

# **THAILAND ECONOMIC MONITOR**

## **APRIL-JUNE 2009**

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## **ABBREVIATIONS**

<b>ACMECS</b>	Ayeyawady-Chao Phraya-Mekong Economic Corporation Strategy
<b>ARMS</b>	Advanced Resilient Matching System
<b>ASEAN</b>	Association of Southeast Asian Nations
<b>ASSET</b>	Automated System for the Stock Exchange of Thailand
<b>BAAC</b>	Bank for Agriculture and Agricultural Cooperatives
<b>BIMSTEC</b>	Bay of Bengal Initiative for MultiSectoral Technical and Economic Cooperation
<b>BIS</b>	Bank for International Settlement
<b>BOB</b>	Bureau of Budget
<b>BOI</b>	Board of Investment
<b>BOP</b>	Balance of Payments
<b>BOT</b>	Bank of Thailand
<b>CDS</b>	Credit Default Swaps
<b>CMDF</b>	Capital Market Development Fund
<b>CPI</b>	Consumer Price Index
<b>CSMBS</b>	Civil Service Medical Benefit Scheme
<b>DALY</b>	Disability-adjusted Life Year
<b>DPA</b>	Deposit Protection Agency
<b>ETF</b>	Exchange-traded Fund
<b>EU</b>	European Union
<b>EXIM Bank</b>	Export-Import Bank of Thailand
<b>FDI</b>	Foreign Direct Investments
<b>FIBA</b>	Financial Institution Business Act
<b>FIDF</b>	Financial Institutions Development Fund
<b>FPO</b>	Fiscal Policy Office
<b>FSMP</b>	Financial Sector Master Plan
<b>FTA</b>	Free Trade Agreements
<b>FY</b>	Fiscal Year
<b>GDP</b>	Gross Domestic Product
<b>ICT</b>	Information and Communications Technology
<b>JTEPA</b>	Japan-Thailand Economic Partnership Agreement
<b>KEI</b>	Knowledge Economy Index
<b>KPIs</b>	Key Performance Indicators
<b>LGO</b>	Local Government Organizations
<b>LTF</b>	Long Term Fund
<b>MOC</b>	Ministry of Commerce
<b>MOPH</b>	Ministry of Public Health
<b>MTEF</b>	Medium Term Expenditure Framework
<b>NCB</b>	National Credit Bureau

<b>NCD</b>	Non-Communicable Diseases
<b>NEER</b>	Nominal Effective Exchange Rate
<b>NESDB</b>	National Economic and Social Development Board
<b>NHSO</b>	National Health Security Office
<b>NPLs</b>	Non-performing loans
<b>NSO</b>	National Statistic Office
<b>OCSC</b>	Office of Civil Service Commission
<b>OECD</b>	Organization for Economic Cooperation and Development
<b>OPDC</b>	Office of Public Development Commission
<b>REER</b>	Real Effective Exchange Rate
<b>RMF</b>	Retirement Mutual Fund
<b>ROH</b>	Regional Operating Headquarters
<b>SET</b>	Stock Exchange of Thailand
<b>SMEs</b>	Small and Medium Enterprises
<b>SML</b>	Small-Medium-Large
<b>SOEs</b>	State-owned Enterprises
<b>SSO</b>	Social Security Office
<b>SSS</b>	Social Security Scheme
<b>TCH</b>	Thailand Clearing House Co., Ltd.
<b>TFEX</b>	Thailand Futures Exchange
<b>TSD</b>	Thailand Security Depositary Co., Ltd.
<b>UC</b>	Universal Coverage Scheme
<b>WB</b>	World Bank
<b>WTO</b>	World Trade Organization
<b>yoy</b>	Year-on-year

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## SECTION 1

# OVERVIEW

**A solid financial armor could not protect Thailand against the impact of the global financial crisis on its real economy.** Despite a sound banking system and low external vulnerabilities, the Thai economy contracted 5.7 percent between October 2008 and March 2009, as the magnitude and speed of the contraction in foreign demand – and resulting shock to the real economy – has been greater than anticipated. There continues to be little impact of the global financial crisis on Thailand's banks: liquidity remained adequate as financial institutions did not face solvency concerns given their adequate capitalization and lack of exposure to “toxic” assets or risky derivative contracts. The combination of a sound financial sector, low external roll-over and balance-of-payment financing requirements, and, more recently, large current account surpluses, has led to capital inflows, build-up in reserves and an appreciation of the Baht relative to other currencies in the region. However, the impact of the global crisis on the real sector was far more severe than expected. Export volumes contracted by 8.9 percent in the fourth quarter of 2008, compared to the World Bank's forecast in December of a 3.0 percent expansion. Exports contracted a further 16 percent in the first quarter of 2009. The aggravation of Thailand's political crisis, which had been dampening investor and consumer confidence since 2006, compounded the shock to the real economy. As a result, real GDP contracted in the fourth quarter of 2008 and first quarter of 2009 after 38 quarters of growth, and is expected to contract for 2009 as a whole, the first annual contraction since the Asian financial crisis of 1997/1998.

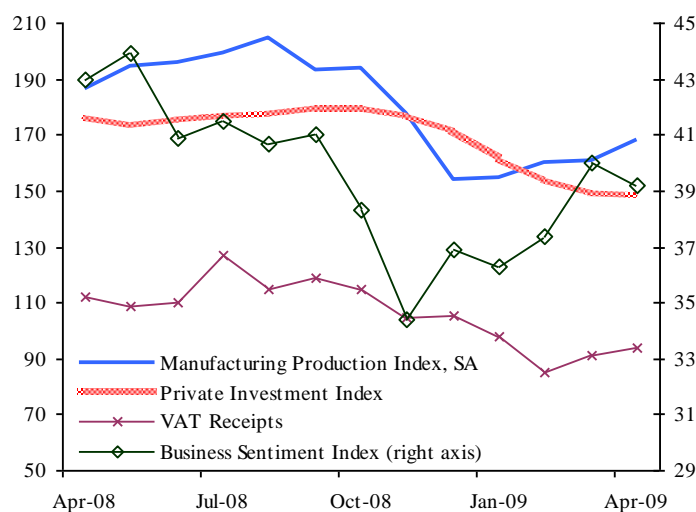
**Despite some recent signs of improvement, real GDP is projected to contract by 2.7 percent in 2009 as the global outlook remains negative and the shock to external demand propagates to the domestic economy in a negative multiplier effect.** Fiscal stimulus and monetary expansion may partially mitigate the impact of the slowdown, and signs of recovery in the global economy, including a possible bottoming out of trade volumes, support the view that positive growth may return in the fourth quarter of 2009. There are a number of downside risks, however. Although the political unrest that erupted in mid-April seems to have had limited impact on the economy, renewed tensions could further worsen the outlook for the year. In addition, whereas employment and purchasing managers' index data for April and May seem to point to stabilization in the global economy, much uncertainty remains about the sustainability of the recovery, and substantial risks remain of new negative developments that could lead to a more negative outlook for the second half of 2009 and 2010.

**Thailand's immediate prospects depend primarily on an improvement in external demand.** With domestic consumption subdued because of heightened uncertainties about employment prospects and political uncertainty, the pace of recovery of the Thai economy in 2009 will depend on a pick-up in external demand. Recent signs have been mostly encouraging, even if risks remain elevated. The pace of export contraction to ASEAN and China has declined in the first four months of 2009 compared to the last quarter of 2008, although exports to the “G3” (EU, the US and Japan) have, on aggregate, contracted at a faster pace (see Section 2.4.1). This reflects the recovery in China, which has been fairly robust. Stabilization in the economies of the G3, through its direct impact on Thai exports, as well as on Thailand's East Asian trading partners, remains essential to a recovery in Thailand. On that front, there are mixed signs: purchasing managers' and employment data have shown marked improvements in April and May, but at this point it is still unclear whether increases in industrial production are due to restocking or a more sustainable recovery.

**Fiscal policy has become expansionary and will help mitigate the impact of the crisis.** The government has announced two sets of stimulus measures, one of 1.5 percent of GDP targeted at FY09 (announced in January) and a plan for FY10-12 that focuses heavily on public investment and could add as much as 2.3 percent of GDP on average per year. Public investment has been sluggish since the 1998 crisis, but is expected to increase in 2009 given the political imperative to respond to the slowdown in the export sector. In the last twelve months ending in March 2009, public investment contracted by over 7 percent in real terms, largely as a result of political uncertainties, which delayed investment decisions. There is potential for government to catalyze private investment in the process of expanding public investments, but this will depend on effective and timely execution of investments, as well as an effective framework for private participation in public projects.

**Recent data suggests a possible bottoming out of economic activity, but it is unclear whether the pick-up can be sustained.** As shown in Figure 1, the Manufacturing Production Index (MPI) and the Business Sentiment Index (BSI), which also tracks manufacturing production, bottomed between November and January, and posted at least three months of month-on-month improvement until April. The decline in the BSI in April may not be informative given the political unrest that took place, and manufacturing production continued to improve on a seasonally-adjusted (SA) basis. The private investment index stabilized in April, although it still posted a decline for the sixth consecutive month. On the positive side, VAT receipts, a key indicator of private consumption, has been on an upward trend since bottoming in February. While consumer confidence continued to decline in April, the increased VAT receipts reflect that the fiscal stimulus disbursements of late March and early April have been put to work, which would have a positive multiplier effect on the economy. The key question remains whether the pick-up in production reflects an adjustment to over-shooting in the first quarter, but to a lower level of production, or a sustained recovery towards long-term year-on-year growth.

**Figure 1. Key Real Sector Indices: April 2008 – April 2009**



Source: BoT, World Bank calculations

**Market indicators confirm Thailand's relatively strong financial position, which would be supportive of a recovery.** Less than two weeks after the state of emergency was imposed, credit default swap (CDS) spreads were still about 35 bps lower, on average, than those of other East Asian countries since the onset of the global financial crisis in mid-September. The SET gaining 36 percent in 2009, close to the regional average and recovering some of the 48 percent decline posted in 2008 (a decline that was nonetheless in line with other regional markets). The Thai Baht had depreciated against the US dollar in the first quarter of the year, but in line with other emerging market currencies has appreciated since mid-

March. The Nominal Effective Exchange Rate (NEER) has been quite stable, appreciating by 0.6 percent since September 2008; in contrast, the average movement in other developing Asian countries' NEERs since September has been around 6 percent.

**The labor market response has been primarily through a reduction in the quantity of labor, leading to increases in unemployment and reduced number of hours worked.** Employment has contracted in 2009 as agricultural employment failed to absorb lay-offs from the manufacturing sector (as it had been doing since May 2008) and employers reduced work hours in an attempt to avoid outright layoffs, especially for employees with scarce skills. The unemployment rate has risen by nearly one percentage point or 329,000 more unemployed in the first quarter of 2009 compared to the third quarter of 2008, and the number of hours has also been reduced, with an additional 539 thousand individuals working less than 20 hours per week. Real wages were up 3.6 percent in the fourth quarter of 2008 and although they declined in the first quarter of 2009 by 6.6 percent, they come from a very high base (real wages were up 13.1 percent in Q1 2008). There are reports of declines in wages in low-productivity informal sector jobs, however, as individuals seek to make up income lost to reduced hours in primary jobs.

**The social impact of the global financial crisis is expected to be felt primarily by the urban informal sector.** The structure of Thailand's economy and trade patterns suggest that the most immediate impact of the crisis is likely to come will come from falling employment in manufacturing, tourism and construction. These sectors are concentrated in urban areas, and most marginal jobs are informal (from day labor, for example). The impact on the rural poor will be mainly from the decline in commodity prices. Falling urban employment and incomes would also lower the ability of urban workers to send remittances to their families in the rural areas, and indeed some may return to their rural households, putting pressure on already limited incomes. As a result of the crisis, poverty is expected to increase in 2009 for the first time since 2002. Factors may mitigate these developments are a decline in food and fuel prices, and public spending, including transfers to the low-income and poor households and public investment, which may be supportive of continued growth.

**Returning to a high growth rate is essential for poverty reduction as well as the sustainability of fiscal policy.** Thailand implemented important reforms following the 1998 crisis that are largely responsible for the low levels of external vulnerabilities and the health of the financial sector. This crisis should be used as an opportunity to promote reforms and investments that will restore Thailand to a high steady-state level of growth that will contribute to continued improvement in standards of living and poverty reduction. The planned expansion in public investments can help reduce infrastructure bottlenecks and could be supportive of long-term growth. Nevertheless, care must be taken that the planned public investments complement rather than replace timely expenditures to support a reduction in unemployment and protect the poor during the crisis.

**Positioning Thailand for the post-crisis environment will be vital to a resumption of robust long-term growth.** The post-crisis global economic environment is likely to be characterized by lower steady-state consumption in the G3 economies, higher demand from the "BRICs" (Brazil, Russia, India and China) and ASEAN, and increased capital flows to developing countries as savings in the US increase and returns in mature economies remain depressed. It is essential for Thailand to position itself for this new economic environment by removing constraints to domestic consumption growth, as well as binding constraints for productivity improvements that would allow exports of higher value-added products to new markets that are abundant in low-skill labor. This will require, among others, improving the quality of education, which both addresses skills shortages for firms as well as income inequality. Reducing income inequality increases the purchasing power of the middle class, which along with stronger social safety nets that reduce precautionary savings from individuals may help boost domestic demand. Finally, it is necessary to deepen reforms of the regulatory framework, such as restrictions on the services sector – where productivity has lagged over the years – to enhance competitiveness.

## RECENT DEVELOPMENTS AND OUTLOOK

### 2.1 Real GDP Growth and Macroeconomic Developments

**Real GDP growth slowed to 2.6 percent in 2008 down from 4.8 percent in 2007.** Real GDP grew a robust 5.1 percent in the first three quarters of 2008 year-on-year, compared to the 4.6 percent in the same period of 2007. Growth was driven by exports and investment, which contributed about 80 percent of the growth rate. Exports of goods and services expanded by 26 percent in US dollar terms and by 11 percent in real terms in that period, while private investment picked up 4.8 percent following a contraction in the same period a year earlier; inventory build-up contributed significantly as well. Starting in October, however, the combined impact of the global financial crisis and domestic political crisis took a toll on growth, leading to a 9 percent contraction in exports in the fourth quarter (net foreign demand contracted by 38 percent due to a 1 percent increase in the volume of imports). As a result, GDP contracted by 4.3 percent year-on-year in the fourth quarter, reducing the 2008 growth rate to 2.6 percent (see Table 1 and Figure 2).

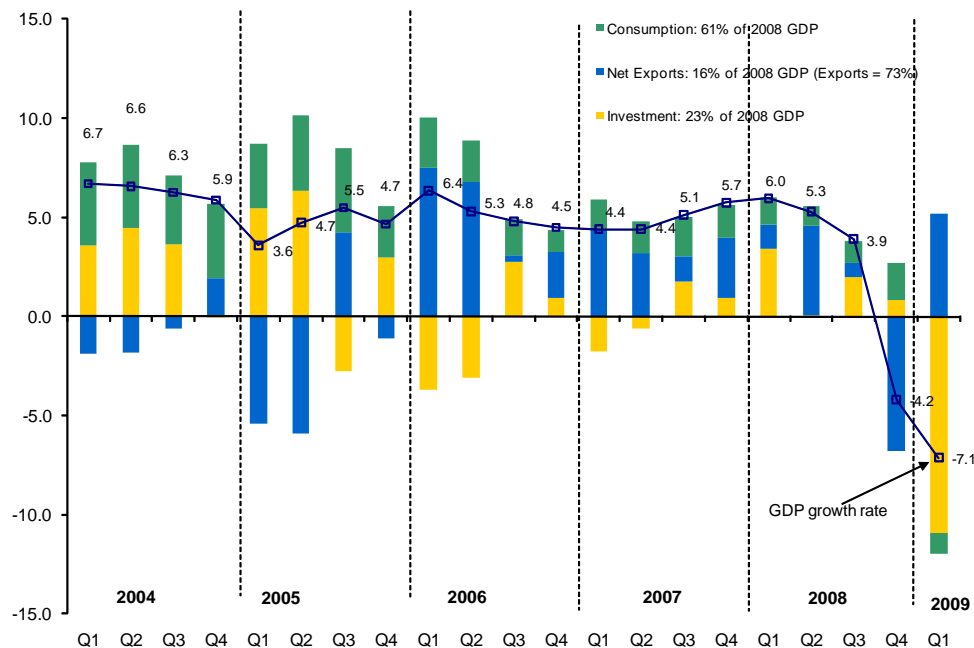
**Table 1. Real GDP Growth, 2008-2009**  
(Percent, year-on-year)

	Share in	2008					2009				
	2008 GDP	Q1	Q2	Q3	Q4	Year	Q1	Q2p	Q3p	Q4p	Year(p)
<b>Consumption</b>	<b>61.0</b>	<b>2.3</b>	<b>1.6</b>	<b>1.7</b>	<b>3.3</b>	<b>2.2</b>	<b>-1.8</b>	<b>1.7</b>	<b>1.2</b>	<b>1.6</b>	<b>0.7</b>
Private	52.1	2.7	2.5	2.7	2.1	2.5	-2.6	-0.5	0.0	1.0	-0.5
Public	8.9	-0.4	-3.7	-2.9	11.0	0.5	2.8	15.0	7.0	5.5	7.6
<b>Gross Fixed Capital Formation</b>	<b>22.1</b>	<b>5.4</b>	<b>1.9</b>	<b>0.6</b>	<b>-3.3</b>	<b>1.1</b>	<b>-15.8</b>	<b>-3.7</b>	<b>-1.4</b>	<b>1.6</b>	<b>-4.9</b>
Public	5.3	1.9	-5.2	-5.5	-10.2	-4.8	-9.1	7.0	7.0	7.5	3.3
Private	16.8	6.5	4.3	3.5	-1.3	3.2	-17.7	-7.0	-5.0	0.0	-7.5
<b>Total Domestic Demand</b>	<b>84.5</b>	<b>5.9</b>	<b>1.2</b>	<b>3.6</b>	<b>3.4</b>	<b>3.5</b>	<b>-14.9</b>	<b>0.3</b>	<b>-0.3</b>	<b>-0.8</b>	<b>-3.9</b>
<b>Exports</b>	<b>72.5</b>	<b>8.9</b>	<b>11.9</b>	<b>11.2</b>	<b>-8.9</b>	<b>5.4</b>	<b>-16.4</b>	<b>-20.0</b>	<b>-16.0</b>	<b>0.2</b>	<b>-13.4</b>
Goods	58.9	8.3	13.2	12.6	-8.9	6.0	-17.9	-22.0	-18.0	-0.2	-15.0
Services	13.5	11.1	5.6	4.9	-8.7	2.9	-11.0	-10.0	-6.0	2.0	-6.4
<b>Imports</b>	<b>57.0</b>	<b>9.3</b>	<b>6.7</b>	<b>13.1</b>	<b>1.0</b>	<b>7.5</b>	<b>-31.4</b>	<b>-20.1</b>	<b>-16.5</b>	<b>-4.0</b>	<b>-18.0</b>
Goods	45.8	10.0	5.2	12.5	0.1	6.9	-36.1	-24.0	-20.0	-5.0	-21.3
Services	11.2	6.9	13.7	16.2	4.6	10.0	-12.3	-3.0	-1.0	-0.5	-4.1
<b>Net Foreign Demand</b>	<b>15.5</b>	<b>7.4</b>	<b>33.6</b>	<b>4.5</b>	<b>-39.2</b>	<b>-1.4</b>	<b>30.2</b>	<b>-19.5</b>	<b>-14.2</b>	<b>22.0</b>	<b>3.5</b>
<b>GDP</b>	<b>100.0</b>	<b>6.0</b>	<b>5.3</b>	<b>3.9</b>	<b>-4.2</b>	<b>2.6</b>	<b>-7.1</b>	<b>-3.1</b>	<b>-2.5</b>	<b>1.8</b>	<b>-2.7</b>

Source: NESDB and WB staff calculations

Note: p = World Bank projection

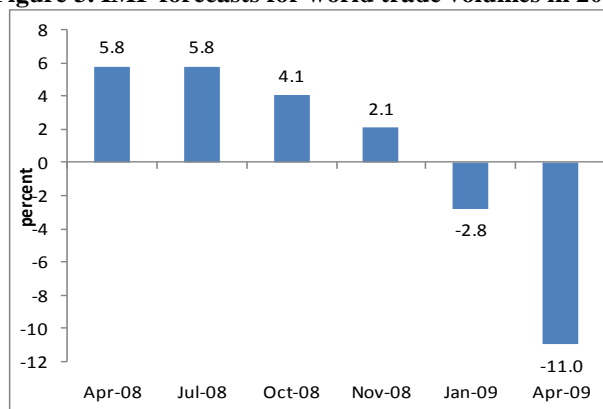
**Figure 2. Contribution to the GDP Growth Rate**



Source: NESDB, World Bank calculations

**The contraction in foreign demand has been deeper and swifter than projected at the outset of the crisis, setting the stage for a sharp economic contraction in 2009.** In the December edition of the Thailand Economic Monitor, the World Bank forecast that exports would grow by 3 percent in the fourth quarter of 2008, with net foreign demand expanding by 1.2 percent. Instead, exports contracted by 8.9 percent in the fourth quarter and net foreign demand plunged 38.2 percent. This reflected a more general pattern where the impact of the global financial crisis on global trade was deeper and more immediate than most observers had predicted. As figures for global trade and manufacturing were released, forecasts were revised downward even in the absence of new shocks such as the bankruptcy of Lehman Brothers in mid-September or the failure of the US congress to pass a financial rescue package in mid-October. Figure 3 illustrates this point with the IMF's forecasts of global trade volumes in 2009. As late as November 2009 (after the onset of the crisis), the IMF was forecasting global trade volumes to grow by 2.1 percent in 2009; within five months, the forecast had been reduced by 13.1 percentage points.

**Figure 3. IMF forecasts for world trade volumes in 2009**



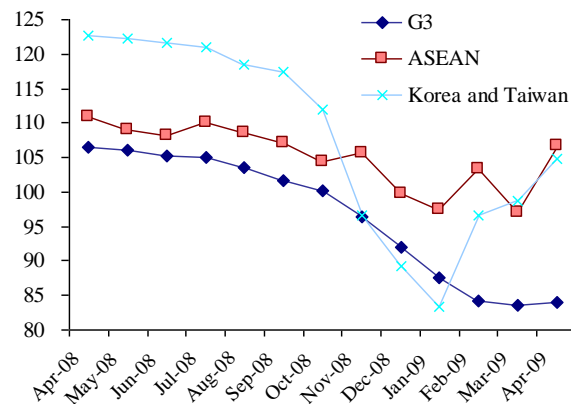
Source: IMF World Economic Outlook, various editions

**GDP contracted by 7.1 percent in the first quarter driven by inventory drawdowns and a contraction in domestic demand.** Exports of goods were down by nearly 18 percent year-on-year in the in real terms compared with a 9 percent decline in the previous quarter. Net foreign demand made a positive contribution to GDP, however, as imports contracted 36 percent in the same period. The contraction in imports is linked to a massive reduction in inventories, confirming anecdotal evidence that inventories are largely composed of imported inputs used in production, mainly of exports. Accordingly, if the contribution of inventories is included in net foreign demand rather than investment, the net contribution of “external factors” would be -2.5 percent, while domestic demand (excluding inventories) contributed -4.5 percent to growth as fixed investment slumped by nearly 16 percent and private consumption contracted 2.6 percent. In comparison, in the fourth quarter the comparable contributions to growth were -5.3 and +1.2 percentage points. This suggests the contraction in net foreign demand is now contributing negatively to growth through negative multiplier effects on investment and consumption rather than directly.

**GDP is expected to contract by 2.7 percent in 2009 as Thailand remains dependent on the fate of the global economy** (Table 1). Between 2006 and the third quarter of 2008, net foreign demand contributed on average 64 percent of Thailand’s economic growth, compared with a small negative contribution in the period between 2000 and 2005 (Figure 1). Given ongoing political uncertainties and continued weakness in the global economy, the outlook for private investment remains negative, with recovery primarily dependent on a pick-up in global demand, which is not expected until 2010. The volume of exports of goods is expected to contract, as are service receipts, more than half of which come from tourism. Import volumes are likely to contract by more than exports due to businesses running down inventories and a contraction in overall investment and consumption of imports. Net foreign demand will therefore contribute positively to growth, although only marginally since in real terms exports represent a much larger share of GDP than imports (73 vs. 57 percent, respectively). Private consumption is expected to be generally flat as low consumer confidence and worsening labor market prospects are partially mitigated by expansionary fiscal policy, whereas private investment will continue to grow less (contract more) than overall GDP.

**Economic activity in Thailand and its trading partners seems to have reached a bottom earlier this year, but doubts remain regarding the sustainability of the recovery.** Industrial production in Thailand and abroad has increased since from their trough between December and February. In Thailand, on a seasonally-adjusted basis, the MPI is up 12 percent from its low in January and capacity utilization is up from February lows, which registered the lowest levels of capacity utilization since the 1997/1998 financial crisis (Figure 1 and Figure 6). A similar pattern is observed in most East Asian countries (Figure 4). In mature markets, purchasing managers’ indices, a leading indicator of business activity, have been on an improving trend during the same time period, and employment indicators have shown the first signs of stabilization. However, two possible hypotheses can explain this improvement in economic activity indicators. On the one hand, the improvement in indicators suggests the “green shoots” of a sustained recovery, which has been sparked by coordinated high levels of fiscal and monetary stimulus and supported by improved liquidity in the financial systems of mature economies. On the other hand, higher production between February and April 2009 may be explained by one-off restocking in response to overshooting in inventory contractions in the first quarter. Therefore, while the outlook appears to be moderately favorable for a recovery in the second half 2009 (with year-on-year positive growth in the fourth quarter), the elevated uncertainties suggest risks are currently on the down side.

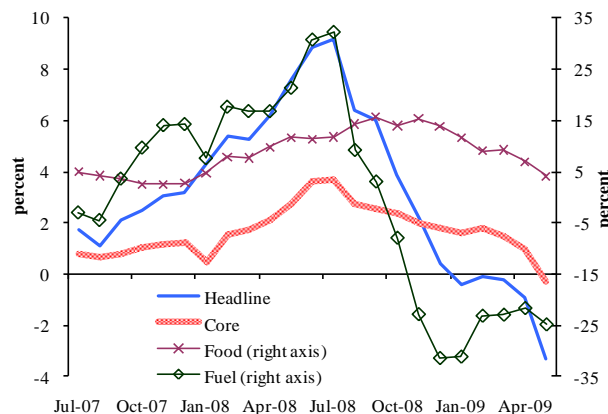
**Figure 4. Industrial Production Indices**



Source: World Bank Global Economic Prospects

**Lower energy prices and the slowdown in economic activity have resulted in negative headline inflation readings since January.** After reaching 9.3 percent in July 2008, headline inflation was only 0.4 percent in December and averaged 5.5 percent in 2008 compared to 2.3 percent in 2007. Core inflation averaged 2.3 percent in 2008 – within the Bank of Thailand’s (BOT) target of 0 – 3.5 percent. In the first five months of 2009 prices declined 1.1 percent from the same period in 2008, mostly driven by energy prices, which are down by about 25 percent (see Figure 5), as well as energy-related prices (transportation, vehicle operation and utilities). With the increased excess capacity in the economy and a stable new level in global oil and food prices this year, headline inflation in 2009 is expected to be flat, while core inflation should stay under 1 percent.

**Figure 5. CPI Inflation**

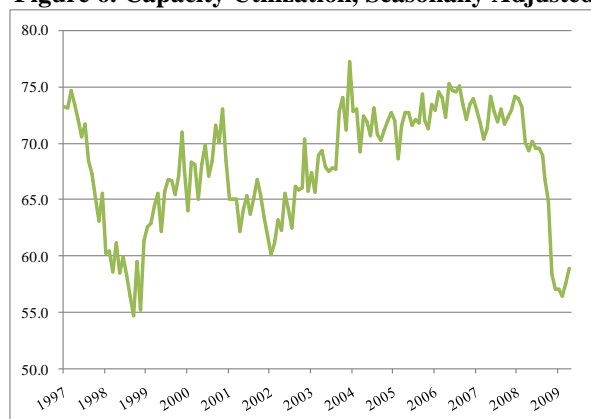


Source: Ministry of Commerce

**Low capacity utilization, limited prospects for export-related investments and heightened political uncertainty are expected to lead to a substantial contraction in private investment 2009.** Private investment has been subdued in the past three years due to increased political risks: in 2006-2008, investment grew an average of 2.7 percent annually, compared to GDP growth of 4.3 percent in the same period and growth of 14.8 percent during the period 2003-2005. This earlier retrenchment of investment has dampened somewhat the impact of the financial crisis, most notably on FDI. Little new FDI is expected, and in the first quarter of 2009 FDI net inflows contracted by 22 percent year-on-year. On the

other hand, there has been no rush to exit from foreign investors, and the reduction in inflows is not expected to turn to investment outflows. Private investment is expected to contract by 7.5 percent in 2009 as capacity utilization remains below 60 percent for March and April; levels that were not seen since the 1997/1998 financial crisis (see Figure 6). Growth could resume in the fourth quarter on the back of increased public investment, a better outlook for the global economy, and the low base, but the recent intensification of the political crisis could lead to a further re-pricing of risks.

**Figure 6. Capacity Utilization, Seasonally Adjusted**



Source: Bank of Thailand, World Bank calculations

**The Thai financial sector remains sound, but asset quality needs to be monitored in case of a protracted recession.** The average capital adequacy ratio stood around 14 percent at end-2008, compared to the BIS requirement of 8.5. Profitability indicators in the banking sector improved in 2008, and asset growth has been significant, averaging about 5 percent per year. On the back of this growth, asset quality has generally improved among commercial banks, with net NPLs declining to about 2.9 percent of total assets at end-2008. Nevertheless, this trend has already started to reverse in 2009, and net NPLs were up to 3.1 percent in March. Thai banks appear to have enough room, at least in the short-term, to cope with higher NPLs, but asset quality could become a greater concern if recovery is delayed. At the individual bank level, isolated capital inadequacies have been observed, but regulators have been proactive in addressing these.

**Despite adequate liquidity in the financial sector, credit growth has slowed, affecting primarily small and medium enterprises (SMEs) and supplier credits.** Credit growth has been declining on a month-to-month basis since November. Since large corporations have switched partially from foreign to domestic financing, this decline probably underestimates the overall contraction of credit to businesses, especially to marginal borrowers such as SMEs. The government has reacted by increasing the capital of the state-owned SME Bank, and instructed another state financial institution (SFI) to provide guarantees to SMEs. Credit growth to individuals is likely to continue to decelerate, and growth was down to 8 percent in March from 12 percent in September. Credit expanded by 9 percent in 2008, initially due to higher demand for working capital facilities, then as a consequence of large domestic firms switching from foreign to domestic borrowing. Credit growth slowed down in 2009, and the ratio of loan to deposit plus bills of exchange decreased to 84 percent in April, suggesting room for future loan growth.

**Household consumption grew modestly in 2008 supported by rising farm incomes, but is likely to be flat in 2009.** Household consumption, which accounts for 52 percent of GDP, grew by 2.5 percent in 2008, a modest improvement over the 1.6 percent rate registered in 2007 and still well below average growth of 5.2 percent between 2002 and 2006. Crop production and volumes expanded substantially in 2008, leading to a 35 percent growth in farm incomes and supporting an increase in consumption among

the rural population (70 percent of the population). Consumption is expected to be generally flat in 2009 as greater uncertainty about employment and income prospects may be offset by public transfers and a more positive outlook in the second half of the year. The slowdown in the export sector has already led to increased unemployment, with the manufacturing sector shedding over 360,000 jobs in the first quarter of 2009 compared to the fourth quarter of 2008. Farm income growth decelerated to near zero in the first quarter of 2009 and is expected to fall during the year as agricultural prices decline from their high levels in 2008. However, incomes will likely remain higher than their pre-2008 levels. The government's stimulus package provided substantial transfers to households in the bottom four quintiles, which may help offset the decline in consumer confidence, especially in the second quarter of 2009, when most of the package is expected to be disbursed. Nevertheless, this will only prevent a contraction, and private consumption is expected to be overall flat in 2009.

**Global trade is expected to contract around 10 percent in 2009, dragging down Thailand's crucial export sector.** The World Bank forecasts that global trade volumes will decline by nearly 10 percent in 2009, while the latest IMF forecasts anticipate an 11 percent drop. Thailand has diversified its export destinations so that traditional export markets (US, Europe, and Japan) now account for a little over one-third of Thai exports, while emerging markets (primarily China and ASEAN) account for another one-third. However, the contraction in global trade has been synchronized, and shipments to all major destinations decreased sharply. Moreover, Thailand's move in the past twenty years away from commodities and into higher value-added exports such as high technology products also increased its vulnerability to a contraction of export demand, since the elasticity of demand of these products is higher than that of commodities: the volume of high technology exports contracted by 31 percent in the first quarter, whereas agricultural exports contracted by 21 percent. Exports of services, of which more than half are tourist receipts will be heavily impacted by the slowdown in the incomes of developed countries (which represent around 40 percent of tourists in Thailand each year).

**Exports of goods and services started contracting in November, and are expected to be sharply down in 2009.** Since November 2008, goods exports have fallen by 21 percent on average per month. The current shipment level is at only 67 percent of the peak in July 2008. Travel receipts plunged 25 percent on average per quarter since the third quarter of last year, and room occupancy rate is at the lowest level since mid-2003. Unlike goods exports, overseas visitors to Thailand have shirked more significantly than those to other Asian countries, partly attributable to increased political instability. There is some early signs that exports may have bottomed out, with (seasonally-adjusted) exports up 4 percent month-on-month in April; however, as noted earlier in the context of industrial production it is not clear whether the recovery seen in March and April is sustainable. Following a contraction of nearly 18 percent in the first quarter, the volume of exports of goods is expected to contract by 15.0 percent in 2009, compared to a 6.0 percent expansion in 2008. Exports of services are projected to contract by 6.4 percent this year, less than the contraction in the last quarter of 2008, which was affected by the airport closure (see Table 1).

**Imports are expected to contract by more than exports in 2009 as businesses run down inventories and demand for imported consumer and capital goods lags.** Following strong growth in 2008 due to high commodity and energy prices and a modest pick-up in investment, imports shrunk by 38 percent in nominal terms (36 percent in real terms) in the first quarter of 2009. The decline in import volumes was driven primarily by businesses running down inventories and a contraction in overall investment and consumption. Inventories are comprised primarily of raw materials, the category of imports that suffered the largest contraction in the first quarter of 2009 (see Table 2). In line with the declines in energy and commodity prices, the value of imported raw materials and fuel and lubricant fell by close to 50 percent, though all categories posted contractions in both value and volumes in the double-digits (see Figure 7). Given that inventories were reduced by more than the entire build-up in 2009, the imports are likely to decline less sharply in the remainder of the year. For 2009 as a whole, imports of goods are expected to

contract by about 20 percent. Imports could pick up towards the end of the year, however, if public investment, especially in transport infrastructure, accelerates.

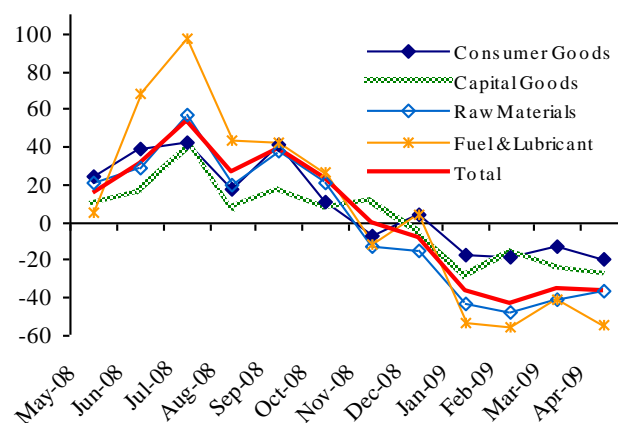
**Table 2. Import Value and Volume Growth**

(Percent)

	2006	2007	2008	Q1 2009
<b>Consumer goods</b>				
Value	15.3	13.8	25.1	-16.0
Volume	15.2	9.6	21.1	-15.1
<b>Raw materials</b>				
Value	5.7	15.0	21.9	-44.1
Volume	1.7	8.7	10.5	-45.2
<b>Capital goods</b>				
Value	8.0	3.6	19.5	-23.2
Volume	5.8	1.4	14.6	-21.9
<b>Fuel and lubricant</b>				
Value	20.3	2.7	44.2	-50.2
Volume	-2.4	-4.8	10.7	-29.1
<b>Total</b>				
Value	7.9	9.1	26.4	-38.3
Volume	1.3	3.5	12.1	-35.0

Source: Bank of Thailand

**Figure 7. Monthly import growth by product groups  
(% Year-on-Year)**



Source: Bank of Thailand

**Since imports are expected to contract more than exports in nominal terms, the current account is expected to turn to a sizeable surplus in 2009.** The current account registered a small deficit of 0.1 percent of GDP in 2008, mostly due to the increase in the value of fuel and commodity imports as well as reduced exports and service receipts in the second half of the year. Given that imports and exports are similar in nominal terms, despite a substantial contraction in exports, a greater reduction in imports is likely to lead to a sizeable current account surplus of 4% of GDP in 2009. Just in the first quarter, the current account posted a surplus equivalent to 25 percent of the quarterly GDP (Table 4).

**Table 3. Net Capital Flows**

(Million US\$)

	2008	2008				2009
		Q1	Q2	Q3	Q4	Q1
1. Monetary authorities	61	641	-375	-56	-149	-148
2. Government	-502	441	-284	-504	-156	-163
3. State Enterprises	-1,252	3	-603	-338	-313	-570
4. Bank	8,052	6,123	-603	2,065	467	-2,250
5. Non-Bank Private	6,429	5,956	-1,264	-54	1,790	179
FDI	9,811	2,760	2,303	2,525	2,224	2,157
- Equity investment	9,759	2,363	2,417	2,407	2,571	2,182
- Direct loans	53	397	-114	118	-348	-24
Portfolio	-2,188	3,454	-3,714	-2,505	576	-60
- Foreign	-875	814	-652	-512	-525	-448
- Equity securities	-1,004	263	-416	-503	-348	-280
- Debt securities	129	551	-236	-9	-177	-168
- Thai	-1,313	2,640	-3,062	-1,993	1,101	388
Loans (foreign)	287	-1,246	412	388	734	-85
Trade Credits	714	1,555	421	51	-1,313	...
Others	-2,195	-566	-686	-513	-431	-1,834
<b>Total capital flows</b>	<b>12,788</b>	<b>13,165</b>	<b>-3,129</b>	<b>1,113</b>	<b>1,639</b>	<b>-2,953</b>

Source: Bank of Thailand

**Given the current account surplus and the health of Thai banks, capital flows should remain strong and reserves are likely to continue to build in the Bank of Thailand.** The financial account posted large inflows in 2008, mostly from banks, which brought US\$8 billion, although FDI was also significant at US\$8 billion (see Table 3). Capital controls were lifted in February, leading to large capital inflows in the first quarter; those inflows were quickly reversed (and more) in the second and third quarters as the political crisis built up, but in the fourth quarter, Thais who had taken funds out of the country in the previous two years repatriated some assets (including through portfolio investments) since Thailand became a relatively safer choice to other overseas markets that were hit harder by the crisis. The financial account is expected to register modest net outflows in 2009 as portfolio investments show outflows, while FDI net inflows will continue to be positive, but at a lower level compared to the past few years. Partly due to unusually large errors and omissions at nearly 5 percent of GDP, the overall balance of payments (BOP) was in surplus of over 9 percent of GDP in 2008. The BOP is expected to post a smaller surplus in 2009 (see Table 4). International reserves have continued to grow since September, reaching US\$111 billion as of end-December and US\$121 billion as of end-May. Current reserve levels represent over 8 months of imports or 4.7 times short-term external debt. High levels of reserves and capital inflows may suggest a tendency for the Baht to appreciate, but such tendency is likely to be mitigated by further rate cuts and other interventions from the BoT amid a concern about the competitiveness of Thai exports in a difficult international environment. These opposing forces should lead to a stable Baht, trading between 34 and 36 to the dollar.

**Table 4. Balance of Payments**

(Million US\$)

	2006	2007	2008	2009p
Exports of Goods	127,941	150,048	175,297	146,017
(% change)	17.0	17.3	16.8	-16.7
Imports of Goods	126,947	138,477	175,060	137,515
(% change)	7.9	9.1	26.4	-21.4
Trade Account	994	11,571	237	8,502
as % GDP	0.48	4.70	0.09	3.46
Net services income & transfers	1,321	2,477	-416	1,375
<b>Current Account</b>	<b>2,315</b>	<b>14,048</b>	<b>-179</b>	<b>9,877</b>
as % GDP	1.12	5.71	-0.07	4.01
<b>Capital and financial account including net errors and omissions</b>	<b>10,426</b>	<b>3,053</b>	<b>24,872</b>	<b>-4,921</b>
<b>Balance of payments</b>	<b>12,741</b>	<b>17,101</b>	<b>24,692</b>	<b>4,955</b>
Foreign Reserves (year-end)	66,985	87,455	111,008	115,963

Source: BOT and WB projections; p = projections

**Monetary policy has been easing since December, but its impact has been limited given the demand-side nature of the economic slowdown.** With inflation less of a concern since the onset of the global financial crisis, the Bank of Thailand has lowered its key policy rate by 250 basis points since December, from 3.75 percent to 1.25 percent. The impact of the rate cuts are starting to be seen in lending rates, although the minimum lending rates charged by banks has declined by less than half of the policy rate cuts. Moreover, credit growth remains subdued. Although the BoT has ruled out the use of quantitative easing at this time, the BoT has been considering a narrower inflation target between 0.5 and 3.0 percent (from the previous 0 to 3.5 percent), which could allow more aggressive action should deflation risks increase. Given that core inflation is forecast to be close to 0.5 percent (and was negative for May – see Figure 5), this change could have important practical implications if the economy deteriorates more than expected in the second half of 2009.

**The government has started to implement a substantial fiscal stimulus in response to the global financial crisis.** With a view of partially reversing the negative multiplier effects of a contraction in external demand, fiscal policy has been expansionary. A supplementary budget of Bt116.7 billion, of which Bt97.6 billion (US\$2.8 billion or 1.1 percent of 2009 GDP) will be used to finance stimulus measures, was approved by Parliament in February along with tax reductions costing around 0.45 percent of GDP. The emphasis of this first round of stimulus was on consumption measures for quick implementation. The first round of stimulus is expected to be fully implemented by the end of the year, boosting public consumption, which is expected to grow 7.6 percent in 2009 following near-zero growth in 2008.

**Public investment contracted sharply in the past four quarters, but is expected to increase in 2009 given the role of investments in the government's fiscal stimulus package and the political imperative to respond to the slowdown in the export sector.** The share of public investment in real GDP averaged only 5.7 percent from 2004-2008 compared more than 10 percent before the 1998 crisis. In

2008, public investment contracted by nearly 5 percent as a result of political uncertainties, which delayed investment decisions. Public investment continued to contract in the first quarter of 2009, largely due to state-owned enterprises reducing investments in light of deteriorating economic conditions. In April 2009, the Cabinet approved a second round of stimulus in an amount of Bt1.57 trillion over the next three years (2010-2012), for an average of 5.8 percent of GDP annually, of which an average of 2 percent of GDP is estimated to be additional to the previous public investment program. Most of the second round of stimulus would be devoted to infrastructure projects, especially in the transportation and water sectors. While the headline figure includes items already planned under the current public investment program and investments by state owned enterprises, it is estimated that about Bt 700 billion represent additional investments. Although the second round of stimulus is expected to boost investment starting in 2010, given the low base public investment is projected to grow at 3.3 percent in 2009 as the implementation of large infrastructure projects step up.

**Prudent fiscal policies in the past have provided the fiscal space to implement the stimulus without jeopardizing fiscal sustainability – provided that growth returns.** In 2009, the budget deficit will be about 6 percent of GDP after taking into account the fiscal stimulus and the steep shortfall in revenues. While this is much higher than recent levels, a debt sustainability analysis suggests that Government can afford the announced stimulus package, provided that deficits are not sustained at this level and growth resumes its long-term potential. (Box 1) The Thai government has continuously pursued a conservative fiscal stance of low budget deficits or even a surplus. Since 2002, budget deficits were no more than 2 percent of GDP and the primary balance was in surplus in two of the past three years. As a result, the Thai government's fiscal ratios have been within the fiscal sustainability guidelines which have been established since the 1998 Asian financial crisis, creating the room for needed borrowing in a time of crisis.

**Returning to a high steady-state growth rate as the global economy recovers will require structural reforms to enhance long-term competitiveness.** In this respect, it is essential to use the crisis as opportunity to promote reforms and investments that will ensure that Thailand return to a high level of growth in the long-run. The planned expansion in public investments announced as the second round of fiscal stimulus can help in reducing infrastructure bottlenecks that have been identified as a bottleneck to private investment and growth. Other binding constraints to long-term growth should also be addressed, notably in education and the services sectors, which are areas where structural reforms may yield large dividends given Thailand's skill shortages and low productivity in services.

### **Box 1. Can Thailand Afford Fiscal Stimulus?**

**In January and April 2009, the Government announced a stimulus package totaling Bt1.88 trillion for 2009-2012.** The component planned for disbursement in 2009, which amounts to Bt145.6 billion (1.6 percent of GDP) is well defined and under implementation. For 2010-2012, the announcement provided the broad outline of a packages and areas expected to be supported, with details of specific projects to be announced later. The headline figure of Bt1.73 trillion (average of 5.8 percent of GDP per year) includes the already planned public investment program, and spending by state owned enterprises and government agencies. Since the budget for public investment for 2010 has not been announced yet it is difficult to identify the actual additional spending. Our estimates in Table 5 below are that the additional spending by the central government and state owned enterprises for 2010-2012 is between 1.7-2.3 percent of GDP per year.

**Financing the stimulus will require borrowing in addition to that currently allowed under the public debt management law.** The public debt management law limits domestic borrowing in any fiscal year to 20 percent of approved expenditures plus 80 percent of principal repayments. For 2009, this is expected to limit

domestic borrowing to 415 billion baht compared to gross financing needs of over 600 billion baht (equivalent to 6.8 percent of GDP; see Table 5). The financing plan calls for 530 billion baht in domestic financing, with the remainder coming from official creditors (ADB, JICA and World Bank). Domestic interest rates have remained low, and financing needs in the domestic markets should be met on attractive terms. As of mid-June, the yield on 5-year Government debt was 3.3 percent.

**Table 5. Central Government's Financing Plan for FY 2009 – 2012**  
(Billion Baht)

<b>Fiscal Framework</b>	<b>2009</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>
Revenues	15.5	15.5	16.5	17.2
Expenditures	21.4	21.0	20.8	21.4
<i>of which additional stimulus package</i>	<i>1.6</i>	<i>2.1</i>	<i>1.7</i>	<i>2.3</i>
Budget Deficit	5.9	5.5	4.3	4.2
<b>Gross Financing Needs</b>	<b>6.8</b>	<b>6.0</b>	<b>5.8</b>	<b>8.2</b>
<b>New debt (billion Baht)</b>				
New Domestic Debt CG & SOE	529.6	478.6	497.2	750.4
<i>of which stimulus package</i>		64.2	89.7	113.1
New External Debt CG	72.0	72.0	72.0	117.0
<i>of which stimulus package</i>	72.0	72.0	72.0	117.0
New External Debt SOE		78.7	94.4	99.8
<i>of which stimulus package</i>		67.5	59.7	37.0
<b>Total Borrowing for stimulus package</b>		<b>203.7</b>	<b>221.4</b>	<b>267.1</b>

Source: FPO, PDMO, BOT, World Bank projections

**A debt sustainability analysis (DSA) suggests that the government has the fiscal space to implement the stimulus.** In 2009, the budget deficit will be around 6 percent of GDP after taking into account the fiscal stimulus and the steep shortfall in revenues. While this is much higher than recent levels, the analysis suggests that Government can afford the announced stimulus package without jeopardizing debt sustainability, provided that deficits are not sustained at this level and that GDP growth returns to its steady-state average of 5 percent per year. The Thai government has continuously pursued a conservative fiscal stance of low budget deficits or even a surplus. Since 2002, budget deficits were no more than 2 percent of GDP and the primary balance was in surplus in two of the past three years. As a result, the Thai government's fiscal ratios have been within the fiscal sustainability guidelines which have been established since the 1998 Asian financial crisis.

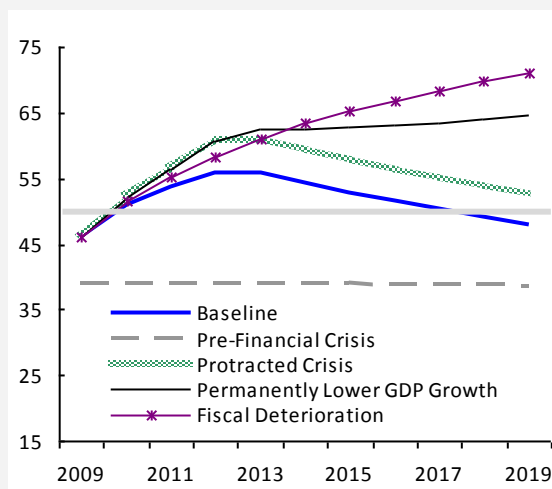
**Public debt stocks have been declining and the debt composition has been managed to minimize the impact of external shocks.** Public debt, including non-guaranteed debt of state-owned enterprises, has been falling as a share of GDP from a peak of 58 percent in 2000 to 38 percent at end-2008. The composition of the debt stock has also shifted. Foreign-currency debt, which accounted for about 39 percent of public debt in 1999, has been reduced to about 12 percent of the portfolio. From that amount, about half has been swapped back into baht, so that risks from exchange rate fluctuations are minimal. There has also been a move towards issuing fixed-rate government bonds, and less than 15 percent of the debt carries a variable interest rate, therefore minimizing risks from interest rate volatility.

**Under a baseline scenario that assumes a resumption of potential growth by 2013, Thailand's public debt-to-GDP ratio declines gradually by the end of the projection period.** After an initial spike due to the substantial financing needs that arise from the fiscal stimulus (Figure 8), debt ratios resume their downward trend. The debt-to-GDP ratio is expected to be approximately 49 percent of GDP by 2018 following a peak of 55.8 percent in 2013. The slow decline under the baseline arises from conservative assumptions on fiscal balances, which remain lower than their post-crisis average throughout the projection period. The DSA also allows for a counter-factual analysis of the impact of the global financial crisis (and reality-check of our baseline): it is estimated that the financial crisis adds as much as 17 percentage points to the debt-to-GDP ratio

by 2012 (Figure 9).

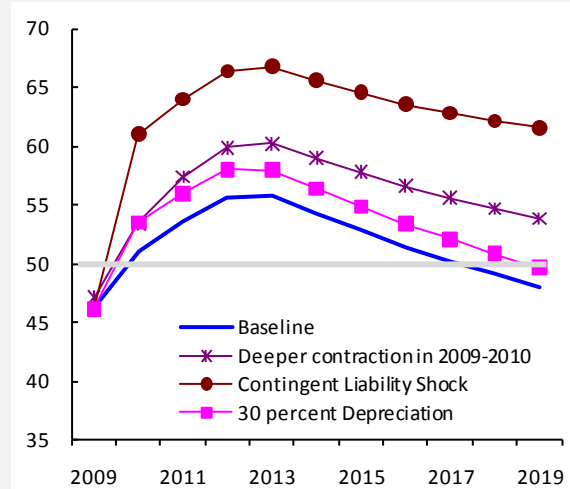
**Public debt sustainability is generally resilient to worst-than-expected outcomes in 2009-2010, but contingent liabilities must be closely monitored.** The DSA considered the effect on debt sustainability of (i) a real GDP contraction of 4.9 percent in both 2009 and zero growth in 2010; (ii) a 30 percent nominal depreciation of the Thai baht; and (iii) the realization of contingent liabilities adding up to 10 percent of GDP (Figure 9), resulting in an increase of funding costs. The contingent liability and higher financing costs shock is the most severe, leading the debt-to-GDP ratio to peak at 67 percent. This shock is especially relevant in the context of the current financial crisis in Thailand as the government faces possible contingent liabilities from the special financial institutions, Thai Airways (which has been hit hard by the airport closure and the financial crisis overall, and requested sizeable guarantees from the government), and the government's crop support schemes. However, under all shocks, the path of debt indicators is eventually declining, suggesting an overall sustainable dynamic of public debt.

**Figure 8.**  
**Public Debt: Baseline and Alternative Scenarios**  
(percent of GDP)



Source: World Bank based on PDMO data

**Figure 9.**  
**Public Debt: Baseline and Stress Tests**  
(percent of GDP)



Source: World Bank based on PDMO data

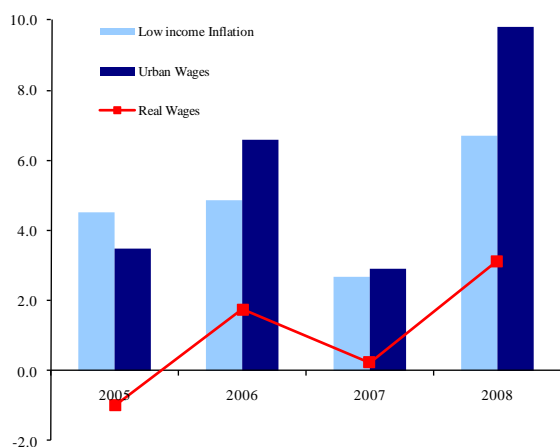
**However, the greatest risks to debt sustainability come from protracted growth slowdown and lack of fiscal consolidation following the resumption of growth (Figure 8).** Should the government be unable to promote fiscal consolidation following the crisis and deficits remain close to their 2009 levels, the debt-to-GDP ratio remains on a rising trend and would remain above 50 percent and on an increasing trend in the longer term. This highlights the important of ensuring that deficits are reduced once growth resumes. Moreover, the scenario where a protracted crisis is followed by low growth also keeps debt ratios rising and above the indicative fiscal sustainability threshold. This emphasizes the importance of taking advantage of the crisis to enhance competitiveness and ensure long-term growth. The role of growth in reducing debt levels can be seen when the scenario "permanently lower GDP growth" is compared with the "protracted crisis" scenario: both have the same short-term assumptions of -2.7 percent growth in 2009 and 2010 and zero growth in 2011-2013, but in the latter GDP growth converges to a steady-state of 5 percent whereas the "permanently lower growth" converges to growth of 2.0 percent.

## 2.2 Poverty

**The social impact of the global financial crisis in Thailand is likely to be substantial and poverty will increase in 2009.** A preliminary estimate suggests that the 2.7 percent GDP contraction forecast for 2009 will result in between 200 and 700 thousand vulnerable individuals falling into poverty in the next year, leading the poverty rate to increase for the first time since 2000. The crisis is expected to impact poverty in two main ways: (i) a contraction in formal urban employment and shift towards informal and rural employment, which will add pressure on earnings of vulnerable individuals in the rural and informal sectors; and (ii) a decline in agricultural prices, which will reduce income in rural areas, where most of the poor are concentrated. Factors that may mitigate these developments include (i) decline in the prices of food, which comprise over 50 percent of expenditures of low-income individuals, and (ii) government interventions, including transfers to the poor under the fiscal stimulus package and existing (if limited) social safety nets, as well as public investment, some of which reaches the poor, and which may be supportive of continued growth.

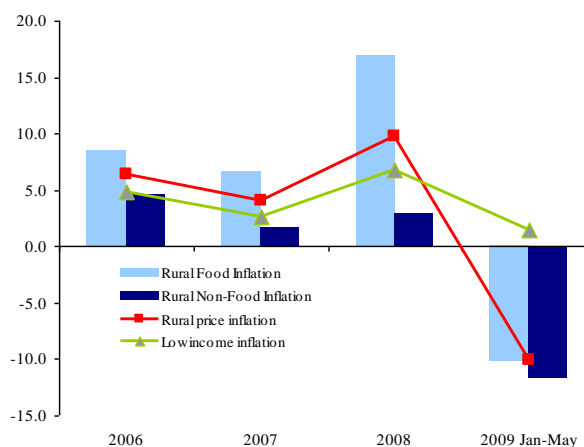
**The global financial crisis will affect the poor and vulnerable in Thailand primarily through the spillover from the reduction in formal economic activity in urban areas.** As a consequence of the contraction in private investment, the construction business, which employs a large number of low-skilled and hourly workers, has been hit hard. Developers have delayed projects, resulting in a year-on-year contraction of over 10 percent in construction in the past two quarters. Similarly, tourist receipts will also grow at a slow pace next year, affecting the labor-intensive retail, restaurant, and hotel businesses. The sharp contraction in the export sector affects not only manufacturing workers, but also day laborers who work in the ports. While workers in these hard-hit sectors are not necessarily poor, many are vulnerable: average real wage growth in construction, manufacturing, retail and hospitality has been sluggish over the past four years, suggesting workers in those sectors have limited buffers against the economic downturn (see Figure 10). The return of these displaced urban workers to the informal or rural economies will put pressure on the earnings of other vulnerable groups. In addition, many of these affected workers had been supporting households in rural areas through remittances, which are likely to be reduced (see Box 2). Declining food prices will cushion the impact of the loss of earnings on the poor, although prices faced by low income consumers, as measured by the low income price index, are still increasing (albeit at a slower pace) in 2009 (see Figure 11).

**Figure 10. Growth in real wages in the non-agricultural sector**



Source: MOC and NSO.

**Figure 11. Rural and Low Income Price Indices**

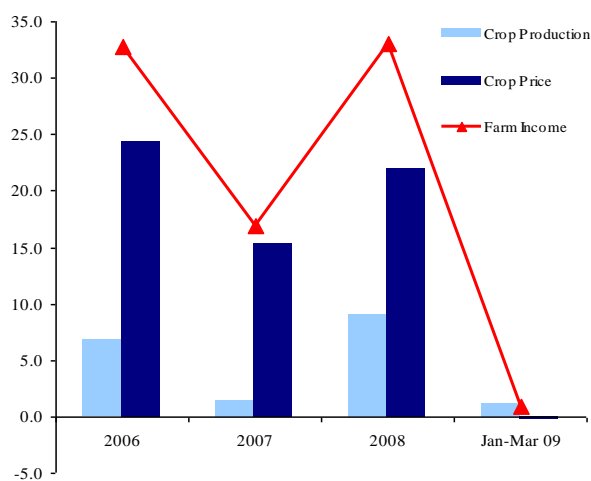


Source: MOC

**The negative impact of the global crisis on employment and earnings started to be felt in the fourth quarter of 2008 and continued in the first quarter of 2009.** The number of unemployed individuals went up by about 280 thousand between September and March, bringing the unemployment rate to 1.9 percent from 1.1 percent in the same period. An additional 180 thousand workers reported becoming “under-employed” (working fewer than 30 hours per week and available to work more). Formal employment declined by an estimated 0.6 percent in the fourth quarter. Real average wages (both agricultural and non-agricultural) were still up slightly on a year-on-year basis in December based on gains in the first three quarters, but real wages declined by 6.6 percent in the first quarter of 2009. As a consequence of declines in formal employment, agricultural employment increased by 11 percent in December from November, compared to a 5-year average increase of 6 percent (likely due to seasonal reasons). Manufacturing employment has been contracting since May, with the agricultural and services sector absorbing most of the displaced workers. Since January, agriculture has not picked up the slack, leading to a spike in unemployment.

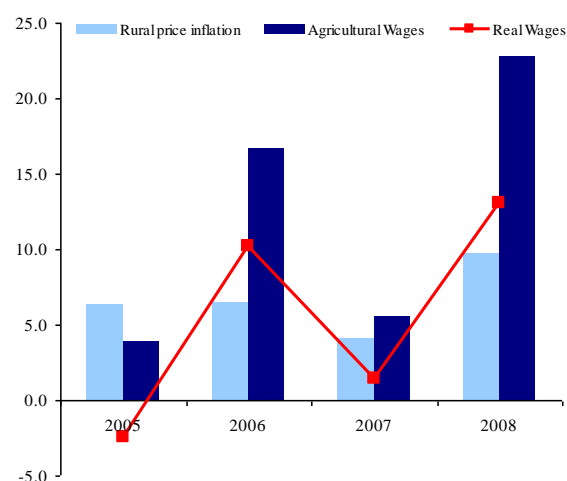
**The decline in agricultural prices, increased labor supply in agriculture and reduced domestic and external remittances represent another key channel through which the crisis is affecting vulnerable populations.** Out of 5.4 million poor in Thailand at end-2007, 88 percent lived in rural areas. Eleven percent of the rural population is poor as compared to 3.3 percent in the urban areas. Therefore, the impacts of the crisis on rural areas have important consequences for poverty. The prices of key crops are expected to fall from their 2008 record high levels by around 25-30 percent, while their production is estimated to grow modestly. While many vulnerable groups were hurt by high food and fuel prices, on average, households in the lowest deciles produce a surplus of rice and therefore benefited from higher prices. Moreover, the decline in input prices (oil, fertilizer) produces only modest benefits, since they represent only about 20 percent of production costs of major agricultural products. The current decline in commodity prices will therefore likely reduce farm incomes from their high levels this year by more than the decline in inflation. As a result, farm incomes, which had risen by 33 percent in 2008, have been flat in the first quarter of 2009 (see Figure 12). Wages in the agricultural sector rose by 23 percent in 2008 (see Figure 13), more than offsetting higher prices in rural areas, where inflation was nearly 10 percent on average (see Figure 11) in the same period. The sharp fall in rural prices in 2009 may provide some cushion to the rural poor as farm incomes and agricultural wages decline (see Figure 11).

**Figure 12. Growth in crop production and price and farm incomes**



Source: BOT

**Figure 13. Growth in real wages in the agricultural sector**



Source: MOC and NSO

**A preliminary assessment done by the World Bank of the impacts of the crisis on vulnerable groups shows a paradox of reduced work hours but more hours worked (see Box 2).** Workers have reported a reduction in the number of hours available for work in their primary employment, which is often related to a formal sector activity even if the work is informal. To compensate for the loss of income, workers have shifted to less productive activities, invariably in the informal sector, that require a greater number of hours worked to make up the lost income from the primary form of employment. One prominent example is the increased number of individuals working on salvaging garbage, which contributed to a reduction in the price paid for recyclable materials. The rapid assessment study also shows that remittances are being reduced, straining already vulnerable households.

**Despite the lack of formal social safety nets, the institutional framework for reaching the poor has improved since the Asian financial crisis, and the government's stimulus package, while imperfectly targeted, is likely to reach many vulnerable individuals.** A number of institutions were put in place over the course of the last decade that will allow government programs to reach those in need. The most important of these are the Universal Coverage Scheme for health insurance and the Sufficiency Funds (formerly known as the S-M-L community development program). As unemployment rises, and workers face the prospect of falling out of the formal social security system, the UC scheme is an important buffer. Secondly, the Sufficiency Funds make it possible to disburse funds at the village level for community infrastructure, and this scheme has now reached all villages. While both programs, particularly the Sufficiency Funds face serious implementation challenges, they do provide a vehicle for reaching a large portion of the population. Indeed, the Sufficiency Funds are being used in the government's fiscal stimulus program to direct transfers at rural areas. A key pro-poor measure in the fiscal stimulus is the cash transfer to the elderly. The elderly are over-represented among the poor and the measure targets specifically those that do not currently receive another form of pension. Other pro-poor measures include the subsidies for water and transportation and small village-level infrastructure construction projects. Table 6 shows that the fiscal stimulus package had a small pro-poor bias: nearly 10 percent of the beneficiaries of the package are poor, compared to 8.5 percent of poor in the population.

**Although the consumption measures of the government's fiscal stimulus have been pro-poor (if modestly), the focus on quick execution biased the package against the vulnerable in the urban informal sector.** For timeliness of implementation, the Government chose to use existing mechanisms – such as the social security system – for reaching the beneficiaries of the consumption measures of the stimulus package. This resulted in benefits falling disproportionately on the urban formal sector. As Table 6 shows, approximately 23 percent of the package went to this sector, which accounts for about 11 percent of the population. Meanwhile, the urban informal sector was the most under-represented, with 19 percent of the population receiving only 13 percent of the package. Although specific measures targeted at populations living in rural areas ensured that a large portion (about 64 percent) of the package reached this sector, it was also somewhat under-represented. This is largely because the Bt2,000 baht cash transfer and subsidies to urban transportation, water and electricity, which comprise about a third of the consumption measures, are expected to reach only a small proportion of those in rural areas.

**Table 6. Beneficiaries of Cash Transfer Measures under Fiscal Stimulus in 2009**

	Group		Group			Total
				Urban		
	Non-Poor	Poor	Rural	Formal	Informal	
Amount from cash transfer measures going to group (US\$ million)	2,527	261	1,781	638	368	2,787
Proportion of package going to group (%)	90.6	9.4	63.9	22.9	13.2	100.0
Proportion of group in population (%)	91.5	8.5	70.0	11.2	18.8	100.0

Source: World Bank staff estimates based on the 2007 Socio-Economic Survey and 2007 Informal Labor Survey

**Additional measures should be considered to support vulnerable individuals in the urban informal sector.** Individuals in the urban informal sector are not only vulnerable themselves, but they often serve as sources of income to vulnerable households in rural areas; or conversely a decline in their income may increase strains in vulnerable households through greater dependency on family as a social safety net. The Government may take this opportunity to accelerate the implementation of certain social safety net policies, such as increasing the length of eligibility for unemployment insurance benefits, targeted transfers to the poorest districts in the poorest regions, and incorporating public works programs into its second round of stimulus, which is focused on public investments in infrastructure. The incidence of this additional stimulus will depend on the ability of projects to create demand for such labor that is displaced from the informal sector.

**Box 2. Findings on the poverty and social impacts of the economic downturn in Thailand from a Rapid Assessment**

**A rapid assessment of the impacts of the economic crisis was conducted in three major provinces of Thailand (Bangkok, Samutsakorn and Nakornrachsrma) between February and March, 2009.** The assessment included focus group discussions with workers in the informal sector workers in Bangkok, workers in enterprises dependent on export markets and rural households reliant on remittances from domestic and international migrants. A series of in-depth interviews were also conducted with the business, employers and, where available, community-based organizations.

**Some industrial sectors were more resilient to the impact of the crisis than others.** Interviews suggested that closures and associated lay-offs of staff were more usual in the automobile and IT sectors than other sectors. Garment and tourism sectors had also experienced a decline in demand, but enterprises were more frequently reducing hours of staff rather than laying off large numbers of staff. Representatives of the garment industry explained that competition had stiffened over many years and that the current problems were not entirely new. Several enterprises mentioned their intention to switch production to alternative products, but that access to credit was constraining their ability to do so. Certain agriculture sectors (for example, tapioca) seemed to be robust, however, boosted by buoyant demand from China

**Workers in both the formal and informal sectors were experiencing a reduction in working hours for their main job, though long hours were worked overall.** In the formal sector, workers commonly described a cessation of overtime, compulsory days off and an erosion of benefits. Worker responses to this were mixed; some had left their jobs voluntarily as the consequent loss of earnings meant that they could no longer cover subsistence costs plus travel costs. Others were remaining in their jobs, but taking

on supplementary work, typically in the informal sector, to augment earnings. In the informal sector, workers were similarly compensating for reduced hours in their main work with less well-remunerated work. For example, port workers unable to find a whole day's work at the docks were salvaging garbage for recycling to supplement earnings. An increase in garbage collection activities meant the price paid per plastic bottle was reducing. Men, in particular, were travelling further afield to seek supplementary construction work. Workers were typically working longer hours to maintain satisfactory incomes and some noted the impact on child care.

**Workers in the informal sector appeared particularly vulnerable and indicated high levels of income insecurity and no access to formal safety nets.** The rapid assessment included discussions with port workers, construction workers, laundry service providers, home-based seamstresses, garland makers and souvenir manufacturers. Not only were hours in the main occupations reducing, many also reported declining earnings per hour or per piece. Indebtedness was common, with near total reliance on the informal sector for loans (friends, family and moneylenders were primary sources of credit). There was no recorded access to formal safety nets. Both Thai and migrant workers from overseas noted increased competition for work in certain sectors. In some cases, unregistered migrants were working for very low wages and were perceived as posing unfair competition. However certain jobs, such as particular tasks in seafood processing, were performed almost entirely by migrants and seemed unappealing to Thai workers.

**Though the agriculture sector seemed relatively robust, rural families reported a reduction in remittance flows.** The research included households receiving remittances from overseas and from within Thailand in Nakornrachsrma province. All these households had experienced a reduction in remittance flows. Those households having most difficulty coping with these reductions were those without agricultural land or savings and there were instances of children having to work for cash after school hours in order to compensate for some of the shortfall in household incomes. Some households reported selling jewelry in order to fund daily consumption. Others felt that they were able to get by without the remittances and had told migrant family members to retain the money to supplement the migrant's living conditions as migrants' earnings fell.

## 2.3 External Environment<sup>1</sup>

**The external environment remains challenging as the impact of the global financial crisis is felt worldwide.** The global financial crisis that began in September 2008 spread from the financial sector to the real economy and from the United States to the entire global economy with dramatic speed. As the valuation of a large share of assets in the financial sector was called into question, investors liquidated positions and credit markets froze. The sharp and massive contraction in global liquidity dried out trade credit and led to the postponement of capital spending plans. Faced with unprecedented loss of wealth and rapidly weakening labor markets, consumers reined-in spending, especially for durable goods, further reinforcing the contraction in trade and investment. Industrial production collapsed, and trade volumes have contracted in unprecedented magnitudes.

**The World Bank estimates that global GDP is expected to contract by 2.9 percent in 2009, which would be the first decline in world output on record.** High-income countries are in deep recession this year, with OECD economies likely to contract over 4 percent along with other high-income countries. GDP among developing economies should ease from an advance of 5.9 percent in 2008 to 1.2 percent. Volumes of world trade in goods and services are expected to drop by nearly ten percent in 2009, with a significantly sharper contraction in trade volumes of manufactured products. Oil prices are expected to

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<sup>1</sup> Material in this section is drawn from the World Bank's "Global Economic Prospects".

remain nearly 50 percent below 2008 levels, averaging \$56 per barrel for the year, while the decline in non-oil commodity prices is forecast to remain around 30 percent (see Table 7).

**Table 7. International economic environment**  
(percentage change from previous year)

	2007	2008	2009f	2010f	2011f
GDP Growth a/					
World	3.8	1.9	-2.9	2.0	3.2
High Income OECD	2.6	0.7	-4.2	1.3	2.4
USA	2.0	1.1	-3.0	1.8	2.5
Euro-zone	2.7	0.6	-4.5	0.5	1.9
Japan	2.3	-0.7	-6.8	1.0	2.0
Emerging East Asia	11.4	8.0	5.0	6.6	7.8
China	13.0	9.0	7.2	7.7	8.5
World trade volume	7.5	3.7	-9.7	3.8	6.9
Oil prices	10.6	36.4	-42.7	13.4	4.6
Non-oil commodity	17.1	21.0	-30.2	-2.1	1.4

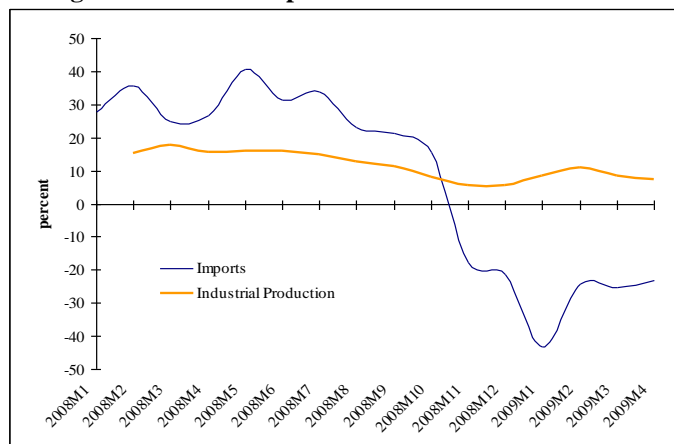
Source: World Bank

**The global character of the recession has carried a dramatic impact on economic performance among high-income countries.** Until mid-2008 the slowing of OECD domestic demand was partially offset by continued strong growth in exports of capital- and higher-tech products, supplying the investment that underpinned fast growth in the developing countries. Conditions have now reversed, as the collapse of high-income exports is reinforcing contraction in domestic demand in high-income countries. The tight global links between trade in manufactured products and the capital expenditures needed to support economic activity have now transformed into a vicious circle.

**The deceleration in economic growth in low-and middle income countries as a group is expected to match the deceleration in high-income countries.** This highly synchronous growth collapse cannot be solely explained by trade linkages, but illustrates also that developing countries have been directly hit in their domestic economies by the financial crisis. The reversal of capital flows, collapse in stock markets, and in general the deterioration in financing conditions have brought investment growth in the developing countries to a halt, and in many developing countries investment is sharply declining.

**East Asia and the Pacific is likely to be most affected by the falloff in global investment and trade, crimping industrial production and fostering declines in capital spending.** Investment stood at 36.3 percent of GDP in 2008, compared to 26.5 percent for developing countries excluding EAP, and contraction in capital outlays is likely to carry proportionately larger effects on regional growth. Regional exports shift from gains of 15 and 10 percent in 2007 and 2008 respectively, to decline of 1 percent in 2009. Against this background, GDP eases to under 6 percent in 2009, as growth in China slumps to 7.2 percent, and several ASEAN members, including Thailand fall to recession. In China, imports were up strongly in April, as was domestic investment, and OECD leading indicators suggest that Chinese GDP growth has bottomed out in March (Figure 14). Chinese exports contracted by 26.4 percent in May, however, several percentage points more than expected and more than the 22.6 percent decline in April. May's decline was the steepest since data began being released in 1995. Imports fell by 25% (more than the 23% in April).

**Figure 14. China: Imports and Industrial Production**



Source: National Bureau of Statistics of China

**Inflation is slated to slow substantially into 2009-10 as economic activity slows and commodity prices decline from their peak in 2008.** Inflation in the G-7 economies has eased to 0.4 percent from 2.9 percent in 2008 as commodity prices retrench and weak demand and continued rise in unemployment keep price pressures at bay. Central bank fears of deflation will likely be offset by continued additions of liquidity to economies through stimulus programs and financial support measures. If prices temporarily fall in some developing countries, the risk of widespread deflation is still small, as the fall in commodity prices is expected to be a one-time event, and core inflation was until recently on an upward trend in response to the surge in food prices during 2008. Moreover, many countries may experience further weakening of their currencies, which would curb disinflationary pressures.

**The outlook for the second half of 2009 and 2010 remains highly uncertain, but signs of recovery have started to emerge as massive fiscal and monetary policy stimulus start to take effect.** Although recovery in the second quarter may be a one-off restocking following an overshooting of inventory draw-downs in the first quarter, some indicators, especially purchasing managers' indices, point to signs of a possible global recovery. The pronounced cycle in worldwide investment could have sufficient dynamic to carry global growth back to positive territory by 2010, as the pace of decline in investment moderates, and postponed demand for durable consumer goods begins to catch up. However, continued banking problems or even new waves of tension in financial markets could lead to stagnation in global GDP or even to another year of decline in 2010. In all cases, the estimated output gap would increase in 2010 because growth is likely to fall well short of potential. This implies that unemployment and fiscal deficits will increase further into 2010, in high-income and developing countries alike, while disinflationary conditions could persist well into the year.

## 2.4 Export Performance

**The global economic recession has hit Thailand's goods and services exports hard.** Since November 2008, goods exports have fallen by 21 percent on average per month. Current shipment levels are at only 67 percent of their peak in July 2008. Nearly all products have experienced a decline, with agricultural products and high-tech goods leading the declines. Shipments to all major destinations decreased sharply. Apart from subdued export volume, less supportive prices also contributed to poor performance, especially in recent months. Nevertheless, Thailand's goods exports have so far dropped less steeply than in most other East Asian countries. Travel receipts plunged 25 percent on average per quarter since the third quarter of last year. Room occupancy rate is at the lowest level since mid-2003, while room prices

started to fall. Unlike goods exports, the number of overseas visitors to Thailand has shrunk more significantly than in other Asian countries, partly attributable to increased political tensions and the unrest seen in December and April. Going forward, there are some early signs of easing contraction in the world economy but a quick, robust recovery is not expected. The World Bank estimated that goods exports in US dollar terms would decline by nearly 15 percent in 2009. Sections 2.4.1 and 2.4.2 below will discuss Thailand's exports of goods and services in more detail.

**The government has introduced policies to support exporters and tourism operators.** In response to a collapse in world demand, the government has launched several measures to assist Thai exporters. For example, it has allocated to the Export-Import Bank of Thailand ("EXIM Bank") ten and five billion baht, respectively, for export credit and export insurance. Tariff cuts for imported materials are also under review. In addition to these short-term, financial measures, long-term responses include marketing campaigns to explore new export markets and incentives to enhance product quality through innovation, branding, and specialised services institutes. For the tourism industry, government's short-term programmes include marketing campaigns, a temporary waiver of tourist visa fees, reduced electricity insurance fee for hotel operators, and lower landing and parking fees at the airports.<sup>2</sup> Despite these efforts, the latest monthly data on goods exports and tourist arrivals remain very weak.

**The global economic crisis presents new trade opportunities and challenges for Thailand.** The current downturn has led to lower wealth in major industrial economies as a result of job losses, lower wages, reduced property values, and tighter access to finance. Many analysts believe that this will shift the post-crisis international trade pattern. In particular, large emerging economies such as China and India will play a stronger role as final consumers, rather than assemblers of goods destined to the US and Europe.<sup>3</sup> Thailand therefore requires new policies to benefit from new opportunities in these emerging economies. At the same time, new policies are needed to cope with fiercer competition in mature economies due to fewer orders. Purchasing power in rich countries is still much higher than emerging economies so they will remain critical.<sup>4</sup>

## 2.4.1 Merchandise Exports

**Since November 2008, Thailand's export performance deteriorated sharply.** Exports in US dollar terms fell around 21 percent year-on-year in the first quarter of 2009, the largest quarterly drop in more than a decade. The pace of decline increased further to 26-27 percent in April and May (Figure 15). In terms of value, the current level of exports is only 67 percent of the peak in July 2008 (Figure 16).

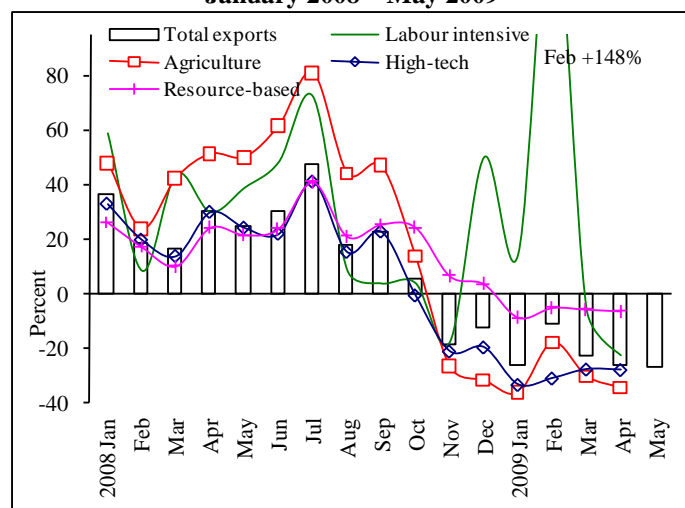
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<sup>2</sup> Monthly employment conditions survey by the National Statistical Office does not yet seem to indicate lower employment level in the hotels/restaurants sector, which currently hires about 2.7 million workers. Nonetheless, reduced working hours and lower wages are widely reported but not captured by the survey (the survey defines employed persons as those who work at least one hour in the seven days prior the survey).

<sup>3</sup> Currently, much of Thailand's exports to China are intermediate goods and parts and components. During January 2007 to mid-2008 (before export slump), although computers alone accounted for one-fifth of total shipments, other major items were electronic integrated circuits, computer parts, and various chemical substances.

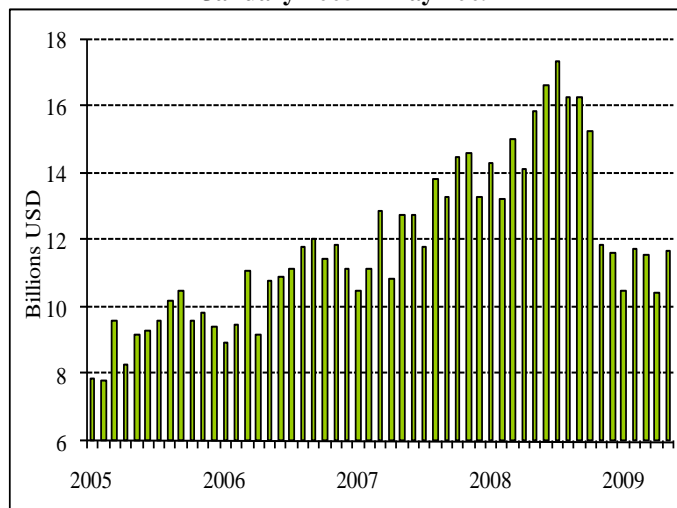
<sup>4</sup> For example, China's gross national income per capita was 20 times lower than the US level in 2007, although the gaps are shrinking following the downturn. This was over 15 times relative to the Euro Area and Japan. For India, this ranged between 38-49 times.

**Figure 15: Monthly export growth rates (%) (YoY), January 2008 – May 2009**



Source: Bank of Thailand and Ministry of Commerce

**Figure 16: Monthly export values (billions US dollar), January 2005 – May 2009**



Source: Bank of Thailand and Ministry of Commerce

**Agricultural products and high-tech goods have been the main drivers of the decline in exports.**

Overall, exports grew reasonably well at 17 percent in 2008, which was comparable to 2006 and 2007 (Table 8). Shipments were very solid in the first three quarters (+27 percent), supported by then stable (if weakening) world economy and favorable agricultural prices. A synchronised output contraction in developed economies however quickly translated into poor performance in the final quarter, especially for agricultural and high-tech items. The rates of decline for these two product groups, accounting for three quarters of total export value in 2008, extended from around 15 percent in the fourth quarter of last year to 30 percent during the period between January and April 2009. Although Table 8 shows that exports of labour-intensive goods continued to expand, this was virtually driven by precious metals exports especially gold in February 2009 (Figure 15). In April, all product groups now experienced negative growth.

**Table 8: Export growth rates by major product groups (%) (YoY), 2006 – April 2009**

	Share (%)	Growth (%)					
				2008			2009
				Year	Q1-Q3	Q4	
<b>Agriculture 1/</b>	<b>10.5</b>	<b>26.7</b>	<b>15.0</b>	<b>30.5</b>	<b>49.8</b>	<b>-15.5</b>	<b>-30.2</b>
<b>Manufacturing</b>	<b>88.0</b>	<b>16.1</b>	<b>18.8</b>	<b>16.5</b>	<b>25.8</b>	<b>-7.8</b>	<b>-20.6</b>
Labour intensive products	9.3	6.8	18.9	25.3	32.0	9.4	30.4
High-tech products	62.7	17.8	17.7	13.5	24.0	-13.8	-30.2
Resource-based products	10.5	13.8	21.6	19.9	23.0	11.4	-6.5
Other manufactured products	5.5	16.9	28.8	32.3	45.2	0.5	-15.2
<b>Others 2/</b>	<b>1.5</b>	<b>12.4</b>	<b>-18.2</b>	<b>-22.1</b>	<b>-25.3</b>	<b>-6.2</b>	<b>-40.6</b>
<b>Total exports</b>	<b>100.0</b>	<b>16.9</b>	<b>17.2</b>	<b>16.9</b>	<b>26.7</b>	<b>-8.5</b>	<b>-21.9</b>

Source: Bank of Thailand

Notes: 1/ "Agriculture" includes agricultural, fishery and forestry products

2/ "Others" refers to mining, samples & other unclassified goods, and re-exports

**Exports of all major products experienced a sharp decline.** Except for precious stones and jewellery, Thai exporters in all sectors have suffered from the global economic recession (Table 9). The situation worsened quickly in 2009 relative to the fourth quarter of last year, either in terms of much lower positive growth, a shift from positive to negative growth, or more negative growth. Key products such as computers, integrated circuits, and passenger cars registered a decline between 32-35 percent, much higher than the all-product average. Table 10 below suggests that although some products (mostly resource-based such as sugar and processed food items) continued to record an expansion, their shares are very small.

**Shipments to all key markets contracted, but recent data suggests exports to emerging Asia may be stabilising.** Table 10 shows that exports to some destinations such as Australia and Myanmar continued to grow but their market shares are relatively small.<sup>5</sup> Figure 17 depicts contribution to Thailand's export growth by markets, and appears to suggest that the contraction in exports to developing Asian economies has stabilised in recent months. In the final quarter of last year, ASEAN and China together accounted for 72 percent of a decline in Thailand's total exports. This softened significantly to 42 percent in the first four months of 2009. For example, exports to China decreased by around 13 percent in April compared to the average of 28 percent in the first quarter. In contrast, exports to Japan and the EU fell more heavily so far this year than in late 2008.<sup>6</sup> The positive contribution to overall exports by alternative markets such as the Middle East and "other markets" that was still observable in the final quarter of 2008 also recently vanished.<sup>7</sup> Overall, this provides a mixed picture. Shipments to industrial economies remain very weak, while alternative markets also lost steam. There is however some sign of stabilisation in Asian destinations, partly supported by higher orders from high-income markets, although this could be fragile.<sup>8</sup>

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<sup>5</sup> Gold mainly explain a remarkable expansion in shipments to Switzerland.

<sup>6</sup> For the EU, growth in last year's final quarter was -7.6 percent but significantly extended to -31.5 percent so far in 2009. For Japan, these figures are -4.9 and -26.9 percent, respectively.

<sup>7</sup> Among others, "other markets" include Australia, Hong Kong, India, South Korea, Russia, South Africa, and Taiwan (China).

<sup>8</sup> US new orders for manufactured goods rose 0.7 percent in April 2009 (month-on-month, seasonally adjusted) after a mere two percent contraction in March. Household appliances, electrical equipment, and motor vehicles and parts registered between 2.2 to 10.5 percent expansion. New orders for computers however plunged by 7.1 percent.

**Table 9: Export growth rates by key products (%) (YoY), 2006 – April 2009**

	Share (%)	Growth (%)					
	2008	2006	2007	2008			2009
				Year	Q1-Q3	Q4	Jan-Apr
<b>Agriculture</b>							
Rubber	3.8	45.5	4.5	20.4	37.6	-21.3	-47.5
Rice	3.5	10.9	34.3	78.9	134.4	-18.0	-19.4
Tapioca products	0.8	34.3	23.2	3.6	18.2	-35.3	-40.4
Fresh and frozen prawns	0.7	20.2	10.5	4.5	3.3	8.2	2.2
<b>Resource-based products</b>							
Rubber products	2.3	23.5	22.1	21.3	25.3	10.4	-17.6
Canned food	1.9	13.7	28.5	32.8	44.6	6.5	-15.5
Sugar	0.8	5.0	70.7	14.7	8.1	55.5	26.8
Furniture & furnishing items	0.6	-1.3	-9.4	-5.4	-3.9	-9.6	-24.6
<b>Labour-intensive products</b>							
Precious stones & jewellery	4.6	13.7	46.7	53.7	70.3	22.9	85.3
Garments	1.7	1.5	-6.5	3.3	4.2	0.6	-10.2
Other textile products	0.9	8.7	14.2	12.6	16.6	1.6	-12.5
Wood products	0.7	18.6	11.1	1.1	10.0	-23.4	-25.6
<b>High-tech products</b>							
Machinery & mecha. appliances	14.2	25.2	16.4	7.8	19.5	-19.9	-30.0
Electrical apparatus for circuits	8.7	8.0	12.1	-0.7	4.9	-17.3	-31.0
Vehicles, parts & accessories	9.4	22.1	28.2	30.0	39.7	3.0	-35.2
Electrical appliances	6.8	9.4	17.4	6.5	12.8	-12.3	-29.9
<b>Top 5 sub-products</b>							
Computers	7.5	28.7	14.8	8.3	20.3	-20.7	-31.6
Rubber	3.8	45.5	4.5	20.4	37.6	-21.3	-47.5
Integrated circuits	3.7	16.4	16.9	-10.1	-3.4	-31.0	-34.0
Rice	3.5	10.9	34.3	78.9	134.4	-18.0	-19.4
Passenger cars	2.4	32.7	10.1	35.7	50.6	0.4	-35.1

Source: Bank of Thailand

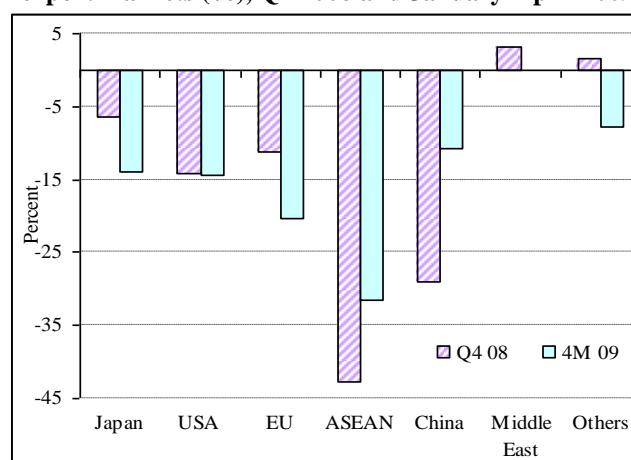
Note: Products in each category are the four products with the highest market shares in 2008.

**Table 10: Export growth of some products & markets with positive growth, Q4 2008 and Jan-Apr 2009 (%)**

	Share in 2008 (%)	Q4 08	Jan-Apr 09
<b>Products</b>			
Precious metals and stones	4.7	22.9	85.3
Sugar	0.8	55.5	26.8
Fresh & frozen prawns	0.7	8.2	2.2
Dog and cat food	0.4	15.9	5.8
Misc. canned food	0.2	30.7	2.9
Forestry products	0.1	77.9	8.8
Salted dried fish	0.0	11.4	5.0
<b>Markets</b>			
Middle East	5.3	5.4	0.4
Australia	4.5	9.1	7.2
Switzerland	1.1	111.1	250.7
Myanmar	0.7	16.4	5.9

Source: Bank of Thailand

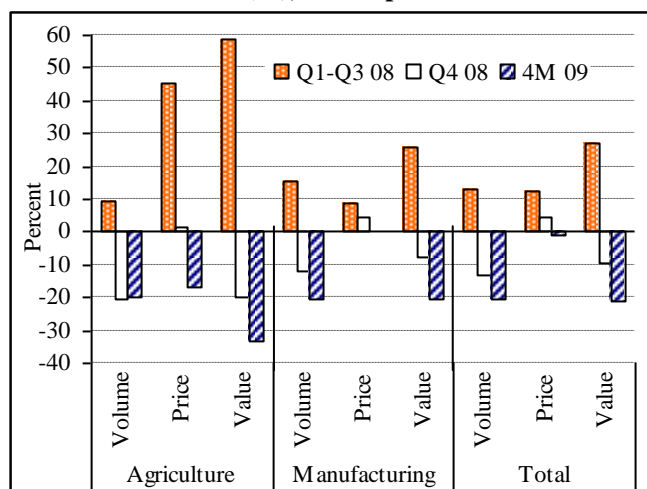
**Figure 17: Contribution to total export growth by export markets (%), Q4 2008 and January-April 2009**



Source: Bank of Thailand

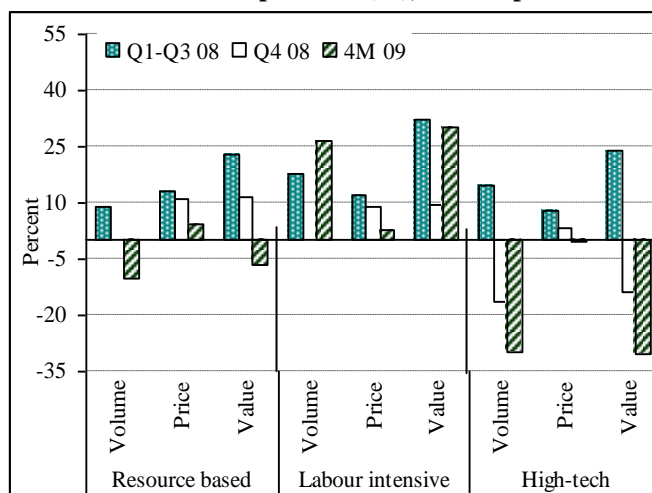
**In addition to lower export volume, less supportive prices contributed to the decline in the dollar value of exports.** Figure 18 depicts changes in export volumes and export prices of different product categories. Prices have been very volatile for agricultural commodities: prices went up by 45 percent on average in the first nine months of 2008 and fell nearly 20 percent in the first four months of this year. For instance, the average export prices (US dollar per ton) of rice and smoked Para rubber sheet dropped 8 and 46 percent so far in 2009 relative to the 2008 level, respectively. So a sharp fall in rubber and rice exports highlighted in Table 9 can be largely attributed to the price effect.<sup>9</sup> The price effect has generally been less dramatic for manufactured goods, and fewer orders mainly explain weaker performance. While price changes of other manufactured goods remain positive, prices for high-tech items decreased on average one percentage point per month since February 2009.

**Figure 18: Changes in overall export volume, price and value (%), 2008-April 2009**



Source: Bank of Thailand

**Figure 19: Changes in export volume, price and value of manufactured products (%), 2008-April 2009**

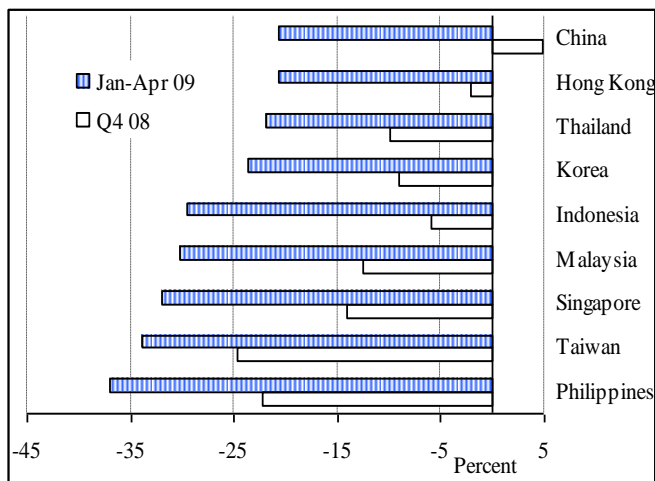


Source: Bank of Thailand

**Thailand's exports dropped less severely than in most other East Asian countries.** Despite a very poor performance relative to its own history, the global economic recession has so far dampened Thailand's exports less heavily than most other regional economies. In Figure 20, exports in the Philippines and Taiwan (China) declined by 33-34 percent on average per month between November 2008 (the first month that all countries faced negative export growth) and April 2009. The comparable figure is -20 percent for Thailand, which is only outperformed by China and Hong Kong. Meanwhile, Figure 21 shows that the movements in the region's real effective exchange rates have been generally limited since late 2008. As in the booming period, the relationship between changes in the exchange rate and export performance appears weak during the export collapse period. Both China and Hong Kong's currencies appreciated since the last quarter of 2008 yet they have exhibited the smallest export decline so far.

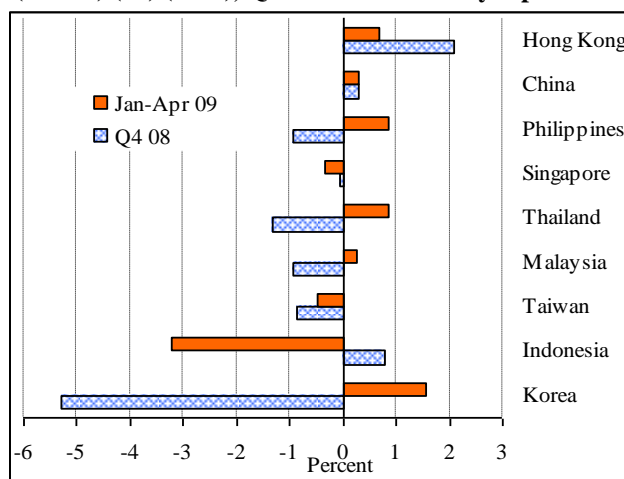
<sup>9</sup> Prices of key fishery products also fell. Average export prices (US dollar per ton) for preserved tuna fish and chilled and frozen fresh fish also dropped by 16.2 and 7.4 percent respectively so far this year.

**Figure 20: Export growth rates in selected East Asian economies (%) (YoY), Q4 2008 and January-April 2009**



Source: World Bank and national authorities

**Figure 21: Changes in real effective exchange rate (REER) (%) (YoY), Q4 2008 and January-April 2009**

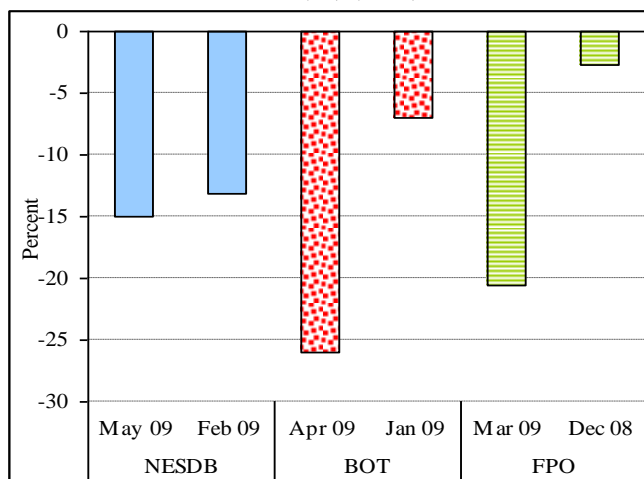


Source: World Bank estimates, (+)=appreciation

**Export prospects remain dim but there are signs that a bottom may have been reached.** Figure 22 depicts forecast export growth rates in US dollar term in 2009 by different public agencies. The outlook sharply deteriorated between December 2008 (-2.7 percent by the Fiscal Policy Office) to April 2009 (-26 percent by the Bank of Thailand).<sup>10</sup> Among agencies, newer estimates always reflected lower growth, but the latest estimate by NESDB in May (-15 percent) seems to suggest a view on the stabilisation of the decline. This is largely in line with World Bank's projection of -14.6 percent (as of June 2009). Across the world, there appears to be an early sign of stabilisation. OECD's latest composite of leading indicators shows slower pace of decline. Inventory drawdown resulted in improved purchasing managers' indices in many industrial and emerging economies in April. Consumer confidence in the United States and the European Union also rose, while import demand by Asian economies fell more slowly. Despite these developments, a sharp turnaround in world economic conditions is unlikely given that growth constraints in high-income countries still prevail. These include among others poor commercial banks' balance sheet and much lower wealth due to weak labour markets, reduced property prices, and relatively high household debts. Scarcer trade finance worldwide and less favourable agricultural prices also limit a strong recovery in Thai exports. The World Bank's food price index is predicted to fall by 26 percent this year relative to 2008. International prices of rubber could drop up to 70 percent, while this is -11 and -23 percent for prawns and rice respectively.

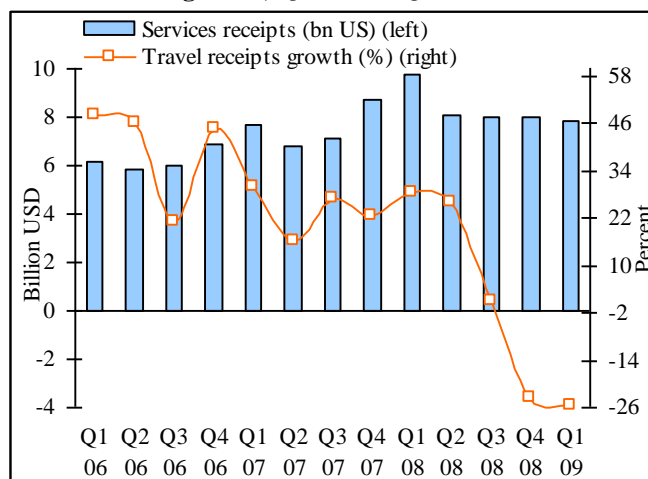
<sup>10</sup> Bank of Thailand's official estimate is -27.5 to -24.5 percent. Figure 22 presents the average value.

**Figure 22: Forecast export growth in US dollar terms for 2009 (%) (YoY)**



Source: World Bank staff compilation

**Figure 23: Services receipts value and travel receipts growth, Q1 2006 – Q1 2009**



Source: Bank of Thailand

## 2.4.2 Services Exports

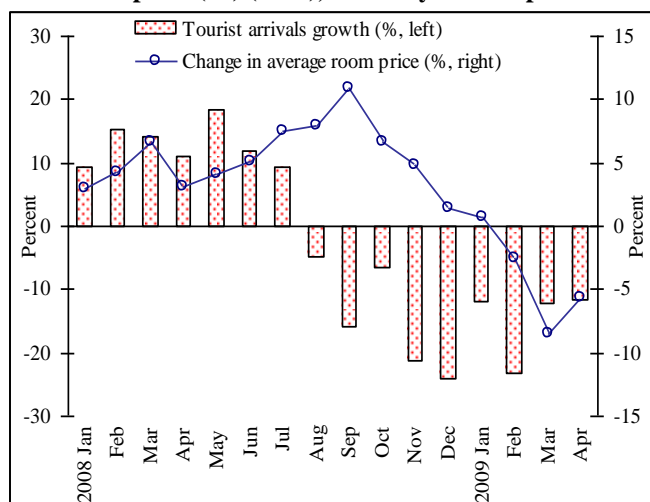
**Travel receipts fell even more steeply than goods exports.** Travel receipts, which are mainly income earned by the tourism sector, have deteriorated quickly since the second half of last year. Receipts barely expanded in the third quarter of 2008 before contracting between 23-26 percent (year-on-year) during the following two quarters (Figure 23 above). Faced with both the global economic recession and domestic political unrest, Thailand's tourism businesses appear to have been more swiftly and severely hurt than exporters.<sup>11</sup> Accounting for over half of total services receipts, lower travel receipts also led to a fall in services receipts of 8.4 percent in the fourth quarter of 2008 and 19.3 percent in the first quarter of this year. Figure 23 shows that a noticeable decrease is driven by high base. The values are not significantly lower than the preceding periods.

**Tourist arrivals continued to fall and started placing pressure on room prices.** International tourist arrivals to Thailand have plunged since August 2008 (Figure 24). The latest data in April 2009 registered a decline of 11.6 percent, which is comparable to March. While the impact on tourist arrivals of the political violence in mid-April appears to have been less severe than most analysts anticipated<sup>12</sup>, room occupancy rates currently stand at only 43 percent. This is similar to December last year and is the lowest level since July 2003. In terms of origin, Figure 25 shows that since October last year, the number of visitors from East Asia (Japan, South Korea, and China) have dropped significantly, between 30-45 percent on average. The decline is less steep for tourists from other regions, while the Middle East still recorded a positive growth of over 10 percent. Meanwhile, year-on-year changes in average room price eventually turned negative in February 2009, after exhibiting decelerated growth since September last year (Figure 24). Hotel operators now suffer from both lower occupancy rates and room prices.

<sup>11</sup> Goods exports still expanded strongly at 28.4 percent in the third quarter of 2008, and fell on average 14.7 percent during the two quarters that followed.

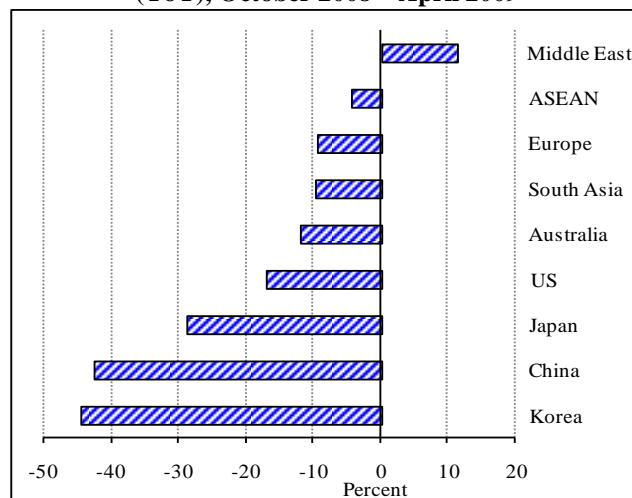
<sup>12</sup> This is perhaps because demand had already been weak. The violence was also only limited to certain areas in Bangkok. Similarly, social unrest in early October 2008 had a small effect on visitor numbers. This is in contrast to the airport closure in December last year, when tourist arrivals dropped 24 percent year-on-year.

**Figure 24: Changes in monthly tourist arrivals and average room price (%) (YoY), January 2008–April 2009**



Source: Bank of Thailand

**Figure 25: Tourist arrivals growth by nationality (%) (YoY), October 2008 – April 2009**



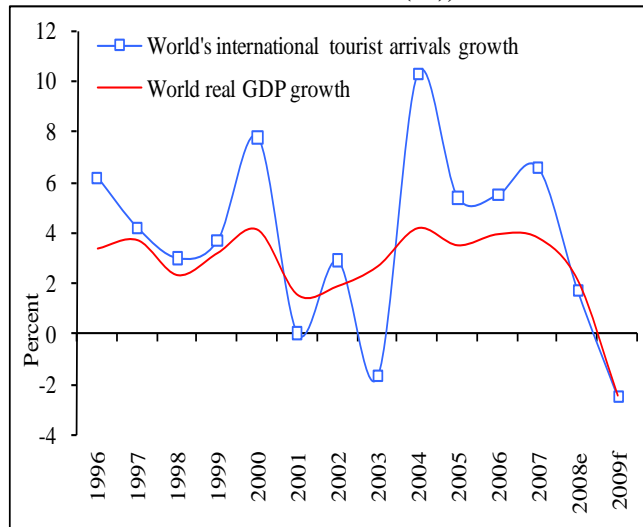
Source: World Tourism Organisation and World Bank  
E=estimate, f = forecast

**The number of overseas visitors to Thailand has shrunk more significantly than those to other Asian countries.** Tourism is weak worldwide. During the first two months of 2009, world tourist arrivals dropped by 7.7 percent according to the World Tourism Organisation (UNWTO). This represents a deterioration from a 2.7 percent contraction in the final quarter of 2008. The spread of influenza A (H1N1) will further dampen tourism worldwide. By region, the number of visitors to Asia and the Pacific decreased by nearly seven percent during this period, and about 4.7 percent for South East Asia.<sup>13</sup> Therefore, unlike goods exports where the magnitude of decline in Thailand has so far been smaller than many other regional economies, the number of overseas visitors has dropped more sharply (-17.5 percent for Thailand). In addition to the global downturn, the domestic political crisis has played an important role.

**Prospects for the tourism sector remain poor.** Looking forward, the tourism industry is anticipated to remain subdued worldwide. In May this year, the UNWTO revised downwards its 2009 forecast for world's international tourist arrivals to -2 to -3 percent from zero to -2 percent in January (Figure 26 displays the mean value). For Thailand, tourists from the G-3 economies, accounting for 40 percent of all visitors before the slump in August 2008, are not expected to pick up soon. Although the prospect for ASEAN and China (one-third of all tourists) is arguably more positive, this remains fragile.

<sup>13</sup> Between January and February 2009, international visitors to Europe and Americas went down by 8.4 and 1.4 percent respectively. Africa still gained four percent more tourists during this period.

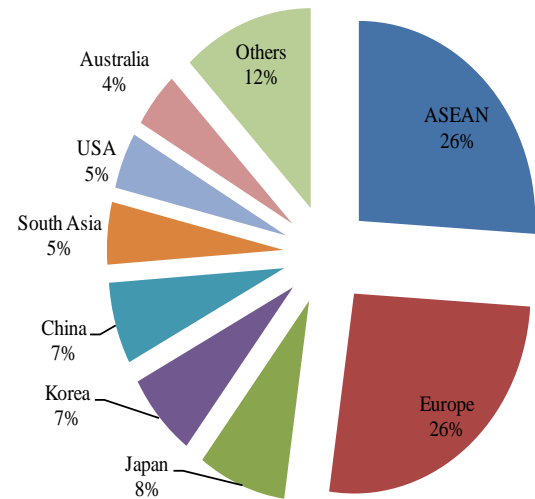
**Figure 26: Growth rates of world's international tourist arrival and real GDP (%), 1996-2009**



Source: Office of Tourism Development

Note: Within “others”, the larger ones are Taiwan, Hong Kong, and Middle East.

**Figure 27: Tourist arrivals to Thailand by nationality (%) (YoY), January 2007– July 2008**



Source: Office of Tourism Development

## 2.5 Household Consumption

### **Boosted by a jump in vehicle sales, private consumption posted modest but steady growth in 2008.**

Private consumption, which accounts for over half of GDP in real terms, has been the least volatile component of aggregate demand, growing by 2.2 percent in the fourth quarter and 2.5 percent for 2008 as a whole. Household consumption growth was supported by overall stable employment, increasing real wages and credit growth to households. Despite a contraction in manufacturing employment since May, gains in services and agriculture led employment to grow slightly more than the labor force in 2008. Unemployment, on the other hand, averaged 1.4 percent for the year, about the same as in 2007 (Figure 28 and Figure 29). Meanwhile, despite increased inflation, real wages were up 4.8 percent (Figure 30) year-on-year, and growth in credit to individuals was up by 5.3 percent in real terms. The largest contribution to private consumption growth came from vehicle sales, which jumped 14.4 percent in 2008 compared to a contraction of 11.6 percent in 2007.

### **The deteriorating outlook in the labor market has eroded consumer confidence and caused household consumption to contract in the first quarter of 2009.**

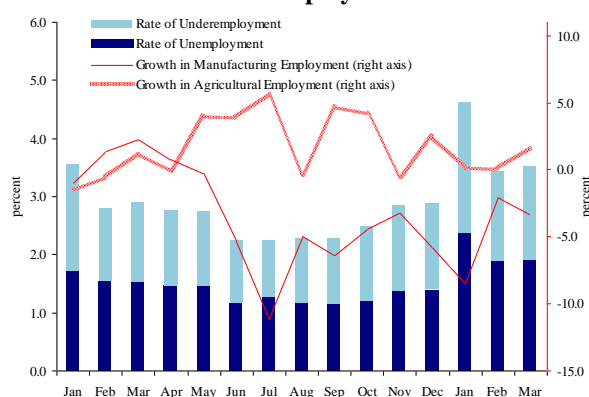
Household consumption contracted by 2.6 percent in the first quarter of 2009 dragged by a decline in vehicle sales, which plunged by 16 percent. The drop in consumer confidence is linked to a deteriorating outlook in the labor markets, which is likely to remain a drag on the consumer throughout 2009. The deep contraction in industrial production and construction observed in the fourth quarter of 2008 started to become visible in January's employment figures: the unemployment and under-employment rates spiked to their highest levels since 2005<sup>14</sup> (Figure 28). The labor market response to the crisis appears to be primarily through adjustments in the quantity of labor. Firms have shed jobs outright, but to retain qualified workers they have also cut the hours of a significant number of workers. The number of persons working less than 35 hours and available to work

<sup>14</sup> Under-employed individuals are defined as those who worked 35 hours a week or less, but were available to work more.

more jumped 26 percent year-on-year in February, in line with increase in the number of unemployed, which went up by 27 percent; employment growth (net of increases in the labor force) has been negative since November (Figure 29). Between May 2008 and January 2009, job losses in manufacturing had been largely compensated by increases in agricultural employment (Figure 28). Service sector jobs also grew in the period, although many are likely to be in the informal sector. These employment dynamics have been biased towards greater employment in sectors where wages are generally lower, such as agriculture and construction (see Table 11), and should put further pressure on household incomes in 2009.

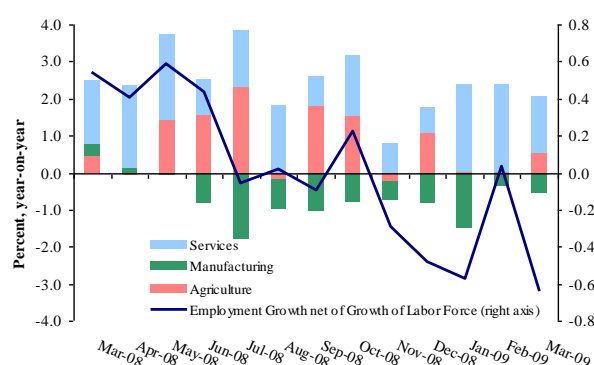
**Recent data on consumption indicators shows a mixed picture.** VAT collections have increased in April, suggesting that the fiscal stimulus checks given by the government in late March and early April were making their way into the economy. On the other hand the consumer confidence index and the private consumption index continued to decline, the latter led by weakness in vehicle sales (Figure 31).

**Figure 28. Employment Growth, Underemployment and Unemployment**



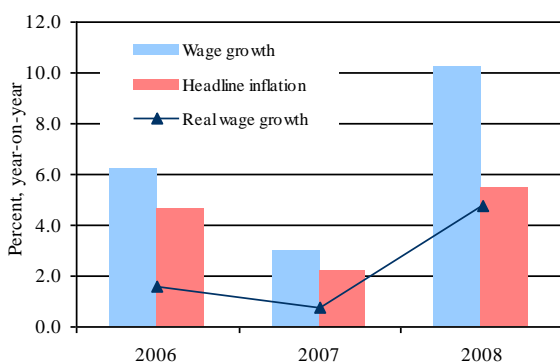
Source: NSO

**Figure 29. Employment Growth by Sector**



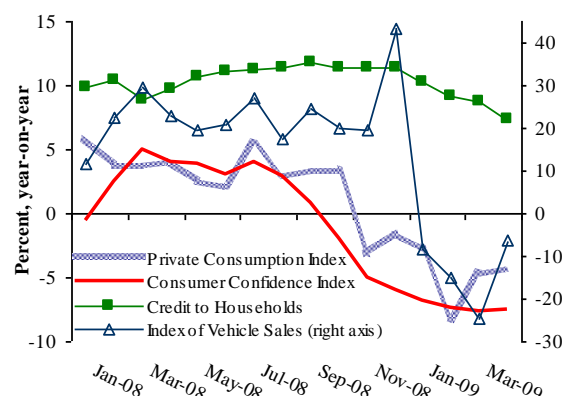
Source: NSO

**Figure 30. Wage and Real Wage Growth**



Source: NSO, MOC, WB calculations

**Figure 31. Private Consumption Index and Indicators**



Source: BOT and UTCC

**The government's fiscal stimulus package may help mitigate the decline in consumer confidence.** The stimulus package announced in January was aimed at boosting private consumption through substantial tax reductions and income transfers. Transfers include a one-time transfer of Bt2,000 per person to nearly 10 million formal-sector workers receiving a monthly salary of less than Bt15,000, monthly transfers of Bt500 per person to 3.8 million elderly who currently do not receive another form of

pension or transfer, full subsidy on education for 15 years for around 11.8 million students, and an allowance of Bt600 per month to each of the 987,000 community healthcare volunteers. In addition, subsidies on public service are being provided for 6 months (February to July 2009), including electricity and water subsidy for households with low usage, fare waiver on many routes of non-air-conditioned public buses in Bangkok, fare waiver on third class train rides, and subsidy of cooking gas for household use. These measures started to be implemented in late March and should start taking effect in the second quarter.

**Table 11. Average Wage and Change in Employment by Sector**

	Average Wage (Baht per month)	Change in employment (y-o-y) (Million persons)			
	2008	2008 Q2	Q3	Q4	2009 Q1
<b>Total</b>	<b>8,913</b>	<b>1,109</b>	<b>715</b>	<b>677</b>	<b>683</b>
<i>Memo: Increase in the labor force</i>		<i>1,044</i>	<i>723</i>	<i>769</i>	<i>1,833</i>
<b>Agricultural</b>	<b>4,266</b>	<b>497</b>	<b>575</b>	<b>451</b>	<b>109</b>
<b>Non-Agricultural</b>	<b>9,749</b>	<b>613</b>	<b>139</b>	<b>226</b>	<b>574</b>
Manufacturing	7,685	-123	-362	-205	-216
Construction	5,954	46	73	129	83
Wholesale and retail trade, repair of motor vehicles motorcycles and personal household goods	8,128	194	110	281	320
Hotel and restaurants	6,843	58	51	28	184
Transport, storage and communication	13,662	93	64	7	51
Real estate, renting and business activities	11,705	93	73	-11	20
Public administration and defense, compulsory social security	12,833	103	16	22	82
Education	18,060	-7	13	19	25
Others	...	155	101	-43	24

Source: NSO

## 2.6 Investment

**The investment component of GDP posted robust growth in 2008, though primarily due to a build-up of inventories.** Investment grew by 6.7 percent in real terms in 2008, but 83 percent of this growth was due to inventory accumulation, especially in the fourth quarter. Private fixed investment picked up from almost zero growth in 2007, adding 3.2 percent for the year, mostly due to increased investment in equipment (which grew by 4.3 percent). Private construction investment contracted slightly, while construction investment overall contracted by 5 percent on weak public investments, which declined by 4.8 percent during the year due to implementation delays exacerbated by the growing political crisis. In the fourth quarter, which corresponded to the height of the political crisis, gross fixed capital formation

declined by 3.3 percent led by a 10 percent fall in public investment (public construction declined by 26 percent). Private investment also fell in the fourth quarter, and investment only grew overall due to the accumulation of inventories.

**Investment was weak across the board in the first quarter of 2009, contracting nearly 50 percent.** All investment components posted substantial contractions in the first quarter, led by a drawdown in inventories that was larger than the inventory accumulation in all of 2008. Private investment was also weak, contracting 18 percent, while public investment also contracted 9 percent despite relative political stability and a political imperative to accelerate government spending. Investment in equipment plunged by 20 percent, while construction fell 8 percent.

**Investment is likely to contract more modestly during the rest of 2009 as inventories are replenished and the outlook improves only slowly towards the end of the year.** The high levels of inventory drawdown in the first quarter suggest overall investment is likely to contract by less in the coming quarters since there are few inventories left for drawing down upon. The continuation of the financial and political crises that dragged down investment in the past two quarters have not been reversed and will continue to drag down investment growth 2009. Although public investment is expected to rebound, overall investment is expected to decline by nearly 18 percent in 2009. Private investment is likely to decline by 7.5 percent during the year given high levels of capacity utilization and substantial uncertainties on the domestic political and international economic outlooks. Public investment is expected to accelerate by 3.3 percent given the implementation of the second round of stimulus measures, which is focused on public investment, as well as the low base from the previous year.

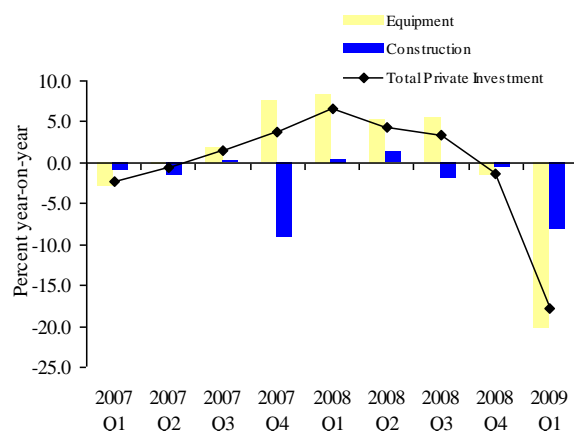
## 2.6.1 Private Investment

**Despite political uncertainty, investment picked up modestly in the first three quarters of 2008, before contracting sharply in the last quarter of 2008 and first quarter of 2009 as a result of the global financial crisis.** Private investment grew by 3.2 percent in 2008 overall compared to near-zero growth in 2007, but contracted by 9.5 percent year-on-year since the onset of the financial crisis in October (nearly 18 percent in the first quarter of 2009 alone). The expansion in investment in 2008 was primarily driven by equipment purchases, as construction contracted, especially in the last quarter of 2008 when the sector posted a 13 percent contraction (Figure 32). The pattern was reversed in the first quarter of 2009, when equipment investment plummeted by over 20 percent and construction contracted by 8 percent. Credit to businesses increased in 2008, supporting investment, and liquidity remains adequate, though banks have become more cautious, especially towards small and medium enterprises (SMEs). The share of private sector investment in GDP fell from 18.5 percent of GDP in the second quarter of 2006 to 15 percent in the first quarter of 2009 as private investment has continued to grow by less than overall GDP, suggesting that businesses have been pricing in substantial risks to the economic and political outlook.

**The outlook for private investment in the near term and 2009 overall remains negative, but a return to positive growth is possible in the fourth quarter.** Although it is likely that the contraction in the first quarter represented overshooting, private investment is still likely to post negative year-on-year growth in the second and third quarters. Negative factors weighing down investment growth in this period include high capacity utilization, which fell again in April to 56 percent (Figure 39), as well as credit constraints to SMEs, which have found it more difficult to obtain financing despite ample liquidity in the banking system. Recent indicators such as the private investment index, which closely tracks investment growth, suggest that a bottom may be within reach, but there is substantial uncertainty as to the sustainability of these improvements (Figure 33). Assuming prospects for economic recovery have

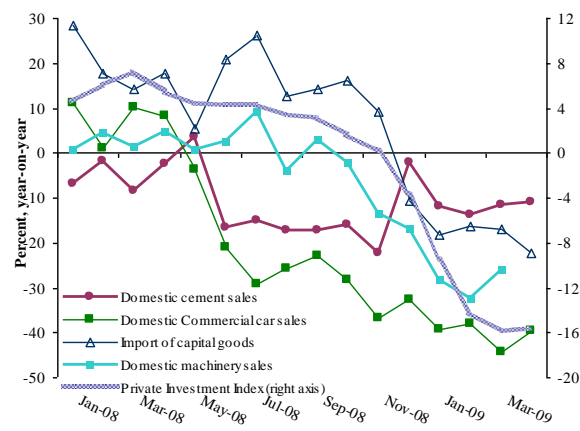
consolidated and political stability is maintained, improving business sentiment and still-low interest rates should support a return to positive growth in the fourth quarter, however, and private investment is expected to contract by 7.5 percent in 2009 overall.

**Figure 32. Private Investment Growth**



Source: NESDB

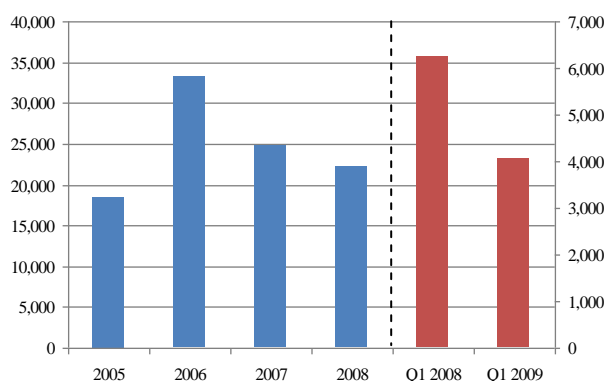
**Figure 33. Private Investment Indicators**



Source: BOT

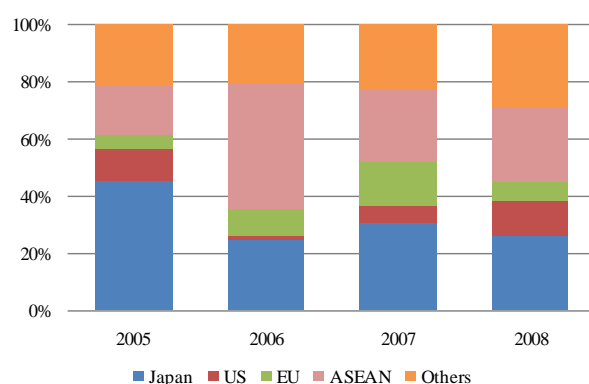
**Foreign Direct Investment (FDI) has been contracting, but outflows are not expected since investors appear to have largely priced in high political and economic risks.** Gross FDI flows contracted by nearly 40 percent in the first quarter of 2009 from one year earlier, while net FDI contracted by 20 percent (therefore in line with private investment overall) (See Figure 34). FDI will continue to decline in 2009 as Thailand's top two investors over the past three years – Japan and Singapore – are currently going through severe economic contractions (Figure 35). Moreover, the heightened risks of political instability are likely to weigh down on investment and FDI in particular as foreign investors. Notwithstanding these negative factors, no exodus of foreign investment is expected, since most investors had already priced in substantial political risks since 2006. Moreover, Thailand continues to be very well-ranked in the World Bank's "Doing Business" Survey (ranked 13<sup>th</sup> globally for ease of doing business), suggesting that it still retains a comparatively favorable business environment that is likely to be beneficial in the current environment.

**Figure 34. Gross Foreign Direct Investment Inflow**



Source: BOT

**Figure 35. Foreign Direct Investment Inflow by Country**

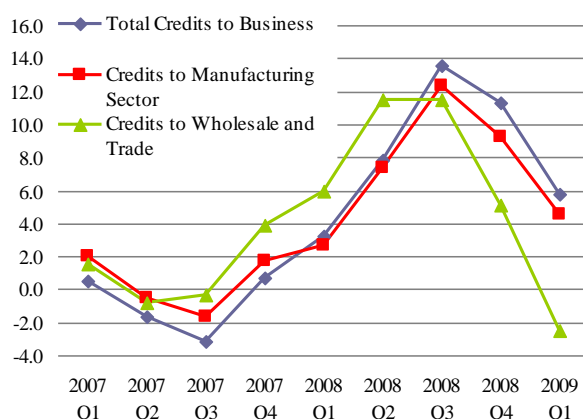


Source: BOT

**Credit to SMEs may be a constraint on private investment in 2009.** Total credits to business – including to the manufacturing sector – have continued to grow through the first quarter of 2009, though the growth rate has decelerated starting in the fourth quarter of 2008 (Figure 36). There is adequate liquidity in the banking sector, and part of the growth reflects the switch of large firms from foreign to domestic financing. Nonetheless, there is a concern that small enterprises are finding it harder to obtain credit because of heightened scrutiny of credit quality in a deteriorating economic environment. Anecdotal evidence of reduced credit to SMEs is reinforced by the contraction in credit to the wholesale and trade sector – which is more likely to include smaller firms. As a reflection of these concerns, the government has increased the capital of the SME Bank, a government specialized financial institution, as part of its stimulus package. This aims at increasing credit and supporting continued investments by these small businesses.

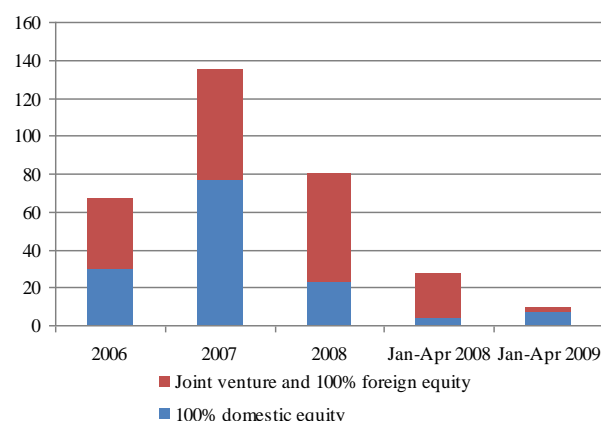
**Approvals of investment privileges by the Board of Investments (BOI) declined in 2008 from 2007, but were still 20 percent higher than in 2006.** In the first four months of 2009, approvals of joint-venture and foreign financed investment plummeted by nearly 90 percent compared to 2008 (Figure 37). This confirms the notion that new foreign investments will be scarce in 2009, even if earlier investments are not retrenched. It is likely that BOI approvals lead actual investment by several quarters since private investment was flat in 2007, when BOI approvals peaked. Therefore, the sharp decline in BOI approvals of foreign-financed investments suggests that recovery in private investment in 2010 will have to come primarily from Thai investors.

**Figure 36. Commercial Bank Credit Growth to Business Sector**



Source: BOT

**Figure 37. BOI Approvals of Applications**

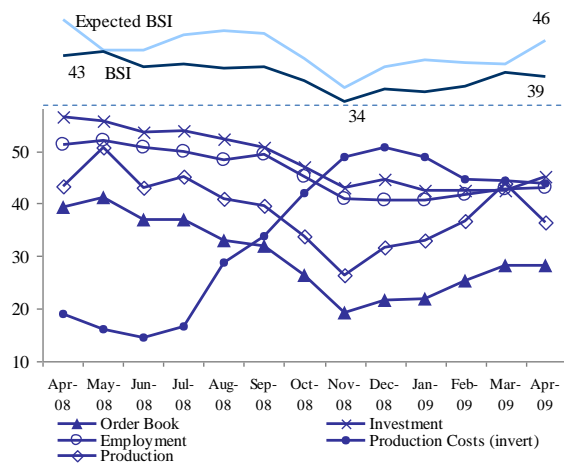


Source: BOI

**Business sentiment has been deteriorating since the beginning of the year suggesting an unfavorable outlook for investment.** The business sentiment index (BSI) deteriorated throughout 2008, reaching its lowest levels since 1999 in November.<sup>15</sup> The BSI has since improved, although it has remained below 50, suggesting business operators continue to see conditions deteriorate, albeit at a slower pace (see Figure 38), and the BSI deteriorated in April. The expected BSI also remains below 50, but is now back to levels of September 2008. BSI components provide a mixed picture regarding the outlook for investment: on the one hand, order book and production had been steadily increasing since November, but the production component fell again in April, while the order book remained stable. In all cases, however, the indices remain below 50, so that improvements still imply less rapid deterioration rather than improvements.

<sup>15</sup> Survey covered 521 medium and large sized businesses.

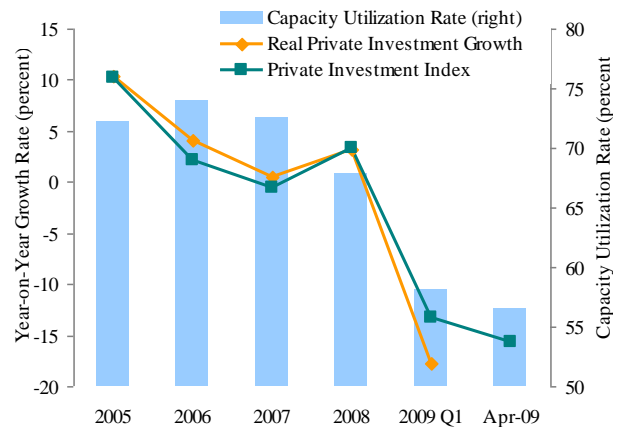
**Figure 38. Business Sentiment Index and Components**



Source: BOT

Index = 50 indicates that business sentiment remains stable.  
 Index > 50 indicates that business sentiment has improved.  
 Index < 50 indicates that business sentiment has worsened.

**Figure 39. Real Private Investment Growth and Capacity Utilization**

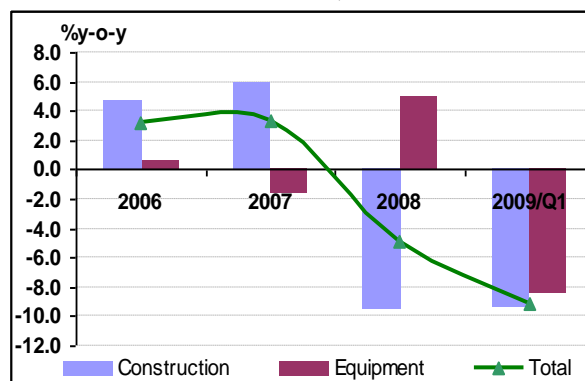


Source: NESDB and BOT

## 2.6.2 Public Investment

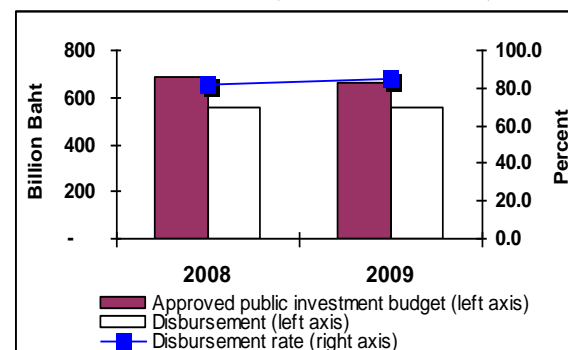
**Public investment contracted significantly in the first quarter of 2009 from a sharp decrease in construction.** In the first quarter of 2009, public investment in real term contracted by 9.1 percent, a continuation of negative growth from the last quarter of 2008 of 10.2 percent, mainly attributable from a contraction in construction. Public investment in construction though remained in a negative growth improved from the previous quarter's contraction of 26.2 percent because the material prices, particularly steel and concrete products have been declining. The delay disbursement in small construction projects under the stimulus package 1, accounted for 7 percent of the total package (excluding replenishment to the treasury reserves) made the public investment not improved as much as otherwise should have been.

**Figure 40. Public Investment Growth (in Real Terms)**



Source: NESDB

**Figure 41. Public Investment Budget, Disbursement, and Growth (in Nominal Terms)**



Source: FPO, NESDB, and WB calculations

Note: Public investment includes investment of central government, local government organizations, and state-owned enterprises

**Public investment in FY2009 is expected to grow significantly, attributable to additional small shovel-ready investment projects under stimulus packages and low base effect from last year's contraction.** Although public investment budget in FY2009, with supplementary budget incorporated slightly declined from the budget in FY2008 due mainly to a decrease in SOE investment budget, higher disbursement rates together with low-based effect from last year's contraction would help raise public investment growth this year. Accelerating disbursement is one of the government's measures to help stimulate the economy amidst the economic slowdown from global financial crisis. Additional small shovel-ready investment projects on water resource development and construction projects of housing for police in the first stimulus package would also further help boost public investment. The second stimulus package which was announced by the government in May 2009 is essentially a central government and some SOEs' investment plan over FY2010-2012 and mostly contains large investment projects, particularly water resources and transports with the total amount of budget of Bt 1.43 trillion. Given improvement in political situation as well as the Parliamentary approval on loan decree of 400 Billion Baht, the government would be able to implement the second stimulus package by the beginning of fiscal year. Public investment this year therefore is expected to grow by 3.3 percent in real term, significantly up from a contraction of 4.8 percent of last year.

**Disbursements on larger investment projects which are planned for FY2010-2012 will take more time unless institutional and political factors that had delayed them in the past are addressed.** The second stimulus package aims at medium term target to help generate growth, while enhances country's competitiveness. The package has been approved in principle with total budget of Bt 1.43 trillion by the economic cabinet in May 2009. If the government can implement infrastructure projects under the second stimulus package in a timely manner, it could help raise public investment growth to around 4-5 percent in real terms during FY2010-2012.

## 2.7 Financial and Corporate Sector Developments

### *Financial sector developments*

**The financial sector has been a source of strength in the Thai economy.** Total financial assets of the entire financial sector have represented approximately 180% of GDP for the last 5 years. Total assets of the financial sector have gradually increased at an average of 5% each year. While the financial system continues to be dominated by commercial banks (private, government and mixed ownership), the government-sponsored Specialized Financial Institutions (SFIs) represent a substantial share at approximately 20%. The SFIs generally aim to meet gaps in access to affordable financial services to those often overlooked by the commercial banks. After the financial crisis in 1997, the allowable ownership limit of foreigners in Thai commercial banks can be increased from 25% to 49% by Bank of Thailand's approval. Under the Financial Institutions Business Acts, Thai commercial banks are allowed to maintain foreign shareholding over 49% under the exemption offered by the Ministry of Finance. As seen in Table 12, the ownership structure of Thai commercial banks has changed in the last two years, now showing greater share of foreign ownership.

**Table 12: Foreign ownership of Thai Commercial Banks**

Ownership Interest	Less than or equal 25.00 %	25.00 % – 49.00 %	More than 49.00%
December 2006	5 banks (3 are Gov-owned)	7 banks	2 banks
December 2008	4 banks (1 is Gov-owned.)	6 banks	4 banks

Source: 1 Bank of Thailand Discussion Paper: DP/03/2007

2 Stock Exchange of Thailand

**A large share of the Thai population has access to formal financial sector services.** The ratio of population to bank branch ranges from 3,000 in the capital city, Bangkok, to 33,000 in the north-eastern part of Thailand. 33% of bank branches are located in Bangkok with the official population of 6.32 million (equal to 10% of total population). The substantial number of ATMs provides an increasing ability for access to basic financial services. At the end of 2008, there were 32,910 ATMs nationwide or on average 1 ATM for every 2,000 people. In addition, the big players in the banking sector now offer internet banking and telephone banking to accommodate customers' needs anytime anywhere.

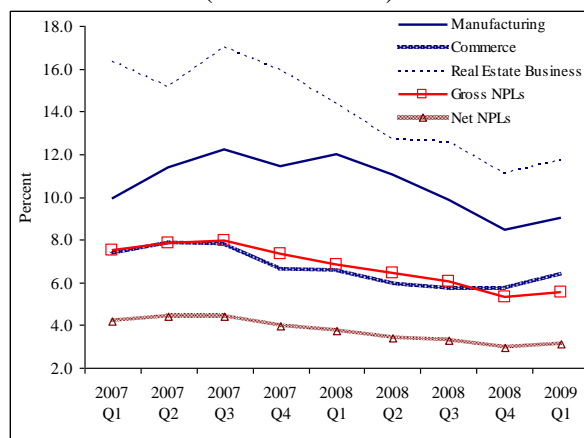
**The Thai banking sector has so far proven to be resilient against the immediate impact of the global financial troubles.** The Thai financial sector entered this financial crisis much better prepared than the last crisis in 1997. Most of Thai banks have performed well and are generally well capitalized. Capital adequacy ratios averaged at 13 percent over the last four years, well above the regulatory requirement of 8.5%. At the individual bank level, isolated capital inadequacies have occurred, but regulators have been proactive in addressing them. Most recently, for example, a capital problem at a small bank is being addressed through a capital injection from a Malaysian bank and the private placements of hybrid bonds. Profitability indicators have improved recently, jumping from THB 20 billion at the end of 2007 to THB 99 billion in 2008, in part due to full provisioning since 2007. Asset growth has been significant, averaging at about 5 percent per year. On the back of this growth, asset quality has improved among commercial banks, with net NPL to total loans declining to low levels of about 2.9 percent at the end of 2008. However the trend of the net NPL has been increasing and net NPLs of Thai banks have increased to 3.36% as of the end of March 2009. Likewise liquidity indicators have remained strong. Thai banks are basically funded by domestic deposits so funding and liquidity are less of concern than in some other markets. It is expected that money market liquidity could increase further because of expected capital inflows from redeeming investment in foreign-denominated currency assets.

**As the impact from the global financial crisis has spilled over to the real economy, the possibility of a spillover effect on the banking sector will need to be closely monitored.** Due to a decline in profitability of the corporate sector and elevated household risks, asset growth will likely weaken and asset quality deteriorate, which will cause NPL ratios to rise. As banks will need to provision for these anticipated losses, profitability and capitalization are expected to come under some pressure, which could create isolated pockets of vulnerability in the sector. Where vulnerabilities arise, the authorities will need to intervene rapidly and comprehensively so as to ensure that isolated confidence problem is not harmed and does not negatively spill over and amplify. Asset quality problems have occurred in some Specialized Financial Institutions (SFIs), which are regulated by the Ministry of Finance (MOF) and are not bound by the prudential requirements of the Bank of Thailand. As per Cabinet Resolution on February 17, 2009, the government approved the capital injection to the Export- Import Bank of Thailand of THB 5 billion and the Small Industry Credit Guarantee Corporation of THB 3 billion.

**The soundness of the banking sector is due in part to conservative regulations and tightened credit standards.** Bank of Thailand strictly follows international prudential regulations and has implemented IAS 39 and strengthened capital adequacy standards. The objective of the IAS 39 is to establish principles for recognizing and measuring financial assets/liabilities/contingencies. Following fully complying with Pillar 1 of the BASEL II guidelines in December 2008, the Thai banking sector's capital adequacy ratio (CAR) dropped by 123 bps representing market risk and operational risk. As of the first quarter of 2009, the CAR ratio stands at 14.74%, well above the regulatory requirement of 8.5%, serving as a cushion against a worse than expected deterioration of asset quality. In addition, commercial banks maintain their actual allowance in the level of 122% of their required allowance. Likewise, financial institutions have tightened their credit standards for both corporate and consumer loans, reflecting caution in their business operations amid increased risk involved both in general economic and industry-specific conditions.

**NPL have gradually declined but are expected to increase due to the effects of the global crisis on the real sector.** The direct impact on financial institution's NPL figure in the past periods was minimal. As can be seen in Figure 42, net NPLs have continued to decline, reaching 2.93% which is the lowest figure since prior to the Asian financial crisis in 1997. The economic outlook however, could be challenging this year, considering the global recession and the subsequent deterioration in credit quality of financial institutions' assets. In order to maintain their healthy balance sheets, commercial banks need to maintain good lending standards. This may result in some borrowers feeling it to be more difficult to access financing from the formal financial sector. The Bank of Thailand has categorically ruled out direct lending to companies, despite pressure to do so and the fact that it previously extended "soft loans" to companies through the financial sector prior to the passage of the amendment to the Central Bank Act in 2008. The BOT is instead working with the Ministry of Finance (MOF) so that the Specialized Financial Institutions (SFIs) under the MOF may increase credit to small and medium enterprises (SMEs). However, a fine line must be maintained between promoting access to finance and containing contingent public liabilities.

**Figure 42. Non-Performing Loans**  
(% Total Loans)



Source: Bank of Thailand

**Monetary policy has been eased to fight the economic downturn but the effectiveness of any further interest rate cut is likely to be limited.** The Bank of Thailand (BOT) lowered the policy interest rate by 0.25 percent on April 8, from 1.50 percent to 1.25 percent. This was the fourth rate cut since December 3. Given the ample liquidity in the domestic financial system, the market does not expect any more rate cuts in the near future due to the limited effect of the government's monetary policy.

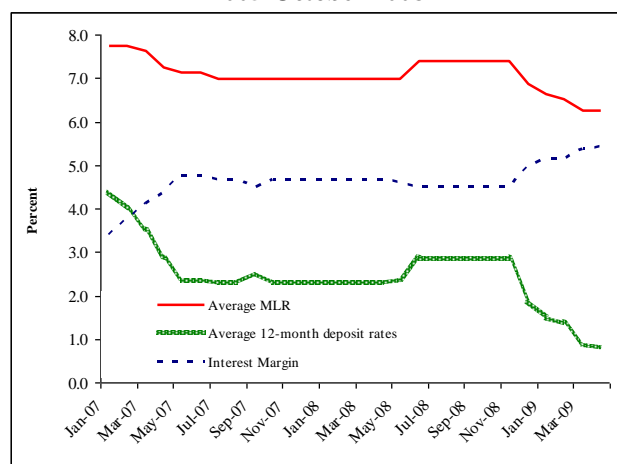
**Interest rates in the financial markets tend to respond to the trend in the BOT's monetary policy committee (MPC) rates, but not in the same magnitude.** Consequently, the net interest margin (NIM) has widened (Figure 43). Given the significant decline in economic environment, the MPC decided to ease monetary policy to help support economic recovery, particularly as the current economy faced numerous negative risks. As per Table 13, the market interest rate followed in the same direction but in a different magnitude. The deposit rate declined more than double that of the lending rate. As a result, the net interest rate margin (NIM) has gradually widened. Most recently, as an example, the BOT lowered the policy interest rate for a cumulative of 175 bps from 3.75% in October 2008 to 2.00% in January 2009. While the average 1-day overnight interbank rate was lower by 158 bps, the average 12 months deposit rate and the average minimum lending rate (MLR) decreased by 138 and 75 bps from third quarter of 2008. As a result, the net interest margin in the banking sector widened from 4.5% in Q3 2008 to 5.13% in January 2009.

**Table 13: Market interest rates**

As of December 31	2006	2007	2008	Jan 09
MPC Rate (as at period-end)	5.00	3.25	2.75	2.00
Avg 1-day Overnight Rate	4.64	3.75	3.28	2.12
Avg 12-mth Depo Rate	4.26	2.80	2.56	1.50
Avg MLR	7.53	7.21	7.17	6.63
Net Interest Margin (NIM)	3.27	4.42	4.61	5.13

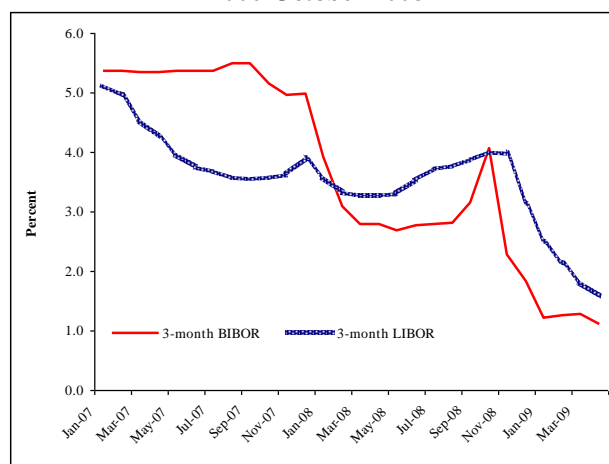
Source: Bank of Thailand

**Figure 43. Lending and Deposit rates (%), 2005-October 2008**



Source: Bank of Thailand

**Figure 44. BIBOR and LIBOR (%), 2006-October 2008**

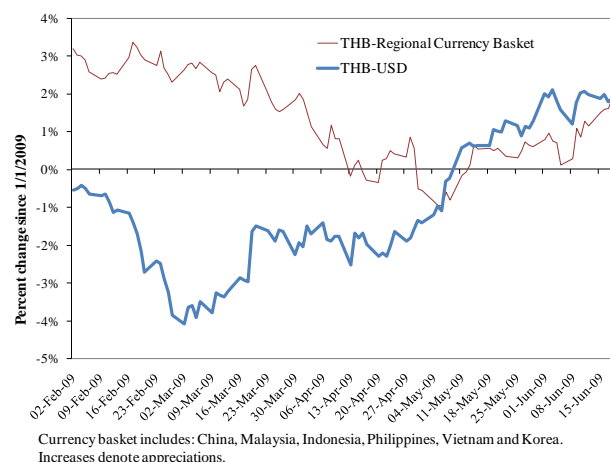


Source: Bank of Thailand

**The Thai baht as well as several other Asian currencies devalued against the USD with the hope of boosting economic growth via the cheaper pricing of export items.** The Thai baht has weakened since the beginning of 2008, with its strongest level being at 31.18 on March 19, 2008. Its decline is in part due to capital outflows as foreign investors sell Thai stocks, contributing to the SET Index's fall of almost 50% from the end of 2007. The Thai baht also suffered from investor's lack of confidence in monetary policy and political instability, especially after the closure of Bangkok's international airports which seriously damaged the tourism industry, an important source of foreign income. The weaker baht policy which boosts economic growth through cheaper exports has been in line with the value of other currencies in the region. The baht however, has performed surprisingly better when compared to other currencies. The Thai baht is down by 11%, compared to 54% for the South Korean Won and 18% for the Philippine Peso over the past year. Spreads in the CDS (Credit Default Swap) of Thai baht doubled in the past year

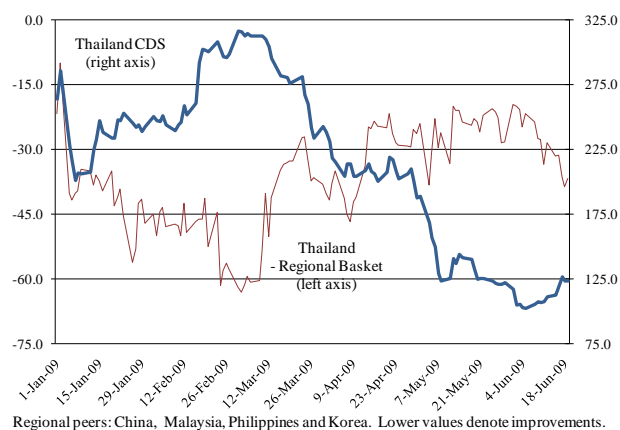
which followed the same direction of other regional currencies. This implies the financial risks of these currencies in the crisis era.

**Figure 45. Exchange Rates**



Source: Datastream, World Bank calculations

**Figure 46. CDS Spreads**



Source: Datastream, World Bank calculations

**The primary bond market almost doubled its size in 2008 due to downward trend in interest rates and issuance volumes increased further in 2009 as large corporations switched to domestic funding.** Last year, THB 11.33 trillion worth of new bonds were issued in the primary market, jumping from 6.27 and 3.10 trillion in 2007 and 2006 respectively. Government Securities dominated the primary market while Corporate Debts accounted for less than 12 %. BOT Bonds in the amount of THB 9.2 trillion were issued in 2008 in order to absorb excess liquidity in the money market. Recently, big corporates shifted their overseas funding to domestic funding due to the downward pressure in interest rate. In 2008, Thai corporates issued new bonds worth THB 1.27 trillion which is the highest level of issuances since 2000. And we expect that the new issued bond will test the high level again this year. The primary reason behind these new issuances is to refinance higher costing bonds and working capital. This has been a good opportunity for corporates to issue medium to long term fixed-income instruments including corporate bonds and commercial paper. During the last year, long-term bonds accounted for 34% of total new corporate bonds. The top 3 industries which issued new bonds in 2008 were the banking, energy and construction materials sectors.

**Trading volumes in the secondary bond market have increased, especially in low-risk, highly rated bonds.** Trading value of the total bond market increased 65% from THB10.53 trillion in 2007 to THB 17.36 trillion in 2008. Average daily trading values substantially increased from THB 356 billion in 2007 to 878 billion at the end of 2008. 91.84% of secondary market trading was accounted for short-term bonds, especially BOT Bonds. Moreover, the issuers increased the liquidity of bonds by registering them in the Bond Electronic Exchange (BEX) Market. The BEX has started performing a prominent role in fixed income trading. The supply of tradable bonds in the secondary market has increased from THB 3.94 trillion in 2007 to THB 9.18 trillion in 2008. As per Table 15, 418 Government bonds and 30 corporate bonds are currently traded in BEX with a value of 8.98 and 0.2 trillion respectively. The value of tradable corporate bonds increased 150% from 79 billion in 2007 to 198 billion in 2008. However due to the serious global economic turmoil, players in financial market like banks, investors and asset management firms have become more risk-averse and shifted their investments to what they considered to be lower-risk assets. As a result, the trading value of corporate bonds reduced from THB 135 billion in 2007 to THB 115 billion in 2008 or a 15% decrease.

**Table 14: Trading Value in Bond Electronic Exchange**

Trading Value (THB Billion)	2004	2005	2006	2007	2008
Gov Debt	2,855	3,794	4,183	10,389	17,242
Corp Debt	114	89	93	135	115
Foreign Bond	0	0	2	7	5
Total	2,969	3,884	4,278	10,532	17,362
Monthly Trading Value (Avg)	217	247	323	356	878
Daily Trading Value (Avg)	11	12	16	18	43

Source: Thai BMA

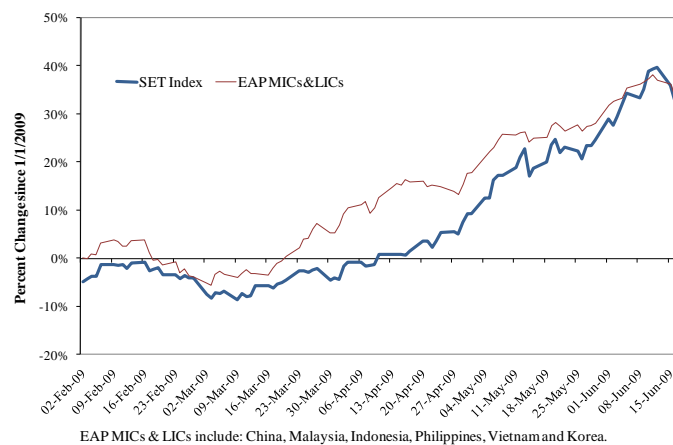
**Table 15: THB Bonds registered in Bond Electronic Exchange for secondary market trading**

Type	2007		2008	
	No. of Issue (Units)	Value (THB Billion)	No. of Issue (Units)	Value (THB Billion)
Gov Debt	330	3,856.49	418	8,981.06
Corp Debt	19	79.43	30	198.39
Total	349	3,935.93	448	9,179.45

Source: BEX

### *Corporate sector developments*

**The stock market has gained nearly 30 percent in 2009, recovering some of the steep losses of 2008.** As at the end of May 2009, the Stock Exchange of Thailand (SET) index stood at 560, up from 450 at end-2008 but still well below the end-2007 levels of 858. Thai stocks have generally followed other markets in the region, underperforming in March and April due to the political unrest but catching up since May (Figure 47). At the end of May 2009, market capitalization amounted to 4.4 trillion baht, which was 25 percent higher than the level at the beginning of this year. During this period, the price-earnings ratio increased sharply to 19.00 from 7.01 times.

**Figure 47. Recent Stock Market Performance**

Source: Stock Exchange of Thailand, Datastream and World Bank calculations

**Thai companies have been hard hit during the global economic downturn and persistent future business risks will continue to test their resilience.** Total assets of listed firms remain stable at 156% contribution to GDP in the last two years. Even though corporates are struggling in the global crisis, listed companies managed to increase their total assets by 8% from THB 13.297 trillion to 14.355 trillion in 2008. But the direct effect from the global crisis can be felt in stock price. Thai stocks are priced at 7

times earnings as of end-2008, compared to 12 times a year before. As a result, SET index dropped almost 50% in 2008 and the market capitalization significantly halved in value from THB 6.67 trillion at the beginning of the year to 3.59 trillion at the end. Even the total trading volume increased last year from 605 to 839 billion shares, however, the total trading value reduced from THB 4.188 trillion to 3.919. Profitability indicators of listed companies also felt the pinch from the economic downturn. 25% of listed firms or 122 out of 495 firms experienced a loss in 2008, compared to 21% (103/490) in 2007. As per Table 7, Thai companies reported reducing net profits even while seeing increased sales revenues. Net profit dropped by 25% due to a significant decrease in their gross profit margin from the average of 20% to 16%. When looking forward, Thai companies who rely mostly on exports may struggle to survive in a prolonged crisis. Their sustainability depends heavily on their ability to manage their cash flow, control costs and diversify their customer portfolio.

**Table 16. Financial performance of listed firms, 2006-2008**

(THB Billion)	2006	2007	2008
Total Assets	12,553	13,297	14,353
Profit / Loss	468	416	310
Sales Revenue	5,541	6,010	7,326
COGS	4,453	4,835	6,136
Gross Profit (%)	20	20	16

Source: Stock Exchange of Thailand

**Unlike large companies, SMEs face additional challenges.** Even in a highly liquid market it is difficult for SMEs to get funding from the formal banking sector due to their higher risk profile. The Government believes that sharing credit risks between commercial banks and the Government through credit guarantees would lead to more lending for borrowers, especially SMEs. Recently, 16 commercial banks signed agreements with the state-owned Small Industry Credit Guarantee Corporation to participate in the 30 billion baht Portfolio Guarantee Scheme. Under the guarantee program, each of the private banks can designate a portfolio of 1-5 billion baht to be eligible for guarantee of up to 25-30% of outstanding loans.

## 2.8 Medium Term Development

**Thailand has to position itself in the new global economic environment, if it wants to sustain its growth and competitiveness post-crisis.** The world economy is poised to recover and stabilize over the next couple of years. However, the global economic landscape post financial crisis will be different from that of pre-crisis. Overall world consumption level in the world post-crisis will be lower than that of pre-crisis with the downward adjustment of the consumption levels of developed countries. This calls for a re-examination of Thailand's export strategy, as well as an analysis of binding constraints to domestic consumption, to allow Thailand to join the band-wagon of global economic recovery and sustain growth going forward. More importantly, actions by both the government and the private sector must start today for them to be useful in time for the recovery in the next couple of years.

**Thailand will have to diversify its export destinations.** Demand for Thai exports from its traditional export markets – US, EU, and Japan – will not be as strong post-crisis compared to that of pre-crisis. Hence, for Thailand to continue to sustain its export growth of over 10 percent (in US dollar terms) as it did in the decade pre-crisis, it must maintain existing market shares in traditional markets and aggressively seek new markets. Thai exports to emerging markets such as the Russia and the Middle East have expanded quickly over the past couple of years. However, their shares are still small compared to those of the traditional markets. Thai exports to China, India and Russia have also expanded rapidly over the past few years (from 4 percent of total Thai exports in 1999 to 12 percent in 2008). Many of the

exports to China are, however, intermediate goods for the manufacture of final products which are exported to developed countries. Thus, if Thailand were to maintain its exports shares in the Chinese market in the future, a greater number of products that serve Chinese domestic final demand would need to penetrate the Chinese market.

**Higher value-added products will be needed for Thai exports to penetrate new markets, as competition for these new markets will intensify.** As most emerging markets are developing countries, their import demand is different than that of Thailand's traditional developed markets. In addition, many of the emerging markets can produce products similar to as current Thai exports, such as low- cost, low value-added, labor-intensive products. Thai firms will therefore need to export higher-quality or higher value-added products, if they were to be competitive with domestically produced ones.

**Firms must be prepared for a strong Baht as equilibrium levels of savings in mature economies are likely to rise in the aftermath of the crisis.** Post crisis, large capital flows from developed countries will likely flow to East Asia as savings rates in developed countries increase and East Asia is expected to have adequate investment returns within a sound financial infrastructure, especially compared to other regions. With the large capital flows, the Baht as well as other currencies in the region will likely appreciate relative to those of export competitors in other regions. Thailand will therefore find it hard to compete in price for export markets, as an appreciated exchange rate will not be supportive of cheap exports. This underscores the importance for Thai exports to be competitive based on its quality and value-added that responds to new market demands.

**Commodity prices, including oil prices, and inflation will rise as the global economy recovers.** This would raise the cost of production may reduce firm competitiveness, unless firms can become more cost effective through productivity growth. Transportation costs for firms can also be reduced if Thailand's logistics and transportation costs are lowered by improved transport infrastructure and logistics systems. The government has realized this and will embark on a large infrastructure investment program from FY2010-2012 under its Stimulus Package 2. Promotion of energy efficiency and development of alternative fuels will therefore continue to be important when oil prices are on the rising trend.

**The fundamental changes expected in the post-crisis economic environment underscore the need for greater investments and productivity, if Thailand is to remain competitive and resume high levels of growth.** Private investment growth, which has been sluggish over the past few years, will need to rise post-crisis. New investments are needed not only to build up existing capacity, but more importantly to improve the quality and productivity of production. These will enable Thai producers to transition to new, higher-value added products that will generate competitiveness for Thai products in both the export and domestic markets. New investments may not only be for new production technology, but also for better design and marketing.

**An improved investment climate in Thailand as well as adjustments made by firms will help bring about needed investments and productivity.** A better investment climate would not only reduce costs for firms but also promote higher productivity. The investment climate issues as voiced by firms in the 2007 Thailand Investment Climate Assessment are still very much relevant for Thailand's productivity and competitiveness post-crisis. The four top constraints to investments that were reported are macroeconomic volatility, mismatch of skills, inadequate public infrastructure, and cumbersome regulations and regulatory procedures. As discussed earlier, volatility of macroeconomic variables such as exchange rate and prices will be greater post-crisis when the global financial sector recovers. For firms to be able to sustain their competitive post-crisis, they must be able to a large certain extent manage the macroeconomic volatility. This is particularly important for small enterprises which have voice in the survey their inability to cope with the macroeconomic volatility. In addition higher skills, better

infrastructure, and supporting regulatory environment will be increasingly important post-crisis if firms were to become productive and cost-effective.

**Improving skills and reducing skills mismatch will be key for Thailand's competitiveness and growth post-crisis.** Thai firms will need to be more productive, cost-effective, and innovative if they were to compete in the tougher global trade environment post-crisis. High quality human resource is the key element to achieving these. It is now the time for all stakeholders – government, private, sector, and research and academic institutions – to strongly join hands to raise the quality of education and skills, reduce mismatch, and move Thailand towards a creative, knowledge economy. Higher skills of entrepreneurs and workers and productivity of firms will bring higher returns to them. These could also stimulate domestic consumption and investment growth, which has been low in the past few years. In the longer run, these would be important in reducing the income disparities and social inequalities.

**A regulatory environment that is conducive to business growth and competition, especially in the services sector, can help unleash Thailand's growth potential.** Another major area for potential improvement in Thailand's investment climate is the regulatory framework, as well as the bureaucratic processes that firms have to deal with. Long and uncertain bureaucratic processes not only raise costs for firms in dealing with government agencies, but also reduces firm's competitiveness vis-à-vis their competitors in other countries with a more efficient bureaucratic interface with businesses. In addition, regulations that limit competition among firms in certain sectors also limit their productivity and innovativeness. An example is the service sector which holds a high potential for productivity improvements and growth. However, many services industries have long been protected for domestic players only. The gradual liberalization of service industries, which could start with a few, would introduce competition and thus higher productivity of these industries in the medium term. The service sector has a high non-tradable component. Thus, a growing and more productive service sector would also lead to higher domestic consumption.

**Removing constraints to domestic consumption growth could help reduce growth volatility, but exports will likely remain the main engine of growth in Thailand.** In the medium term, there is room for domestic consumption growth which has been sluggish in the past few years to rise when consumer confidence and incomes increase. The latter could come about from higher worker and firm productivity if actions discussed above start today. Restored consumer confidence and mechanisms that would allow individuals to save less for the future would also help to promote private consumption. The latter is true for countries with a developed social safety net system in which individuals in the system are protected in times of income-loss, sickness, old age. Thailand has been developing its social safety net system since the East Asian crisis. Currently, there is the universal health scheme, 15-year free schooling, and unemployment benefits and pension for formal sector employees, including government officials. Because formal sector employees are only a third of Thailand's labor force, extending the latter two schemes to those in the informal sector would not only socially protect them, but also to a certain extent provide them with the confidence to consume more in the present. However, because domestic household consumption generally does not expand rapidly relative to exports, this will be unlikely to replace exports as an engine of Thailand's future growth. Domestic consumption could, however, help promote Thailand's future growth.

## SECTION 3

# IMPLEMENTATION OF STRUCTURAL REFORMS

### 3.1 Financial and Corporate Sector Reforms and Restructuring

**Thailand has been gradually reforming the financial and corporate sectors in order to be better prepared for the economic recovery.** There are some acts waiting to be effective this year where some are delayed. These reforms are summarized in Appendix 2: Monitoring Matrices for Structural Reform Implementation. However this section will elaborate some in more details.

**The 5-year Financial Sector Master Plan (FSMP) Phase II is expected to be implemented in 2009 and concluded in 2013.** This plan aims to liberalize the banking system; to reduce operating costs of financial institutions; to increase competition among financial institutions and non-bank entities through expanding the business scope permitted banks and greater foreign participation; and to improve market architecture with the development of limited deposit insurance and greater variety in risk-management instruments. The new plan allows greater competition in the banking industry. The plan would strengthen the banking system by lowering the Non-Performing Loan (NPL) ratio to less than 2% in 5 years (2013). The Bank of Thailand (BOT) will introduce three practices to abolish NPLs; (1) create incentives to promote asset-sales transactions; (2) encourage debtors to participate in debt restructuring and hasten the legal process for asset foreclosures; and (3) promote asset-backed financial instruments to boost assets' liquidity. In addition, the Mortgage Insurance Companies will be set up in order to develop infrastructure and credit information system to facilitate bank's risk management.

**In line with the international practices of the Bank for International Settlement (BIS), the BOT implemented the Pillar 1 of the new international standard, commonly known as “Basel II”.** This was done on a solo basis on January 1, 2009. The Pillar 1 requires commercial banks to provide capital reserve for credit, market and operational risks. The accord has three main “pillars”; capital requirements for risk; supervisory review, or how regulators respond to different risks; and market discipline. The implementation of the Pillar 1 resulted in a drop of 1.23% in CAR Ratio (Capital Adequacy Ratio) from 15.21% in Q3 2008 to 13.98% in Q4 2008 which represent the capital required to cover market and operational risks in Thai banking industry. The Basel II will continue to require banks to maintain a minimum CAR of 8.5% of risk assets.

**Under the Demutualization of the Stock Exchange of Thailand (SET), the SET will become a listed company on the Exchange by 2011 in order to improve the governance structure.** The plan will encourage customer's satisfaction by promoting effective resource management, cost efficiency and maximize returns from fund-raising in the capital market. By 2011, the SET will have achieved its 5-year strategic targets including doubling capitalization of the cash equity market and its revenue by 2013 – with 25% of this income coming from new products. In addition, the Exchange will increase foreign listings to not less than 5% of total market capitalization. The new structure proposes 2 major groups: (1) The Stock Exchange of Thailand and (2) the Capital Market Development Fund (CMDf). The SET will focus mainly on the capital market functions while the CMDf will deal with long-term capital

development through investor education, capital market personnel development and support for SET Research Institute, corporate governance and corporate social responsibility. According to the plan, the Thailand Securities Depository Co.Ltd. (TSD) would be spun off from the SET and, hopefully, competes with new-comer players in the securities depository business. In addition, the securities depository company will be directly supervised by the Securities and Exchange Commission (SEC) instead of the existing SET.

**The first gold future contract was launched on February 2, 2009.** The underlying of the gold future is the Gold Bullion with a purity of 96.5% which is commonly traded in Thailand. Contract size is 50 Thai Gold Baht or 762.20 grams. The contract months are February, April, June, August, October and December. The gold future is traded by cash settlement via the Thailand Clearing House Co.Ltd (TCH). The commission on gold futures will be on a sliding scale ranged from THB 300 to THB 500 per contract. The initial and maintenance margin are set at THB 66,500 and THB 46,550 per contract.

**The Government launched two sets of stimulus measures to reduce the negative effect of Thai population.** The Government's priority is to reinvigorate the Thai economy, which continues to be seriously affected by a series of problems such as the global financial crisis in 2008, the airport closure in December 2008 and the cancellation of ASEAN+6 Summit in April 2009. The following are stimulus packages concerning the financial and corporate sectors up to the date of writing.

1. With the objective to provide more credit facility to the private sector, cabinet approved the capital injection in two Specialized Financial Institutions (SFIs). Cabinet resolution on February 17, 2009 approved the capital injection to EXIM Bank of THB 5 billion and Small Industry Credit Guarantee Corporation (SBCG) of THB 3 billion. With the addition capital of THB 5 billion, EXIM Bank is able to extend credit guarantee for exporters in the expected amount of THB 150 billion within the 3 years period. With the gearing ratio of 10, the additional THB 3 billion results in THB 30 billion credit limit under the Portfolio Guarantee Scheme to commercial banks. Consequently, the commercial banks can hopefully extend their credit facilities up to THB 60 billion to the SME operators.
2. On April 28, 2009, the cabinet approved the Financial Assistance Program for Tourism Operators. After the airport closure in December 2008 and the cancellation of ASEAN+6 Summit, the tourism-related industries was hard hit and shows sign of business instability. The cabinet approved the SME Banks to provide revolving loan for tourism-related SMEs at the interest rate of MLR – 3% with the grace period of 1 year. Each SME is eligible for up to THB 5 million-loan with the tenor up to 5 years. Properties, personal guarantee, cross guarantee or SBCG's guarantee can be pledged as collateral under this scheme.
3. Cabinet approved one-year loan to SMEs for tax payment purpose. According to the cabinet resolutions on April 28, 2009, the Small Industry Credit Guarantee Corporation (SBCG) will provide THB 10 billion full credit guarantee for tax payment purpose through commercial banks and SFIs. Under this scheme, the SMEs can apply 1-year Tax Loan from any banks at the interest rate of 4% and the repayment is scheduled on a monthly basis with 3-month grace period. The loan proceed from this scheme has to be directly paid to the Inland Revenue Department for corporate-income tax payment only.

**Thailand eased business start up process by merging procedures.** According to Amendment to CCC B.E. 2551 (A.D. 2008) which has been effective since 1 July 2008, the application for registration of memorandum and the application for registration of establishment of company can be filed at the Registrar at the same date and completed within one day.

## 3.2 Recent Trade Reforms

### *Tariff reform*

**Various products now enjoy lower or no import tariff.** These include both universal tariff reductions, which are applicable to goods from all countries, and specific tariff reductions that result from free trade agreements (FTAs) with other countries and regions. An example of the former includes lower duty for oil cake under the WTO agreement announced in February this year. For the latter, the major changes are ASEAN's agreements with China and Japan announced in April-May 2009. For China, tariffs of the following items are cut or cancelled: various food items, building materials (such as stones and metal wires), shoes, jewellery, certain vehicles and motorcycles and parts, and electrical appliances (such as fans, water pump, freezers, electrical motors and power generators). For Japan, these cover among others live animals for breeding purpose, various food and beverage items, flowers, smoked rubber sheet, minerals, chemical substances, office supplies, furniture, wearing apparels, wooden and paper products, computers and computing machines, toys, and household electrical appliances.

**Multilateral FTAs between ASEAN and other partners showed a significant progress.**<sup>16</sup> For the pact between ASEAN, Australia, and New Zealand, tariff rates under the normal track for the six ASEAN foundation members will be cancelled in 2013 for most products, and 2015 for the rest. Most details on trade in services, investments, and rules of origin also agreed. Finance Ministers of all member countries signed the agreement in February 2009. Meanwhile, the ASEAN-Korea agreements on goods trade and services trade were also signed in February this year. While services trade agreement is effective since 1 June 2009, the pact on goods trade is expected to be effective in October. Korea and Thailand will cancel around 90 and 80 of all tariff lines that are being traded, respectively. The agreement also covers various areas of services trade and economic cooperation. The pact between ASEAN and India is also agreed. Currently over 70 percent of goods that are being traded will enjoy no tariffs by end-2012, although this is still subject to changes. The agreement is expected to become effective in early 2010. For BIMSTEC<sup>17</sup>, the member countries agreed in June 2009 to cut or waive import tariffs of over 5,000 products. The three faster-growing nations (India, Sri Lanka, and Thailand) will cut tariffs for 10 percent of their agreed items by January 2010. By January 2011, all members will offer at least half of listed items duty-free. The negative list is about 19 percent of all products being traded. Finally, Thailand signed the ASEAN-Japan agreement in April 2008. Japan will abolish 90 percent of tariff lines that are being traded with an immediate effect, while Thailand will eliminate import tariffs that worth 93 percent of imports from Japan within 10 years. The pact will also result in closer economic cooperation in a range of issues, such as intellectual property, energy, ICT, and agriculture.

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<sup>16</sup> Table 17 reviews the recent progress on free trade agreements that involve Thailand in more details.

<sup>17</sup> Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation consists of Bangladesh, Bhutan, India, Myanmar, Nepal, Sri Lanka and Thailand.

**Table 17: Major progress on Thailand's Free Trade Agreements (FTAs)**

Agreements	Details of recent progress
Thailand - India	In September 2004, Thailand and India agreed to reduce and lift import tariffs of 82 products under the Early Harvest Scheme. Since 1 September 2006, tariffs of these products, such as certain tropical fruits, canned seafood, jewelry, vehicles parts, and electrical appliances, became zero percent. The two countries now reached a preliminary agreement, which could be effective in 2009. The negative list (no tariff reduction) has around 500 products or 10 percent of all goods that the two countries are willing to reduce or cancel import duties. Examples include textiles products, automotive parts, and steel products for Thailand, and textiles products, vehicles, and certain agricultural products for India. As of June 2009, Thailand awaits India to confirm the extent of tariff reduction that was previously agreed. The next steps are to review the agreement and start negotiation on services trade and investments.
Thailand - Japan	The JTEPA was signed in April 2007 and has been effective since 1 November 2007. Over 90 percent of all goods now have lower or zero tariff rates. The Agreement also eased the rules that restrict investments from Thailand and employment of Thai workers in Japan. There are joint committees that are set up to monitor the compliance of the agreements.
BIMSTEC	The 18th meeting of the TNC in June 2009 resulted in a significant progress. In addition to certain terms on rules of origin, the member countries agreed to cut or waive import tariffs of over 5,000 products. The three faster-growing nations (India, Sri Lanka, and Thailand) will cut tariffs for 10 percent of their agreed items by 1 January 2010. By January 2011, all members will offer at least half of listed items duty-free. The negative list is about 19 percent of all products being traded. For next step, the pact will proceed with negotiations on investment and services.
ASEAN - China	Since October 2003, Thailand and China have reduced their import tariffs for certain vegetables, fruits and nuts products following the Early Harvest Scheme. Tariffs of agricultural products under HS1-HS8 were also lifted in 2006 in six ASEAN foundation members. On goods trade, the latest meeting in March 2009 mainly focused on trade facilitation, non-tariff barriers, and sanitary and phyto-sanitary standards. The second package of services trade negotiation continued. Both parties are now exchanging revised offers. Thailand and China reached the agreement on investment, which will be further discussed at the ASEAN level.
ASEAN-Australia-New Zealand	The meeting in August 2008 made a significant progress. Tariff rates under the normal track for the six ASEAN foundation members will be cancelled in 2013 for most products, and 2015 for the rest. All parties also agreed on trade in services and investments. Most issues on rules of origin also reached an agreement (except, for example, soybean oil between Thailand and Vietnam). The agreement is already drafted. Finance Ministers of all member countries signed the agreement in February 2009.
ASEAN - Korea	In May 2006, Korea and ASEAN member countries initiated free trade agreement on goods. The agreements on goods trade and services trade were signed by all parties in February 2009, and June for the agreement on investment. While services trade agreement is now effective (since 1 June 2009), the pact on goods trade is expected to be effective in October this year. Korea and Thailand will cancel around 90 and 80 of all tariff lines that are being traded, respectively. The remaining will be subsequently abolished in 2012 and 2017, depending on product types. On trade in services, Korea liberalizes 43 areas such as legal services, construction, and entertainment. On economic cooperation, there are 19 areas in total, e.g. customs procedure, SMEs, and tourism.

Agreements	Details of recent progress
ASEAN - India	The pact between ASEAN and India is preliminarily now agreed. On lowering trade barriers, about 70 percent of goods that are being traded will enjoy no tariffs by end-2012. Tariff rates on items in the sensitive list will be reduced to five percent or lower by end-2015. India and Thailand placed 5 and 14 items in the highly sensitive list, respectively. Import duties on these products will be 25-50 percent lower by end-2021. The agreement also sets the maximum number of goods in the exclusion list to 489 items. The May 2009 meeting discussed some of these proposals, which are still subject to changes. It is expected to be effective in early 2010.
ASEAN - Japan	The free trade agreement between ASEAN and Japan was signed in March 2008. Japan abolishes 90 percent of tariff lines that are being traded immediately after the agreement becomes effective (from 1 June 2009 with Thailand, and since December 2008 for many other ASEAN countries). Thailand will eliminate import tariffs that are worth 93 percent of imports from Japan within 10 years. In addition to merchandise trade, the pact will also result in closer economic cooperation between ASEAN and Japan in the following areas, among others: business environment, intellectual property, energy, ICT, human resources development, SMEs, tourism, transportation, agriculture, and competition policy. Looking forward, both parties will set up two sub-committees on services trade and on investments within one year.
ASEAN - EU	The initiative for the partnership began in May 2007. The October 2008 meeting mostly discussed about the overall framework of the agreement, including modality (e.g. whether ASEAN could open up the markets later than the EU) and approach (e.g. whether investment liberalization, protection, and promotion should be negotiated together or separately). Both parties also exchanged ideas on rules of origin, trade facilitation, sanitary and phyto-sanitary standards (SPS), intellectual property, and trade competition. The latest meeting in March 2009 saw limited progress.

Source: Department of Trade Negotiations

Note: The members of the BIMSTEC are Bangladesh, Bhutan, India, Myanmar, Nepal, Sri Lanka and Thailand. Bilateral trade agreements between Thailand and Bahrain, Peru, the United States, and the EU exhibited no significant progress in recent months.

### *Export promotion and assistance*

**The e-Customs system is now used at all key customs points.** The paperless customs speeds up customs procedures, enhances the transparency of these processes, and reduces the transaction costs incurred to importers/exporters. The paperless customs procedure for exports or e-Export was introduced at the Leam Chabang seaport and the Suvarnabhumi airport in 2007. In 2008, the e-Customs system was adopted for both import and export transactions at most customs points (large and small seaports and airports) nationwide.

**The Export-Import Bank of Thailand works more closely with other banks to assist exporters.** Last year, the EXIM bank offered the export insurance services, which guarantee to pay Thai exporters in case of a default by foreign buyers, to clients of Siam City Bank, SME Bank, Government Savings Bank, and Krung Thai Bank.<sup>18</sup> The export insurance services are now available at six additional commercial banks

<sup>18</sup> The EXIM Bank has offered export insurance services since 1995. Currently, the services cover transactions between Thai exporters and foreign traders in over 200 countries. In addition to default by foreign buyers, the scheme also compensates Thai exporters when foreign traders become bankrupted and refuse to accept delivery. The Bank also assisted local exporters to check the credibility of their foreign partners. The compensation rate is up to 90

and specialised financial institutions. This expansion benefited from the injection of five-billion baht capital by the government. Current and potential exporters will benefit from both traditional financial services provided by these banks and trade finance offered by the EXIM bank. For example, the EXIM bank will issue domestic letter of credit (L/C) and standby letter of credit that can be used as an assurance in auctions and foreign investments. The banks will also co-finance loans.

**The EXIM bank introduced more targeted additional financial services.** For example, the EXIM bank recently launched a new services designed to support SMEs. The premium for export insurance services purchased by exporters with export value below 100 million baht is now 35 percent lower. The Bank also signed the memorandum of understanding with SME Bank, Small Business Credit Guarantee Corporation (SBCGC) and Thai Gems and Jewellery Traders Association to support Thai jewellery businesses. The SME bank will provide traditional financial services, while SBCGC guarantees credits for jewellery firms with insufficient collateral and EXIM bank insures payment default by foreign partners.

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percent of actual loss. So far, industries that had incurred the highest loss are jewellery, furniture, canned food, and plastics products businesses.

### 3.3 Public Sector Reforms

**The draft of OCSC regulation on civil service discharge was approved in principle by the cabinet.** Civil Service Act (2008), section 110 (5) mandate that a civil servant shall be discharged from government service when is unable to perform official functions efficiently and at a level of effectiveness satisfactory to the official authorities, while remaining eligible to receive compensatory gratuities and pensions. In that connection, the OCSC drafted the regulation to be consistent with the act. In principle, a civil servant who fails to meet the performance satisfactory level to the official authorities has one time chance to improve performance in accordance with the agreement plan made to the respective authorities. In the case where the second evaluation does not meet the criteria, a civil servant is subjected to be discharged from government service. However, civil servant has a right to appeal to the Merit System Protection Board within 30 days after receiving notice.

**The Public Finance Act is tentatively scheduled to be effective by the beginning of FY2010.** The 2007 Constitution mandated the government to develop a new Public Financial Act and be enacted within 2 years after the first day of 4-year government policy's announcement. MOF as a key responsible agency prepared this draft Act, held inter-agency consultations, and submitted the revised draft to the cabinet with expected to be approved by the first half of this year. By the beginning of FY2010, Public Financial Act and respective regulations is tentatively to be approved by the Parliament, and implementation commences.

**The amendment of royal decree of the establishment of the Office of Knowledge Management and Development (Public Organization) was approved in principle.** The current royal decree to establish the OKMD (2004) needs to be amended to remove existing constraints by providing more flexibility for government to deliver service in a more efficient way. In particular, head of the office will have an extended authorization to all every staff in the organization to improve administrative practice.

**The Revenue Department announced the criteria and procedures for money donation to political parties.** Revenue Department in collaboration with Office of the Election Commission of Thailand drafted the criteria and procedures for donation to political parties. The core concept of the draft includes 1) Money donated to political parties must be filed in the annual PIT form of donor 2) Political parties who received donation must register to the Election Committee before the deadline of tax submission in every March 3) Office of the Election Commission of Thailand must inform list of political parties as well as their relevant codes to the Director General of the Revenue Department to further promulgate to public and 4) Revenue Department shall provide the list of political parties who received donation to registrar of relevant political parties and also transfer the total amount of donation to Political Party Development Fund.

## Appendix 1: Key Indicators Table

	2007	2008	2008	2008	2009	2009		
	Year	Year	Q2	Q3	Q4	Q1	Apr	May
<b>Output, Employment and Prices</b>								
GDP (% change, previous year)	4.9	2.6	5.3	3.9	-4.2	-7.1	..	..
Industrial production index (2000=100)	180.7	190.2	189.3	195.8	176.4	162.2	161.8	..
(% change, previous year)	8.2	5.3	10.1	7.6	-8.0	-18.6	-9.7	..
Unemployment rate (%)	1.4	1.4	1.4	1.2	1.3	2.0	2.1	..
Real wage growth (%) 1/	0.7	4.8	1.2	1.7	3.6	-6.6	..	..
Consumer price index (% change, previous year)	2.2	5.5	7.5	7.3	2.1	-0.2	-0.9	-3.3
<b>Public Sector</b>								
Government balance (% GDP) 2/	-1.7	-1.1	5.2	1.7	-6.7	-11.1	..	..
Domestic public sector debt (% GDP, end-period) 3/	37.7	38.1	37.1	37.4	38.1	41.9	42.9	..
<b>Foreign Trade, BOP and External Debt</b>								
Trade balance (US\$ million)	11.6	0.2	2.8	4.6	0.2	1.5	0.6	..
Exports of goods (fob, US\$ million)	150.0	175.3	46.0	49.4	38.3	33.4	10.3	..
(% change, previous year)	17.3	16.8	28.8	28.4	-9.4	-19.9	-25.2	..
Key exports: Machinery & mach. appliances (% chg in US\$)	16.2	7.8	26.6	9.4	-19.9	-31.3	..	..
Imports of goods (cif, US\$ million)	138.5	175.1	44.4	49.5	39.6	25.6	9.7	..
(% change, previous year)	9.1	26.4	28.7	39.1	5.3	-38.3	-36.4	..
Current account balance (US\$ million)	14.0	-0.2	6.2	6.2	6.2	6.2	0.4	..
(% GDP)	5.7	-0.1	8.7	9.0	9.8	10.0	..	..
Foreign direct investment, net (US\$ million) 4/	10.2	9.8	1.0	2.4	1.5	0.0	0.6	..
Total external debt (US\$ million) 5/	61.7	67.7	66.2	65.2	64.8	..	..	..
(% GDP)	24.9	24.8	24.3	23.9	23.8	..	..	..
Short-term external debt (US\$ million) 5/	21.6	24.1	25.6	25.2	24.1	..	..	..
Debt service ratio (% exports of goods and services) 6/	11.9	6.9	6.1	5.7	7.1	..	..	..
Reserves, including gold (US\$ million)	87.5	111.0	105.7	102.4	111.0	116.2	116.8	121.5
(months of imports of goods)	6.4	6.5	6.2	5.4	7.1	13.6	9.1	10.4

	2007	2008	2008	2008	2009	2009		
	Year	Year	Q2	Q3	Q4	Q1	Apr	May
<b>Financial Markets</b>								
Domestic credit (% change, previous year) 6/	4.9	9.3	4.1	6.6	7.7	5.7	..	..
Short-term interest rate (average period) 7/	3.69	3.40	3.25	3.67	3.42	1.67	1.25	1.25
Exchange rate (average period)	34.2	33.4	32.3	33.9	34.8	35.3	35.3	34.3
Real effective exchange rate (2000=100, + = appn) 8/	116.5	119.2	124.1	121.9	110.2	108.8	109.5	113.0
(% change, previous year)	4.7	2.4	6.2	4.3	-6.3	-9.9	-10.4	-9.4
Stock market index (SET), end of period	858	450	769	597	450	432	492	560
Credit default swaps (basis points, end of period)	55	256	135	172	256	233	187	122
<i>Memo Items:</i>								
Nominal GDP (Billion Baht)	248.0	272.9	70.7	68.5	63.2	61.7	..	..
Nominal GDP (Billion USD)	8,493.3	9,105.0	2,283.1	2,321.4	2,203.3	2,179.7	..	..
Real per capita GNI (constant 2000 US dollars)	2,866.7	3,004.6	2,996.1	2,898.3	2,880.9	2,747.7	..	..

1/ Average wage of employed person from Labour force survey, National Statistical Office deflated by CPI inflation

2/ Cash balance of central government.

3/ Include domestic central government (CG) debt, domestic debt of non-financial state enterprise and Financial institutions Development fund (FIDF) debt.

4/ Non-Bank FDI

5/ Source: Bank of Thailand

6/ IFS definition (net credit to the nonfinancial public sector, credit to the private sector, and other accounts).

7/ BoT Policy Rate (end of day liquidity adjustment window, average of borrowing and lending facilities).

8/ Source: World Bank's estimates (average-period)

## **Appendix 2: Monitoring Matrices for Structural Reform Implementation**

1. Poverty Reduction
2. Financial and Corporate Sector Reforms
3. Reforms to Improve Business and Investment Environment and Trade Regime
4. Public Sector and Governance Reform
5. Social Protection

## 1. Poverty Reduction

	Objective	Reform Measures Taken
A.	Improve quality of life for the poor by enhancing self-reliance and creating opportunities in the local economy	<p><i>Measures taken over last 6 months and their significance</i></p> <ul style="list-style-type: none"> <li>• <b>The government's fiscal stimulus package approved by Cabinet in January 2009 contains a number of pro-poor measures:</b> (i) a one-time transfer of Bt2,000 (US\$57) per person to 8.1 million workers registered with the social security system; (ii) monthly transfers of Bt500 (US\$14) per person to 3.8 million elderly who currently do not receive another form of pension or transfer; (iii) full subsidy on education for 15 years (kindergarten to grade 12 or vocational school) for around 11.8 million students; and (iv) subsidies on public service are being provided for 6 months (February to July 2009); subsidies include electricity and water subsidy for households with low usage, fare waiver on many routes of non-air-conditioned public buses in Bangkok, fare waiver on third class train rides, and subsidy of cooking gas for household use. See Appendix 2.5 for details on these programs.</li> <li>• <b>As part of the stimulus package, the cabinet approved in January 2009 an exceptional transfer of Bt15.2 billion (US\$434 million) for the Sufficiency Economy Fund (formerly known as SML Village program).</b> The funds have been allocated to the 78,300 villages and communities in Thailand. Small villages are slated to receive 400,000 baht each, whereas medium-sized villages would receive 500,000 baht and large villages would get 600,000 baht. The villages and communities will need to submit proposals for the use of the funds and will receive the transfer once their proposals are approved.</li> </ul>

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## 2. Financial and Corporate Sectors Reforms

Objective		Reform Measures Taken
A.	Enable sharing of credit information among financial institutions	<p><i>Measure to be taken in the next 6-12 months</i></p> <ul style="list-style-type: none"> <li>• <b>A national credit-scoring system is planned.</b> The National Credit Bureau (NCB) plans to implement a national credit-scoring system in terms of individual credit information. The Credit Information Business Act has been effective since February 14, 2008. The bill allows the agency to set up a credit-scoring system which will benefit the credit analysis of financial institutions. Under this credit-scoring system, the borrowers would be classified with credit scores ranging from 300 to 900 points. The score below 700 points is considered to be quite negative while the score over 700 points represents a relatively healthy figure.</li> </ul> <p><i>Measure to be taken, but delayed</i></p> <ul style="list-style-type: none"> <li>• <b>Submission of credit information by insurance firms is not yet decided.</b> The decision on whether insurance companies are required to report their information of customers, who could not afford to pay their premiums and have received automatic lending from an insurance company to the National Credit Bureau (NCB) have not yet been made. At this stage, only financial institutions, leasing companies and nonbank credit companies are members of the NCB.</li> </ul>
B.	Formulate and implement a medium-term strategy for Thai financial sector	<p><i>Measure to be taken in the next 6-12 months</i></p> <ul style="list-style-type: none"> <li>• <b>The Financial Sector Master Plan (FSMP) Phase II is expected this year.</b> The second phase of the FSMP, which expected to be implemented in 2009, aims to reduce operating costs of financial institutions; increase competition among financial institutions and non-bank entities through expanding the business scope permitted banks and greater foreign participation; and improve market architecture with the development of limited deposit insurance and greater variety in risk-management instruments. The new plan allows greater competition in the banking industry. The plan would strengthen the banking system by lowering the NPL ratio to less than 2% in 5 years (2013). Lower NPLs would improve the banks' efficiency to generate more income and reduce costs due to the declining burden from provision.</li> </ul> <p><i>Measure to be taken, but delayed</i></p> <ul style="list-style-type: none"> <li>• <b>The Financial and Fiscal Master Plan for the Better Society, 2008 – 2011, which was expected to be submitted to the Cabinet at the end of 2007, is delayed.</b> This plan was expected to be submitted to the Cabinet as the end of 2007 but it is delayed. The master plan aims to achieve four objectives which are (1) building sustainable self-sufficiency by encouraging knowledge development and occupation trainings in the communities; (2) supporting social safety net by focusing on improving health and welfare of the poor and vulnerable people; (3) promoting good culture through family and religion; and (4) creating equilibrium society by reducing the income gap and the difference between rural and urban opportunities. According to the plan, the Ministry of Finance (MOF) will encourage government financial institutions to provide credit to projects which are consistent with the plan and reconsider various tax measures especially environmental tax, excise tax on harmful consumer products, inheritance tax and housing tax etc.</li> </ul>

Objective		Reform Measures Taken
C.	Transition from the current blanket government guarantee on deposits to a limited deposit insurance scheme	<p><i>Measure to be taken, but delayed</i></p> <ul style="list-style-type: none"> <li>• <b>Customer Deposit Protection Scheme is effective with extended full protection period.</b> The Deposit Protection Act (DPA) has been enacted and effective on August 11, 2008. Due to the recent global financial crisis, the full government guarantee period has been extended until 10 August 2011 instead of 2009 as per the approved Draft Royal Decree on Extension Bank Deposit Guarantee Act. After the 100% protection period, the protection limit will be reduced to THB 50 million and THB 1 million per person per financial institution on 11 August 2011 and 2012 respectively.</li> </ul>
D.	Remove legal impediments and provide an enabling environment for derivative products.	<p><i>Measure taken over last 6 months and significance</i></p> <ul style="list-style-type: none"> <li>• <b>No Significant Measures Taken</b></li> </ul>
E.	Development the domestic financial markets, including bond, capital, and money markets	
	(1) Domestic financial markets	<p><i>Measure taken over last 6 months and significance</i></p> <ul style="list-style-type: none"> <li>• <b>Pillar 1 of Basel II Standards is fully implemented on 1 January 2009.</b> BOT implemented the new capital accord, commonly known as the Basel II, on a solo basis on 1 January 2009. The Basel II aims to define how much capital a bank must maintain to account for various risks including credit, market and operational risks.</li> </ul>
	(2) Capital markets	<p><i>Measure to be taken in the next 6-12 months</i></p> <ul style="list-style-type: none"> <li>• <b>The SET Demutualization Plan aims to restructure the SET organization by the year 2013.</b> The new structure of the SET group under the Demutualization plan will come into effect in 1 January 2009. The SET are preparing its five-year strategic plans to ensure that it achieves its target of becoming a listed company on schedule. The strategic target of the SET include doubling the Exchange's market capitalization and revenue by the year 2013, with 25% of this income came from new products and increase the foreign listing to not less than 5% of total market capitalization.</li> <li>• <b>The Thailand Securities Depository Co.Ltd. (TSD) plans to adjust its regulation to comply with the amended Securities and Exchange Act.</b> In response to the potential impact of the Securities and Exchange Act B.E.2535 (1991) which was amended in March 5<sup>th</sup>, 2008, the TSD will adjust its rules and regulations to comply with the Capital Market Supervisory Board's conditions and modify its processes and system accordingly.</li> <li>• <b>Some regulations will be amended to accommodate the Share Repurchase Program.</b> After the stock value severely plunged, the SET encourage the share repurchase program and is approaching the Ministry of Commerce for an approval to amend related regulations to facilitate share buy-back program. Under the existing regulation, the firms are banned to sell their bought shares which have been bought back during the first six months. Also, such shares must be sold within 3 years, or else the firm must decrease its capital.</li> <li>• <b>E-Dividend is introduced to replace current dividend payment system.</b> TSD plans to persuade the BOT to review set limit of dividend transferred via bank account of THB of maximum THB 2 million per account, in order to encourage the e-dividend system. The e-dividend system has increased the speed of the dividend payment to shareholders and the efficiency of the payment system.</li> </ul>

Objective		Reform Measures Taken
		<p><i>Measure to be taken, but delayed</i></p> <ul style="list-style-type: none"> <li>• <b>New Settlement Cycle, which planned to be implemented by the end of 2008, is delayed.</b> Thailand Securities Depository Co.Ltd (TSD) has delayed the introduction of the proposed shortened trading settlement cycle – from three days after the trading day (T+3) to two days (T+2), which was originally planned for implementation by end-2008. The T+2 settlement cycle is part of SET's strategy to reduce investors' trading costs.</li> </ul>
	(3) Derivatives markets	<p><i>Measure taken over last 6 months and significance</i></p> <ul style="list-style-type: none"> <li>• <b>Gold Future was officially traded in TFEX on February 2, 2009.</b> The underlying of the gold future is the 96.5% Gold Bar which is commonly traded in Thailand. The gold future is traded by cash settlement via the Thailand Clearing House Co. Ltd (TCH). Gold futures were first introduced with the contract size of 50 Thai Gold Baht. The initial margin and maintenance margin for gold future are THB 66,500 and THB 46,550 per contract respectively.</li> </ul>
F.	Rationalize state holding of specialized financial institutions, state-owned enterprises, and state commercial banks	<p><i>Measure taken over last 6 months and significance</i></p> <ul style="list-style-type: none"> <li>• No significant measures taken</li> </ul>
G.	Enable corporate sector restructuring through out-of-court mediation, streamline the legal execution process for old foreclosed properties, and reduce the fees on the sale of foreclosed assets	<p><i>Measure taken over last 6 months and significance</i></p> <ul style="list-style-type: none"> <li>• No significant measures taken</li> </ul>
H.	Government's stimulus package to support weakened industries during the global financial crisis.	<p><i>Measure taken over last 6 months and significance</i></p> <ul style="list-style-type: none"> <li>• <b>With the objective to provide more credit facility to the private sector, cabinet approved the capital injection in two Specialized Financial Institutions (SFIs).</b> Cabinet resolution on February 17, 2009 approved the capital injection to EXIM Bank of THB 5 billion and Small Industry Credit Guarantee Corporation (SBCG) of THB 3 billion. EXIM Bank and SBCG will be able to extend credit guarantee for exporters and operators of SMEs in the expected amount of THB 150 billion and 30 billion respectively.</li> <li>• <b>On April 28, 2009, the cabinet approved the Financial Assistance Program for Tourism Operators.</b> After the airport closure in December 2008 and the cancellation of ASEAN+6 Summit, the tourism-related industries was hard hit and shows sign of business instability. The cabinet approved the SME Banks to provide revolving loan for tourism-related SMEs at the interest rate of MLR – 3% with the grace period of 1 year.</li> <li>• <b>Cabinet approved 1-year loan to SMEs for tax payment purpose.</b> According to the cabinet resolutions on April 28, 2009, the Small Industry Credit Guarantee Corporation (SBCG) will provide THB 10 billion full credit guarantee for tax payment purpose through commercial banks and SFIs.</li> </ul>

### 3. Reforms to Improve Business and Investment Environment and Trade Regime

Objective		Reform Measures Taken
A.	Improve competitiveness of business sector	<p><i>Measures taken over last 6 months and significance</i></p> <ul style="list-style-type: none"> <li>• <b>The cabinet endorses a comprehensive approach to develop agricultural products</b>, as proposed by NESDB. Cassava committee and feeding corns committee will be established as key agencies that design and implement strategic plans for the two industries. The cabinet also assigned Ministry of Commerce to reconsider the scope of work of the national rice policy committee and to draft a strategic plan for a comprehensive rice management (from price stability, farmers' registration, production and processing, quality control, stock management, marketing, research and development, and supply chain). Similarly, Ministry of Agriculture and Cooperatives will introduce a new committee on natural rubber policy that oversees the entire production process and pricing mechanism.</li> <li>• <b>The cabinet approved a master plan on fishery management (2009-2018)</b>. There are various agencies and departments that work on managing fishery resources in Thailand, such as Ministry of Agriculture and Cooperatives, Ministry of Natural Resources and Environment, Ministry of Transport, Ministry of Commerce, Ministry of Industry, and Royal Thai Navy. Proposed by Ministry of Agriculture and Cooperatives, this master plan will help to strengthen collaboration between these agencies, with Department of Fishery as a coordinating agency. The plan also seeks to manage Thai fishery resources and environment more effectively by enhancing human capital and relevant institutions.</li> <li>• <b>A draft Act on National Farmers Council is approved</b>. Put forward by Ministry of Agriculture and Cooperatives, the council is set up to (i) design overall policies to strengthen farmers and organizations on agricultural development, (ii) protect farmers' rights and benefits, (iii) promote collaboration among farmer groups, and (iv) advise the cabinet on agricultural issues. The committee will also draft a national agricultural development master plan. The members will comprise of representatives from provincial farmers councils and others from different agricultural organisations.</li> <li>• <b>The cabinet approved a draft Act on Thai Rubber Organisation</b>. Proposed by Ministry of Agriculture and Cooperatives, this new entity is responsible for overall management of Para rubber in Thailand. It manages Para rubber development fund, strengthens Thailand's central role in world rubber industry, assists entrepreneurs and workers in rubber business, aims to stabilise rubber prices, and promotes rubber quality improvement.</li> <li>• <b>The cabinet passed a draft Act on National Land Policy Committee</b>. There are currently several agencies under different ministries that involve land management. Proposed by Ministry of Natural Resources and Environment, this new committee is responsible for overall soil resources and land management by designing national policies and giving a verdict on any conflicting issues that may arise between government agencies. This central committee, which will have coordinating committees at the provincial level, will also work on land titling, land reforms, urban planning, buildings control, and legal documents on land.</li> <li>• <b>Registration of migrant workers in 19 business types is permitted</b>. To lessen labour shortages in businesses that local workers are in short supply or not willing to participate, the Cabinet now allowed irregular migrant workers to legally register. This covers workers from Cambodia, Lao PDR, and Myanmar. Examples of the nineteen business areas are plantation, livestock, recycling activities, mining, metal work, soil products, building materials, stone processing, chemical production, vehicle batteries, goods transport, retail trade, and gas stations.</li> </ul>

Objective		Reform Measures Taken
		<ul style="list-style-type: none"> <li>• <b>The Cabinet agreed with a strategy to promote the photographic and cinematographic industry.</b> Proposed by the Ministry of Culture, the plan is for 2009-2011. The strategy aims to promote Thailand as one of the world's key movie production sites, mainly through training more local personnel, streamlining regulatory burden, and setting up a new agency that is jointly managed by public and private sectors.</li> <li>• <b>The Cabinet agrees with a national strategy on coffee industry (2009-2013).</b> Initiated by Ministry of Agriculture and Cooperatives, the strategy primarily seeks to prepare Thai coffee growers for a more liberalized coffee market in 2010 as part of the ASEAN free trade agreement. It aims to raise yield rate and enhance the quality and safety of Thai coffee. This will be achieved through more technology transfer and stronger links across coffee grower groups. There will be pilot projects to enhance production efficiency in 15 provinces, where analysis on several issues such as potential plantation areas, logistics, pricing and returns will be conducted. Total budget is around 213 million baht.</li> <li>• <b>The Board of Investment extends investment incentives in many business areas.</b> Since November 2008, the BOI has offered special investment benefits to approved investments in six priority industries that are located in any provinces except Bangkok, as part of Thailand Investment Year 2008-2009. The six sectors are businesses that are related to (i) energy saving and alternative energy, (ii) high-technology, (iii) environmental-friendly materials and products, (iv) mega projects, (v) tourism and real estates, and (vi) high-technology, material-based agriculture. In March 2009, the BOI extends sub-industries covered by these six industries. These include among others broadcasting and telecommunications equipment, electronic components, rail and electric rail, stainless steel pipe, concrete for public infrastructure purpose, medical food, and vehicles tires. In addition to these six target industries, investment incentives for other industries are also more generous. For examples, promoted firms in the ship building and repair industry are now permitted to locate in any investment zone (previously limited to zones 2 and 3 only), while incentives for solar cell production is now offered to raw material production stage such silicon and coating glass. Import duty exemption is also given to imported machinery that is used to product new variations of products, which meet BOI requirements.</li> </ul>
B.	Reform of legal and judicial regime	<p><i>Measure taken over last 6 months and significance</i></p> <ul style="list-style-type: none"> <li>• <b>The Cabinet agreed with the draft Act on Legal Reforms Agency.</b> This will result in an independent committee on legal reform, which is responsible for improving and developing laws that comply with the constitution. The committee will study current laws and prepare projects for a systemic law reform. It will also advise the cabinet on new laws and provides recommendations on draft laws proposed by members of parliament, courts, independent agencies, and the public.</li> </ul>
C.	Improve the skills and quality of labor	<p><i>Measure taken over last 6 months and significance</i></p> <ul style="list-style-type: none"> <li>• <b>The Cabinet approved a strategy to enhance the quality and management of secondary education.</b> Currently, progression rate to upper secondary education in Thailand is relatively low, while dropout rate is high. The aims are thus to broaden opportunities and promote equity on access to secondary education. The plan will also seek to enhance school quality and encourage decentralization in management. The implementation period is four years (2009-2012), with the budget over 9 billion baht.</li> </ul>

Objective		Reform Measures Taken
D.	Reduce tariff to improve Thailand's competitiveness 1/	<p><i>Measure taken over last 6 months and significance</i></p> <ul style="list-style-type: none"> <li>• <b>Various products now enjoy lower or no import tariff.</b> A universal tariff reduction includes oil cake under the WTO agreement announced in February 2009. For specific tariff cuts that result from free trade agreements, the major changes are ASEAN's agreements with China and Japan, announced in April-May. For China, tariffs of the following items are cut or cancelled: various food items, building materials (such as stones and metal wires), shoes, jewellery, certain vehicles and motorcycles and parts, and electrical appliances (such as fans, water pump, freezers, electrical motors and power generators). For Japan, these cover among others live animals for breeding purpose, various food and beverage items, flowers, smoked rubber sheet, minerals, chemical substances, office supplies, furniture, wearing apparels, wooden and paper products, computers and computing machines, toys, and household electrical appliances.</li> </ul>
E.	Promote Thai exports to new markets 2/	<p><i>Measure taken over last 6 months and significance</i></p> <ul style="list-style-type: none"> <li>• <b>Multilateral FTAs between ASEAN and other partners showed a significant progress.</b> For the pact between ASEAN, Australia, and New Zealand, tariff rates under the normal track for the six ASEAN foundation members will be cancelled in 2013 for most products, and 2015 for the rest. Most details on trade in services, investments, and rules of origin also agreed. Finance Ministers of all member countries signed the agreement in February 2009. Meanwhile, the ASEAN-Korea agreements on goods trade and services trade were also signed in February this year. While services trade agreement is effective since 1 June 2009, the pact on goods trade is expected to be effective in October. Korea and Thailand will cancel around 90 and 80 of all tariff lines that are being traded, respectively. The agreement also covers various areas of services trade and economic cooperation. The pact between ASEAN and India is also agreed. Currently over 70 percent of goods that are being traded will enjoy no tariffs by end-2012, although this is still subject to changes. The agreement is expected to become effective in early 2010. For BIMSTEC, the member countries agreed in June 2009 to cut or waive import tariffs of over 5,000 products. The three faster-growing nations (India, Sri Lanka, and Thailand) will cut tariffs for 10 percent of their agreed items by January 2010. By January 2011, all members will offer at least half of listed items duty-free. Finally, Thailand signed the ASEAN-Japan agreement in April 2008. Japan will abolish 90 percent of tariff lines that are being traded with an immediate effect, while Thailand will eliminate import tariffs that worth 93 percent of imports from Japan within 10 years.</li> </ul>

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Note: 1/ See *Tariff Reform* in Section 3.2 on Recent Trade Reforms for a more detailed discussion.

2/ See Table 17 for more details.

#### 4. Public Sector and Governance Reform<sup>19</sup>

Objective		Reform Measures Taken
A.	Improving public service quality by streamlining and redesigning work processes and procedures	<p><i>Measures taken over last 6 months and significance</i></p> <ul style="list-style-type: none"> <li>No significant measures taken</li> </ul>
B.	Changing roles, responsibilities, and rightsizing the government bureaucracy by restructuring public administration and improving intergovernmental relations at all levels	<p><i>Measures taken over last 6 months and significance</i></p> <ul style="list-style-type: none"> <li><b>The draft of OCSC regulation on civil service discharge was approved in principle by the cabinet.</b> The OCSC drafted the regulation to be consistent with the Civil Service Act (2008). In principle, a civil servant who fails to meet the performance satisfactory level to the official authorities has one time chance to improve performance in accordance with the agreement plan made to the respective authorities. In the case where the second evaluation does not meet the criteria, a civil servant is subjected to be discharged from government service. However, civil servant has a right to appeal to the Merit System Protection Board within 30 days of receiving notice.</li> <li><b>The amendment of royal decree of the establishment of the Office of Knowledge Management and Development (Public Organization) was approved in principle.</b> The current royal decree to establish the OKMD (2004) needs to be amended to remove existing constraints with providing more flexibility for government to deliver service in a more efficient way. In particular, the authority of the head of office will be extended to every staff under the organization to enhance administration.</li> </ul>
C.	Enhancing capacity and performance of public sector to efficiently and effectively perform their functions by reforming financial and budgetary system, reviewing system of human resource management and compensation, developing a new mindset, work culture and value, and modernizing government operation.	<p><i>Measures to be taken in the next 6-12 months</i></p> <ul style="list-style-type: none"> <li><b>Public Finance Act is tentatively to be effective by the beginning of FY2010.</b> The 2007 Constitution mandated the government to develop a new Public Financial Act. MOF as a key responsible agency prepared this draft Act, held inter-agency consultations, and submitted the revised draft to the cabinet with expected to be approved by the first half of this year. By the beginning of FY2010, Public Financial Act and respective regulations is tentatively to be approved by the Parliament, and implementation commences.</li> </ul>

<sup>19</sup> The objectives detailed in this matrix are consistent with the Government's Public Sector Development Strategy (2003-2007) and the more recent Public Affairs Management Plan.

Objective		Reform Measures Taken
D.	Improving governance in public sector through participation, accountability, and transparency	<p><i>Measures taken over the last 6 months and their significance</i></p> <ul style="list-style-type: none"> <li>• <b>The Revenue Department announced the criteria and procedures for money donation to political parties.</b> Revenue Department in collaboration with Office of the Election Commission of Thailand drafted the criteria and procedures for donation to political parties. The core concept of the draft includes 1) Money donated to political parties must be filed in the annual PIT form of donor 2) Political parties who received donation must register to the Election Committee before the deadline of tax submission in every March 3) Office of the Election Commission of Thailand must inform list of political parties as well as their relevant codes to the Director General of the Revenue Department to further promulgate to public and 4) Revenue Department shall provide the list of political parties who received donation to registrar of relevant political parties and also transfer the total amount of donation to Political Party Development Fund.</li> </ul>

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## 5. Social Protection

Objective		Reform Measures Taken
A.	Develop social insurance mechanisms for the elderly and those affected by unemployment, work-related injuries or other shocks to income.	<p><i>Measures to be taken in the last 6 months and their significance</i></p> <ul style="list-style-type: none"> <li>• <b>The Cabinet, on February 3<sup>rd</sup>, 2009, acknowledged the Thailand's Elderly People Report on 2007 proposed by the National Committee on Elderly People.</b> According to the report, in 2007, there were 7 million aging people who were over 60 years old. There were, however, 35.1 percent of the elderly people inclined to continue working. Since Thailand is gradually moving toward an elderly society, many agencies advocate conducting four activities related to elderly people related to: 1) National Elderly People day, 2) Tax measures for elderly people, 3) Role of local community in taking care of elderly people, and 4) Pension system for elderly people.</li> <li>• <b>The Cabinet, on January 28<sup>th</sup>, 2009, approved the extension of unemployment compensation period for laid-off workers from 6 months (180 days) to 8 months (240 days) for workers who are unemployed in the year 2009.</b> Proposed by Ministry of Labour, this program helps to support the workers under the social security system who become unemployed because of the economic downturn. One-stop services were established in each province to facilitate access to social security provisions, assist in job search and provide skill-building training. A budget of 120 million baht was also endorsed for the Office of the Permanent Secretary to organize training workshops for the unemployed.</li> <li>• <b>The cabinet, on January 13<sup>th</sup>, 2009, approved 9,000 million baht for the distribution of 500 Baht allowances for a period of six months to senior citizens of 60 years or older</b> who do not receive support from other government institutions and register themselves at local administration offices. Under this new scheme, participants are not selected on the basis of poverty criteria.</li> </ul>
B.	Establish a safe work environment through standards and enforcement and increase labor market efficiency by facilitating job matches and placement.	<p><i>Measures taken in the last 6 months and their significance</i></p> <ul style="list-style-type: none"> <li>• <b>The cabinet, on January 13<sup>th</sup>, 2009, approved 6,900 million baht of budget for the “Tonkla Archeep (career sprout)” intensive vocational training program.</b> The project aims to train workers and enhance capacity-building activities for 500,000 unemployed, soon to be unemployed, and new graduates. Trainees will receive cash allowance after completing the course.</li> <li>• <b>The cabinet, on March 24<sup>th</sup>, 2009, approved the principle on draft Act of sanitation safety and work related to machine, crane, and boiler.</b> Proposed by the Ministry of Labor, employers who possess machine, crane, and boiler have to maintain safety measures according to the industrial standard. This is to ensure that the equipment will not cause dangers or jeopardize workers.</li> </ul>
C.	Provide effective poverty alleviation and social assistance programs for those with limited or no other means of support	<p><i>Measures taken in the last 6 months and their significance</i></p> <ul style="list-style-type: none"> <li>• <b>The Cabinet, on January 28<sup>th</sup>, 2009, approved 607 million baht to buy back the farmers' debt in order to keep their land and houses. This program was proposed by the Ministry of Agriculture and Cooperatives.</b> The buy-back farmlands were previously auctioned for 1,187 farmers. Among these, 1,140 farmers had their lands seized by financial institutions. However, the land price for each piece of land was limited to 2.5 million baht.</li> <li>• <b>The Cabinet, on January 20<sup>th</sup>, 2009, approved 11,409 million baht to extend 5 measures of the “6 Measures</b></li> </ul>

Objective	Reform Measures Taken
	<p><b>For 6 Months Programs” to another six months from February 1, 2009.</b> Around 13,901 million baht has been set aside from the annual fiscal budget of 2009. Four government’s measures aim to lessen live burden on the cost of transportation and utility service including public water, household electricity, bus and 3<sup>rd</sup> - class train fare for six months. This renewal of 6 months measures will cover more people in various provinces.</p> <ul style="list-style-type: none"> <li>• <b>The Cabinet, on March 3<sup>rd</sup>, 2009, approved the “2,000 Baht Check Chuay Chart (Save-the-Nation Check)” to workers who contribute to the SSF, state enterprises’ employees and civil servants (including tambon and village heads).</b> The target beneficiaries are those who are earning less than 15,000 baht per month for a total of 19 billion Baht out of 34 billion Baht earmarked for short-term stimulus. The handouts are to be paid in cashier's checks to be used to purchase goods at local stores and be later cashed by businesses at designated banks. This program aims in alleviating financial burden to low income formal workers. At the same time, the government hopes that the program will help stimulate the economy when cashier’s checks are used to purchase goods.</li> <li>• <b>The cabinet, on January 28<sup>th</sup>, 2009, approved the principle 9 projects of the Administrative Center of southern border provinces.</b> Proposed by the Ministry of Agriculture and Cooperatives, 9 approved projects are to initiate 1) Administrative Center of Southern Border Provinces’ Learning Class, 2) Fostering Family for Children and Youth in Southern Border, 3) Happy School in Yala, 4) Education cooperation for Youth in Southern Border provinces, 5) Islamic Teacher Development Program, 6) Program to promote graduate students from vocational school to further training in Japan, 7) Scholarship and education equipment supporting program, 8) Supporting Good man to attend Haj, and 9) Development Program of industries in Yala.</li> <li>• <b>The cabinet, on January 13<sup>th</sup>, 2009, approved the extension of free public education to 15 years of schooling by allocating 19,000 million baht to more than 40,000 local schools throughout the country.</b> The program provides students’ uniforms, text books, and exercise books free-of-charge, as well as subsidizes other school costs. This program aims to alleviate the financial burden carried by parents and help stimulate the economy.</li> </ul>

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