Economic Crises of Thailand

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Abstract: ***While Thailand is presently the second largest economy in Southeast Asia it experienced an economic crisis in 1997. The crisis in Thailand was mostly owing to the heavy export driven economy and financial liberalisation undergone by the country at an inopportune moment. The lack of proper government actions at the time was what made the crisis a sovereign debt crisis. In this paper, data from IDS has been taken and has been used to graphically depict the debt indicators of Thailand.***

Keywords: Financial Liberalization in Thailand, Asian Financial Crisis, Sovereign Debt Crisis of Thailand

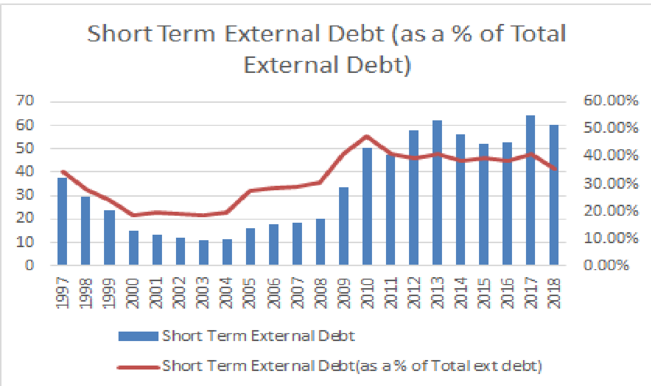
1. Debt Analysis of Thailand

Thailand Economy

The economy of Thailand is dependent on exports, which accounts for more than two-thirds of the country's gross domestic product (GDP). Thailand itself is a newly industrialized country, with a GDP of 16.316 trillion baht (US$505 billion) in 2018, the 8th largest economy of Asia, according to the World Bank. Thailand is the second-largest economy in Southeast Asia, after Indonesia. The GDP of Thailand as of 2018 was 506 billion US dollars. While the country had experienced a financial crisis in 1997 it has since come a far way in developing.

Major Debt Indicators

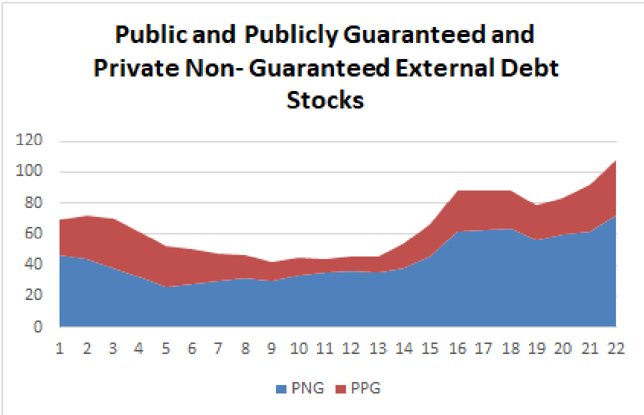
Even though before 1996, Thailand had a per capita GNP growth averaging more than 8 the economy began to slow down in 1996. The overheated economy was expected to experience a steeper downturn in 1997. Short term external debts defined as those maturing in the next 12 months, amounted to US$36 billion, half of which was from loans from Japanese banks. In fact, in 1997 short term external debt as a percentage of external debt was 34.48%.



Source: IDS Data, Graph created by author

The Stock Exchange of Thailand fell steadily from 816.79 points to 385.25 in 1997 which accounted for a loss of more than half of its value and was at a nine-year low. The Thai baht, dropped 20% in value. It continued its decline and had depreciated by 77% of the fixed raste by the end of 1997.

Massive bad debts had been accumulated because of over lending on the part of private sector financial institutions. While the Public and Publicly Guaranteed External Debt Stocks (PPG) were US$22.32 billion, the Private Non-Guaranteed External Debt was US$47.14 billion. Due to this disparity there was a permanent closure of 56 out of a total of 89 financial companies. Throughout the years the PNG has been higher accumulated than PPG. Thailand's economic growth relied mostly on excessive private debt viz-a-viz public debt. Out of the total external debt 70% accounts for private debt.



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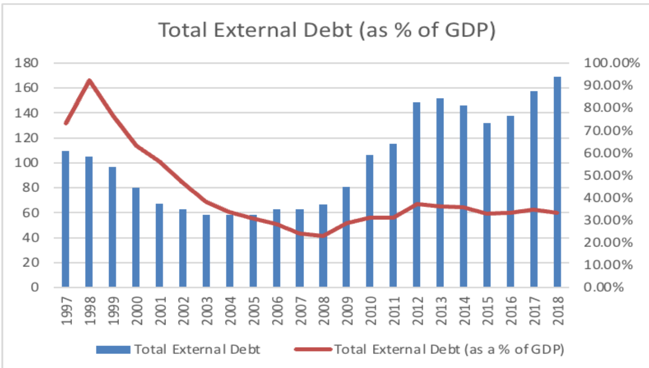
During their boom years Thailand did not use the increase in equity to lower debt dependence but rather it was used to leverage more debt. Total External Debt formed 73 percent of the GDP in 1997 and 92.32% in 1998. In contrast, the Total Reserves as a percentage of GDP were 17.43% in 1997 and 25.36% in 1998. Not only that, the total reserves in comparison to public debt in the period of financial crisis were low. Total reserves as a percentage of total external debt was 23.86% in 1997.



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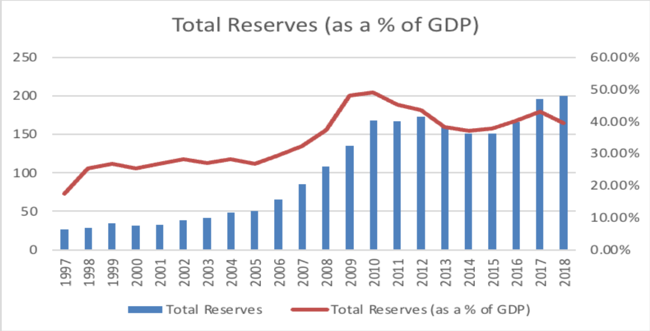

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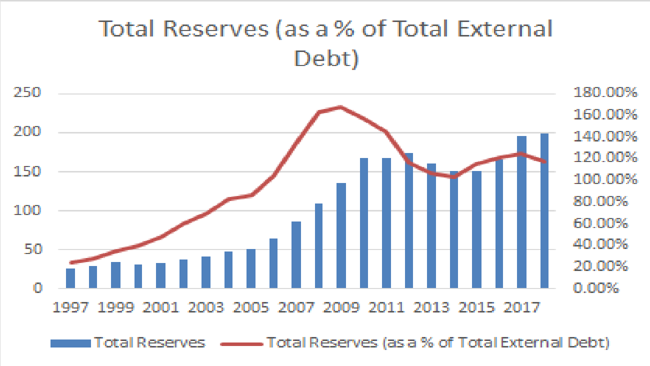

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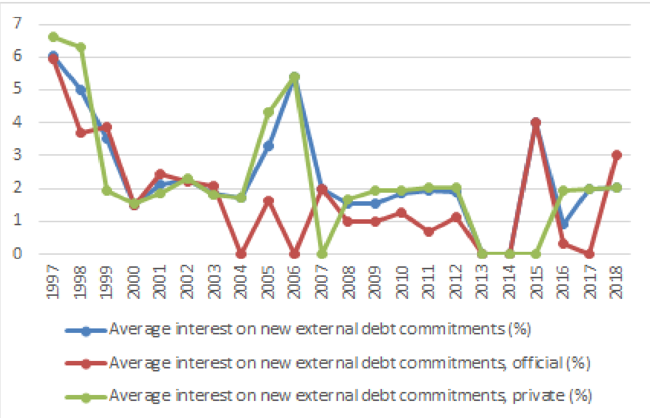
The average interest on new external debt commitments was higher for the private players than the official players. In 1997, average interest on private debt was 6.63% while that on official debt was 5.9%. Over the years, in Thailand average interest on new external debt commitments has been higher for the private players as compared to the official or government concerns.



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The Crisis

The devaluation of the baht was what led to the Asian Financial Crisis. The crisis was rooted in several threads of industrial, financial, and monetary phenomena. In general, many of these relate to the economic strategy of export led growth that had been adopted across developing East Asian economies in the years leading up to the crisis. This strategy involves close government co-operation with manufacturers of export products, including subsidies, favorable financial deals, and a currency peg to the U.S. dollar to ensure an exchange rate favorable to exporters.

While this benefited the growing industries of East Asia, it also involved some risks. Explicit and implicit government guarantees to bail out domestic industries and banks; cozy relationships between East Asian conglomerates, financial institutions, and regulators; and a wash of foreign financial inflows with little attention to potential risks, all contributed to a massive moral hazard in East Asian economies, encouraging major investment in marginal, and potentially unsound projects.

Thailand much like the other Asian economies followed a similar economic system. The focus was more on private financial institutions. Even during the financial crisis, the central bank decided to provide private financial institutions with a bail out of $11 billion without assessing their assets and liquidity problems.

Before July 1997, Thailand still pegged the value of baht to a number of currencies, out of which more than 80% weight was attached to the USD. In the early 1990s, an attempt was made to abolish the ceiling of interest rates to achieve Financial Liberalisation. The numbers of financial institutions were also increased to promote competition. In 1993 the Bangkok International Banking Facilities were created to lure foreign funds through the provision of tax incentives. This ended in 1995 with the overheating of the economy, raising price levels and unsustainable current account deficits.

The expansion of credit in the economy became exceptionally large. The premature liberalization policy had made any attempts by the Central bank to regulate and supervise the complex financial transactions permissible under financial liberalisation. As a result the financial system weakened due to the presence of credit concentration. The problems with the failing financial institutions also bring up an important failure of the bank. Their decision to inject bail outs in failing institutions in order to avoid bank runs did not prove fruitful. The result of their actions had contagion effects on domestic markets and raised domestic interest rates. The apparent lack of strict regulations of financial institutions can be prudently termed as a cause of their very failure.

Source: IDS Data, Graph created by the author

While the Thai exports increased in 1994 at the rate of 22.2%, in 1996 exports suddenly declined by 1.9% and 0.2% in dollar and baht terms. This sharp decline stemmed mainly from the United States, Japan, and Singapore. The sudden decline of exports was mainly because of the recession in Japan and its increased consumption tax that led to a decline in Japanese demand for imports. The shock also further had an impact on Singapore which further reduced its demand for imports from Thailand. The sudden slump in Thai exports can be seen as Debt Servicing as a percentage of exports was at only 15% in 1997. This sudden slump led to speculative attacks on the baht because of a rumour in Hong Kong regarding baht devaluation in response to the large current account deficit and poor export performance (Nidhiprabha, 1998).

The devaluation of the baht led to a period of recession in 1998. By the end of 1997, the total short-term debt was US$37 billion, while the long-term debt amounted to US$67.2 billion. The currency crisis is reflected in a widening current account deficit, which was as high as 8% of GDP in both 1995 and 1996. In 1997, it dropped sharply to only 0.8%.

The IMF imposed stringent conditions on the fiscal standing of US$17.2 billion bailout programme stipulated that the fiscal budget must be in surplus at least 1% of GDP. However after realising that the fiscal restraint imposed had plunged the economy into further recession, it was conferred to increase it to 3%. Still it was not enough to defer Thailand's recession.

Sovereign Debt Crisis

While banking crisis is not an uncommon phenomena the Chavalit government at the time, dithered when decisions were needed. The failure of the Government to handle the economy reproved the public confidence. Regardless of the IMF intervention, the economy further went into a period of recession. The situation where the debt crisis is only exacerbated by the Government's failure to recognise the problem and act on it gives way to a sovereign debt crisis.

It was only later when the then Prime Minister resigned and a democratic led coalition was elected. Under Prime Minister Chuan Leekpai, greater public confidence especially in the economic ministers was prevalent. Also, in October 1997, the constitution was ratified under which an attempt was made to limit the influence of money on the Thai politics.

Concluding Remarks

The debt crisis in Thailand was mainly owing to the premature timing of financial liberalisation. The amount of debt accumulation on the hands of financial institutions and the lack of regulatory framework on them paved the way for the financial crisis to hit Thailand. However over the years the Total External Debt as a percentage of GDP has fallen considerably to an average of 30% which is a big difference from the situation in 1997 and 1998.

References

[1] Nidhiprabha, B. (1998). Economic crises and the Debt-Deflation episode in Thailand. ASEAN Economic Bulletin