though it comes off a low base (GDP in 2009 was barely above that of 2007). Growth is forecast to pick up to 4.5% in 2011 as exports and investment strengthens.

3.30.5 Merchandise trade growth



Note: Based on customs data.
Source: CEIC Data Company (accessed 31 March 2010).
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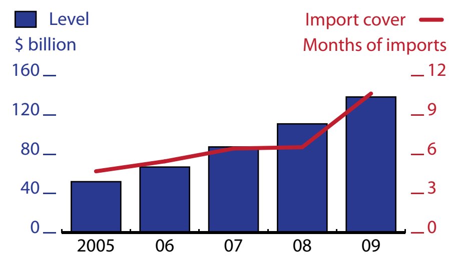
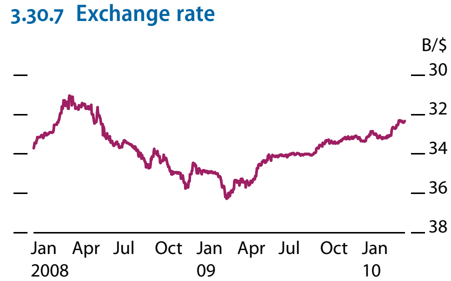
3.30.6 Gross international reserves



Sources: Bank of Thailand. http://www.bot.or.th (accessed 8 March 2010); *Asian Development Outlook* database.
Click here for figure data

3.30.7 Exchange rate



Source: Bloomberg (accessed 31 March 2010).
Click here for figure data

3.30.1 Selected economic indicators (%)

	2010	2011
GDP growth	4.0	4.5
Inflation	3.5	3.0
Current account balance (share of GDP)	4.0	2.0

Source: ADB estimates.

The rebound in exports that started late last year will accelerate in 2010, boosting manufacturing production, employment, and investment. Industries like electronic products, household appliances, and motor vehicles are benefiting from inventory restocking in industrial economies and strong growth in many Asian countries.

Private consumption is forecast to rise by about 3% this year. It is getting support from growth in employment and wages (minimum wages were raised in January 2010), increases in rural incomes based on higher prices for agricultural products, and rising consumer confidence (Figure 3.30.9). Sales of automobiles soared by just over 60% in January, and motor cycle sales jumped by 24% (from a low base in the prior-year period).

Investment will recover from last year's low levels, and is expected to move up by about 6% in 2010, quickening in 2011. Stronger export demand has led to a rise in industrial capacity utilization (Figure 3.30.10), which, if continued, will pave the way for an expansion of capacity in industries such as food processing, petroleum products, and construction materials.

Interest rates are expected to stay relatively low, and growth in credit is edging up this year. The infrastructure program should stimulate private investment, particularly in construction and buildings materials. The Board of Investment reported a surge in applications for investment incentives late last year, and the index of business confidence has turned up. Nevertheless, the recovery in investment will be constrained for at least part of 2010 by uncertainties over the election and the Map Ta Phut issue.

Political protests in the streets of Bangkok during March and April 2010 set back the recovery in tourism, but arrivals for 2010 are still expected to rise from last year's levels.

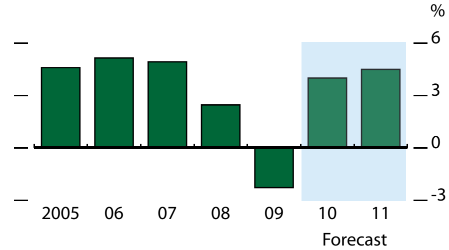
Fiscal policy will be expansionary this year, with the extent of the stimulation depending in large part on the ability to disburse budget and infrastructure funds. The government has budgeted for a reduction in spending in FY2010 and an increase in revenue, with a deficit target of 2.7% of GDP. The budget will be supplemented by the off-budget spending on the Thai Khem Kaeng program. Furthermore, the budget proposed for FY2011 (starting in October 2010) includes a significant increase in spending over the FY2010 level.

However, disbursement of the Thai Khem Kaeng program has sputtered. Of B486 billion ($14.5 billion) allocated for FY2010, only about 22% was disbursed in the October 2009–March 2010 fiscal half-year. The government will need to accelerate disbursement of the infrastructure program if it is to meet its target spending for FY2010.

Political tensions have caused delays as meetings on investment projects were postponed. The government is likely to be cautious in approving projects and disbursing funds during periods of disruption. Moreover, cases of alleged corruption have delayed disbursement in health and education projects.

Merchandise exports are forecast to increase by 16.0% in 2010 and merchandise imports by 26.0% from last year's low base. (Customs based exports rose by 27% and imports by 58% in the first 2 months of 2010.) The trade surplus is projected to decline and the current account surplus will fall to a still sizable 4.0% of GDP this year.

3.30.8 GDP growth



Source: Asian Development Outlook database.

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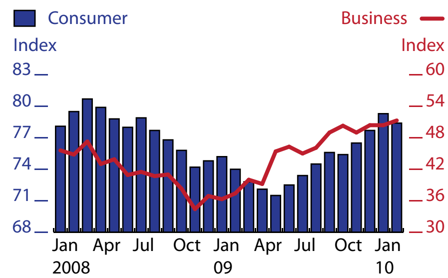
3.30.9 Consumer and business attitudes



Note: A reading of less than 100 for consumer confidence and less than 50 for business sentiment denotes a deterioration.

Source: CEIC Data Company (accessed 31 March 2010).

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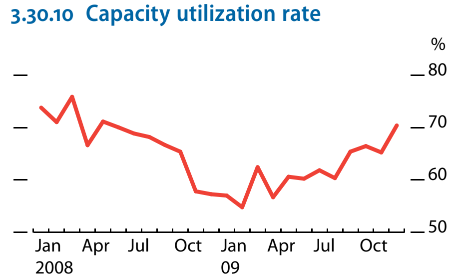
3.30.10 Capacity utilization rate



Source: Bank of Thailand. http://www.bot.or.th (accessed 5 March 2010).

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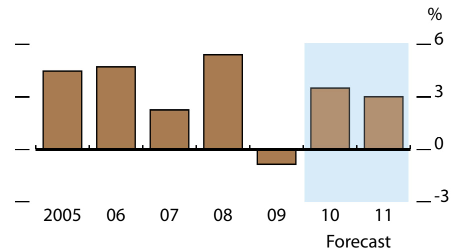
Inflation is forecast to rise to 3.5% in 2010 (Figure 3.30.11), due mainly to higher food and fuel prices. The rate for the first quarter was 3.7%, but core inflation, excluding food and energy prices, remained within the central bank's target range. The government again extended the fee-free electricity, water, and public transportation for low income earners, this time through to June 2010.

The Bank of Thailand is expected to gradually move its policy interest rate up to more normal levels, from the exceptionally low level set in 2009. It also appears likely to favor a moderate appreciation of the baht against the US dollar, in line with other Asian currencies, as a means of keeping inflation in check. In February 2010 the central bank eased foreign-exchange rules on overseas investment and hedging transactions in a further move that is expected to facilitate capital outflows.

Downside risks to the forecasts from domestic factors are headed by the political tensions and uncertainty, which if prolonged, could further delay fiscal implementation and hamper policy making in general. More significant disruptions would hurt consumer and investor sentiment, and fiscal revenue. On the other hand, a more settled political situation and resolution of the Map Ta Phut issues would likely spur stronger growth.

3.30.11 Inflation



Source: Asian Development Outlook database.
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Development challenges

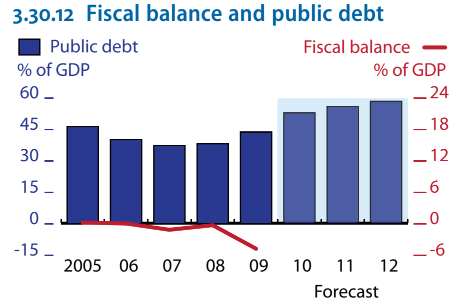
Investment in infrastructure has lagged during the past 4 years, in large part a result of the political turbulence. Thailand's rank in terms of infrastructure in the 2009 IMD World Competitive Yearbook fell to 42 of 55 countries, from 39 in the previous year. A $40 billion "megaprojects" infrastructure plan prepared in 2005 was only partly implemented. The challenge is to do better with the Thai Khem Kaeng program, which also involves about $40 billion in projects, although they are mostly smaller and more manageable than the previous plan.

Reforms in the regulatory environment to encourage public–private partnerships would increase the private sector's contribution to infrastructure. The establishment of a high-level committee on public-private partnership issues chaired by the deputy prime minister has been an important step in this direction. What is needed now are clear policy framework guidelines for assessing bankable projects, and transparent regulations and procedure for private sector participation.

The government has the scope to borrow to fund much of its contribution to infrastructure. Public debt is at manageable levels—it rose last year to the equivalent of 43.9% of GDP (90% domestic) and is projected to peak at 58.5% in 2012 (Figure 3.30.12), then decline as economic growth accelerates. Total external debt has declined to about 27% of GDP, from over 70% a decade ago, and foreign reserves have increased by $100 billion in this period.

Still, the fiscal deficit and public debt need to be reined in when economic growth is stronger and sustained. (At this stage, the government aims to run budget deficits through 2014.) Broadening the tax base would be helpful in this regard.

3.30.12 Fiscal balance and public debt



Sources: Bank of Thailand. http://www.bot.or.th (accessed 8 March 2010); *Asian Development Outlook* database.
Click here for figure data