Economic overview

	1990-94	1995	1996	1997
Growth rate of real GDP (%)	9.2	8.7	6.4	-1.3
CPI growth rate %	4.8	5.8	5.8	5.6
Exports (as % of GDP)	29.2	33.5	30.0	37.5
Fixed investment (as % of GDP)	40.1	41.8	40.8	35.6
Gross domestic savings (% of GDP)	35.4	36.2	35.3	34.0
Current account balance (% of GDP)	-6.5	-8.0	-7.9	-4.6
Reserve money growth (%)	16.1	22.6	13.5	15.8
Narrow money growth rate (%)	14.7	12.1	9.1	1.5
Broad money growth rate (%)	18.7	17.0	12.6	16.5
Government expenditures (% of GDP)	15.2	15.8	16.1	18.1
Government budget balance (% of GDP)	3.2	2.9	2.3	-0.6
Foreign debt (as % of GNP)	40.1	50.4	50.3	59.6
Debt service ratio for all external debt	14.2	10.4	12.1	15.8
Exchange rates (vis-à-vis US$)	25.3	25.2	25.6	47.2
Real exchange rate (1990=100) WPI based	94.7	89.6	80.1	123.8
Nominal wage index	130.5	189.7	189.3	217.1
Real wage index	118.1	150.1	141.4	148.0
Current account balance (US$ million)	-7,121	-13,554	-14,691	-2,916
Capital account balance (US$ million)	10,599	21,908	19,486	-15,440
Foreign direct investment (US$ million)	1,948	2,068	2,335	3,028
Export value (US$ million)	33,174	56,458	55,720	57,533
Composition of export, value of highest four exports (according to 1996 rank), US$million				
Office machines & automatic data processing	2,551	5,557	9,310	n/a
Electrical machinery, apparatus & appliances	3,050	6,404	6,106	n/a
Fish, crustaceans, mollucs	3,227	4,472	3,852	n/a
Telecommunications	1,884	3,049	3,020	n/a
Import value (US$ million)	42,407	70,775	72,331	62,853
Composition of import, value of highest four imports (according to 1996 rank), US$ million				
Electrical machinery, apparatus & appliances	4,786	9,691	8,367	n/a
Road vehicles	3,060	5,392	4,877.	n/a
Specialized machinery	2,860	4,502	4,434	n/a
General industrial machinery & equipment	2,648	4,761	4,294	n/a
Exports dependence on unaffected markets (%)	45.8	36.7	37.8	n/a
Volume of exports (index)	135.9	202.0	193.0	n/a
Volume of imports (index)	121.3	175.0	170.3	n/a
International reserves minus gold (US$ million)	20,997	35,982	37,731	26,179
Value of total foreign debt (US$ billion)	45.2	83.2	90.8	91.7
Short term foreign debt (US$ billion)	17.5	41.1	37.6	n/a
DS Stock Market Index ($)	662.4	963.4	609.6	141.7
DS Stock Market Index (local currency)	660.9	958.4	617.4	269.4
Bangkok SET index	1,052.1	1,280.8	831.6	372.7
Nominal lending rate (%)	12.8	13.3	13.4	13.6
Nominal deposit rate (%)	10.4	11.6	10.3	10.5
Nonperforming loans (% of total loans)	8.6	7.7	9.0	20.0

By Frank Flatters, Queen's University, Canada[1]

The unpegging and subsequent collapse of the Thai baht in July 1997 triggered what was initially a regional crisis but now has become a global problem. The floating of the baht was made necessary by the exhaustion of Thai foreign exchange reserves, after months of futile efforts to stave off necessary policy adjustments and structural reforms. It was preceded by an investment bubble, especially in real estate and stock markets, by widespread structural and prudential problems in the financial sector, and by a very rapid build-up of short-term foreign debt liabilities. Foreign borrowing and lending behavior was encouraged by a false sense of security about the fixed exchange rate, and by confidence that downside risks would be covered by sovereign assumption of private debt obligations.

Denial and unwillingness to adjust preceded the floating of the baht by at least six months and arguably up to two years, and persisted for at least several months afterwards.[2] It made the crisis much worse and the recovery much longer than necessary. Nevertheless, following the change of government in November 1997, Thailand has been regarded as the IMF's "star partner" in dealing with the crisis.

Since late last year Thailand has been, in many respects, much more resolute than its Asian neighbors in its crisis management and economic recovery program. It has been flexible and pragmatic in adjusting the program to changing circumstances and to new knowledge about the crisis and about the impacts of government policies.

The baht began to stabilize against the dollar in March 1998. In August the government began to ease its fiscal and monetary policies. Since then bank lending rates have fallen considerably, and the baht showed unexpected signs of further strengthening in October and November. Inflation has remained remarkably low since the onslaught of the crisis, and has begun to decline. Will Thailand, the country that started the crisis (at least temporally), be equally fast in emerging from it?

A review of recent economic data shows that recovery is still some way off. Significant gaps remain in the government's economic program, especially in dealing with corporate debt restructuring and with the large and growing non-performing loans (NPLs) in the banking system. Political factors and social pressures are impeding further progress. But failure to act will also aggravate social tensions and threaten future stability. Previously offered government guarantees to banking system creditors and depositors eventually might have to be put back on the table. External factors are another serious threat to recovery. Finally, the crisis has distracted attention from fundamental long-run problems of Thai competitiveness.

The state of the economy

The first indicators of the impending crisis are in the trade data. Import and export growth stopped in 1996; exports resumed very sluggish growth in 1997, and collapsed again in 1998. Imports show the most dramatic drop, from 31.8% growth in 1995 to a 37.2% decline in 1998.

The simultaneous fall in exports and imports in 1996 left the current account almost unchanged. The following year, however, saw a huge reversal in capital flows, from a surplus of $19.5 billion in 1996 to an $8.7 billion deficit in 1997. Almost all of this was accounted for by net private capital flows, which changed from an inflow of $18.2 billion in 1996 to an outflow of $8.8 billion the next year.

The collapse of capital flows reflected a sudden crisis of confidence.[3] The investment bubble that had been created in the first half of the 1990s was self-sustaining as long as growth continued to justify expectations. However, growth could not be maintained on the basis of expectations alone. Among the factors contributing to the vulnerability of the system were:

- large and growing short term foreign liabilities relative to foreign exchange reserves, which themselves were rapidly diminishing as the Bank of Thailand (BOT) tried to maintain the baht's peg,
- the increasing over-supply of real estate, especially in Bangkok, which hurt the property and construction sectors directly, and also threatened the value of the principal form of collateral used in much bank lending,
- falling stock market values as prices outran growth in earnings capacities of listed companies,
- underlying problems of corporate governance and serious weaknesses in regulation of financial markets,
- macroeconomic mismanagement, especially unwillingness to float the baht,
- realization that overvaluation of the baht, together with more fundamental problems of human resource development and protection of special interests, were eroding Thailand's competitiveness in labor-intensive exports and undermining its ability to move up the ladder of comparative advantage.

Effects of the crisis[4]

The huge reversal of capital flows between 1996 and 1997 required major economic adjustments. The government delayed floating the baht until net foreign exchange reserves had been exhausted. Since many domestic debts were foreign-currency-denominated, the depreciation aggravated the already serious NPL problems in the banking and financial system. In June 1997, prior to the float, 16 finance companies were shut down. To reassure creditors and depositors and to avoid financial panic, the government stated that remaining banks and finance companies were financially sound, and that all their credits and deposits would be guaranteed by the government. By the end of 1997 the Financial Institutions Development Fund (FIDF) had provided almost Bt1.2 trillion (about $30 billion) in liquidity support to banks and finance companies, of which at most one-half might be recoverable.[5]

The main goal of macroeconomic policy after July 2 was to stem the free fall of the baht, mainly through tight monetary policies and correspondingly high interest rates. This further aggravated NPL problems of banks and finance companies, and 42 more financial institutions were shut down in August 1997. Restoration of financial market stability became the other top policy priority. Measures implemented or being planned include: tightening of NPL

The changing situation

Changes in labor employment and output composition

	Composition of output		Composition of labor force	
	1986	1996	1970	1990
Agriculture	15.7	10.7	79.8	64.1
Industry	33.1	39.8	6.0	14.0
Services	51.3	49.5	14.2	22.0

Ratings of Long-Term Debt Denominated in Foreign Currencies

	Moody Rating	Standard & Poor Rating	Date	Moody's Banking Financial Strength Ratings
January 15, 1996	A2	A	Jun-96	D+
December 2, 1996	A2	A	Dec-96	D+
June 24, 1997	A3	A	Jun-97	D
October 24,1997	Baa1	BBB	Dec-97	D
December 31, 1997	Ba1	BBB	May-98	E+

Rating Systems, from highest to lowest. The ratings range from A (highest) to E (lowest).

Moody's: Aaa, Aa1, Aa2, Aa3, A1, A2, A3, Baa1, Baa2, Baa3, Ba1, Ba2, Ba3

S&P's: AAA, AA+, AA, AA-, A+, A, A-, BBB+, BBB, BBB-, BB+, BB, BB-

Forecasts on 1998 and 1999 Situation

		GDP growth (%)		CPI inflation (%)	
		1998	1999	1998	1999
International Monetary Fund	May-98	-3.1		11.6	
Salomon Smith Barney, Hong Kong	Jun-98	-8.7			
Unctad	Sep-98	-8.0			
Political & Economic Risk Consultancy, HK	Oct-98	-8.0	-1.0	11.0	7.5
International Monetary Fund	Oct-98	-8.0		9.0	
The Pacific Economic Cooperation Council	Nov-98	-7.0	0.5	9.2	6.1
International Monetary Fund	Dec-98	-8.0	1.0	8.0	2.5

reporting and provisioning rules; deadlines for and measures to encourage recapitalization of banks and finance companies according to international capital requirements standards; introduction of workable bankruptcy and foreclosure laws, and of complementary debt workout systems; disposal of assets of closed companies; and reorganization of good and bad assets of remaining firms.

The negative wealth effects of the depreciation and the collapse of asset markets, together with the failure of credit markets due to the financial turmoil, depressed domestic demand. The export slump has continued, as has the even more severe contraction of imports, in order for the current account to adjust to the net capital outflows. GDP started to decline in the second half of 1997, and continued through 1998. The effects are mirrored in the decline of manufacturing output.

The social implications are serious. Labor market adjustment is taking several forms. The number of unemployed has tripled from 1996 until the end of 1998. There also have been major reductions both in hours worked and in nominal wages.[6] While the initial labor force impacts have been largely in urban areas, the effects are also being felt in the countryside through both return migration of urban workers, and reduced remittances. On the other hand, agriculture has benefited from depreciation-induced increases in domestic currency prices of tradable goods. Fortunately, CPI inflation has been remarkably low, despite the large baht depreciation.

Thailand does not have a well-developed formal social safety net. There is no unemployment insurance. Many basic social benefits, such as health care, are tied to employment and, until very recently, ceased when employment with the firm ended. The main social insurance systems have been the extended family and the informal labor market. These have been severely tested in the crisis. Arguably the most important government contribution to social insurance has been the severance penalties specified in Thai labor law, which make it costly for firms to lay off workers. This is the main explanation for the high proportion of labor market adjustment that has occurred through reduced wages and hours, rather than unemployment. This has ensured a certain amount of so-called income spreading that could not have been accomplished under the formal social security system.

Evolution of policy responses

In the midst of the crisis, when the ruling coalition lost the confidence of parliament in November 1997, Thailand had a peaceful and orderly change of government. Unlike its predecessors, the leading party in the new government had a reputation for being relatively clean and corruption-free, and it appointed several widely respected economic technocrats to the cabinet.

Their initial set of economic policies followed quite closely the IMF orthodoxy – tight monetary and fiscal policies and strict enforcement of high standards of financial sector governance. The initial letters of intent with

Tracking economic developments

	1997 Q1	1997 Q2	1997 Q3	1997 Q4	1998 Q1	1998 Q2	1998 Q3
Growth rate of real GDP (%)	7.0	7.5	-4.2	-11.5	-16.8	-15.3	-11.3
Exchange rates (against US$)	26.0	25.8	36.5	47.2	38.8	42.3	39.3
Real exchange rate (1990=100) WPI based	75.1	75.5	100.7	123.8	95.9	101.1	95.3
International reserves minus gold (US$ million)	37073.8	31361.0	28621.8	26179.5	26892.5	25784.8	26578.0
Reserve money growth (%)	18.3	31.0	19.8	15.8	1.0	-10.8	
Narrow money growth rate (%)	2.3	0.8	-1.9	1.5	-5.7	-3.3	
Broad money growth rate (%)	10.0	11.9	16.6	16.5	15.6	13.8	
CPI growth rate (YOY%)	4.4	4.3	6.2	7.5	9.0	10.3	8.1
Nominal lending rate (%)	13.0	12.8	13.9	14.9	15.3	15.3	
Nominal deposit rate (%)	9.8	9.3	11.5	11.5	12.0	12.2	
Export value (US$ million)	14128.8	14028.1	14548.8	14827.8	13872.4		
Import value (US$ million)	17487.2	17206.3	15203.4	12956.7	11082.1		
DS stock market index ($)	517.9	391.2	292.3	141.7	205.4	117.2	124.9
DS stock market index (national currency)	531.4	400.3	419.2	269.4	318.5	195.8	195.0
Bangkok SET index	705.4	527.3	544.5	372.7	459.1	267.3	253.8

the IMF trumpeted the government's pride in its strict fiscal and monetary discipline. By this standard, monetary and fiscal policies were quite successful. An immediate symptom was the continued rise in interest rates. Unfortunately, as a result of the regional confidence contagion, and of continued (and justified) concerns about the health of the financial sector, the baht tumbled further in early 1998. It finally began to stabilize in March 1998.

Financial sector reform and recapitalization, debt restructuring, and the implementation of effective bankruptcy and foreclosure laws proceeded much more slowly. A bankruptcy law was passed in February 1998, but in response to pressures from influential debtors it had been watered down to the point of almost complete ineffectiveness.

While initial forecasts were of a speedy V-shaped recovery, it became increasingly apparent that the recession would be deeper and much longer lasting than anyone had predicted. One result was the gradual relaxation, in consultation and agreement with the IMF, of official fiscal targets, especially on the revenue side. By August 1998, there was widespread and increasingly vocal public pressure on the government to reverse its strict monetary and fiscal policies, which were seen to be the main cause of the alarming contraction of the real sector and the continuing growth of NPLs. In response to and in general sympathy with this view, the government and the IMF agreed, as part of the fifth letter of intent, on a major relaxation of the macroeconomic policy regime.[7] The goal was to assist the real sector through lower interest rates, and to stimulate domestic demand. Lower interest rates were also seen as a means of easing loan payment burdens on debtors. At the same time, the government announced additional initiatives intended to speed up the recapitalization of the banks, restructure debts of the corporate and banking sectors, and increase bank and finance company lending.

The monetary and fiscal easing had the predicted effect on interest rates, as both lending and deposit rates began to fall substantially and rapidly.[8] This led to a resurgence of stock market investment and a significant increase in the Stock Exchange of Thailand (SET) index in the fourth quarter. Slightly more surprising was a further strengthening of the baht, which the BOT attempted to restrain. Falling interest rates and improvements in the baht and the SET index have led some observers to suggest that the Thai economy has bottomed out and that recovery is now on the horizon. However, while there are some small promising signs (FDI is beginning to return, and will be significantly higher than in 1997), most of the real economic indicators – exports, imports, manufacturing output, investment, employment – show little sign of reversal.

What is the problem?

Remaining obstacles to recovery[9]

The principal obstacle to Thai economic recovery is the restructuring of the financial system. The economy remains saddled with foreign debts of almost $90 billion; the FIDF has debts of about $30 billion; NPLs in the banking system are now greater than 40% and are likely to reach 45-50% by mid-1999; banks are in need of massive recapitalization.

The government has developed a debt workout program modeled after the "London approach".[10] However, of the almost $18 billion of bad loans owed by the 353 firms eligible for this program, not a single one had been resolved by the beginning of November. According to another survey, of the approximately $80 billion of bad loans outside of this scheme, only $310 million had been restructured by late October. The absence of effective bankruptcy and foreclosure laws has been a major reason for this. This is discussed again below.

The tightening of NPL reporting rules and the phasing in of new loan provisioning requirements has put increased pressure on bank profits. This will continue until the provisioning rules are fully in effect. As losses eat into the banks' equity, recapitalization becomes even more urgent. However, as NPLs continue to expand, it becomes more obvious that, even for the most healthy of the remaining banks, full provisioning will effectively wipe out most if not all existing shareholders' equity. It is understandable, therefore, that banks are reluctant to adjust.

The August 1998 measures were aimed at providing government recapitalization support to the banks, subject to conditions related to increased bank lending and more immediate provisioning for bad loans. As of the end of October, there was practically no interest expressed by any banks in joining the new schemes. Some observers feel the measures to be too lenient on the banks both in terms of the requirements to be met to join the schemes, and in their voluntary nature, which allow the banks to postpone necessary adjustments, including further writing down of shareholders' capital. From their reaction to the schemes, the bankers seem to feel they are not sufficiently attractive. One obstacle to the design and implementation of financial sector restructuring policies has been the influence of some of the largest banks through their close links with the military and other highly influential and respected parties. It is politically difficult for the government to force such stakeholders to absorb the kinds of losses and make other adjustments necessary for recapitalization and restructuring.

According to the Thailand's agreements with the IMF, effective new foreclosure and bankruptcy laws should have been in place by October 1998. This deadline was not met, and the measures were postponed for at least several months. Meanwhile, an odd coalition of influential large debtors, who are well represented in the Thai senate, and of poor, small, indebted farmers is exerting considerable public pressure to dilute the new measures. The absence of an effective legal framework for bankruptcy and foreclosure was one of the causes of the crisis. Delays in implementing these laws are a major obstacle to progress on debt restructuring.

Thailand's crisis is a financial crisis. To achieve recovery, there needs to be resolution of problems paralyzing the financial sector. The government has made many of the right steps. But it needs to be much more aggressive. Shareholders and management of major banks will have to be forced to make much greater adjustments than they undertaken so far. The government will have to tackle the NPL problems much more directly. Like all other countries that have gone through this kind of banking crisis, it almost certainly will have to find a mechanism to take the NPLs out of the banking system and manage them separately. Some more effective cost-sharing mechanisms will have to be found to limit the crushing long-term burdens of hastily made guarantees to creditors and depositors.

Political stability

Thailand had the good fortune to have undertaken a major constitutional reform just prior to the crisis. As a result, and unlike Indonesia, for instance, Thailand accomplished a peaceful, legitimate, constitutional change of government in the midst of the crisis. The competence and legitimacy of the new government have been very beneficial. A principal goal of the new constitution and of the current government is to root out long-standing traditions of "money politics" and of bureaucratic corruption. Whether these goals will be met is still unclear.

As a democratic government, the ruling coalition is pressured by competing and sometimes very powerful special interests. The government's very slim parliamentary majority made it difficult to overcome vested interests or implement "unpopular" measures. This was seen in the weakness of the initial new bankruptcy law, in continuing difficulties passing a new one as well as a foreclosure law, and in lack of aggressiveness with financial sector restructuring and recapitalization. In October 1998 the government admitted another large and influential party to the coalition. This provides a safer parliamentary majority, but also expands the range of interests and competing forces that must be satisfied within the coalition in order to keep it together. An election will have to be held by 2000, and is likely to be forced much earlier. Many of the old pros from Thailand's money politics regime are still in the game – some are in the current cabinet – and there is no guarantee that they will not win the next election.

The government faces pressures from debtors who fear tougher bankruptcy and foreclosure laws, from bankers and other creditors who want them to be more effective, from bankers who want assistance with recapitalization without significant capital write-downs, and from international creditors who want to ensure that government guarantees of their loans are honored. Meeting many of these wishes will involve huge fiscal expenditures. One of the greatest challenges will be to explain to ordinary workers and farmers why they must bear the burden of inflation and/or future taxes to pay these costs. There are indications that the government plans to use recent structural adjustment loans to fashion special schemes for farmers and small- and medium-sized businesses, in order to gain a broader base of popular support for the economic program. While this might make short-term political sense, it may not be consistent with medium- or long-term economic recovery needs.[11]

Popular support for the economic recovery program will be helped if those responsible for Thailand's economic mess are seen to be paying some of the costs. The Nukul Commission report, requested by the new government in November 1997, provides an excellent analysis of the policy failures and some of the corporate and banking misdeeds that led to the crisis. Charges have begun to be laid against some of the senior banking and finance executives whose irresponsible and fraudulent lending behavior led to bank and finance company failures. Continuation of these investigations and charges will not only provide political legitimacy for difficult and possibly controversial measures that remain to be taken, but should also help lay the foundations for a sounder financial system and structure of corporate and policy governance.

Whether the current government will have the ability and the necessary political support to do what is necessary is still difficult to predict. The most important indicators will be its success in passing and implementing effective new bankruptcy and foreclosure laws, in resisting pressures to exclude foreigners from participating in recapitalization of the financial and real sectors, and in forcing bank shareholders and influential large debtors to accept necessary capital losses to achieve financial restructuring.

The external environment

The external environment will play an important role in determining the speed of recovery. Slow growth in east and southeast Asia is hurting Thai exports. The same factors will also make foreign capital much more scarce. The effects of the crisis on investors' risk perceptions and "hassle aversion", especially in this region, will take a long time to overcome. The threatening external environment makes strong and effective domestic policies even more important.

Problems of long-run competitiveness

Even before the crisis, Thailand faced some serious problems with long-run competitiveness. While overall productivity growth was moderate, most of it was in agriculture or arose from inter-industry shifts. There was little indication of growth of technological capabilities, or movements "up the ladder of comparative advantage."[12] Among the widely recognized barriers to growth in competitiveness were very low levels and quality of education, serious deficiencies in infrastructural development, and a policy regime at the microeconomic level which was too much geared to creating and preserving rents rather than fostering market competition.[13] Monopolies in basic services (such as telecommunications) and protection of upstream industries (like steel and petrochemicals) were among the most obvious and egregious examples of misguided protectionism. While prudent macroeconomic policies had always been regarded as an area of strength in Thailand, the financial and macro mismanagement that led up to the crisis has called that into question as well. Political and bureaucratic corruption has been another continuing source of concern.

While the crisis has drawn attention to some of these issues and provoked some policy improvements, many of the problems have been left on hold and some have become worse. One immediate effect of the crisis has been a reduction in school enrolments, which will lower rather than raise future education levels. While the government has attempted to exempt major export industries from the costs of upstream protection, it has done little to attack the protection problem directly. There has been considerable talk and some action in dealing with corruption in various ministries, and yet there has been little progress in systematic public service reform and introduction of realistic wage systems.

This is a very tough policy agenda, and it not surprising that progress has been difficult in the crisis environment. But resolution of these problems is essential to restoration and sustainability of Thailand's long-term growth and competitiveness.

Conclusion

Thailand has made a very good start at improving its governance structures and laying the political and economic foundations for recovery. But, despite the recent recovery and stabilization of the baht, falling interest rates, and rising stock prices, real economic data suggest that a resumption of growth is still far away. Significant gaps remain in the short- and medium-term recovery program, particularly with handling massive NPL problems and corporate debt restructuring. Without additional measures, burdens of official credit and deposit guarantees will remain a long-term drag on the economy. Political and social pressures might impede further progress on needed structural reforms. Failure to act might also aggravate social tensions and threaten future stability. While external factors will also impede recovery, the most important barriers are domestic. A variety of competitiveness issues that were apparent before the crisis will remain when it is over.

Will Thailand emerge quickly from the crisis? It is better equipped in many respects than most other countries in the region to face the challenges of the new global environment. It is doing many of the right things, and this at least gives it a good head start. But forecasts about recovery have been consistently optimistic. The crisis has now spread within and beyond the region. There are major gaps and delays in implementation of some of the most important elements of the reform program. Current forecasts of recovery by mid-1999, therefore, appear once again to be overly optimistic. There is still a long way to go.

Notes

1 Email address: <ff@qed.econ.queensu.ca>. Thanks to Wing Thye Woo for comments on an earlier draft, to Popon Kangpenkae for assistance with data, and to Duangkamol Chotana for many helpful discussions and observations, and for insisting on necessary clarification.

2 See the report of the Commission Tasked with Making Recommendations to Improve the Efficiency and Management of Thailand's Financial System (Nukul Commission Report), especially chapter 2, for an excellent account of the government's mishandling of financial and exchange rate policies in 1996 and 1997. The report is interesting as well for its account, based on evidence from Thai officials, of the IMF's extensive efforts to alert the government to emerging problems, and of the government's refusal to take advantage of this advice.

3 The Thai crisis of confidence is broadly consistent with the characterization provided by Radelet and Sachs (1998).

4 For further discussion of the lead-up to and the effects of the crisis in Thailand, see Siamwalla (1997) and Siamwalla and Sopchokchai (1998).

5 The FIDF had been established in 1985, as a juristic institution under the Bank of Thailand, with a mandate and very broad powers "to rehabilitate and develop financial institutions and to improve their stability." Prior to 1996, short term liquidity support had been rarely used by FIDF. See chapter 5 of the Nukul Commission Report for a brief history of the role of FIDF and for a critique of its emergency measures, including massive liquidity injections, in 1997.

6 The incidence of significant decreases in wages and hours worked is widely acknowledged. Twenty to thirty percent wage reductions have been common in many sectors. However, poor labor market data make it difficult to make reliable quantitative estimates of the overall incidence or magnitude of these decreases. See Kakwani (1998) for some preliminary evidence on the importance of wage decreases and of underemployment in the adjustment of labor markets to the crisis.

7 The fiscal deficit targets had been gradually easing over the successive Letters of Intent (LOIs). The target in the first LOI had been for a surplus of 1 percent of GDP. In the fourth, fifth and sixth LOIs the target was reduced successively to -2.5 percent, -3.5 percent, and -5 percent of GDP, excluding the costs of financial sector assistance. Until the fifth LOI, monetary targets had been expressed primarily in terms of the interest rates needed to try to maintain exchange rate stability. The fifth LOI changed the emphasis towards a substantial easing of interest rates and liquidity in order to stimulate domestic demand.

8 Because of the profit squeeze on banks from NPLs, however, lending rates have not fallen nearly as quickly as those on deposits.

9 See also Flatters (1998) which reviews positive and negative lessons that can be drawn from the responses to the crisis in Indonesia, Malaysia and Thailand.

10 The Thai version of the “London approach” is an informal and voluntary system under supervision of the Bank of Thailand under which creditors and debtors are provided a schedule and a set of steps for achieving agreement on debt restructuring. The scheme is supported by some relevant tax incentives and is meant to be both a substitute for (in the sense of being invoked earlier) and complementary to (in the sense that it does not replace them if they become necessary) formal bankruptcy and foreclosure procedures.
11 Relatively stable foreign prices and the depreciation of the baht have protected farmers from many of the worst effects of the crisis. Anticipated drought conditions in 1998, falling world agricultural prices in response to the regional recession, together with the recovery of the baht would shatter this safety net and could create considerable political and social unrest in rural areas. Many of these rural areas are the stronghold of old-style opposition parties. The longer is the delay in economic recovery, therefore, the greater is the threat to overall social and political stability.
12 See Tinakorn and Sussankarn (1996).
13 For an early review of these challenges to Thailand's competitiveness see Akrasanee, Dapice and Flatters (1991).

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