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The State of the Nation 1981

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* The team wishes to thank Business in Thailand Magazine for allowing the report to be published for academic purpose. It is hoped that students and interested persons will find the report useful.

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I. An Overview Prospects for 1982: Fighting previous wars?

The year 1981 was rich in crises, events and controversies on the economic scene. In the sections that follow, these are reviewed and analysed in detail. Our previous review (BIT September 1981) selected the inconsistencies in government policy as a major theme. That emphasis is continued here to some extent, and many additional examples are cited. It is also a logical prelude to our own perception of what may be the most significant trend or, at least, a possibility of change in economic policy.

On 5 January 1982 the local press reported that the economic ministers agreed that a drive to export will be the top policy of the Commerce Ministry this year. Furthermore they directed that " all measures and regulations which obstruct smooth exports will be rectified." Ordinarily we might interpret this as a pleasing generalization without much real content. But against the background of some recent events, there may be good reason to be more hopeful.

As explained below , early in December of 1981 the export trade in rice and maize was freed considerably by the removal or lessening of certain restrictions. A few days later a stern warning about the likely damage to the rice and maize trade was issued by the Commerce Ministry. Subsequently that Ministry and the Rice Policy Committee ordered exporters to set up stocks of 500,000 tons of rice and also instituted detailed reporting requirements. There is the obvious inference that the freeing of the export trade can hardly have been a unanimous decision. Further, there can be speculation about possible underlying political rhythms. But what about the consequences so far? A week after the freeing of the maize trade, it was reported that local feed mills were buying heavily in the expectation of price rises because of additional export demand. The following day, the Commerce Minister announced that both maize and rice prices had increased significantly. One day later, the Marketing Organization for Farmers reported that the local price for maize was 25 % above that for November. In addition, it was noted that the MOF was having trouble buying maize at that price because farmers could do better elsewhere. Two weeks after freeing the maize trade, the Agricultural Co-operatives Federation president reported that more ships were coming to take delivery on maize. At about the same time, a spodesman for the Rice Exporters' Association said that the paddy price up-country had increased by 200-250 baht per ton depending upon quality.

There is another, earlier, and even more conclusive example as well. On 28 July 1981, export taxes on rubber were reduced by two baht per kilo. Dr. Trent Bertrand of Thammasat University is carrying out a research project on the impact of this change. By comparing local rubber prices in Thailand and Malaysia he can isolate the effects of the tax change from the effect of the declines in prices due to world demand conditions. During the first five months of 1981, the local Haad Yai rubber price was, on average .924 baht per kilo below the Malaysian price. In the three - month period immediately after the tax change, the Thailand local price was on average 1.03 baht above the Malaysian price. Malaysian export taxes were 1.06 baht lower than Thai taxes in the first period and 0.85 baht higher than Thai taxes in the second period. This increase in the Thai local price relative to the corresponding Malaysian price gives strong support to the conclusion that reducing export taxes is an effective way to increase farm income and that marketing channels in Thailand, where not hampered by government policy, are highly competitive.

So there were, in the year 1981, three highly instructive examples of what certain types of export restrictions can do, and what is likely to happen if they are eased or removed. And no one should think that the existing policies have small or negligible effects. Estimating them is a complex problem. But to refer to Professor Bertrand's work again, he has used three different assumptions about the elasticity of world demand for Thai rice. These procedures yield estimates of a real income transfer from rice farmers ranging from 8000 to 14,000 million baht. The corresponding subsidy to non-farm consumers ranges from 5000 to 9000 million baht. These numbers are far from insignificant. Certainly they should cause us to hope that the policy to remove restrictions to exports will indeed be carried out firmly .

Not entirely separate from the export issue is a second major question or theme in this review. Almost everyone expected a higher inflation rate for 1981 than was the case. A detailed, though tentative, explanation of this appears below. But a possible summary judgment is that almost all of the forecasters had a rather near-sighted "Bangkok bias". Thailand is still an agricultural we should repeat to ourselves. Good weather, good crops and healthy agriculture have proven that they can provide some shelter from internationally transmitted inflation, at least when accompanied by fiscal and monetary measures of the right type. If this judgment has validity, it strongly implies a much greater effort to maintain and improve the health of Thai agriculture.

There is an old saying among historians that military leaders are always "preparing to fight the previous war". This review appears to reveal an analogy in Thailand's agricultural policy. Regulations, broadly speaking, are based on assumptions of a sellers' market; in particular a world of food shortages where Thailand should guard a precious granary. Yet the evidence accumulates that the next year may be quite different. In a world where only a small fraction of rice production is traded on world market, the predictions of a huge crop next season should be persuasive that new strategies and tactics should be planned and carried out. Similar signals on the vast numbers of new entrants to the labour force and indications of layoffs and reduced demands for both farm and non-farm labour also imply a policy mobilization to anticipate unemployment problems before they become crises.

There is real cause for optimism in some respects as pointed out in the review. Thailand's growth rate was much better than respectable during this past year. The materialization of domestic sources of fossil fuels, despite some smags, can bring about tremendous gains for the economy. But it is not like a goose that lays golden eggs. The resource availability requires management of a high order (just remember Indonesia's problems). Proper utilization requires a great deal of investment. The Eastern Seaboard will not become a metropolis overnight. The 'gift' of gas and oil should not be considered to be the same as a winning lottery ticket. A correct perspective is that it will release resources for other, high priority uses. It is fair to ask, and keep asking, whether the priorities are "ritht".

Under the heading of priorities comes the Fifth Plan. Like every plan, it must promise something for everyone. But for the government to command resources, it has to collect them. And the discussion below suggests that the revenue aims of the Plan may be optimistic. A major achievement, that we may hope receives sufficient resources for implementation, is the target of a large number of the poorest rural areas for intensive development efforts. The high-level interest and the impressive reorganization of the bureaucracy indicate a very strong beginning. But even resources, in the absence of patient, strong and competent management will not be enough.

"Adjustment of the baht" had just occurred at the time of the mid-year review. Now we can look calmly at the event. With perspective , as shown in the review on money and finance, we should give high marks to those who made hard decisions on these issues during 1981 . A crisis was weathered, confidence is returning and rational steps have been taken to guard against similar dangers in the future.

On the whole, this review is critical but hopeful. The economy is much better off at the end of the year than at the beginning. Once again, the Thai farmer, despite hindrances, has performed nobly. But the signs are that the farmer's task will be harder in 1982 than ever before. So we should hope that the experiments of 1981, with results that are quite clear, will be extended and efforts made to support, rather than hinder the farmer's efforts to get his goods to the markets of the world.

II. MONEY AND FINANCE: The dust settles

Implications of the first half-year

Financial adversities abounded during the first half of 1981. The unsettling external conditions kept the domestic financial market under constant pressure. The restrictive monetary policy has gained unanimous support worldwide. Interest rates of the world's strongest currencies went up to record heights. As before the beggar-thy-neighbour policy was espoused with the only difference that interest rates were used as the mode of operation rather than the exchange rate. The urge was to maintain the strength of the currency in order to curb imported inflation. The balance of payments was more or less left to itself, naturally with the expectation that the contracted domestic demand would prevent its deterioration. In case this is not so, some protectionist measures could always be relied on to do the trick.

With the emphasis on money supply and interest rate, the movements in the exchange rate were allowed to be relatively freer than in the past. This was reflected in the more violent gyrations in the exchange rates between important currencies in the first half of 1981 than in the preceding year. Taken over the whole year the discrepancies were mitigated due to the more tranquil financial conditions and the upward adjustment in other currentcies in the second half of 1981, These two factors of persistently high overseas interest rates and the exchange rate gyrations had contributed to the exposing of a basic weakness in the Thai financial system, ie, its over-reliance on the overseas financial markets. The commercial banks, particularly the branches of foreign banks and the larger Thai banks, have traditionally been increasing their foreign liabilities over the past few years. Only in 1980 did this pattern begin to switch to a lower degree of reliance by the banking sector and a greater degree of reliance by the non-bank private sector. Under the trying circumstances of the first half of 1981, both commercial banks and private corporations had to shift their foreign borrowings to a lower gear all of a sudden. The resulting tight liquidity condition was more or less because of these circumstances rather than an explicit monetary belt-tightening policy.

The liquidity squeeze was aggravated by the record balance of payments deficit of more than five billion baht for the first half-year compared with a surplus of 14.5 billion baht during the same period last year. The major differences between those two periods lie in the speed of export growth and the deterioration of the capital account balance. The total baht downward adjustment of around 2% during the period January-May turned out to be inadequate to improve the payments imbalance. This adjustment moved the baht a little back into line with the basket-of-currency index but fell far short of restoring the pre-1981 alignment due to the ascending US dollar. After this adjustment, doubts lingered on in the domestic foreign exchange market as to its adequacy. Most of the commercial banks saw the May baht dollar adjustment as a warning signal and moved to square their foreign exchange position.

Such actions dit not help to ease the domestic liquidity position, considering that banks in Thailand normally maintained an oversold foreign exchange position. Reducing this short open position implies a drain on the domestic liquidity. During the first half of the year, claims on the available funds therefore piled up from all sides. The private corporations were obliged to revert to domestic sources due to excessive interest rates abroad. Commercial banks had to take precautionary measures and make the effort to square their foreign exchange positions. The public sector saw its financial gap widen and had to step up its domestic borrowing programme, also in view of the increasing interest burden from its overseas borrowings.

It was therefore rather fortunate that the mobilisation of domestic savings through commercial banks expanded at a rate which was only slightly below that of last year's . The expansion of domestic private borrowings, however, more than doubled the rate of last year, while government borrowings maintained the same hot pace. Still, the growth in money supply was not as fast as last year's due to the net decrease in the foreign asset position due to the payments deficit. From these evidences, it can be derived that the constraint on the money supply growth was not explicitly forthcoming from the domestic contraction of credit demand due to an overt credit-tightening policy. On the whole, the tight money situation as exogeneously created came in handy through its restraining effect on inflationary pressure and trade deficit. There was therefore really no haste in supplementing the domestic money market with additional liquidity.

Easing tendency in the second half-year

In the second half of 1981, there was a more explicit monetary policy towards the easing up of the liquidity squeeze that threatened to be choking the economy. In July the situation worsened as overseas interest rates were still stuck at the lofty level with no sign of sliding. However, the measures to increase domestic liquidity could not be carried out too soon lest they might ultimately lead to the drain of foreign exchange, defeating the original intention of the measures. In other words, the easing process had to be implemented in steps, firstly by limiting the distortions created by external circumstances, and then by introducing measures to induce liquidity expansion.

In the month of July (on the 1st and the 15th) the interest rate structure was slightly adjusted. First the ceiling deposit and loan rates applied to commercial banks were raised by 1% to 14 and 19% respectively. Then two weeks thereafter a similar measure was announced for finance companies, making their ceiling loan rate equal to 21% per annum. These measures should be seen in the light of the necessity to keep lending rates in line with foreign interest rates so that more inflow of funds could be induced, and net outflow prevented. Of course, this measure made credits dearer but at the same time enhanced the possibility of obtaining them. The concomitant rise in the deposit rate was supposed to be a boost to the savings mobilization effort since the pace of deposit growth seemed to have slackened. At any rate the simultaneous increase in both deposit and loan rates helped to prevent an criticism of dearer credit as the old spread was maintained while savers for the first time in the last few years were able to earn a positive real interest rate on their saving. This, however, was not enough to prevent the deposit growth rate in the second half year from slackening further (see table).

Also in the month of July (on the 15th) another adjustment in the baht-dollar exchange rate was put through. The baht value was adjusted downward by 8.7% against the US dollar, making the central exchange rate 23 baht to one dollar. Apparently the May adjustment of the baht value was to small to be effective. During the two weeks preceding the second baht adjustment the Exchange Equalisation Fund (EEF) had to intervene heavily in the foreign exchange market, selling something like \$ 250 million in the process. The speculative mood was rife as the market was keenly aware of the substantial payments imbalance and the exceptionally strong US dollar to which the baht is closely tied. Importers adopted the inclination to lead their payments while exporters tried to lag the sale of their foreign exchange receipts, expecting more baht in the future for their proceeds. This lead-and-lag pattern worked in full force to aggravate the already deteriorating foreign exchange market condition. The premium rates for the forward purchase of US dollars were kept at a high level averaging close to 8% per annum, compared with the normal premium of 2%.

The July baht adjustment should therefore be seen in the light of this speculative drift and the distortions in the foreign exchange market. The drain on the country's international reserves was not a spectre but a real prospect that had to be averted. The baht adjustment brought a certain relief in that currency speculation subsequently ground to a half. The wave of selling foreign exchange by the EEF became more evenly balanced with alternate buying spree. The correction in the exchange rate distortions brought about by the baht adjustment helped to lend support to the exporters. If anything, as a consequence of the exchange rate adjustment, exporters were taxed less while importers were subsidised less than before. The payments deficit in the second half-year contracted to around 500 million US dollar compared with \$5000 million for the first half-year.

It is undeniable that exchange rate adjustments also carry with them various negative side effects. The inflationary impact is one, and the most feared. In the case of Thailand this impact was rather limited due to the inability of importers to pass on the increasing cost to the public as the demand was already very slack and some of the importers who had used other currencies than the US dollar had already handsomely profited from the depreciation in these currencies.

Following up on these corrective measures were others aimed directly at the easing of the liquidity condition.

The exemption of the withholding tax on the interest payable on foreign borrowings was expended to include all foreign loans. The regulation in use from October 1980 to September 1981 stipulated that only foreign loans with maturity of one year and longer were eligible for with/holding tax exemption. This regulation was repealed in August 1981 and took effect until the end of the year.

The swap arrangement was introduced in September to cultivate confidence in the baht currency. This arrangement enables the borrowers of foreign funds to draw on forward cover with the EEF by entering into a swap agreement, i.e. the sales of foreing funds against the Thai currency with a contract to repurchase at a set exchange rate. The swap facility, available until the end of the year, offered a cover of up to three-month maturity at the premium rate of 4 satang for this period which is equivalent to the spread between the buying (22.98 baht) and selling rate (23.02 baht) of US dollar by the EEF. The introduction of this swap facility was timed to coincide with the fall in interest rates abroad which gave the additional incentive to overseas borrowings. From the preceeding tables, it is clear that private corporations could more easily tap funds from abroad and reduced the demand for domestic credit in the second half of the year. The swap arrangement, however, is most effective when used temporarily for a short period to tide the economy over a crisis of confidence. When overextended, it creates distortion in the market and encourages excessive inflow of short-term funds that may be most volatile. The decision to terminate this swap facility by the end of 1981 could be justified because of these reasons.*

As usual, rediscount facilities are instrumental in regulating the liquidity condition besides bearing on the direction of bank credits. During the second half-year the following measures in this regard were introduced.

In August, the rediscountfacility based on the trade in agricultural commodities was announced to coincide with the start

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* After this was written, the facility was extended with the current year.

of the new marketing season for crops. This facility, carrying the credit line of 5,000 million baht, aims at providing concessional funds to be used in purchasing agricultural products early in the season to prevent the price downslide. Originally this facility required commercial banks to charge 17.5 per cent interest rate while 80 per cent of the purchased commodities could be rediscounted at the rate of 15 per cent at the Bank of Thailand. When the glut of agricultural commodities threatened to be a severe problem, the Bank of Thailand softened these conditions by reducing the rediscount rate to 12.5 per cent and the interest rate chargeable by commercial banks to 15 per cent p.a. and by increasing the rediscountable proportion of purchased commodities to 90 per cent of the total price.

Since December 1980, the Bank of Thailand has been providing a credit line to finance the stockpiling of paddy in the price-support scheme. The rediscount volume is based on the size of promissory notes issued in this connection by the Public Warehouse Organization and covered 25 per cent of face value of these notes. In order to provide more liquidity to this undertaking, the Bank of Thailand in September 1981 raised the rediscountable proportion to 30 per cent.

To help make agricultural exports more competitive abroad, the Bank of Thailand in December extended the maturity of export credit from 180 days to one year. This should enable Thai exporters to offer more attractive terms to their customers abroad. Although this measure does not have direct bearing on the volume of liquidity, it may indirectly boost export earnings which ultimately contribute to the increasing availabilitty of domestic liquidity.

Concomitant with the cautious short-run counter-cyclical measures, the monetary authorities implemented a few notable policies to improve the financial structure of the country.

As a primary step towards the development of an efficient domestic money market, the repurchase market was reactivated in August after the Central Bank put a limit to the commercial banks' borrowing through the secondtier loan window. The second-tier credit line was confined to one per cent of banks' deposits similar to the first tier quota. This switch in the Central Bank's loan window policy necessitated some difficult adjustments in the commercial banks' liquidity management practice,being used as they were to the unlimited credit line through this loan window. But since the repurchase market was at the same time extended to cater for banks' need to sell government bonds even after the close of the afternoon session, banks' liquidity management could more expediently shift its focus to the repurchase market. Finance companies had already been allowed access into the market on both the buying and selling sides since June 1981.

As a precautionary measure to prevent the deterioration in the international reserves, the Bank of Thailand has begun to line up credit sources from abroad to be used in time of need. The borrowings by the Central Bank facilitates the management of Thailand's external debt in that the volatile short-run borrowings by the private sector can be more or less replaced by more stable sources of funds. Three major types of loans have contracted by the Central Bank in 1981:

- The International Monetary Fund (IMF) has granted Thailand a loan of $212 million through the Compensatory Financing Facility which charges 6.52% interest for five years. This CFF loan is normally granted to countries with substantial shortfall in their export earnings. The loan is attractive for its very low interest rate without any conditions attached.

- The Bank of Thailand concluded a Stand-by Arrangement with the IMF in June this year. The stand-by credit line amounts to $945 million and can be drawn down partially at intervals. The interest rate structure attached to this arrangement has two tiers, namely a concessional one of 6% on one-third of the credit used, and a market rate on two-thirds of the utilised line. The conditionality tied to this Stand-by Arrangement was more lenient for Thailand in view of its moderate external indebtedness, past record of monetary stability, and present adherence to strict monetary discipline.

- In March 1980 for the very first time the Bank of Thailand made a foray into the international money market as a borrower of a syndicated loan worth \$200 million. This loan, with the interest rate of 3/4 over Libor, has a draw-down period of two years. Although this period is terminating in March 1982, the Central Bank has not made any draw-down in view of the adequacy of the international reserves. However, since the period of monetary uncertainty has not yet ended, it was deemed prudent to maintain the access to this source of finance. As the lending terms have begun to soften with the growing liquidity volume in the international market, the Bank of Thailand therefore decided to benefit from the occasion to replace the old syndicated loan with a new one with more favourable terms. This refinancing effort concluded with a standby revolving credit facility worth \$300 million while originally only 200 million was required. There was an oversubscription of an other 100 million, arranged by some of the world's larges banks such as Bank of America, Bank of Tokyo, Manufacturers Hanover etc. The interest spread over Libor was reduced from 3/4 to $\frac{1}{2}$ while the commitment fee dropped from 3/8 of the old loan to $\frac{1}{4}$. This revolving credit arrangement very much suits the Central Bank's need in that the draw-down may not take place until it is really necessary. The utilised part may then be repaid when no more is needed and may be redrawn whenever the need arises.

So in spite of the initial turbulence witnessed in the first half of the year, the second half-year saw improved overall monetary conditions. The blend of the monetary policies in the whole of 1981 was one of parrying immediate external disturbances, providing for a gradual relief from the domestic liquidity crunch, and carrying on with structural adjustment aimed at strengthening of the domestic money market an greater autonomy in monetary management. The number of casualties was therefore rather limited in the field of finance this year, while a firm ground was laid for greater monetary stability in 1982 . The most outstanding case of financial mismanagement this year turned out to be that of the Government Housing Bank. But this was more due to the GHB's own doing rather than the result of the generally difficult monetary conditions. The Bank of Thailand, through not directly responsible for the management of the GHB, had to chip in one billion baht to enable the GHB to continue its activities. Throughout this difficult and confusing year in the monetary respect, a clearcut theme emerged. Although the fine-tuning policy may have been discarded as too interventionist,it has proved to be hightly valuable in a year that most monetary instruments were stretched to the utmost. In addition it can be concluded that an instructive lesson can be learnt from the experiences of 1981. With sound financial practices, a financial institution can sail through the most turbulent periods in one piece. But with imprudent management, one can sink even in still water.

Who pays better ?

Interest rates (one-month maturity) of some selected Euro-currencies(1977-1981)

(per cent)

Currency	December 1978	December 1979	December 1980	1981 June	1981 November
Euro-dollar	11.00	14.37	19.12	18.12	11.62
Euro-mark	3.19	8.50	8.87	12.25	10.56
Euro-yen	-0.69	7.62	9.12	7.00	7.37
Euro-sterling	12.00	16.75	14.75	11.81	15.19
Euro-franc	10.50	13.37	11.12	26.00	16.00

Who's gaining ?

US dollar exchange rates with selected currencies

Currency	Percentage change		
	Between Jan'80-Dec'80	Between Jan'81-June'81	Between Jan'81-Dec'81
Deutsche Mark	- 13	- 18	- 12
Japanese Yen	+ 17	- 11	- 8
Pound Sterling	+ 6	- 31	- 20
French Franc	- 11	- 20	- 20
Swiss Franc	- 12	- 13	0

Note: (1) Minus sign implies a depreciation against US dollar.

Net annual inflow of foreign borrowings by commercial banks and non - bank private sector (1979-1980)

(in million dollars)

	Commercial bank(1)	Non-bank private sector
1979	+ 423	+ 490
1980	- 445	+ 1,000
1981 - first half	+ 152	+ 150
- second half	+ 190	+ 650
- total	+ 342	+ 800

Note: (1) Changes in banks'total foreign liabilities

Annual rate of increase of bank deposits, bank advances, private and public borrowings, and money supply.

(per cent)

	End 1980	June 1981	End 1981
Bank deposits	23.8	21.6	18.4
Advances by banks	12.2	26.7	19.6
Private borrowings	12.2	26.7	18.5
Public borrowings	35.4	32.5	16.4
M_1	13.8	8.8	2.9
M_2	22.4	19.9	15.4

Source : Bank of Thailand

Note : M_1 denotes money supply as narrowly defined while
M_2 denotes money supply as more widely defined

The lofty level overseas

Domestic and overseas interest rates (July- December 1981)

(per cent)

	Domestic Prime				Overseas rates		
	Gov't (1) bond	Interbank	Prime	Repurchase (2)	US Discount	US Prime	Euro (3) dollar
July	13.25	18.5-19.0	18.0	17.625-18.625	14.0	20.0-20.5	17 3/8-20 3/16
August	"	19.0	18.5	18.5	14.0	20.0-20.5	17 3/8-20 3/16
September	"	18.0-19.0	18.5	16.5-18.5	14.0	19.0-20.5	14 15/16-15 5/16
October	"	17.0-19.0	18.0-18.5	14.5-18.0	14.0	17.5-19.5	14 15/16-17
November	"	14.5-19.0	17.5-18.0	12.5-14.5	13.0	15.75-17.5	11 3/4-14 13/16
December	"	14.5	17.0	11.75-12.5	12.0-13.0	15.5-15.75	12 1/16-13 7/8

Notes: Rates are given in ranges.

(1) Medium - term government bond with 5-year maturity. Interest rate was raised from 12.25 to 13.25 % p.a. beginning July.
(2) Seven-day maturity
(3) One-month LIBOR

III. TRADE AND PAYMENTS BALANCES

Some self-inflicted

In a comparative study of 85 non-communist nations, publish, in the October 1981 issue of Euromoney, Thailand was ranked eighth in overall economic performance for the period between 1974 and 1981, surpassing such countries as Japan, Korea, the US, West Germany, and the UK. But in comparing balance of payments situations alone, the ranking for Thailand fell to 68 th, despite two years of payments surplus during the period under review. Reflecting such a poor performance was mainly the inability of the country to reduce the growing trade deficit, which had increased by fourfold from 14,302 million baht in 1974 to 57,985 million baht in 1980.

For 1981, the unfavourable development of the world economy had caused a further deterioration in the trade deficit. This included the economic recession in industrialized countries, the worldwide inflation, the fluctuating and high level of interest rates, and the depreciation of European currencies. While the recession and the high level of interest rates contributed to low demand for Thai exports (the latter worked to limit the demand for inventory stock accumulation), the depreciation of major foreign currencies in which Thai trade was denominated caused a fall in net export earnings, and the world inflation led to a high cost of imports. There had been internal attempts at improving the trade account through trade and exchange rate policy. But, in general, there were retardations in the exercise of appropriate trade policy to curb the effect of falling world price and demand. And this was at the expense of lower export earnings than otherwise might have been the case.

Large trade deficit

The preliminary estimates showed that the trade deficit for the first three quarters of 1981 stood at 48,916 million baht, which represented an increase of 16% over 1980 in the same period. The deficit was expected to reach 65,000 million baht by the end of the year. Much of the worsening in the trade balance was the result of slow growth of exports. For the first nine months, the merchandise exports were valued at 113,244 million baht, as against 98,922 million baht for the corresponding period of last year, or an increase of a mere 14.5 % . In the past two years, the export earnings registered an increase of over 20% per year.

The world recession has dealt a blow to the Thai raw material and manufacturing exports. Early estimates showed, for instance, that textile exports, the largest manufacturing export of the country, commanded an earning of 7,023 million baht during January to August of 1981, an increase of only 8.31% over 6,484 million baht earnings in the same period last year. With the inflation rate being two digits, this reflected a fall in real export receipts. There had been attempts during the year to stimulate textile exports through cost reduction, but these met with little success as fierce competition existed in the world market and import quotas especially to EEC countries were observed. These quotas were the classic response to threats to their own textile industries which arose because of the recession.

Rubber exports were also affected by the world recession, which hit hard at the car industries, especially in the western countries. About half of the natural rubber was used in the automobile tire manufacture. Thus, the demand for rubber was declining, bringing down the price at the same time. To protect their car industires, the US and the European countries had imposed import restrictions on Japanese cars. As Japan had been the largest buyer of their rubber, constituting over two third of the Thai rubber export market, the rubber export, then, suffered a fall in both price and quantity. The price had plunged from 27,028 baht in January to an all time low of 19,941 baht per metric ton in September . For the first three quarters, the quantity exported totalled 344,741 metric tons, in contrast to 357,616 metric tons for the same period last year. This represented a decline of 3.6% in volume. As a consequence, the export earnings from natural rubber fell by 14.3% ie, from 9,684 million baht in 1980 to 8,829 million baht in 1981, for the first nine month period.

To help boost rubber exports, and, at the same time, to prevent the price which rubber tappers got from going further downhill, the government in the middle of the year had reduced the export tariff on rubber by two baht per kilogramme on the average. The call for a change in the export tariff structure was, however, made by rubber planters at the beginning of the year, but was refused then by the government. The tariff structure used at that time had been in effect for a long time and was rather outdated. The duty was 1 % of export price above that figure. The reason for these odd rates was probably to bring all rubber prices received by exporters in line with one another. However, rubber prices had been above 5.98 baht for more than two decades. It was somewhat depressing to learn that during the time of falling world demand, the supply had been curbed by a high rate of export duty. By the time the measure to ease the situation was taken, it was well into the second half of the year. Its impact on the export earning would only be minimal.

The development of tin exports during 1981, with respect to the world demand and the domestic reaction, was almost indentical to that of rubber. The world economic slowdown coupled with the ample supply from the release of the buffer stock held by the US General Service Administration brought down the international price of tin, especially in the early part of the year. The request by tin-producing countries to the International Tin Council to raise its floor price whereby it could interfere with the market in order to stabilize the price, was not approved until the middle of October. All these led to a sharp decline in the Thai export price and volume of tin. The average export price for the first three quarters was only 282,364 baht per metric ton, as compared to 339,568 baht for the corresponding period of 1980 , or a fall of almost 17 %. There was a decline of 9% in the export quantity, ie, from 25,821 metric tons in three quarters in 1980 to 23,498 metric tons in 1981 of the same time period. Consequently, the earning from tin exports was reduced by 24%, that is, from 8,769 million baht received for a period of nine months in 1980 to 6,635 million baht in 1981.

Again, the domestic counteraction to the falling world price did not come until many tin mines had ceased operation due to operating losses. It was in late July when the government agreed to reduce the tin royalty up to 10 percentage points of the old rate. Although the royalty itself was not considered an export tax, its effect on exports was the same. Its reduction would have reduced export cost, leading to expansion of exports.

In the first half of the year, there were several factors contributing to a fall in the tapioca export price. The recession in EEC countries weakened the demand for meat consumption, which, in turn, led to a decline in the feed industry. As tapioca was used as animal feed, there was less demand for the product from t these countries, which normally absorbed some 85% of Thai exports. Meanwhile , the price of soybean cake, a complementary product to the tapioca mixed with the latter to make animal feed, was rising, giving way to further fall in demand for tapioca products. The feed industry has turned to use corn gluten as a substitute for feed. Moreover, as tapioca trade was quoted in deutsche marks which were depreciating at this time, the baht price of the export product was falling. During this period, the internal policy was not directed to ease the situation. On the contrary, export quotas were imposed at the start of the year. Exporters were also levied 10 baht per each ton of export for the purpose of establishing a cassava root price stabilization fund. They were, moreover, required to build up stocks. It was argued by the Commerce Ministry that these measures were necessary to smooth the trade flow to the EEC, to reduct monopoly in the trade especially by foreign trading firms, and to help in setting up drying facilities for cassava roots, which would be of benefit to the farmers. However, these objectives could have been more efficiently met by means other than those which would obstruct the export trade. Under pressure from farmers, the ministry agreed to suspend the measures for six months starting in July. As a consequence of freer trade in the second half of the year, tapioca was ranked the second largest foreign exchange earner, next to rice, in 1981, despite the fall in its export price. The latest report estimated that more than six million tons of tapioca products worth over 15,000 million baht were exported for the whole period of 1981 , as compared with 5.2 million tons valued at 14,887 million baht in 1980.

Maize exports had been stagnant for most of the year, in spite of good crop season which guaranteed plentiful supply. The trade was restrioced by the imposition of export quotas at the beginning of the year. It was the policy of the Foreign Trade Department to slow down the maize export for fear of a domestic shortage. Thus, foreign demand could not be adequately met by several exporters. As a result, those who were apportioned quotas were not interested in making their sale abroad but rather sold the right to export to others, for the quota itself was worth up to $20 per ton of maize. It is amazing that the government office can thus create opportunities for quick profit to businessmen. Turned away from Thai supplies, foreign buyers were directed to other sources of supply, especially from South Africa whose maize output had been on the rise.

There was improvement in the maize trade at the end of the second quarter as more export quotas were allotted. Unfortunately, the second part of the year saw a declining export price, attributable to an ample supply from a good crop in all major producing countries. Under the pressure of falling prices, maize trade was finally freed in December; and attempts were made to barter maize for chemical fertilizer from socialist countries. The latest estimates indicated that about 2.5 million tons of maize valued at about 8500 million baht were exported in 1981 , as against 2.2 million tons worth 7299 million baht of maize exports in 1980.

In contrast to maize, rice exports were relatively free in 1981, but were subjected to export premium and rice stock reserve requirement. All quotas were abolished before the start of the year. The strong demand from abroad coupled with a slack in world production in the last crop season led to rising export prices. For the first three quarters, rice exports amounted to 2.5 million tons, an increase of 12.3 % over the same period last year. The export value stood at 22,215 million baht, which represented an increase of 7,387 million baht or 50% over the same nine month period of last year.

In the last quarter, the world market for rice was weakening due to abundant world supplies made possible by favourable weather conditions. Rice prices started to fall. In a swift move to counteract the laggard price movement, the Commerce Ministry, at the end of October, reduced the export premium up to 300 baht per ton of rice and exporters' requirement to contribute to the Rice Stock Reserve. The latter was further reduced by another 50% in

December, as the world price continued to decline. With relatively free trade, rice export was able to maintain its position as the country's leading foreign exchange earners in 1981. It also registered a record high in terms of both earnings and volume.

Soaring Imports

The value of total merchandise imports for the first nine months of 1981 totalled 162,160 million baht; this amounted to an increase of 14.93 % over the same period last year. Consumer goods imports, which constituted about 10% of total imports, showed the highest increase of 30.73% to 17,195 million baht. Accounting for this was probably the high rate of domestic inflation relative to that abroad, and the decline in the value of major foreign currencies in the early part of the year. Raw materials imports showed an increase of 19.32% over the same nine month periods of last year. Most of the increase in the raw material imports belonged to the products used in manufacturing consumer goods. Intermediate products used to produce capital goods grew only at a rate of 10%.

Imports of capital goods amounted to 40,182 million baht in the first three quarters of 1981, an increase of 17.77% from the same period last year. Of this, an amount of 22,634 million baht was spent for machinery, or about 66% of total capital imports. The relatively slow growth of capital goods imports and imports of intermediate product used chiefly for capital goods was due to high rate of interest abroad.

Fuel and lubricants imports for the first nine months amounted to 48,815 million baht, an increase of 12.56% over the same period last year. Partly responsible for the increase in the oil import bill was the increase in the oil price before the year began. In December 1980, the price of Arabian light crude oil was raised from $30 to $32 a barrel. There was another price increase of $2 a barrel in October 1981. This would raise the oil import bill in the last quarter. Also affecting the expenditure on imported oil was the depreciation of the baht vis-a-vis the US currency of about 10%. After discounting the effect of depreciation and the price increase on the oil import, there appears to be no reduction in the volume of the domestic oil consumption, which signifies that the past government policy on the energy crisis has not been fruitful (except in changing the composition of demands as noted elsewhere in this review). In fact, there is no indication that the government has taken any tough stand to solve the crisis. It would rather hope that the natural gas which has been available since September and the fortunate discovery of oil deposits in the Northeast, would eventually replace part of the oil import. Although this new development would lessen the country's dependence on foreign energy, freeing resources for other useful purposes, the energy crisis will not abate, unless consumption is checked.

As noted earlier, much of the increase in import value was due to the increase in import price. In the first half of the year, the import price index had risen by 7 percentage points over that of the last quarter of 1980. Normally, the world inflation would have an effect of raising both import an export prices. But 1981 seems to be an exception; the price index of exports had fallen by 3 percentage points during the said period, for reasons already mentioned above. Although some export prices rose slightly in the third quarter most agricultrual exports suffered from a decline in their price in the second half of the year, as the world supply became abundant. Consequently, the terms of trade had been deteriorating throughout the year. For the period between the last quarter of 1980 and the first half of 1981 , the terms worsened by some 5 percentage points. The deterioration in the terms of trade had partially been responsible for the increasing trade deficit of the country.

Devaluation: a remedial measure

In an attempt to correct the alarming deficit in the midst of deteriorating export prices and the adverse export trade policy of government agencies, the Bank of Thailand stepped in to devalue the baht. Twice the baht was devalued against the US dollar, the first was on May 12 for 1.083%, and the second was on July 15 for another 8.7%. The devaluation was aimed, among other things, at boosting export earnings and restraining the growth of imports, as it would make Thai exports cheaper in terms of foreign currencies and imports more costly to the Thai. There appeared to be an improvement in the trade balance after the devaluation. However, the extent to which the currency adjustment affected the balance of trade is left for a more complicated analysis. It was nevertheless estimated by the Bank of Thailand at the time of the second devaluation that the 1981 trade deficit would be reduced by some 6,000 million baht. This seems to be an optimistic figure, as trade balance could very well be worsened right after the devaluation. If trade balance should improve, there must be either an increase in export earnings or a decrease in import expenditures or both. But whether export earnings will increase depends pretty much on the supply elasticity. If there is no stock piling up and if production season is over as in the case of agricultural products, there may not be an increase in the export earnings. On the other hand, as most of Thai imports are in the form of raw materials and capital goods, which are relatively price inelastic, devaluation would lead only to an increase in baht price with little impact on the quantity imported. Thus, the import expenditure would rise rather than decline. The positive effect of devaluation may not, therefore, be realized after a very short period lag.

Capital movement

In the past, most of the trade deficit was financed by net inflows of capital, large enough to make possible a surplus in the overall payments balance in several years. However, this was not quite feasible in 1981, especially in the early part, as foreign rates of interest had been fluctuating widely and remained very high relative to the domestic rates. The devaluation of the baht did play a big role to ease the situation. It implies that a unit of foreign currency could be converted into more baht than before. The thrid quarter of 1981 saw a net capital inflow by more than the inflow of the first two quarters combined. The total capital inflow for the third quarter was 14,589 million baht while the first and the second quarters amounted to 7,834 and 6,751 million baht respectively.

Of the total capital movement in the first nine months, less than 20% was in the form of direct foreign investment, over half of which took place in the third quarter. In spite of the devaluation, the short term capital movement registered a net outflow of 721 million baht for the first three quarters. For the third quarter alone, the short-term net outflow was 862 million baht . This probably reflected the hesitation on the part of businessmen, commercial bankers included, to bring in short term foreign funds for fear of another devaluation before the debt was repaid-since this would increase their baht liabilities. To assure the convertability of debt into foreign currency without incurring any exchange risk, the Bank of Thailand introduced an exchange swap system in September. Under the system, those who brought in foreign funds, after having surrendered them to the Bank, would be guaranteed to have it converted back into foreign currency before March 1982 at the rate when it was brought in less a certain discount. With this assurance it was reported that the short-term fund started to flow in.

As more and more of past trade deficit was financed by the external borrowing, the external debt has been growing at an alarming rate. On the average between 1974-1980, the debt had been growing at 31.3% per year, with the last two years being over 45% a year. At the end of 1980, the amount disbursed and outstanding external debt was $5918 million. This large amount of debt could imply a great burden to the economy.

Debt burden

It is necessary to distinguish between two different kinds of external debt burden: the financial burden and the economic burden. The first reflects the need to acquire sufficient foreign exchange to make debt service payments. As foreign exchange can only be obtained, without going further into debt, through earnings from exports, the fluctuation of export receipts and the ratio of debt service to export earnings may, therefore, provide some indication of the degree of financial burden. This is because a fluctuating export receipt leads to the difficulty in meeting the debt service obligation, and the high debt service ratio indicates that a large proportion of export earnings must be devoted to debt service.

As seen above, Thai exports have been at the mercy, not only of weather conditions, local and worldwide, but also of the external demand conditions. Their rate of growth in the recent past ranges from 9.5% in 1975 to 36.3% in 1976. Thus, in the years where earning is relatively low, such as currently experienced, the financial burden would spell a hard time for the economy. On the other hand, the external debt service has been rising much faster than exports, resulting in an increasing debt service ratio ie, from 8.3 in 1974 to 15.5 in 1980. If the ratio is allowed to rise much further, more foreign exchange earning will have to be used to finance past debt, forcing down import, output and consumption.

The economic burden is something else and should be under close watch. It is the reduction of goods and services available for domestic use when the country has to make interest and amortization payments. If the inflow of resources from external debt is not contributing to the growth of output at a rate higher than the outflow of resources to meet the debt service obligation, there will be an increasing economic burden to the economy and further foreign borrowing will be necessary.

As a rough measure, GDP growth rate can be taken as an indication of the average return to foreign borrowing. This can then be compared with the rate of growth of the external debt. For Thailand, the growth rate of foreign debt has outpassed that of output so that the debt/GDP ratio has been rising, eg, from 8.72 in 1974 to 18.12 in 1980. This might reflect that borrowing has been used to finance consumption or projects with low rate of return. Thus, the increasing debt is generating a larger degree of economic burden to the economy.

Although the country was able to attract foreign capital through monetary measures and exchange rate adjustment the inflow was not sufficient to finance the current account deficit. The balance of payments for the first three quarters was in the red by an amount of 6828 million baht. It was officially estimated that the payments deficit reached 8000 million baht for the whole year period. This was one of the largest deficits suffered in the past two decades and was in contrast to a surplus of 5000 million baht enjoyed last year.*

The current deficit was partially financed by the use of the country's international reserves This can be seen in the decline

* After this was written the results of the fourth quarter were issued, showing a dramatic improvement in the balance of payments.

of official holding of foreign exchange, which fell from $2,004 million in September 1980 to $1372 million in September 1981. Normally, the deficit in the past was financed by some other sources. The use of official reserves as a last resource is not only costly, especially when the rate of interest abroad is very high, but also limited to its availability. At the end of September, the official foreign reserves stood at only $2885 million of approximately equivalent to 3.7 months of current imports. There is, therefore, an urgent need to find a suitable course of action to correct the deficit situation as the use of official reserves to finance the deficit must not be any longer relied upon.

Measures to curb the deficits

Considering the limitation on the ability to finance deficits, the most logical choice is to curb the deficit. One way of doing this is through a reduction in imports. This seems at first to be feasible as the import-GDP ratio has been rising since 1976. Currently the ratio of goods and services import to GDP is almost one third, being 31.12 in 1980 as against 23.51 in 1976. This indicates that imports have been rising at a rate faster than income. However, there is only a limited room for the reduction in imports without affecting the income generating capacity of the economy, and without creating severe inflationary pressure in the economy. This is because a bulk of imports is in the form of raw materials, intermediate goods and capital goods, while consumer goods constitute a little over 10% of total imports.

Another way of reducing the deficit is to increase exports. This is not a new discovery, as there have been indications that the country is moving into that direction. Credit must be given to the present and past administrations in their drive toward export expansion, which is not a simple task especially when the world economy is in a state of turmoil. However, when dealing with the question of how to promote exports, most discussions and action would center around comparative advantage, export incentives, the marketing ability and the like. This is quite relevant, particularly when the country wants to get its new product into the world market. But for the existing export commodities which are already in the world market and are commanding a large percentage share of the country's total export, the most sensible way to promote the export of these commodities would be to stop discouraging their exports. At the present time, there exists a host of export-discouraging measures which include export taxes, premium, stock reserve requirement, quotas, royalty, minimum export prices, fees and licenses. All of these undermine export growth. The lessons learned during 1981 in the area of rice, tapioca and maize exports points to the fact that a reduction of self-imposed export disincentives would lead to an increase in export earnings. It goes without saying, then, that if balance of payments objective is to be achieved, a high priority must be assigned to the reduction or elimination of domestic export disincentives. It is also necessary to come to a consensus, esprcially among authorities connected with foreign trade, about the inappropriateness of using trade restrictions as a means to achieve other objectives. A recent incident serves to illustrate the point.

Facing a decline in the international price of foodgrain, the economic ministers agreed in early December to reduce export restrictions on rice and maize. This involved an elimination of quotas for maize, a removal of minimum export price for rice and a 50 % reduction in rice stock reserve requirement. The move was quite appropriate and laudable as it would reduce the export cost and would thereby strengthen the comparative advantage on the export of these commodities in the world market. However, the measure was criticized by several parties, including, surprisingly, (or rather unsurprisingly but most unfortunately), the officials from the Ministry of Commerce. The charge was that the elimination of minimum export price control would make it easy to under-invoice the actual export price. The lowering of rice stock requirement would, they believed, lead the buyers to ask for lower sale price of existing sale contracts. It is very difficult, however, to imagine why attempts at curbing foreign exchange smuggling should be at the expense of a reduction in foreign trade. It is also difficult to justify the maintenance of current earnings at the expense of future gain. The dreadful thing is that the implementation of a sound policy may not be carried out by concerned officials, who are not in agreement with the policy, but would rather invoke other rules and regulations to a contradictory end.

One additional means to help solve the problem of payments deficit is to stop creating it to begin with. Given the existing structure of the foreign trade and exchange sale system, an excessive expansion of money stock would lead to a deficit in the balance of payments. The line of reasoning is quite intuitive. The excess of money supply over and above what the public desire to hold will be gotten rid of partially in the form of greater demand for imports and capital outflows, either for repayment of existing foreign debt or for acquiring foreign assets. This will put a pressure on the balance of payments. On the contrary, a shortage of domestic money supply in relation to its demand would stimulate the public to seek additional money they need by restraining their expenditure both at home and abroad, and by bringing in foreign money through loans. This would tend to increase the surplus in the balance of payments.

Examining the past behaviour of the growth rate of domestic credit, which is taken as an indicator of the growth of the domestic money, and the growth rate of the total money stock, there is a close relationship between the excess domestic money and the balance of payments behaviour. Save the years 1973 and 1979, where there was a large revaluation of official gold holding, the balance of payments showed a deficit whenever there was a high growth rate of money stock (see Table), and a surplus for the year when growth rate of money stock is higher than that of domestic credit. If adjustment should be made to de-emphasize the revaluation of gold, which artificially inflates the net foreign assets and thereby deflating the domestic credit, the above observation should also hold true for 1973 and 1979.

As the expansion of domestic credit is under the control of the Bank of Thailand, a trade-off must, therefore, be made between the balance of payments objective and other goals to be achieved. Would it be appropriate, for instance, to unnecessarily maintain an artificially high rate of economic growth by heating up the economy through budgetary deficits and monetary lubrication at the expense of the balance of payments objectives? If the equilibrium in the balance of payments is to be preserved, an excessive expansion of credit should be resisted and a lower achievement of other conflicting goals contended with.

Balance of payments

(million of baht)

	1979	1980	1981(Jan-Sept.)
Exports (fob)	106,881	132,040	113,244
Imports (cif)	153,934	190,025	162,160
Trade balance	-47,053	-57,985	-48,916
Net services	3,238	6,876	4,180
Trade and services balance	-43,815	-51,109	-44,736
Net transfers	1,224	4,276	2,699
Capital movement	33,767	49,959	29,174
Direct investment	(1,048)	(3,816)	(4,776)
Net long-term capital	(20,604)	(33,086)	(20,626)
Net short-term capital	(3,567)	(6,847)	(-721)
Government	(8,548)	(6,210)	(4,493)
SDR	493	506	488
Net errors and omissions	406	1,547	5,547
Balance of payments	-7,925	5,179	-6,828

Source : Bank of Thailand (P = preliminary)

Exports of major commodities

		1980	1981	percentage change
Rice	Quantity	2,229,002	2,502,454	12.27
	Price	6,652	8,872	33.37
	Value	14,828	22,215	49.82
Rubber	Quantity	357,616	344,741	-3.60
	Price	27,079	24,070	-11.11
	Value	9,684	8,298	-14.31
Tin	Quantity	25,821	23,498	-9.50
	Price	339,568	282,364	-16.85
	Value	8,768	6,635	-24.33
Maize	Quantity	1,388,040	1,471,772	6.03
	Price	3,204	3,377	5.40
	Value	4,448	4,970	11.74
Tapioca	Quantity	3,679,477	4,459,470	21.20
	Price	2,880	2,693	-6.49
	Value	10,597	12,008	13.32
Sugar	Quantity	440,127	845,050	92.00
	Price	6,541	9,133	39.63
	Value	2,879	7,718	168.08
Textiles*	Value	6,484	7,023	8.31

Source: Bank of Thailand and Foreign Trade Department

Note * denotes January-August

Quantity in metric ton

Price in baht/metric ton/value in million baht

Imports by economic classification, Jan-Sept

(value in million baht)

	1980	1981	Percentage change
Consumer goods	13,153 (9.43)	17,195 (10.65)	30.73
Intermediate products	34,398 (24,67)	41,042 (25.42)	19.32
Capital goods	34,119 (24,47)	40,182 (24.89)	17.77
Fuel and lubricants	43,366 (31.10)	48,815 (30.23)	12.56
Others	14,410 (10.33)	14,221 (8.81)	-1.31
Total	139,446 (100.00)	161,455 (100.00)	15.78

Source: Bank of Thailand

Figure in parenthesis is percentage of total

Import/export prices and terms of trade

1975 = 100

		Unit value of export	Unit value of import	Terms of trade
1979	Q 1	117.9	132.8	88.8
	Q 2	131.9	139.8	94.3
	Q 3	135.2	150.6	89.8
	Q 4	135.5	155.7	87.1
1980	Q 1	145.4	170.5	85.3
	Q 2	152.8	176.6	86.5
	Q 3	153.6	184.2	83.4
	Q 4	155.6	188.5	82.5
1981	Q 1	154.0	192.5	80.0
	Q 2	150.8	199.2	75.7

Source: Bank of Thailand

External debts and debt service obligations*

(in million dollars

End of period	Amount disbursed and outstanding						Debt service payments as percentage of exports**	Total debt as percentage of GDP
	Private		Public		Total			
	Amount	Growth rate	Amount	Growth rate	Amount	Growth rate		
1974	648.0	40.56	513.1	16.03	1,161.1	28.54	8.3	8.72
1975	736.2	13.61	609.9	18.86	1,346.1	15.93	12.6	9.19
1976	785.1	6.64	818.8	34.25	1,603.9	19.15	10.6	9.69
1977	879.8	12.06	1,141.5	39.41	2,021.3	26.02	10.8	10.49
1978	930.6	5.77	1,780.6	55.99	2,711.2	34.13	16.6	11.76
1979	1,234.4	33.61	2,707.6	52.06	3,951.0	45.73	14.6	14.51
1980	1,921.7	54.55	3,995.9	47.58	5,917.6	49.77	15.5	18.12

Source: Bank of Thailand * repayable in foreign currency ** goods and non-factor services

International reserves

(in million dollars)

End of period	1978	1979	1980	Sept 1981
Monetary authorities	2,557.3	3,129.0	3,054.9	2,884.9
Commercial banks'				
Net foreign exchange position	-1,263.4	-1,379.9	- 901.1	- 884.3
Net international reserves	1,293.9	1,749.1	2,153.8	2,006.6
Number of months of imports financed by official reserves	5.6	5.1	3.9	3.7

Source : Bank of Thailand

Growth rate of money supply and net domestic credit

(in percent)

	Growth rate of		Balance of payments situation
	Net domestic credit	Money stock (M2)	
1972	22.36	24.01	surplus
1973	29.23	23.02	surplus
1974	14.20	20.39	surplus
1975	23.82	15.21	deficit
1976	27.76	20.01	deficit
1977	31.14	20.01	deficit
1978	28.87	18.48	deficit
1979	12.85	14.76	deficit
1980	14.61	22.44	surplus
Sept. 1980-Sept. 1981	25.01	15.81	deficit

Source: Calculated from data from the Bank of Thailand

IV. PRODUCTION/COMMODITIES: Threatening prospects

In term of economic growth, the NESDB revised figures for growth rates in 1980 and 1981 are 5.8% and 7.8%. Compared with the mid-year estimated growth of 6.8%, the revised rate for 1981 shows that in aggregate production the economy did better than expected. As in the last years of high growth, this is due mainly to the strength of the agricultural sector which last year grew at 5.3%, compared with 1.9% in 1980. Crop production, which carries the biggest weight in agriculture, expanded very strognly last year because of favourable weather in most parts of the country.

Paddy production in the crop year 1981/82 went up from 15.5 million tons of the first crop to 15.8 million tons. The expansion rate in the second crop was even greater. It was estimated that the second paddy crop harvest would increase from 1.3 million tons in 1980 to about two million tons in 1981 because more available irrigation water enabled the farmers to enlarge their planted area from 2.4 million rai in 1980 to 3.6 million rai last year; an expansion rate of 48%.

In the first half of 1981 the higher export price of rice pushed up the wholesale price of rice and the farmgate price of paddy. For instance, the country-wide average price received by farmers for a ton of 100% paddy rose to 3466 baht in the first half of 1981, an 8% increase compared with 3200 baht in the same period of 1980, but still slightly lower than the guaranteed price of 3600 baht. However, all prices of rice and paddy reached their peak between June and August, and tumbled down afterwards. The latest figures indicate that last year, prices in October were even lower than those in January. Nevertheless, the average farmgate price of paddy last year was expected to be still higher than that in 1980 by about 400 baht a ton. Various reasons have been given for the falling prices:

Government policy which restricted or obstructed rice exports.

US and Japan began to release rice from their overflowing stock.

Some importing countries were reluctant to buy Thai rice in anticipation that export prices would change after the baht devaluation in May.

Indonesia reduced their rice import from Thailand because of its good rice crop,

Although the prices of rice and paddy picked up at the end of the year after the government adopted the "free-trade" policy, the problem of oversupply is still looming. The country's ending stock of paddy, which was estimated to increase from 1.5 million tons in 1981, will bulge to 2.6 million tons in 1982, as the second crop in 1982 is expected to be 2.2 million tons; an increase of 10% over last year.

The good rain last year also brought bumper crops for maize, cassava, sugar cane and several other upland crops. Maize production increased from 3.15 million tons in 1980 to 3.45 million tons last year, and is expected to increase further to 3.6 million tons this year. Because of lower export demand and the government's policy of export quotas, the wholesale price of maize has a downward trend for most part of last year. It went up slightly in May when the Department of Foreign Trade relaxed its quota policy, but slid down again until December. The stock of maize at the end of last year was estimated to be 200,000 tons more than twice the stock at the end of 1980.

A large surplus for sugar is also expected this year. After a big drop of cane production caused by a prolonged drought in 1979 , a crop of almost 20 million tons of sugar cane was harvested last year. The 1981/82 production of sugar cane, encouraged by a high minimum farmgate price of 650 baht per ton and good weather, is expected to increase to as much as 25 million tons. Good crops in most big sugar cane producing countries such as Brazil and the Philippines in 1981 have been depressing the world price of sugar since January last year. The decline in the world price prompted the government to lower the minimum cane price received by cane price received by cane growers to only 540 baht per ton, of which 30 baht is subsidized by the sugar export premium revenue collected in the past. A business tax on sugar export was reduced from 7.7% to 1.65% to encourage export of the growing sugar surplus. If prices do not pick up this year, the cane production next year will definitely be lower as the cane growers are expected to turn to other crops. The estimated production of sugar cane is about 23 million tons.

The same situation of excess supply has also been true for cassava. Production of cassava roots rose from 13.8 million tons in 1980 to 16.5 million tons in 1981. High prices in 1980 and favourable weather last year were said to be the main cause of the increase. The farmgate price of fresh roots and the wholesale prices of cassava products fell continuously in the first half of last year, due to lower demand by the EEC which is by far the biggest importer of Thai cassava products, the devaluation of the deutsche mark which made the import prices of cassava products more expensive, and the effort of the Ministry of Commerce to enforce the export quota set by the EEC. The farmgate price of fresh roots ranged from 0.35 to 0.68 baht per kilogramme during January and August of last year, lower than the government support price of 0.71 baht per kilogramme. The end-of-year stock of cassava was estimated to rise from 2.7 million tons in 1980 to 3.3 million tons in 1981 , but should fall considerably as production this year is expected to be rather low, about 14.5 millions tons, as farmers will switch to other, more lucrative activities.

An increase in rubber production last year to 540,000 tons followed a dip of 1980 output which was 480,000 tons. Despite a brief drought in the East and heavy rainfalls in June in the South , last year's production is still higher than in the past and the volume should continue its upward trend as the rubber replanting programme covers wider areas. Lower world demand for rubber due to recession in the automobile tire industry in most industrialized countries sent the export and wholesale prices of Thailand's natural rubber falling throughout 1981, except for slight increases in June and August. The average farm price of rubber fell from 16.88 baht a kilogramme in 1980 to 13.72 baht in 1981. And the 1981 stock doubled from 59,000 tons the year before to 118,000 tons. Rubber growers asked the government to begin to set the support price of rubber at the minimum of 15-16 baht a kilogramme, but the government could only respond by lowering the export tax rates on rubber products.

Oversupplies were also reported for pineapple and most other fruits, and their prices had predictably fallen in 1981. For instance, the factory-gate price of pineapple dropped continously from 1.05 baht per kilogramme in January to 0.75 baht per kilogramme in August.

In the midst of abundant supplies, kenaf and soybean seemed to be two exception last year. The planted area of kenaf was reduced by 24 %, and production fell by 5%, as the northeastern farmers turned to other cash crops in response to low prices in 1980 and several years before. For the same reasons, soybean production declined by 2 % last year. However, due to different market conditions, the price of soybeans improved while that of kenaf deteriorated.

In the meantime, the fishery industry continued its decline in production which began in 1980. For both 1980 and 1981, fish production dropped by 10% because of increasing costs in ocean fishing in which the most important cost is for diesel oil. Falling prices of fishmeal were also said to be responsible for the decline of the industry. The livestock industry, on the other hand, increased its production by 7% in 1981. Most of the increment came from the production of chicken.

The tin mining industry went through a recession in the first half of last year when tin prices fell drastically because of recessions in most industrialized countries and the release of tin from the US's strategic stockpile. A number of mines and dredgers stopped production to cut their losses. In July the government lowered the royalty rates on tin to alleviate the cost burden of tin miners. Since August the prices of tin have improved considerably as several countries started replenishing their stocks and the floor price for the world tin buffer stock was raised by 6.85 % in October. However, the 1981 average price of tin would still be lower than in 1980 ; the average price for the first three-quarters of 1981 was 44% lower than that in 1980. Tin production in the first nine months of last year 31,649 tons which was 1.6% lower than production in the same period of 1980. Production in the last quarter of 1981 was expected to go up because the cost and market conditions improved.

The general picture of industrial production looked better in 1981 than in 1980. The industrial sector grew at 8.4% last year; a significant improvement from 4.8% the year before, but still below the average growth rate of 9.1% during the last five years. However, the situation was not as rosy as expected at the beginning of 1981. Though the problem of energy prices and oil shortages subsided last year, the industry still had to face high and fluctuating interest rates and tight money. A more serious problem came from the demand side where both local and foreign was not at all buoyant. The real purchasing power of farmers for most industrial products remained low as prices óf agricultrual goods dropped. The economic recession in most industrialized countries not only reduced Thailand's export of such primary products as rubber and tin, but also slowed down their imports of some manufactured products from Thailand.

The textile industry, in which 30% of its production goes to foreign markets, suffered a significant set-back when the borders with Laos and Cambodia were closed last year. The border closure was said to have cost Thailand a loss in textiles export worth some billions of baht, although the figure cannot be confirmed since most border trade statistics were usually not officially recorded. The recession in the US and Europe also reduced their purchasing power for Thai textile products. The only textile product which managed to have a good export performance is garments whose exports increased by 40% last year. Textile production was expected to grow by about 5% which is quite low compared with its past performance.

Cement production capacity began to expand again last year, after six years of zero growth. The price control on cement products was finally lifted last February, and production increased from 470,000 tons in February to a peak of 610,000 tons in June.

It was expected that last year's production increased by 40%, and the output exceeded local demand by about 100,000 tons a month. The surplus had been growing since July not only because of higher production but also because local construction declined both in the private and government sectors. With the government approval, the cement industry again started exporting its product to neighbouring countries.

The construction industry experienced a slow growth of 6% last year, compared with 14% in 1980. Private investment in construction did not quite recover from a slump in 1980. High interest rates, tight money, and the economic slowdown in 1980 depressed the demand for housing and left a large number of houses and shophouses (approximately 300,000 units in Bangkok and large cities) unsold. Construction in the government sector, particularly in such public enterprises as the Egat, the PTT, and the Expressway and Rapid Transit Authority of Thailand (ERTAT), registered high growth, though the government budget for construction was reduced considerably. It was expected that the growth of construction activity would improve slightly to 6.3% this year, and while private construction would pick up, construction in the public sector would slow down due to budget cuts and the completion of PTT's and ERTAT's project.

The beverage industry suffered a decline in production since the excise tax on soft drinks was raised early last year. It was reported that about 4,000 workers in the industry were laid off . Consequently, the bottling industry was also adversely affected. The prospect of a lower excise tax rate raised an expectation that production in the two related industries will improve this year. Several industries faced the problem of stagnant demand in the country and abroad, and reacted by cutting production, firing workers and revising planned investment in the future. These industries include iron and steel, vehicle-assembling, paper, and integrated circuits.

The food-processing industry and other agro-industries, on the other hand, registered high increases in activity, obviously because of a large harvest of most agricultural products. Other industries with good prospects for high exports, despite the recession in the industrialized world, included garments, footwear, leather products, artificial flowers, spectacle lenses and watch parts. These industries seemed to expand their output at relatively high rates last year.

The review of last year's performance in both the agricultural and manufacturing sectors show that oversupplies and excess capacity are the key problem. It also proves, and it should be expected, that as a rather open economy, Thailand has been very much subject to the vagaries of world economic conditions. This year the world economy is expected to come out of the recession and Thailand's industrial sector should respond favourably to larger demand for Thai manufactured products in the world market. Unfortunately, the same cannot be said for Thailand's export crops, such as rice , sugar cane and cassava, of which huge stocks will pile up and domestic prices will keep falling unless more markets can be found abroad.

It is easy to blame the middlemen, the millers, the merchants, the government, unfair trade practices by our trading partners, etc for problems in the economy. But the fact is that the world economic stituation is changing more rapidly than before, and every nation, including Thailand, has to learn how to cope with changes if it wants to be part of the increasingly interdependent world. Adjustments have been and will be made in Thailand, as in other countries, for the economy to withstand energy price increases, changeable world trade patterns, and international monetary instability. With a loan from the World Bank, structural adjustments in some manufacturing industries in Thailand will start this year. Besides the rural poverty eradication programme, it is interesting to hear more about how agriculture will be restructured so that it can respond appropriately to the changing world market. These adjustments will take time and we cannot expect to see spectacular results this year.

<u>PRODUCTION/ENERGY:</u> <u>At a turning point</u>

After nearly eight years of suffering from sudden oil supply disruption and massive oil price increases which brought about large trade deficits, high inflation rates and slow economic growth, Thailand's energy situation in 1981 showed some new, encouraging signs. Natural gas from the Gulf of Thailand started flowing on time, to be used as a fuel in electricity generation;

new discoveries of oil and gas were made in some onshore concession areas; and the domestic demand for wil products softened in response to price hikes rather than to Opec's supply restrictions. The nation gradually turned its attention from the difficult question of how it could manage with increasingly expensive imported oil to the complicated question of how it will make the best use of its own new-found energy.Nevertheless, the old familiar debate as to how the retail prices of petroleum products should be set and how energy could be saved continues. And it will never fade away so long as Opec charge higher prices for its oil and oil continues to be the main source of energy in Thailand.

Diclining consumption and distorted prices

Oil consumption in the country was reduced by a few percentage points in 1980 when oil import supply was severely restricted by the Iranian crisis, and the price of Saudi light crude was doubled in 1979 and went up from \$ 26 per barrel in January 1980 to \$ 32 per barrel in December of that year. The percentage increases in Thailand's retail prices of every oil product in 1980 were above 40% ; the second largest increased of oil prices since the 1973/74 oil crisis. The impact of the price increases on oil consumption occurred in 1980 but could also be detected last year when it was reinforced by moderate price increases in January 1981. The local consupmtion of all liquid oil products in the first nine months of 1981 increased by only 1.5 % compared with the corresponding period of 1980, the lowest rate of increase in years of normal oil supply. The quarterly data also show that liquid oil consumption consistently declined throughout the first three quarters of last year. It is expected that the consumption would decline further in the last quarter as natural gas began to substitute for some fuel oil used by the Egat, and the 1981 oil consumption may possibly be lower than in the year before.

The use of electricity increased by only 4.8% in the first seven months of 1981, compared with the same period of 1980. This rate of increase in clearly below the average annual percentage increase of 14% in the past decade. Such a small increase can be attributed to two stiff increases in electricity tariff rates in January and April 1981, which left the rate for the first 35 units consumed by the residential sector unchanged but made the tariff structure more progressive for all electricity users.

There is clear evidence last year that the government's pricing of different oil products directly affected the pattern of oil consumption. The government has been taxing gasoline users very heavily since the product is regarded as being a luxury item mostly consumed by the rich. The present tax rate (including the oil fund contribution) on premium gasoline is 4.8% of its retail price. For such products as kerosene, fuel oil and LPG, all of which are believed to be mainly consumed by the rural poor or vital to the well-being of the majority, the government has been keeping their retail prices low (and lower than their ex-refinery prices)import prices through subsidies from the oil fund. As a result, the differences between the retail prices of various oil products have become substantial, even though their ex-refinery prices and import prices are only slightly different. These price differentials at the retail level have led to substitution among different oil products when it is technically possible and privately profitable, e.g. a subsitution of LPG for gasoline in taxis, and a mixture of kerosene and diesel oil in transport use. The price gaps were widened by the January 1981 oil price adjustment, especially the gaps between the retail prices of gasoline and diesel oil on the one hand, and those of kerosene and LPG on the other. Kerosene, whose retail price was always higher than that of high speed diesel oil before February 1980, was made cheaper than diesel oil in 1980 and again in 1981. The distorted price structure of oil products in 1981 encouraged the use of such subsidized products as kerosene,LPG and, to a lesser extent fuel oil, while stifling the consumption of gasoline and diesel oil. The oil sales figures for the first three quarters of 1981 show that, compared with the same period of 1980, the consumption of kerosene, LPG and fuel oil grew by 35%, 25% and 6% respectively, while that of gasoline and high speed diesel oil declined by 6% and 0.4% respectively.

The oil fund deficit which amounted to 3,600 million baht at the end of 1980 was largely a result of government subsidies given to the Egat for the use of fuel oil and diesel oil from 1975 to 1977 and from 1979 to early 1981 to stabilize the price of electricity. The deficit was reduced by 1,000 million baht after the January 1981 oil price adjustment. However, as more subsidized products were consumed and the baht price of imported oil increased after the baht devaluation in July, more subsidies had to be paid out of the oil fund to keep the retail prices unchanged, and the deficit grew at a rate of about 100 million baht a month. To check the growth of the oil fund deficit, the government decided to raise the retail price of premium gasoline by 13% on December 2, 1981, while leaving the prices of other oil products unchanged. Given the pattern of oil consumption in September 1981, the new price structure would reduce the deficit to only eight million baht a month and increase tax revenue on oil by nearly 40 million baht a month. However, our analysis above should indicate that the latest oil price change, which clearly aggravated the already distorted price structure, would lead to more substitution of the subsidized oil products and regular gasoline for premium gasoline. The price differential between premium and regular gasoline was widened from 50 satang to 2.05 baht per litre, thus making it financially attractive to adjust car engines and switch from premium to regular gasoline. An oil company reported a sales drop of

20% for premium gasoline and a substantial increase of sales for regular gasoline a week after the price change. It is expected that the resulting change in oil consumption pattern will still leave the oil fund deficit growing at 60-70 million baht a month. This may appear to be a financial improvement for the government in the short run. But in the long run, if this price structure continues, people will be encouraged to switch to other oil products, including those subsidized items, and it is possible that the deficit will become even larger than before. What appears to be "politically wise" in the short run can be economically unwise in the long run because interfuel substitution at a large scale does not promote energy and foreign exchange saving. A measure is being introduced to prevent oil adulteration by adding different colours into premium gasoline, regular gasoline, kerosene and diesel oil. Such a measure has never proved to be successful in other countries, and there is no reason why it will be in Thailand.

A senior government official admitted that the last price change, though prompted by an increasing oil fund deficit, was politically decided without any solid economic reasoning. According to him, another round of oil price adjustments seems inevitable in view of the fact that more distortions have been created. It is expected also that price differentials among oil products will be reduced and subsidies from the oil fund will be substantially reduced, if not eliminated.

In the world oil market, the prospect of a stable price of $34 per barrel for the Arabian light crude and more unified prices charged by the Opec throughout 1982 looks very probable. The oil glut in the world market is expected to continue in 1982, resulting in better prices for the buyer. This is good news for an oil-importing country like Thailand. For fuel oil and LPG, some marginal declines in the ex-refinery prices and import prices, which are based on Singaporean ex-refinery prices, already occorred in the fourth quarter of 1981 as a result of the glut. Any further decline in the future should enable Thailand to save some foreign exchange and reduce subsidies on some oil products.

Natural gas: Start of a 'brilliant' hope

The natural gas from the Gulf of Thailand was finally delivered ashore on schedule in mid-August 1981 by Union Oil from its Erawan structure to fuel two power stations in Bang Pakong and South Bangkok. This was accomplished in spite of the problems in the onshore pipeline laying which appeared at first to delay the first phase of Thailand's natural gas project. During the trial run of gas between mid-August and September, the price of gas paid by the PTT was 80% of the normal price which was $2.20 per 1,000 cu ft. The flaring ceremony on September 12 was presided over by the Prime Minister who figuratively called the event as marking the beginning of the era of a "brilliant" hope for Thailand's future.

So far the brilliant hope has not been fully realized. In early October the gas was found to have to much moisture for the operation of some turbines at the Bang Pakong power plant. Once the problem had been quickly solved, excessive heat caused damages to some of the gas wells and prevented Union Oil from supplying the PTT with 200 million cu ft per day of gas which was to start on October 1 last year as agreed upon in the sale contract. Instead, only about 100 million cu ft a day was piped to the Egat which was the only gas consumer. The repair of these damages was expected to be completed in May this year by which time Union Oil will be able to supply the agreed amount of 200 million cu ft a day. The supply shortage caused the power plant to run on fuel oil instead of natural gas. Since fuel oil has to be imported, this means a loss to the country in terms of foreign exchange saving foregone which is estimated to be to the tune of 3,300 million baht. The government will also lose its royalty revenue it should have earned; and the loss in government revenue from gas and condensate due to the shortfall of supply would be about 130 million baht. According to the contract, the compensation to be paid to the PTT for this supply loss will be in terms of a 20% discount of the normal price for the amount of gas equal to the quantity which Union Oil failed to deliver on time. It remains to be seen whether the PTT will regard this breach of contract as a force majeure, in which case no further compensation can be claimed.

Despite the hitches, the gas from the Union Oil wells will substantially reduce this year's oil bill and add another significant source to the government tax revenue. It is estimated that the import value of fuel oil and gasoline would be reduced by 8,200 million baht or almost 12% of this year's import oil bill, which was expected to be 69,000 million baht had there been no natural gas and condensate utilization.

Meanwhile, price negotiation continues between the government and Union Oil for gas in other structures involving the proven reserves of about one trillion cu ft. A high-level committee chaired by Minister Sulee Mahasanthana was appointed to speed up the negotiations. The price negotiations with Texas-Pacific, which have been conducted for over three years, were interrupted last year by a proposal by Texas-Pacific and other interested parties, including the PSA group and a Japanese trading firm to export the gas from Texas-Pacific's 'B' structure. According to Thailand's Petroleum Law, the government can ban any export of petroleum, including natural gas, if it deems necessary to preserve it for domestic use. Therefore, the proposed export project which could involve over $ 3 billion can be undertaken only with the government assurance that gas export will not be prohibited. In response to the Texas-Pacific's request for such an assurance, the Minister of Industry set up a committee headed by the Director-General of the Mineral Resource Department to give recommendations on the issue.

A preliminary finding by the committee was reported to be rather unfavourable to the export proposal. The domestic demand for natural gas in the next 30 years was estimated to be 14 trillion cu ft, while the most expected reserves from Union Oil and Texas-Pacific structures, based on the latest reserve figures, are about 10 trillion cu ft. Therefore, unless more reserves are found, either offshore or onshore, the export of natural gas seems unlikely at the present. A study by a working group at the NESDB also found that in terms of foreign exchange saving, it is better for Thailand to utilize its own gas domestically than to export it as LNG, given the present structures of petroleum taxation and prices.

The prospect of finding oil and gas in onshore concession areas began to look bright as Thai Shell Exploration and Production Company reported in November last year a finding of oil at the flow rate of 3,000 bpd at its Larn Krabue drilling site in Kamphaengphet province. The figure was considered commercially viable, but production will probably not start until more drillings are made to determine the size of the oil deposit. However, it was reported that, if pressed by the government, Shell will probably be able to produce 10,000 bpd within the next 18 months.

Earlier in the year, Esso Exploration and Production Korat Inc also struck 16 million cu ft a day of gas at its drilling wells in Nam Phong, Khon Kaen Province. Unlike in the Gulf, natural gas at Nam Phong was reported to contain a high content of methane, indicating that it is suitable only for burning as a fuel, and not as a feedstock for petrochemicals.

To step up oil and gas exploration, the government last year granted more concessions covering the total area of 54,000 sq km in the Northeast to Esso Udon Inc, Phillips Petroleum Co (Thailand), and Terra Marine International Inc, and awarded three blocks covering 26,700 sq km in the Gulf of Thailand to Pecten Thailand Co. Pecten was expected to begin exploratory drilling early this year, while other companies have just been conducting seismic surveys.

The findings of onshore gas and oil added another factor in Thailand's energy equation. If sizable deposits are found, it may have an important implication to the future plan of utilizing gas from the Gulf, The onshore gas will most likely be cheaper than the offshore gas because the costs of exploration, production and transportation will be less for the former. If circumstances allow, the government will be tempted to exploit the onshore gas rather than the offshore gas. This would probable have some bearing on the price negotiations between the government and the offshore gas producers. It is possible to foresee Texas-Pacific being allowed to export some of its gas as it has been requesting, since the gas reserves would exceed the local demand. However the amount of offshore gas earmarked for feedstock in the future petrochemical industries should not be affected, since the quantity of gas involved is a small fraction of the planned gas supply.

As the potential for striking more petroleum in Thailand looks more promising, the present concession-royalty system would become obsolete and inadequate for the host country in sharing the benefit of its own natural resources. The present Petroleum Law allows the government to collect a royalty which is 12.5% of the sale value of petroleum and a profit tax at the rate of 50%. Although, under the existing law it is possible for the government to extract a larger share from oil and gas producers by demanding signature bonus payments and its share of production as more is produced, the government's share is still smaller than what it would obtain under the production-sharing scheme adopted by Indonesia, Malaysia and most other oil-producing countries. It was reported that the government was contemplating revision of the Petroleum Law in order to introduce some elements of production-sharing.

Supply: More control and more surplus

Some significant moves were made by the government to gain more control over the supply of crude and refined products. These include the government's take-over of its Bangchak refinery from Summit in April and the government-to-government long-term purchase contract with Saudi Arabia which agreed to supply 65,000 bpd of Arabian light crude during the most part of last year, and again this year.

The Thai Oil Refinery Co (TORC), which was handed over to the government in September 1981, became a joint venture in which the government holds a 49% equity, and the rest of the equity is shared among foreign and Thai investors and oil companies. TORC is planning to expand its refining capacity from 65,000 bpd to 154,000 bpd in 1986 . The Esso refinery , which is now the only privately-owned refinery in Thailand,also has a plan to enlarge its capacity from 44,000 bpd to 63,000 bpd in 1985. Therefore, by 1986 the total refining capacity in the country is expected to increase from 175,000 bpd to 282,000 bpd, which is believed to be adequate for local oil consumption until 1991. With the present refining pattern, diesel oil will still have to be imported in the future. However, the locally refined fuel oil and gasoline are likely to excceed local consumption, partly because of energy conservation in transport and manufacturing, but mainly because of the substitution of natural gas for fuel oil in power generation and large energy-consuming industries, such as the cement industry. In terms of foreign exchange saving, there is a study which shows that it is much more economical for Thailand to burn natural gas rather than fuel oil as an energy source. Therefore, in order to cope with future fuel oil surpluses, the country may have to either export those surpluses or change the configuration of the expanded refineries by adding more cracking units to reduce the yield of fuel oil and increase the output of lighter products.

Energy prospect in 1982

It seems likely that the retail prices of oil products will have to be adjusted again early this year to reduce price differentials among the products and perhaps to reduce subsidies given to those sensitive products such as kerosene, diesel oil and LPG. In view of the fact that the Opec oil prices will be stabilized and the world oil glut is expected to continue this year, the domestic oil prices in Thailand will remain stable after the anticipate price adjustment. No rise in electricity rates is foreseen, since the Egat will be able to reduce its fuel cost by using natural gas which is priced more cheaply than fuel oil.

The consumption of gasoline and diesel oil is likely to pick up again after people are accustomed to the new price levels. More LPG will be used in transport and industry because it will still be cheaper than gasoline and its supply will be more readily available as more LPG stations are operated in Bangkok and other provincial cities. The only oil product that will be down in consumption is fuel oil which will be substituted by natural gas in electricity generation at the rate of 2.55 million litres a day in the first half of this year, and at twice that rate in the second half.

For the first time in eight years, Thailand's oil import for this year is expected to be reduced in volume and probable in quantity. And this will help alleviate the trade deficit which had been growing rapidly since the first oil crisis in 1973/74. Barring any political upheaval in the Middle East, no supply shortage of oil is foreseen this year.

It is possible to hear some exciting news about new oil and gas discoveries and more firm figures on the sizes of the tested reserves. Every sign seems to indicate that this year will be a turning point where Thailand will begin to reduce its oil dependence and to rely more on its indigenous energy sources, particularly natural gas. The energy goal in the fifth five-year economic and social plan is to reduce the oil dependence to 42 % in 1968. The performance this year should be a good test as to how and whether that target will be met.

Ending stock

(in 1,000 metric tons)

Crop	1980	1981(E)	1982(E)
Rice paddy	1,473	1,841	2,588
Maize	87	202	77
Cassava	2,675	3,349	671
Rubber	59	118	190

Methods of computing ending stock:

* Ending stock = Total supply less distribution

Total supply = Beginning stock plus production

Distribution = Domestic consumption, export seeds, waste, and other uses

Note: (E) = Estimated

(P) = Projected

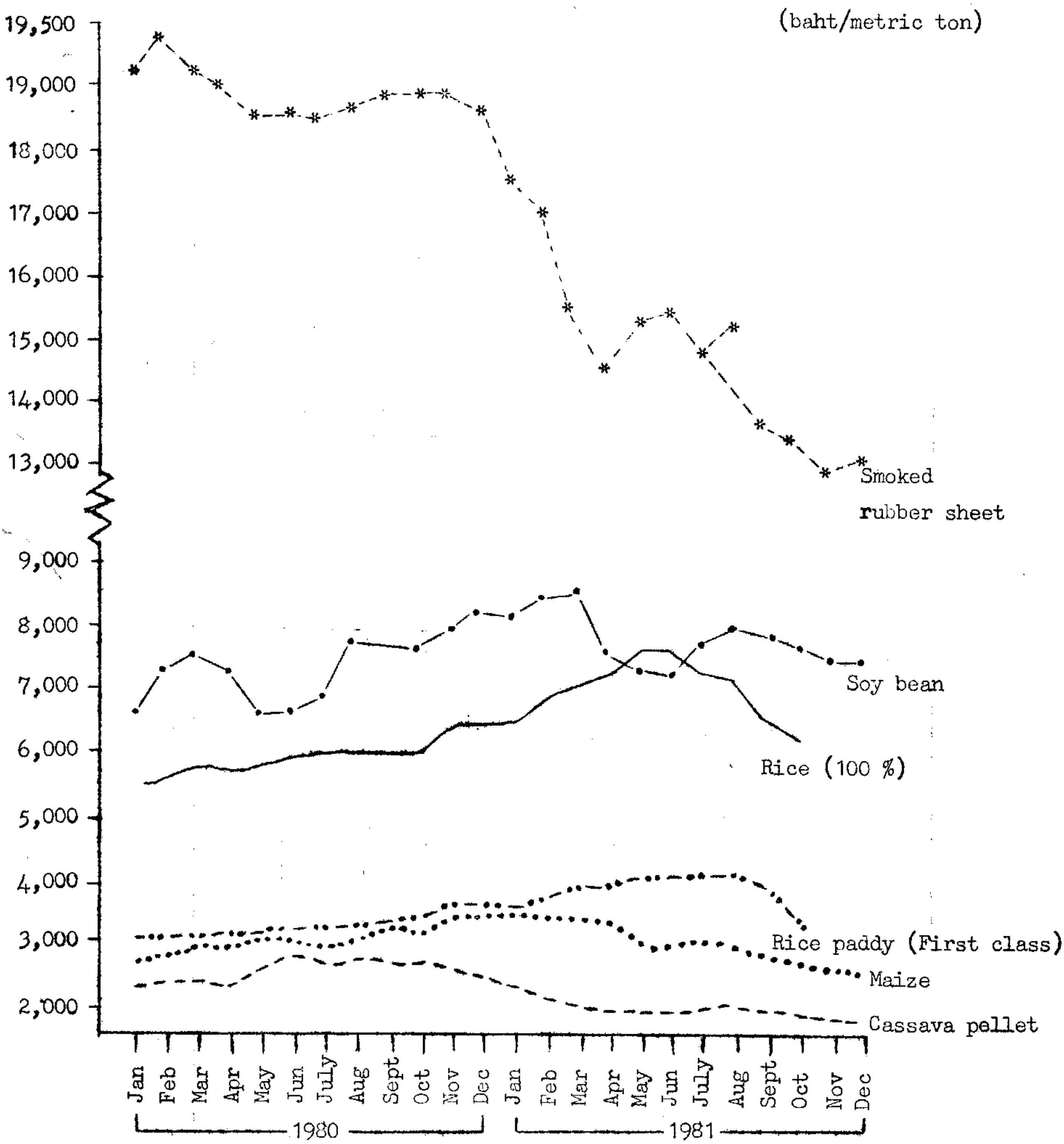
Main crop production

(in millon tons)

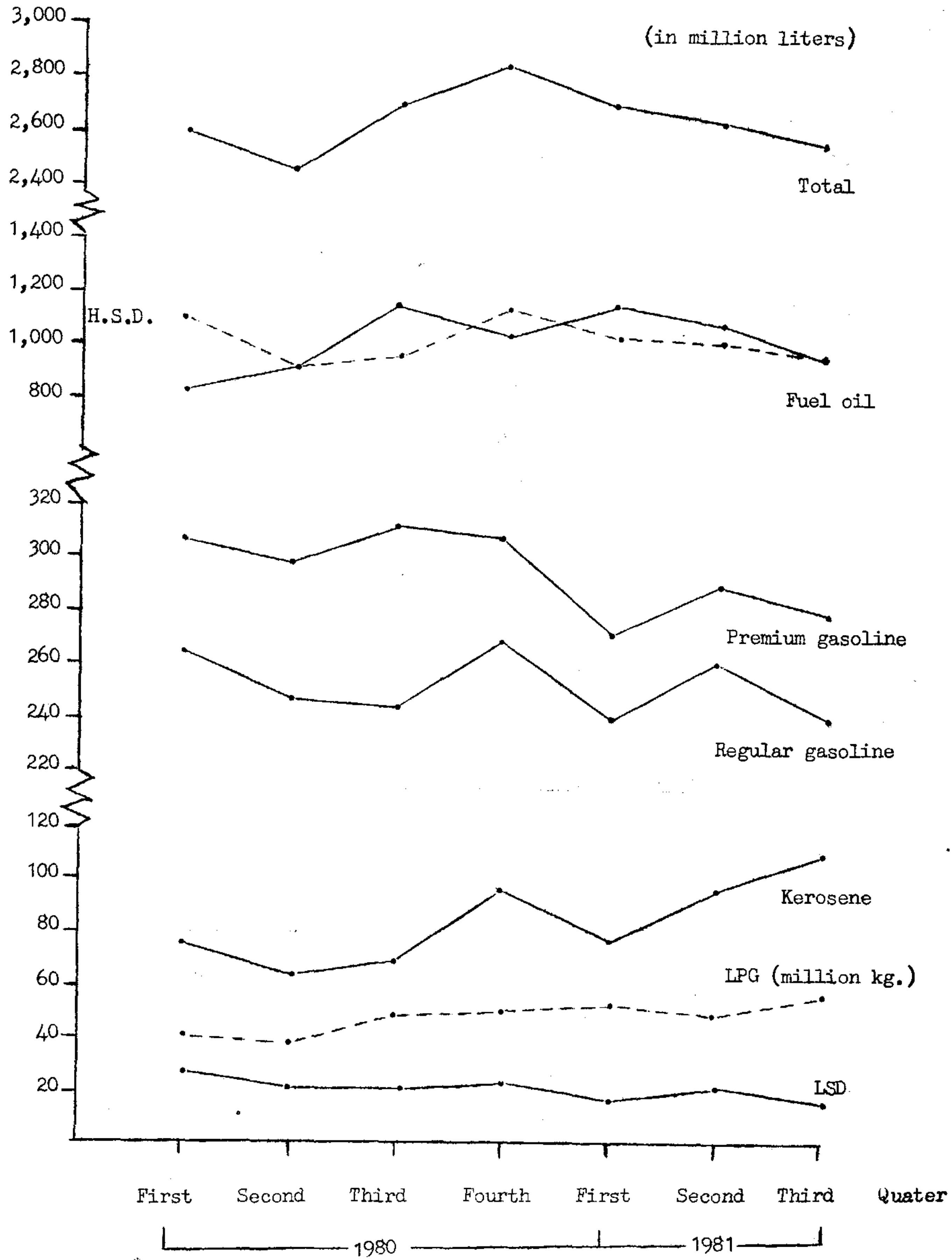
Crop	1979/1980	1980/81	1981/82	%Change		1983/83
				1980/81	1981/82	
Total rice paddy	16.910	16.800	17.800	-1	+6	-
1st crop	14.646	15.500	15.800	+6	+2	-
2nd crop	2.264	1.300	2.000	-43	+54	2.2
Rubber	0.531	0.480	0.540	-10	+13	0.586
Maize	3.300	3.150	3.450	-5	+10	3.6
Cassava	11.140	13.810	16.500	+24	+20	14.54
Sugar Cane	12.460	18.652	25.000	+50	+34	23.24

E = Estimated

Wholesale prices of some crops 1980 - 1981



Quarterly oil consumption in 1980 - 1981



V. PRICE AND INCOME

Inflation slowing down

The encouraging yet rather surprising sign of the 1981 economy is that inflation 1981 slowed down from 20 % in 1980 to 13-14 % in 1981. The slowing down of inflation is more evident especially in the second half of the 1981 despite the prediction by many economists that inflation in the second half of the year would intensify because of baht devaluation, the new minimum wage and the possibility of increase in price of petroleum products due to the decision to increase price of crude oil by our major oil exporter, Saudi Arabia, from $ 32 to $ 34 per barrel. The main point in this section will be to discuss in detail those factors contributing to the slowing down of inflation and the prospect of inflation in 1982.

Inflation in the first half of the year

It is extremely interesting to compare the inflation trend of the first half of the year with that of the second. By the time the end of 1980 came along, many experts shared the view that inflation in 1981 should be lower than that of 1980 where prices rose sharply (20%). The news of the inflation rate in the first six months (especially in the first four) took everyone by surprise. Panic nearly set in for the reason that if the trend of the first three months in particular had continued, Thailand would have achieved an inflation rate of close to 30%, unprecedented in history. The graph here shows CPI by categories, with transport section taking the lead with an increase of 22% from February to March. The main reason was the price adjustment of all petroleum products by an average increase of 20%. This was the first adjustment by the Prem I government despite the series of world crude oil price increases in 1980. Another contributing factor to the sharp rise of the CPI in the transport sector was the government's decision to raise bus fares in Bangkok from 1 baht to 1.50 baht and bus fares for inter-provincial lines went up by 21% in May 1981. The overall increase in CPI in the first six months of this year was also because of government's courageous policy to reduce the subsidy to the urban people (especially in the Bangkok metropolitan areas) by raining the price of electricity twice, on January 10, by 16.6% and in April by 20%. The water rate also increased as of 15 April 1981. During the last two months of 1981 the slowing down of inflation became evident except in the tobacco and alcoholic beverages sector where the CPI went up sharply by 8% during May and June due to the government's decision to raise excise taxes on 29 April 1981. In summary the CPI of the whole country rose by 7.3% in the first three months of this year. At that time, concern was evident that if this rate continued, inflation would have approached 30% for the first time.

Inflation in the second half of the year

As clearly pointed out in the last report, "the state of the nation", that inflation in the second half of 1981 would be classified into two scenarios: (1) the optimistic scenario: using the CPI of the last two months of the first half of the year and adding economic reasons such as the slowing down of the Thai economy due to high interest rate domestically which led to lower demand for loans, and subsequently the reduction of investment resulting in inflation rate around 16%; (2) the pessimistic scenario: many factors were at the time working to fire up the inflation rate especially the government's decision on minimum wage and baht devaluation by 8.7% in July 1981. These factors would lead to inflation rate of around 20% upward for 1981. However, the result of the inflation rate in the second half of the year was not only somewhat closer to our optimistic scenario but also turned out to be better than our optimistic prediction. The overall increase of CPI in the last half of 1981 was only 3% which was much slower than that of the first half of 1981 which rose by 8.7%. The 3.1% increase of CPI in the second half of 1981 reflected the overall uniformly slow rate of all sectors except for food by 2.8%; not-food by 3.2%; clothing by 2.2%; housing by 5.3%; personal and medical care by 3%; transportation by 1.5%; recreation, reading and education 2.1%; with practically no change for tobacco and alcoholic beverages.

Comparing inflation in 1980 and 1981 (see Table), we see that as result of a good harvest, food prices in 1981 increased only by 9.9 % as compared to 18.1% in 1980, whereas the rest of the other sectors show inflation rates in 1981 lower than those in 1980 with CPI transport sector in 1981 showing only a slight increase from the 1980's figure.

<u>Reasons for the slowing down of inflation in the second half of 1981</u>

It is difficuly to exactly pinpoint the reasons contributing to the slowing down of inflation in the second half despite a rather grim prospect at the beginning of the year. Moreover it is difficult to isolate each factor since it appears that various factors interplay with one another, nevertheless, this sector will attempt to discuss them separately. To begin with, many believed that Thailand was entering a so-called semi-recession stage, where production of certain sectors would decline significantly during 1981. The construction sector in 1981 experienced a very slow growth around 6%. There are instances of firms operating at less than full capacity, resulting in a substantial decline in profit margins. This semi-recession leads to a reduction in the purchasing power of the consumers. Secondly, the existence of high domestic interest rates during the first two quarters of this year made it impossible for firms to hold substantial inventories for the purpose of speculation, therefore more goods were released into the market resulting in increasing supplies and price competition among producers tending to keep prices at a stable level. It is the first time for many years that prices of essential consumer goods were rather stable. Thirdly, the world is also facing a period of recession, consequently inflation in the western world has been rather moderate. For example, the 1981 inflation in the US is around 10-11 % and is expected to be around 8-9 % in 1982. Since Thailand is an open economy, the decline in the inflation rate of the western world generated a slowing down of our inflation rate especially through the reduction of import prices. Fourthly, because of abundant supplies of agricultural products as well as lower demand from our buyers, the prices of our agricultural products on average declined significantly. Fifthly, the government attempted to control its own expenditures by holding down government expenses - the so-called "fiscal discipline" - the government sector therefore did not stimulate inflationary pressure as much as it did in the preceding period. Sixthly, the monetary authorities did not increase the amount of money supply M1 as much as in 1980. The available data shows that the rate of increase this year of M1 is around 2.9% as compared to 13.8% in 1980. Lastly, during the last six months of 1981, the government did not increase any major utility prices. In July 1981, due to strong political pressure, the government dicided to roll back electricity prices by six satang per unit. However two major decisions on prices were taken up in December 1981: one was to raise the price of premium gasoline from 11.95 to 13.45 baht; the other was a major rise in the excise tax for cigarettes, but the two decisions have little impact on CPI in 1981.

It is interesting to point out that of the reasons mentioned, with the exception of fiscal discipline and the money supply, none of them was the deliberate government policy to curb inflation. Many of them were uncontrolled factors. There is no reason to be complacent about the whole situation. Looking at the other side of the coin, in the next year, price of other petroleum products will have to be adjusted to narrow the unreasonable gap with premium gasoline. The impact of devaluation is not yet fully realized. It is also expected that world economy is starting to pick up from a very deep and serious recession. Domestic interest rates will be adjusted lower if the present trend of prime rate continues. Price support for rice for 1981/82 season will increase by 250 baht per ton. These factors are likely to add fire to inflation next year. Many are optimistic with the inflation rate of next year but the warning is that the inflation will be around 10-11% with certain conditions already explained. The government will reap some short-run benefits by alleviating pressures of continuing to adjust income of many groups. At the same time, the so-called supply side economics will be allowed to operate by abolishing certain forms of price control. However the price to pay is expensive because looming ahead, a new political time bomb, is the increasingly serious problem of unemployment.

Wage and Income Policy in 1981

Minimum Wage

In October 1981, after a long wait, the new minimum wage legislation was announced. We predicted in the last report that the percentage in increase of the minimum wage this year would not be high as compared to the last two years (see Table 2). For Bangkok and the surrounding provinces, the minimum wage went up from 54 to 61, a 13% increase; while in the Central Plains and the South , the minimum wage went up from 47 to 52, a 10.6% increase; while in the North and the Northeast, the rate rose from 44 to 52 baht, a 14.2% increase. However the breakdown of the regional rates in 1981 underwent a major change. Seven provinces namely Chiang Mai, Nakorn Ratchasima, Saraburi, Chonburi, Ranong, Pang-Nga and Phuket were previously (prior to October 1981) fixed at rates different from Bangkok areas. In October 1981, these seven provinces received a minimum wage of 61 baht. This action created some outcry from the factory owners as well as owners of other enterprises since this arragnement led to an increase in payment for the new minimum wage rate of around 30%. Hotel operators in Pattaya, a major tourist resort, also made their complaints. In Nakorn Ratchasima, owners of gunny bag factories laid off at least 2,000 workers. Equalization of regional minimum wage rates tends to reduce migration but at the same time, it does not yield an advantage in labour cost to investors who want to invest in other provinces out side Bangkok. This point is crucial because the government in the Fifth Plan wants to promote and disperse industries away from Bangkok without providing basic infrastructure as well as transport facilities. To take away an advantage in the labour cost is quite serious in preventing development of industries to other regions of Thailand. However, migration is also a serious problem of unequal minimum wage. This migration problem will be intensified this year because the regional CPI (see Table) shows that the Northeast region has achieved the highest increase in CPI for 1981. It is anticipated that in the future, the government will attempt to further narrow the gap among regions. More thinking to be done by the government is therefore required to look at relative costs and benefits of this policy.

Because of the semi-recession situation in Thailand, the imposition of the minimum wage in 1981 creates many doubts about consequences of this government policy especially regarding the high level of unemployment. This doubt is even expressed by high authorities of the Labour Department. It is therefore hoped that more systematic studies would be conducted before the next round of negotiation of minimum wage comes along around October 1982. What is extremely important is that Thailand is competing with other developing countries for its competitive position in the world market. One case comes to mind, among Asean countries. The real wage in the Philippines had declined while the real wage in Thailand has remained constant or even slightly increased. This does not imply that labour welfare and wellbeing of the workers are not important but distortion in the labour market has a high price, especially in a time of the slowing down in the world economy. Thailand, while still holding some comparative advantage in labour-intensive goods, should try to capitalize while possible.

Trade unions and the minimum wage

The Thai manufacturing sector is usually divided into two sectors: one is called the formal sector where firms are big and the role of trade unions is relatively important; and another one is the informal sector, where firms are small and practically no one belongs to a trade union. Trade unionists support minimum wages since it is only in the big firms where compliance rate is relatively high (see Table). If the minimum wage is aimed at helping to increase the well-being of the workers, it does not usually help the workers in the informal sector and they are the ones who require the most help.

Income policy

It is usually believed that a sound and effective policy dealing with the high cost of living is to make a policy adjustment both on price and on wage and income as one package. In the past, the income policy has not been planned well by the government, usually resembling a " catching up policy". In 1981, however, two elements are important. Given the slowing down of our inflation, at least income for certain groups will rise as fast or even faster than prices. Moreover, it is the first time that government decided to raise salaries for governemnt and public enterprise employees at the same time, effective on January 1, 1982. At least the timing is right. The average increase in salaries for both groups will go up by more than the rise in CPI . The government in 1981 also raised imcome for government pensioners by 20%. Government tax policies in 1981 also affected income indirectly. On December 12, 1981, the government proposed a major reduction in personal income tax for individuals, by raising the amount of deduction as well as the minimum income to be taxed. This change has not yet been implemented, apparently, because of inheritance tax provisions. On 21 December, the government lowered tax on dividends from 15 % to 10 %. Government price support for agricultural products continued but the decline in the world prices made it difficult to operate the price support scheme effectively.

However, despite the encouraging signs being detected, the income policy by the government in 1981 is still considered to be a stop-gap measure. Long-term planning is needed to put everything in one package. With the present existence of political instability, it is difficult to see the package being implemented by 1982. The government sector remains a big question mark despite the increase in salary of around 17 %. It is important to reform the bureaucracy. It is unlikely that a reform will take place in 1982 because of political reasons. In 1982 it appears that income for the rural people (especially the farmers) as compared to urban groups will be much worse off since prices decline substantially while the government and public enterprise employees received salary adjustment and the workers received the minimum wage adjustment.

The labour problems

In the last section regarding minimum wage, it is an example of government's inability to change policy during a slowdown in the economy. The labour or industrial relations problem is a perennial one, and as we have seen, the government only manages by dealing on an ad boc basis with periodic crises (as seen from the recent strike by postal workers).

The government in 1981 still considers the labour problem as politically serious. In 1981 there were no major constructive policies to solve the labour problem. Recently General Arthit Kamlang-ek, acting on behalf of the Bangkok peacekeeper, summoned labour leaders to discuss the situation. Director General of Labour Department, Mr. Vichit Saengthong, was given a special extension for another four years. The statistics from the Table on the preceeding page show an increasing trend in the number of disputes as well as number of strikes in 1981 compared to 1980. Each strike, interestingly enough, lasted longer in 1981 due to the government's authorization for strikes to be legal. The longer duration reflected itself in the statistics of number of mandays lost in 1981 (first nine months) to be 164,136 which is a substantial increase compared to 1980.

Trade unions in public enterprises continued in 1981 to play important and crucial roles. Students in labour relations in Thailand know very well that public enterprise trade unions are very well organized and members belong in the semi-skilled and skilled categories. During 1981, provincial water works unions, telephone and postal workers staged illegal strikes. The government nonetheless yielded to their demands. The main complaint by public enterprise unions is discrepancies in the pay scale. An interesting demand which the government still does not yield to is the abolition of the regulation that each public enterprise can adjust their salary scale without cabinet approval. This issue will undoubtedly intensify this year.

The role of the labour court continued to be important. The statistics (see above Table) of this year show that from January to October, there were 3982 cases for the labour courts which was higher than 2682 cases in 1980. Although 1981 data on types of disputes are not yet available, Table 6 shows that in 1980 most disputes that went to the labour court involved compensation. It is expected in 1982, the labour court will have to deal with more cases since the slowing down of the economy will lead to firms laying off more workers and disputes regarding compensation will increase. It is therefore important to evaluate the role and the effectiveness of the labour court. In general, it appears that the labour court has not solved the major problem of Thai industrial relations ie "immaturity" . The conflict within the three parties involved, the workers, the management and the government still exists among us in 1981 and will continue into 1982 and beyond.

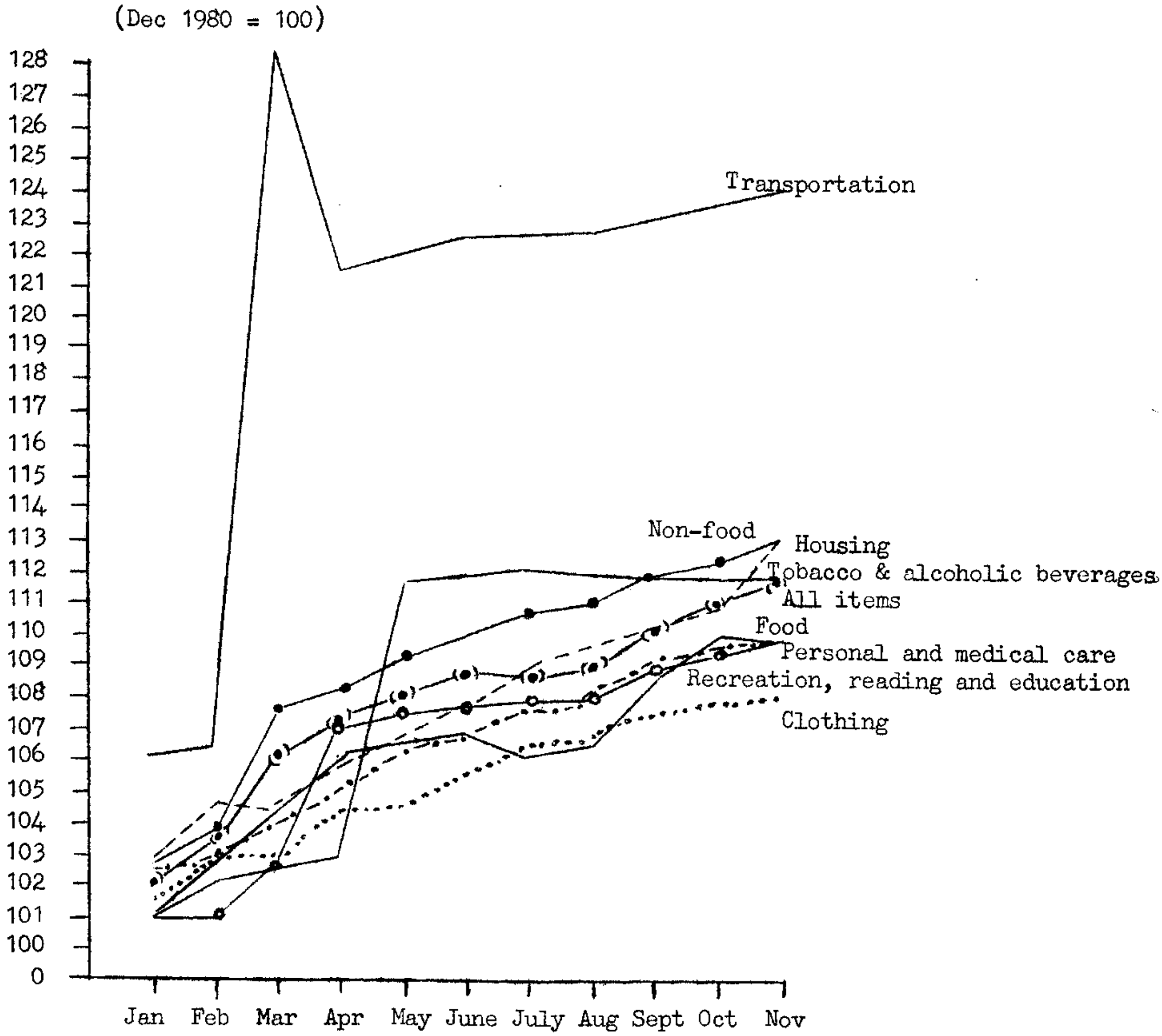
Unemployment

Some people will disregard the problem of unemployment in Thailand as insignificant. Basically the unemployment rate in

Thailand is very low compared to the rest of the other developing countries. Moreover, many focus their major attention on low wages and under employment. Until recently, unemployment has not posed a serious threat to the government as part of the political pressure due to the fact that our agricultural sector has been able to absorb the new labour force fairly well. In addition, the urban informal sector both in services as well as production of goods has been able to absorb labour. The government tends to regard employment or lack of it as a long-term problem, but we will soon recognize that this changed dramatically in 1981. Major daily presses are now talking about the new political problem of unemployment. Only recently has the Labour Department admitted that in 1982 there will be an additional 700,000 people unemployed and 170,000 of these will be those who received technical education and above.

Two major forces affected the unemployment situation rather cruelly in 1981; the first being the drop in the world prices for agricultural products of which Thailand is a major exporter. This will hit the absorptive capacity of our agricultural sector directly, a cushion which is no longer available. The farmers adjust production as part of the supply response to price and in the 1981/82 season, this supply response will be negative. The expected rural-urban migration in 1982 will intensify, despite the strong commitment of the current government to utilize the tambon project fund. This is of a small magnitude compared to the seriousness of the problem. Moreover the tambon project fund can only alleviate unemployment in the dry season. Secondly, the industrial sector in Thailand is and will continue to be experiencing a semi-recession. Many factories are closed down, and lay-offs, in particular the glass and textile industries, which are not commonly practised in Thailand, are prevalent. The seriousness of the problem is that the number of new entrants into the labour force is going to be in the vicinity of 700,000 per year even with a decline in our population growth from 3.3 % in 1965 to 1.9 % in 1981. International migration will solve a few problems but at the same time create new ones. It enables Thailand to receive additional funds through remittance of around 10,000 million baht per year but it demonstrates the fundamental mistake of our policy of promoting capital-intensive industries at the expense of labour-intensive industries. The imposition of the minimum wage intensifies the number of unemployed rather seriously in 1982. Even though the government has begun to regroup and has tried to tackle with the problems, no major long-term policy has been set forth. One recent example of the government's remedy is the postponement of laying off 300,000 temporary government workers to another four months. In 1982 the unemployment question will become very serious and thus solving it will not be easy. Long-term planning is essential whether in education, in agricultural and industrial policy, in manpower planning or in fiscal policy. Once again, in conclusion, we might raise a question, where do responsibility and authority lie?

CPI by categories 1981



Percent change of CPI 1980 and 1981

	1980 (Dec 1979 = 100)*	1981 (Dec 1980 = 100)*
All items	17.3	11.7
Food	18.1	9.9
Non-Food	16.9	13.1
Clothing	14.9	7.8
Housing	17.1	13.0
Personal and medical care	19.3	9.9
Transportation	21.1	24.0
Recreation,reading and education	15.6	9.8
Tabacco and alcoholic beverages	8.8	11.8

* The CPI of 1980 and 1981 are compared for the first 11 months only, the CPI of December 1981 is not yet available

Percent change of CPI by regions 1981

(Dec 1980 = 100)

Regions	Jan - Nov
Central and East	10.0
Northeast	12.0
North	10.7
South	7.0
Whole Kingdom	11.7

Minimum wage from 1973-1981

(baht per day)

Regions	April 17 1973	January 1 1974	June 14 1974	October 1 1975	October 1 1977	October 1 1977	October 1 1979	October 1 1980	October 1 1981**
Bangkok and surrounding	12	16	20	25	28	35	45	54	61
Previnces				(25)	(12)	(25)	(28.6)	(20)	(13)
Central and Southern	-	-	-	18	21	28	38	47	52
				*	(16.7)	(33.3)	(35.7)	(23.7)	(10.6)
North and Northeast	-	-	-	16	19	25	35	44	52
				*	(18.7)	(31.6)	(40.0)	(25.7)	(14.2)
Whole country				19.7	22.7	29.3	39.3	48.3	55.0
					(15.2)	(29.1)	(34.1)	(22.9)	(13.9)

* In brackets ( ) are the % change

** In 1981, seven provinces-Chiang Mai, Nakorn Ratchasima, Saraburi, Chonburi, Ranong, Pang-Nga, Phuket-would receive 61 baht per day.

Compliance rate on minimum wage by firm size

Firm Size	1975	1976	1978
Small			
Less than 5 persons	59.56	47.25	67.60
5-9 persons	63.02	59.28	53.96
10-19 persons	68.49	59.29	59.47
Medium			
20-49 persons	69.81	72.94	63.55
50-99 persons	75.90	80.20	75.85
Large			
100-299 persons	84.66	86.29	83.84
More than 300 persons	87.06	87.79	93.58
No information	40.91	80.00	-
Total	68.62	67.12	68.65

Source: Labour Studies and Planning Division, Department of Labour

Labour disputes and work stoppages 1979-1981

*January - October

	1979	1980	1981 *
Labour Disputes			
No of disputes (cases)	205	164	173
No of workers involved (persons)	75,468	52,697	94,548
Work Stoppages			
No of stoppages (cases)	64	22	48
No of workers involved (persons)	16,203	4,290	15,535
Days lost	119.25	53.20	224
Mandays lost	33,837	9,092	164,136

Source: Labour Statistic Section, Labour Studies and Planning Division, Dept of Labour.

Cases filed with the Labour Court in 1980

Categories	Cases (1980)
Total legal cases filed	2682
Claims for compensation	1668
Claims for overtime, living allowances and pension due	600
Claims for reinstatement of job.	130
Employers sueing employees	3
Employers sueing the Dept of Labour	40
Employers sueing Lab Rel Committee	47
Employees demanding legal prosecution	41

Source : Office Workers' Compensation Committee, Dept of Labour, Ministry of Interior.

VI. THE PUBLIC SECTOR

Pressing issues await solutions

The second half of 1981 has seen changes in a number of public policies and measures. Some of these are for the better while some are rather disappointing . It is without doubt, though, that innumerable policy contradictions and fundamental problems still remain. Most of these will require a more comprehensive rather than piecemeal approach at solving. Whether or not and to what degree the government endeavours are successful hinges a great deal on a basic characteristic which the government itself should know and possess above anyone else - "political courage". But let us review in a systematic way, what has been done.

A clampdown on public expenditures

Various measures undertaken during the first half of 1981 to curb spending in order to solve the cash flow problem of the government seem to have paid off. Since April, government expenditures have slackened resulting in a decline of 4.4 % in the second quarter. This is contrary to the normal established pattern of a higher expenditure level in the second quarter as compared to the first quarter for previous years.

In summing up actual fiscal spending in the first ten months of FY 1981, a level totalling 104,528 million baht which is about 74.4 % of the allocated budget, was recorded. This is smaller than the 78.4 % for the same period of FY 1980. Although public spending may be expected to rise in the last two months as government agencies try to spend their remaining allocations, it seems that the over-spending of FY 1980 will not repeat itself for FY 1981.

A shortfall in revenue collection

On the revenue side, the second quarter of 1981 registered a growth of 36.7 % over the first quarter which is rather impressive. However, when the first ten months of FY 1981 was considered as a whole, the revenue increase was only 19.6 % which is the lowest recorded in recent years. It was 23.5 % in FY 1980 and 20.1 % in FY 1979.

The explanation may be found mainly in the decline of export duties collected. This, in turn, was the result of government measures in reducing the rates of export duties on primary commodities to help prop up their farm prices. Income tax increases in FY 1981 also slowed down considerably. Looking at only the first ten months, growth in personal and corporate income tax collection were only 13.9 % and 23.3 % compared to the 18.7 % and 34.1 % for the same period of FY 1980. In addition, the growth rate of selective sales taxes declined from 32.9 % to 18.3 %.

In term of the revenue target set by the government, revenue collection in the first ten months of FY 1981 has reached only 76.9 % compared to the 83.2% recorded for the same period of FY 1980. It is therefore quite likely that the revenue target of 120,000 million baht for FY 1981 will not be met.

FY 1981-1982 budgetary deficits

Although the government has been successful in holding down expenditures, the revenue shortfall previously mentioned will probably result in a budgetary deficit for FY 1981 of around 18,000-20,000 million baht. The budgetary deficit for FY 1982 is expected not to be any smaller since planned public spending for the year is 161,000 million baht while revenue collection is targeted at 140,000 million baht.

Such continuously large budgetary deficits have resulted in and continued to pose serious financing problems for the government. With the local commercial banks and the Government Savings Bank having absorbed a large proportion of government securities in 1980 and 1981 causing their holdings of such securities to increase by 21 % and 25 %, respectively, and the other local markets being quite limited, the government is finding borrowing especially difficult. In fact, borrowing from the Bank of Thailand during the period of January-July of the past year was about 4114 million baht compared to a budgetary deficit of only 2906 million baht. This excess borrowing from the Bank of Thailand has, in part, been used to retire debts from other sources.

The heavy reliance on the Bank of Thailand in the past few years to finance more than half of all budgetary deficits of the government is a factor of serious concern. Such financing can lead to a rapid expansion of money supply which will fuel the flames of inflation and result in a serious balance of payments deficit problem. The solution for the government is, therefore, to urgently curb budgetary deficits before they get out of hand.

A restructure of the public sector

In an effort to cut down on public spending, the Prem I government has frozen any increase in employment opportunities in the public sector unless approved by the cabinet. This seems to be a stop-gap measure which may be in the right direction. However, it is meaningless and even undesirable if not coupled with a major overhaul of the public administrative structure, since it may seriously obstruct the smooth functioning of the government.

The public sector presently employs approximately 1.3 million permanent and 0.3 million temporary employees. They will be supported by payments in FY 1982 of 45,381 million baht or 28% of the total budget. An increase in efficiency of public employees can, therefore, lead to substantial savings in expenditures especially when it is generally known that efficiency is rather low in the public sector. With the advent of the Prem III government, there have yet to be any serious steps undertaken to restructure the government bureaucracy in order to increase efficiency and cut down on job duplications

There is, however, one encouraging sign in the budgetary process beginning in FY 1982 with the introduction of the programme budgeting system in place of the old line-item budgeting. Such a system may allow for a better monitoring and measurement of the success of each public programme of action and each government agency charged with the programme. It may also help to streamline the duplicative and cumbersome administrative structure. However, programme budgeting requires sufficient manpower with a foresight and understanding of the planning, drawing up, implementing and analysing of each programme to be consistent with the overall framework of governmental policies. This, however, still seems to be a serious bottleneck facing the government sector.

To make restructuring of the government bureaucracy successful, there should also be an overhaul of the public incentive system. Individuals are presently not rewarded based on their merit or competence. This has led to problems in the public sector of recruiting and retaining high calibre manpower, thus resulting in additional inefficiencies. All past governments including the present one have been and still are rather indifferent in their attitude towards such problems. The reason may be because results of such actions, or non-actions for that matter, will not be seen until far into the future when the government is no longer the present one.

One of the clearest examples of such a government attitude in the past year is the plight of university lecturers. Since August, there has been an urgent appeal from university administrators and lecturers calling for the government to undertake steps to help improve the status of lecturers, which has fallen far behind other types of government officials, in order to stop the brain drain from universities. The delay by the government in tackling this problem so far has meant more lecturers leaving state universities for more lucrative positions in the private sector and overseas. This is an area where time may be running out without anyone noticing since the adverse effects will not be felt until much later.

Efforts to collect more taxes

The government normally depends for more than 90 % of its revenues on taxes. Any attempt on the government's part to solve the problem of budgetary deficits through revenues must therefore deal effectively with ways to increase tax collection.

The past and present tax structure of the country relies heavily on indirect taxes such as import duties, export duties, business taxes, selective sales taxes and others which in 1980 were about 81% of all taxes. However, such taxes are generally considered to be regressive and to create distortions in the economy. They are therefore less desirable than direct taxes. Nevertheless, the problem of budgetary deficits has resulted in the government resorting to increasing use of such taxes as shown by various government measures in 1981 to raise the collection of excise taxes, such as those on beer, soft drinks, health, cement and cigarettes.

In the case of beverages, it has clearly affected significantly the demand for these products. This has led to serious difficulties not only for the beverage producers but also to those producing glass containers, cartons and crates for the beverage industry. Now it appears that the Finance Ministry will be rolling back the tax increase. Such mistakes and delays in correcting them only serve to undermine confidence in public actions.

As for the recent price and tax rate increases on cigarettes in December, it may be expected that demand will not be affected significantly in the short term since smoking as compared to the case of soft drinks. A revenue increase of 2,000 million baht as estimated by government officials may therefore actually materialize. However, such a policy seems to be contradictory to the emphasis given in the Fifth Plan of redistributing income since the tax and price increases on cigarettes fall more heavily on the poorer people. In the longer term, it may even be self-defeating as smokers may shift towards smuggled foreign cigarettes. If this is significant enough, tax revenues will not increase as expected.

The answer to more tax revenues should, therefore, lie more in direct taxes or other new forms of taxation. In Thailand, the only direct taxes presently collected to any significant degree are the personal and corporate income taxes. These taxes have been increasing in importance in the last decade from a share of 12% in 1970 to 17% in 1980. Besides the increases in real income of the population, these rapid increases may be attributed to a progressive income tax structure and the high rates of inflation. However, since income taxes start from a much smaller base than indirect taxes, it will take quite some time before income taxes can replace the indirect taxes to a sufficient degree. The answer, therefore, must be coupled with the additional collection of other neglected and newer forms of taxes.

Property tax reform

In order to reduce the reliance on indirect taxes and increase revenues to match government expenditures, more consideration should be given to newer and neglected taxes such as the property, inheritance, estate and gift taxes. These taxes will not only help to generate revenues but will be in line with the policy in the Fifth Plan of redistributing the income and wealth obtained from the fruits of economic development.

The presently collected property taxes are regarded as local taxes, including a house and recent tax and a land development tax. According to figures available in 1977, the former amounted to 331 million baht while the latter totalled 278 million baht. Together they constituted only 0.15 % of GDP or 1.1 % of central government revenues in that year which is exceedingly small. There is, thus, great potential in the collection of such taxes. This is the more so considering the rapid increase in the values of urban and prime agricultural land.

Although these are local instead of central government taxes, the increase in such taxes will mean that the central government can save a large amount of funds which are presently allocated to localities. In addition, a large number of functions which are presently undertaken by the government can be delegated to local authorities and, therefore, result in additional savings. The decentralization of authority from such actions will also help create an environment which is conducive to the development of democracy at the grass roots level. The question is, therefore, whether the Bangkok government and elite are ready to transfer part of their power to other regions.

In view of the inequitable distribution of wealth in the country, the land tax is especially desirable in urban areas since it falls fully on the landowners who are considered to be among the richer classes of society. This may be why resistance to such a tax is usually excessive. However, the government should understand and be in a position to point out to the landowners the various benefits which may accrue from such a tax especially when the proceeds are reinvested in such a way as to increase their land value. The clearest example may be to invest in a flood prevention system in Bangkok which will help increase the value of land and save households and businesses in the city the tremendous amount of money expended each year in their efforts to raise the level of their land over their neighbours' and to invest in various flood prevention schemes which are almost always at the expenses of others.

In addition, the land tax will help to reduce the demand for non-productive utilization of land such as for speculative purposes or holding as a form of asset. This will result in a fall of the exorbitantly high land prices and rents which are hindering development efforts. The economy as a whole can stand to gain from a faster growth through such a measure and the benefits may again trickle down to the landowners.

With the government-sponsored land bill having quietly disappeared from the scene in the past few months, it is suggested here that if the government were serious enough to solve the land and wealth distribution problems, the land tax can achieve the same goals at less cost, since it does not create any distortionary effects on the economy in contrast to the limitation of landholdings under the land bill. Furthermore, the tax will earn the government additional revenues which are not available under the land bill.

To ensure success, the increased collection of property taxes should be coupled with a reform of the tax system. There are presently too many loopholes which make exemptions easily obtainable for just about everyone. The tax base must be difined clearly enough and a method of valuation instituted which would allow for the least possibility of tax evasion. For the land development tax, there must be a reform of the present cumbersome structure of forty-three tax brackets to make it simpler. The existing proportional and regressive rate structure for land values above 1,400 baht per rai should also be replaced with a progressive one.

Other taxes which have not been collected in the country such as the inheritance, estate and gift taxes should also be considered. All these taxes tend to create a more equal opportunity for individuals in society while having little or no effect on the production system of the country. It is, therefore, a pity to see that an effort by the Ministry of Finance to push through an inheritance tax in the latter part of 1981 ran into strong opposition in high places resulting in the freezing of the bill.

State enterprise policy

The past year continued to witness many public enterprises incurring losses. Some of these include the Bangkok Mass Transit Authority (BMTA), the State Railway of Thailand (SRT), the Metropolitan Water Works Authority (MWWA), the National Housing Authority (NHA) and the Cold Storage Organization (CSO). These have prompted the government, which is facing serious liquidity problems, to threaten to disband, transform or sell inefficient state enterprises. So far only one enterprise has been liquidated - the Thai Airways Aircraft Maintenance Co, Ltd.

There are many types of problems plaguing state enterprises but two of the most important are the government policy price control and the mismanagement of enterprises. The key to a solution here lies basically with the political will of the government which so far still seems to be lacking in this area.

The clearest example is the case of the BMTA which is the largest money-losing state enterprise with a loss in FY 1980 of 1600 million baht. A large part of the blame for the financial difficulties and poor services of the BMTA lies with the government which does not seem to have a clear-cut policy towards the enterprise. On the one hand, the government has established the BMTA through the use of debt financing instead of equity financing which leads one to think that the government would like the enterprise to operate in a purely business-like fashion in obtaining profits to repay for the loans. On the other hand, the government has been quite reluctant in allowing bus fare increases in spite of rising costs of fuel, materials and wages. This has led to uncertainties concerning the existence of the enterprise and may have exacerbated the solvency problem of the enterprise. It has also hampered the possibility of any large scale investments to help improve its services since no financial backing is readily available. In an attempt to partially solve the problem of who should subsidize the BMTA, it was placed under the jurisdiction of the Bangkok Metropolitan Administration in the past year.

A large part of the BMTA's troubles also lies in its mismanagement. It is well-known that the enterprise's employees siphoned of a large proportion of the firm's revenues. The services provided are also inadequate and of low quality. The solution here lies in a strong management team which would help cut down operating costs significantly. Instead of attacking this problem head-on, the past year once again showed the government's lack of determination and urgency in this area with its appointment of an acting managing director who does not have any management expertise, in spite of a public outcry from all directions.

The problem of the BMTA as mentioned above is not unique. It also applies to other enterprises such as the SRT which lost 500 million baht in the last fiscal year, the MWWA which lost 775 million baht in FY 1980 and the ETO which lost 49 million baht in FY 1980. Instead of disbanding these state enterprises, the government should seriously consider abandoning its past policy of making political appointments to the board of these enterprises together with the courage to replace the management teams of such enterprises if they do not perform well. Otherwise, there is no one else to blame but the government itself.

A redirection of agricultural policy is needed

Agricultural development in the past has centered on the provision of infrastructure such as irrigation facilities and roads which require large public investment outlays. Such a policy has been maintained up to this day. The FY 1982 budget of continues to see a large chunk or 8165 million baht of the budget devoted to irrigation. This is about 60% of the budget allocated to the Ministry of Agriculture and Cooperatives or 5%

of the total public budget. It is, therefore, rather disappointing to see that there has been no effort to directly recoup such investments especially when this action can be supported on both efficiency and equity grounds.

The collection of fees or taxes from the use of irrigation facilities can help make the utilization of scarce water resources more efficient or less wasteful. The funds collected can in turn, be re-invested in other areas where irrigation facilities are still lacking, thus, helping to diffuse agricultural development at a faster pace. However, such a policy has not been employed by the government. The result is not only a slower pace of agricultural development but an increasing pressure on the public budget.

The justification for a direct tax on those farmers who have gained from agricultural development is even stronger when we consider that there are many cases where these gains have come about at the expense of other farmers. One example is the construction of various dams in the past which have diverted the flow of water resulting in some previously fertile areas having insufficient water supply for farming while other areas receiving such water benefitted greatly. Examples of the former include Ayudhaya and Pathum Thani with the latter including Nakorn Sawan and Singburi.

On top of this, the construction of dams has slowed down the flow of water into the sea considerably which has caused seawater to flow back up the rivers into provinces along the coast resulting in serious damage to farms and orchards. This was most evident during the drought two years ago when there was a conflict between the release of water for farming purposes and the storing of water for electricity generation. Funds are, therefore, needed to help redevelop the adversely affected areas so as to reduce the hardships and conflicts which may result.

The present indirect taxation of agriculture through export duties is an undesirable method to recoup investments since those who did not gain or may even have lost from such investments are also made to pay. The net implicit tax burden, taking account of both benefits and costs falls most heavily on the least-developed farms which is contrary to the rural development policy.

The inequitable effect of the export tax on agricultural products is not only confined in the rural sector. With Thailand being considered small country in world markets, the export tax has the effect of reducing the domestic prices of these products especially rice which is the main staple of the country. The low price of rice constitutes a subsidy provided to consumers especially those in urban areas who do not produce their own rice. Such a tax may, therefore, be considered to be one of the most, if not the most, inequitable or regressive tax collected in Thailand. It taxes the poorer rural masses while subsidizing the richer urban minority.

The low domestic price of rice from an export tax has also been said to encourage more local consumption leading to a smaller available surplus for export. Furthermore, the tax reduces the incentive to produce, leading farmers to switch to crops which may have generated less income for the country.

It is therefore encouraging to see the Foreign Trade Department (FTD) being forced into abolishing export quotas and minimum price controls on the export of rice and maize in addition to the reduction in the rice premium and rice reserve requirement during the latter part of 1981. This has also helped to reduce a source of governmental policy contradictions of promoting local farm price support programmes which are intended to increase farmers' incomes and export controls and duties which reduces the incomes of farmers.

Against this backdrop, though, there still remain other issues of concern. First of all, the free trade policy presently adopted applies only until the end of 1982 . It may still be possible for us to see the return of export restrictions in full force especially when those in the FTD are not too happy with the present policy.

Secondly, the FTD may yet sabotage the policy of free trade through the introduction of other less visible measures. An example of such an action may be the restriction placed on exporters of selling only to FTD designated buyers in foreign countries. Such a case has baken place in the maize trade to Hong Kong in the second half of 1981. This is just about one of the most ridiculous measures undertaken by this public agency. It is tantamount to reducing the competition for the purchase of Thai maize and forcing the left-out importers in Hong Kong to switch to other sources of supply.

Thirdly, the government order to rice exporters to set up rice buffer and working stocks of 500,000 tons at their own costs can be considered as a form of export taxation whose burden will be shifted back towards the form of a lower farmgate price of rice.

Lastly, there are still serious doubts concerning the government's success of guaranteeing a minimum price for agricultural products. Since the government does not have sufficient money, these piecemeal actions may have again benefitted only a small proportion of farmers. It is suspected that farmers who gained are those who are in more developed areas due both to a better transportation and information network system. Corruption and bribery may also result due to competition for the limited funds available and especially when the guaranteed minimum prices are much higher than those offered by private traders.

Since the policy in the Fifth Plan will require a large outlay of funds for rural development, it is imperative that they be spent wisely. It can only be hoped that the government would, through hindsight, be more careful in formulating programmes and investing in projects especially with regard to their indirect side effects together with creating an environment which is conducive to the development of the agricultural sector as a whole instead of the few privileged farms.

Investment policy

Prime Minister Prem Tinsulanond took a number of trips abroad during the second half of 1981 to help promote foreign investments and raise additional development assistance loans for the country. The most important trips were naturally to the US and Japan. Heavy emphasis during these trips has been placed on creating a favourable impression of Thailand among the business communities of these countries visited. For, after all, the Premier took along with him a large contingent of prominent local businessmen.

At one point during the US trip, the Prime Minister was quoted as having cited the reduction of the corporate income tax rate and the elimination of retroactive tax assessments as examples undertaken by the government to help promote foreign investments in the country. However, events soon after that must really be an embarrasment for the Premier. Not only was there a retroactive assessment of taxes on the import of raw materials for type manufacturing, but one of the deputy premiers was also quoted in the press as attacking the "hardnosed and hard-boiled business practices" of American companies. Although the former issues has already been resolved, the Customs Department ruling has not been clear cut enough and may yet lead to a difference of interpretation of the Customs Code in the future. As for the latter issue, it is rather disappointing for one to see so important a government figure not understanding the general practices undertaken by businessmen irrespective of nationalities.

Industrial policy

There were some interesting developments on the industrial front during the second half of 1981. One of these is the conflict which arose between the Board of Investment (BoI) and the Ministry of Industry (MOI) concerning the steel industry.

In this case, the BoI wanted to impose a 10 import surcharge on billets over the import tariff of 10% to protect the few large local steel mills under BoI promotion while the MOI rejected the move on the ground that it would adversely afiect some 40 small rerolling steel mills each with an investment of under one million baht. Furthermore , the MOI, against BoI objections, issued a license allowing the Bangkok Steel Industry (BSI) group which had earlier been unable to obtain BoI promotional privileges to invest over 450 million baht in two new factories producing galvanized corrugated iron sheeting and tinplate.

It is heartening, in this instance, to see the MOI standing up against the BoI which for years has had a bias of promoting only large scale producers using expensive capital-intensive technology which may not be suitable to the resource endowments of the country. To make matters worse , BoI promotional efforts, besides giving promotional privileges, have tended to include the limitation or annihilation of any remaining competition to the promoted firms, thus, leading to many inefficient local industries which are unable to compete with foreign producers and whose survival depended mainly on the high protection wall built up by the BoI.

The steel case seems to show this quite clearly. Even without BoI promotional privileges, the BSI is willing to undertake the risks of making a large sum of money unless they are rather certain of favourable returns. Even if they should be that foolish, it will be difficult to obtain financial backing and services from banks or investment houses. It is difficult to understand how the BoI will be in a better position to assess the profitability of a project than those who have a stake in the project. The duty of government agencies should be confined to the review of whether a firm would generate undesirable externalities to the economy and society, such as, pollution congestion and others.

Another policy conflict which took place between government agencies in the latter part of 1981 is that concerning the automobile industry. The National Economic and Social Development Board (NESDB) would like to see a milder level of protection for this industry through the repeal of a ban on fully built automobile imports while increasing the present local content requirement of 25% to 40%. The MOI, on the contrary, is pushing ahead for additional protection through an increase in the domestic content requirement from 40% to 45% while maintaining the import ban of fully built automobiles.

In both the steel and automobile cases, the provision of protection to the industries may be said to go against the emphasis given in the Fourth and Fifth Plans of promoting export-oriented industries which are able to compete with foreign producers instead of the import-substitution industries which require significant protection as in 1960's. Furthermore, the greater degree of competition through an export-oriented industry is more in line with a basic governmental policy of reducing the cost of production of industries in order to hold the line on product price increases.

There is one other case concerning industrial policy that is worth mentioning and rather puzzling for that matter. In a move which is difficult to understand, the MOI has let it be known that there will probably be no levying of the 45.67% profit-sharing scheme on the export of Mekhong whisky similar to that existing on domestic sales. The explanation given was naturally to help promote the export of excess whisky. But any serious student of economics will know that a tax on profits will not make any difference on the decision to export or not to export. Only taxes which affect the price of whisky, such as, a sales tax or an export duty, are effective in doing so. In addition, if ever there were to be a short fall in the production of Mekhong whisky, it may be expected that foreign markets will be supplied prior to the local market since profits earned from exports are not taxed. This may be the export promotion or, in effect, local shortage promotion they were talking about.

The new plan

FY 1982 witnessed the advent of the Fifth Five Year Economic and Social Development Plan. The plan was highly publicized and touted by the government, thus creating a great deal of public interest, attention, discussion and hope. However, there are still reservations concerning the plan and its actual implementation.

First of all, if history is any guide, the plan may yet turn out to be little more than a well-written document without much binding effect on the public agencies charged with the implementation of governmental policies. Take for example the goal set in the new plan of promoting a greater role for private business in national economic and social development. It is difficult to envisage how such a role can be increased over past plans which had always strongly advocated the free enterprise system. The greater role advocated in the Fifth Plan is therefore partial evidence in itself of government interference with the role of the private sector during past plan periods. The suspicion is that we may yet find history repeating itself here.

Another example in the present plan is the goal of increasing government revenues to 18% of GDP from the existing 14% through the improvement of the tax structure and tax administration. It has been stated in the plan that new taxes such as the inheritance, value-added , capital gains and property taxes will be collected. Past experience in this area has raised serious doubts about the government's political courage in this area.

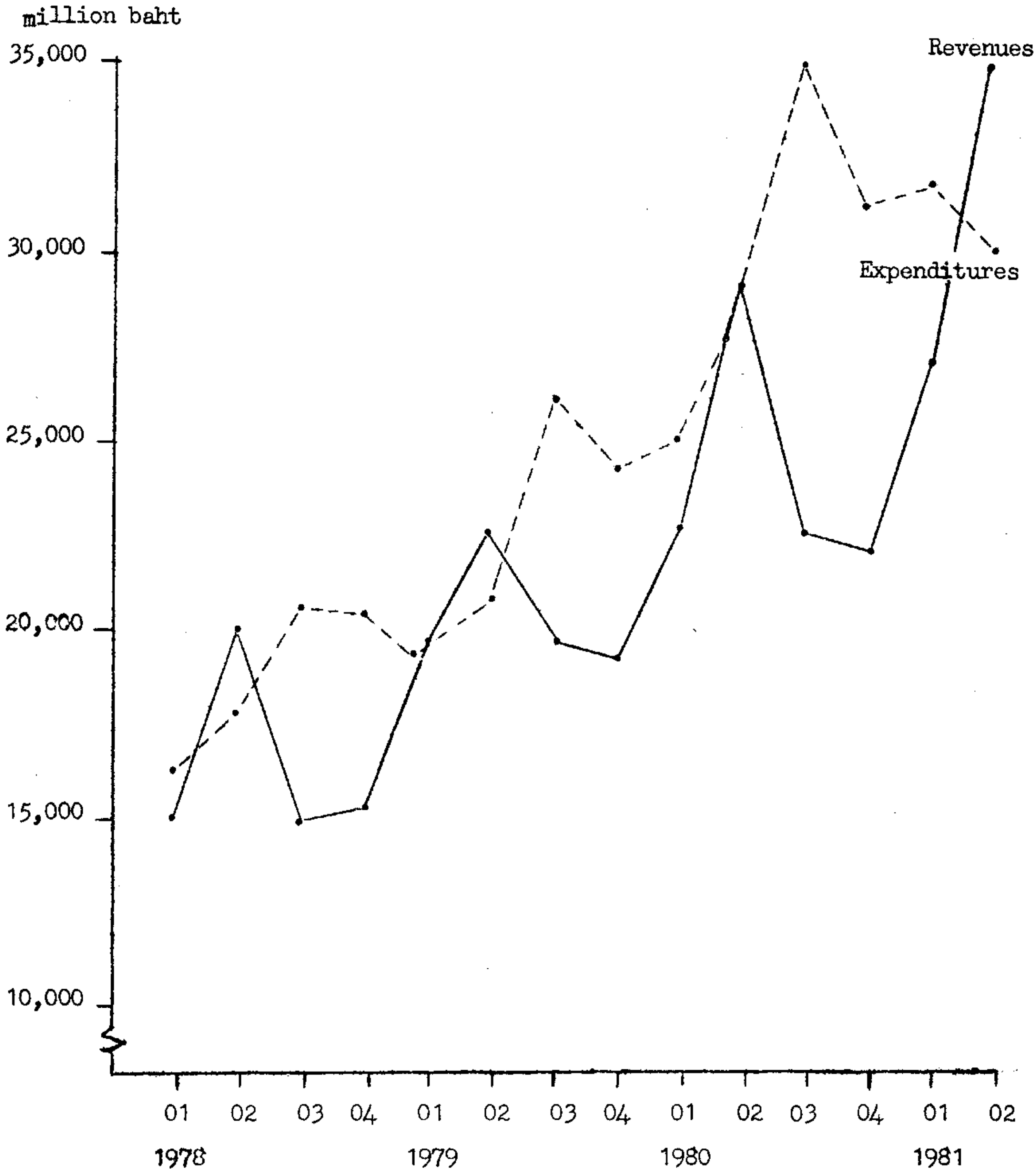
Secondly, history has shown time and again that there is a lack of understanding of the consequences and potential of different measures in reaching the stated goals. The control of primary exports is one of the clearest examples. Such results may be due to the tendency of past plans in giving attention mainly to goal formulations without spelling out in clearer details some of the specific measures which could be undertaken to reach them. It is therefore good to hear from the government that the Fifth Plan has given more attention in this area.

Thirdly, plans have a tendency to be written with the objective of promoting almost everything which is rather laudable. But it must be recognized that resources are limited contradictions can result from the lack of emphasis. An example in the Fourth Plan is the simultaneous promotion of import-substitution and export-oriented industries. There must therefore be a clearer emphasis on which set of problems or issues the government will give priority in tacking.

Lastly, it is rather striking to see defense spending increasing significantly in the Fifth Plan. The target set is an increase of resources up to 4.4% of GDP or 24% of total public spending from the present 3% and 19.20 %, respectively. This is rather high when compared to the US and Japan which has a defense sh share in GDP of only about 5% and 1% respectively. It seems that social and economic development has been given a back seat to defense spending in the plan which may have serious long term consequences.

In closing, there may still be doubts concerning the Fifth Plan. But this is not to say that it is a bad plan. The emphasis on rural development, income distribution, structural adjustments in industry, alleviation of poverty, a greater role for the private sector and others are all aceptable goals. The question is on what policy measures will be employed and how will contradictions which arise be solved. But the most important question left unanswered is how serious will governments of the future be in utilizing the plan as a frame-work for setting their actual policies.

Public expenditures and revenues



Budgetary deficits, October - July *

(in million baht)

FY	Expenditures	Revenues	Deficit
1976	41915 (66.9)	34172 (78.4)	7743 (40.7)
1977	50753 (73.8)	42262 (83.4)	8490 (46.1)
1978	59073 (72.9)	52032 (83.9)	7042 (37.1)
1979	69052 (75.1)	62465 (86.8)	6588 (32.9)
1980	89814 (78.4)	77133 (83.2)	12683 (58.0)
1981	104528 (74.7)	92278 (76.9)	12250 (61.3)

* Figures in parenthesis are percentages of the total value set in the budget for that fiscal year.

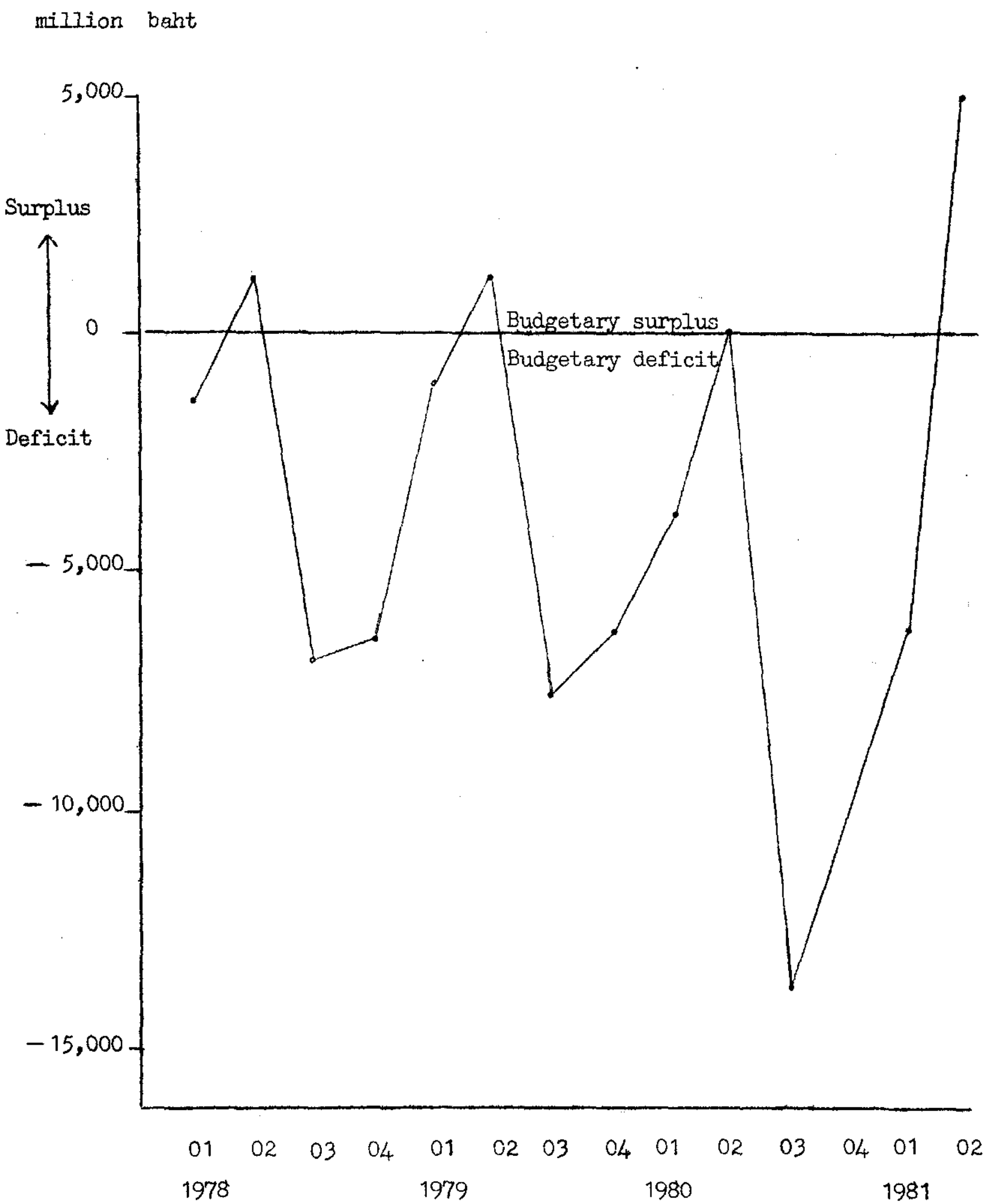
Source: Bank of Thailand

Percentage distribution of budget allocations

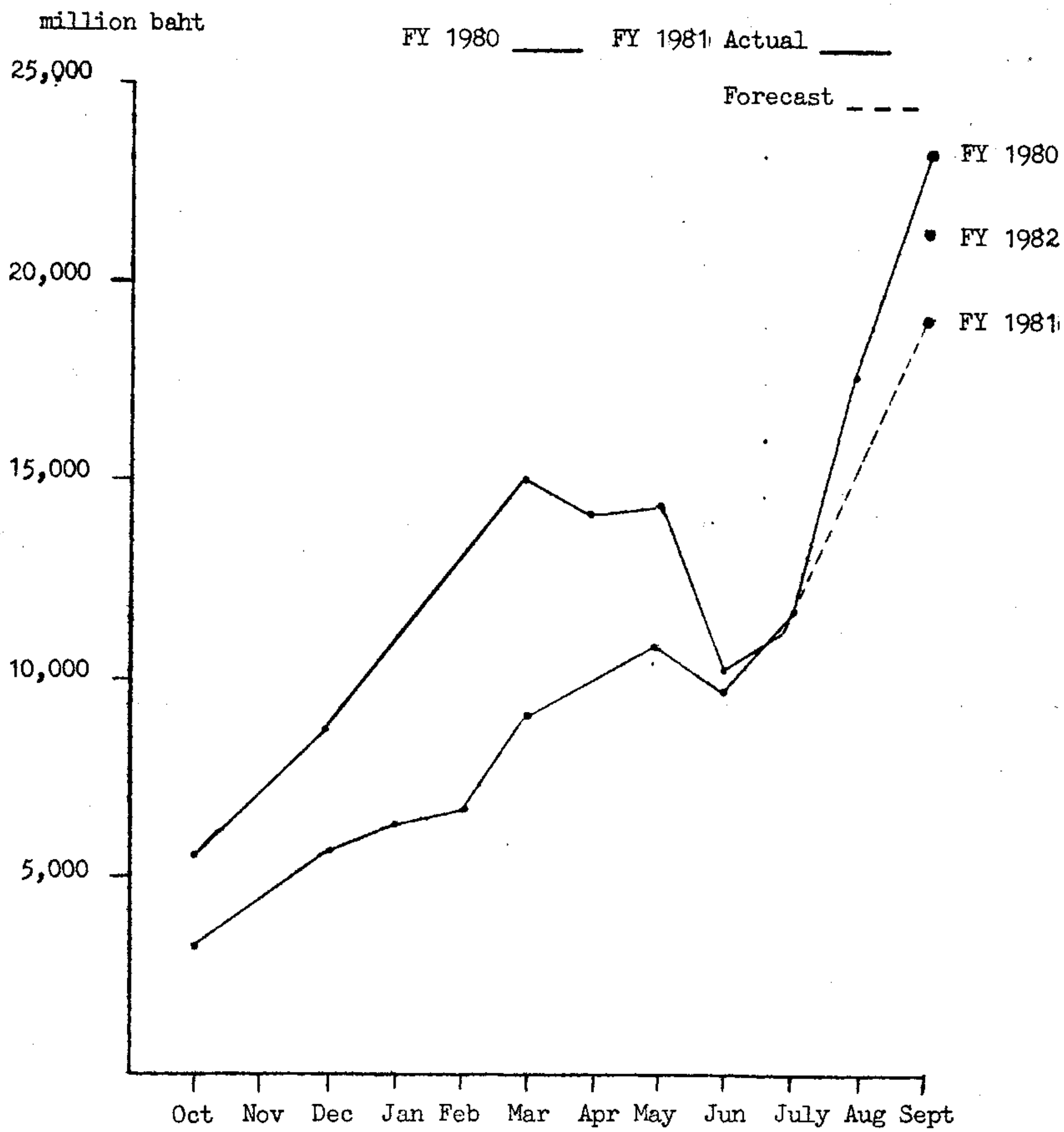
Major Function Classification	FY 1981	FY 1982
Social services	30.8	30.6
Economic services	23.0	20.5
Defense	19.8	19.5
Debt repayment	12.5	13.0
Others	13.9	16.4
Total	100.0	100.0

Source: Budget Bureau

Budgetary surplus



Annual cumulative budgetary deficits



Percentage of government revenues

Types of Revenues	1976	1977	1978	1979	1980	1981*
Direct taxes						
Personal income tax	7.0	7.0	8.2	8.0	7.6	8.4
Corporate income tax	8.6	8.7	9.9	10.0	10.0	14.4
Indirect taxes						
Import duties	21.8	23.0	22.5	22.0	20.3	19.1
Export duties	3.1	3.1	3.0	3.8	3.5	3.0
Business taxes	21.4	21.3	20.9	19.3	19.2	18.1
Selective sales taxes	20.0	19.1	18.5	20.7	22.3	19.2
Others	8.2	9.2	9.4	9.9	9.5	6.5
Non-tax revenues	9.9	8.6	7.6	6.4	7.6	11.4
Total	100.0	100.0	100.0	100.0	100.0	100.0

* Jan-Jul. only

Source: Bank of Thailand