ECONOMIC GROWTH AND SOCIAL WELFARE: EXPERIENCE OF THAILAND AFTER THE 1997 ECONOMIC CRISIS *

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1. Introduction

In July 1997, Thailand became well known as the country that started a currency crisis that quickly spread to neighbouring countries in East Asia and, later, to other parts of the world as well. Many economic experts were quite embarrassed about this because, up until that time, they had had high praise for the way Thailand and other East Asian economies had grown and developed. These experts have since tried to understand the causes of this crisis and suggested ways to avoid the same crisis in the future. ¹ This crisis has also brought about new ways of thinking about present and future development policies in Thailand, especially policies with respect to the trade-off between overall growth of the economy and the level and distribution of economic welfare among the Thai people.

Undoubtedly, the crisis of 1997 has hurt or affected different people differently. Some were hurt more, some less, and some may even benefit from it. But one message from the crisis is clear: the government could not remain inactive and let different segments of the whole population face their own economic consequences. For those citizens in the financial sector who directly benefited from the booming economy and who were involved in causing the economy to collapse, the government should mete out some punishments so that they will be deterred from committing the same mistakes again. At the same time, the government should spearhead institutional and structural reforms that provide legal, economic and regulatory frameworks that help or facilitate economic governance in both public as well as private or corporate sectors to prevent similar crisis in the future, or to lessen the impact in case crisis is unavoidable. For those citizens who were less well-off, and usually victims of the crisis, the state should provide better protection against future economic calamities and a system of economic and social safety nets that cushions the fall of these people. The 1997 crisis has brought about concerns on these issues which have hitherto been neglected or ignored in the Thai modern economic history.

This paper aims to discuss basic development philosophy of Thailand that has brought about impressive growth to the overall economy and increase in average income of the people and reduction in the incidence of poverty, and at the same time has part in causing the recent economic crisis as well. This is done in Section 2. Section 3 discusses economic events and conditions that brought about economic crisis in 1997. Section 4 continues to discuss the ways the government had tried to solve the

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¹ Thai scholars and researchers who had worked on Thai economic crisis include, for example, Ammar Siamwalla and Orapin Sobchokechai (1998), Somsak Tambunlertchaai (1999), Sauwalak Kittiprapas (1999), Medhi Krongkaew (2001), and Ammar Siamwalla (forthcoming).
country’s economic problems. Section 5 describes and evaluates economic policies of the present government that address both issues of economic growth and stability, and social protection and safety nets. Finally, Section 6 concludes with some important policy implications. It is hoped that the Thai experience could give a unique and interesting guideline to those who look for policy mix that helps generate satisfactory economic growth and sustainable social welfare at the same time.

2. Basic Philosophy of Thai Development and Its Outcomes

Thailand was a low income, low growth economy at the end of the 1950s. Close to 85 per cent of the total population were engaged in agriculture of which rice the major agricultural product. Its main exports consisted of rice, rubber, teak and tin. Then its leaders decided to move the country quickly along the path of modern economic development emphasising import substitution and later export promotion. With the help of the World Bank in preparing its first national economic development plan, Thailand adopted market approach to economic development.

Since its inception in 1961, Thailand’s National Economic (and later, Economic and Social) Development plan has played an important part in transforming Thailand from a poor, agrarian society to a middle-income newly industrialised country. The Thai government has done this through a combination of private economic investment and expansion, with the government providing infrastructure support and certain investment incentives. This is in keeping with the development thinking at the time when growth was the most obvious and probably the most important objective of economic development, and investment or capital formation is the most important means to that end. No doubt, plans after plans concentrated on growth and economic expansion. When growth slowed due to external and internal problems, the government would react to stabilise the economy so that growth returns in the shortest of time. Therefore, the development experience of the Thai economy during last three decade has seen alternate emphases on growth and stability, with occasional concerns on other areas such as poverty alleviation, income inequality, energy shortage and environmental degradation thrown in, but the growth orientation of the national economic and social development plan was never in doubt.

Then in mid-1990s things began to change. As early as the 3rd Plan, the development philosophy and strategy of Thailand were already criticised for not paying sufficient attention to the problems of poverty and inequality, environment degradation, and social protection. This was partially corrected in the 5th Plan where the issue of poverty was specifically addressed via a special addendum of operational plan on rural poverty reduction. In the 8th Plan, economic growth was no longer the final objective of the country’s development efforts. It was but one of the many factors that worked towards people’s development, and the development of people leads to enhancement of the capabilities of communities, society and ultimately of the nation. This development strategy is new for Thailand. The earlier emphasis on economic growth has changed. People will now be at the centre and development will revolve around them.

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2 The 1st Plan was a 6-year plan covering the periods 1961 to 1967. Subsequent plans were 5-year plans, including the current one, the 9th Plan, for 2002 to 2007.
Unfortunately before this 8th Plan was put in operation, the crisis struck. The whole five years of the 8th Plan were spent, not on achieving its intended goals and objectives, but on how to get the Thai economy out of the deepest recession in its modern history. At the end of the 8th Plan in 2001, the economy is said to have recovered and is strong enough to consider a new development philosophy and strategy. This new development policy is Sufficiency Economy proposed by His Majesty, King Bhumibol Adulyadej. Box 1 describes the essence of this Philosophy of Sufficiency Economy. It appears that the government has become more careful about how to generate and manage economic growth. The spirit of the Sufficiency Economy has become the guiding principle of the 9th Plan currently under operation.

The success of Thailand in its economic development efforts since the early 1960s was quite extraordinary. The economy grew on average about 6 per cent per annum in real term during the first 25 years of development since 1961 (see Chart 1). In mid-1980s, Thailand suffered some external balance problems which required it to devalue its currency several times, and had to seek credit assistance from the IMF. But in the latter half of the 1980s, Thai economy recovered quickly. The devaluation in 1984 helped increase Thai exports; the influx of Japanese foreign direct investment as a result of yen appreciation following the 1985 Plaza Accord helped speed up domestic manufacturing; and the success of Thai tourism industry in 1987 helped bring in vast amount of foreign exchange earning. While the growth rate of the economy from 1981 to 1986 averaged about 5 per cent per annum, the growth began to jump up in 1987. In 1988, Thailand achieved the highest growth rate in the world for that year at 13.2 per cent. This double-digit growth rate continued for three years ending in 1991. From 1991 to 1995 the growth rate of GDP ranged between 8.1 to 8.9 per cent. The economy began to experience difficulties in 1996, leading to the collapse in 1997.

**Chart 1: GDP Growth of Thailand, 1962 to 2001**

![Chart 1: GDP Growth of Thailand, 1962 to 2001](image)

Source: NESDB, *National Income of Thailand* (various years)

While the growth of the economy is normally depicted by the rate of growth of GDP like that shown in Chart 1, it is probably more instructive to show the welfare of the people through the increase in their household or individual income. The disaggregated household or individual income cannot be obtained from the National Income Account; it has to come from a special survey. The National Statistical Office (NSO) of Thailand has been collecting household income and expenditure data since
1962/63. These surveys form the database in which poverty incidence in Thailand can be calculated. Table 1 shows the relationship between the changes in these household income and poverty incidence in Thailand from 1962/63 to 1998.

There are two series of data in Table 1. The first series shows the household income per capita from 1962/63 to 1986, and the corresponding poverty incidence (head-count ratio) for the same time periods, and the second series shows the same set of information from 1988 to 1998. The main difference between these two series is that the first series uses the poverty line that was originally estimated by the World Bank for its poverty study in Thailand in 1975 (see World Bank, 1980). This calculation of this poverty line for Thailand was based the nutritional requirements for an average Thai, the consumption habit and patterns of Thai households, and the prices of food and non-food items that existed in the early 1960s.

This poverty line was adjusted with inflation index each time a new study is undertaken until early 1990s when many researchers felt that the structure of population, the nutritional requirements, the consumption habit and patterns of the people had changed sufficiently to the point that a new poverty line was needed. Therefore, in 1996, Kakwani and Medhi (1996) computed a set of new poverty lines for Thailand using new nutritional requirements, new age structure of the Thai population, and spatial price differences across the regions. These new poverty lines vary according to the size and age compositions of members in the family, and the location where these families live. These new poverty lines were applied backward to the situations in 1988. Therefore the new poverty series that starts in 1988 represents the most up-to-date poverty measurement in Thailand at present.

At this juncture, it is interesting to look at the simple relationship between economic growth and poverty reduction. Assuming that economic growth raises income of the people, and the increase in income pushes the people out of poverty, it is very obvious from looking at Table 1 that there exists a clear relationship between the increase in household income and the reduction in the incidence of poverty in Thailand. As will be mentioned later, this reduction in poverty in Thailand did not come about as a result of any specific, well-targeted poverty reduction policies or measures. It could be safely concluded that poverty reduction in Thailand has come as a result of an overall economic growth. ³

Prior to 1988, the NSO conducted the nation-wide socio-economic survey (SES) irregularly about once in every five years or so. From 1988 onward, however, the

³ A simple regression of head-count ratio (HCR) on household income per capita (Yp) on the two series gives the following results:

For Series 1: $HCR = 53.920 - 0.0036 Yp$  
$R^2 = 0.659$  
$(7.123)$  
$(-2.409)$

For Series 2: $HCR = 43.2675 - 0.0109 Yp$  
$R^2 = 0.9827$  
$(25.193)$  
$(-13.052)$

The figures in parentheses are t-values.
government had asked the NSO to conduct this SES every two years. Professor Nanak Kakwani of the University of New South Wales in his work with the NESDB had made an extensive use of these SES data, and had produced the results of his studies in a series of newsletters issued by the NESDB itself. Table 2, for example, shows the overall poverty situations for the whole kingdom from 1988 to 1998 (with preliminary information on 2000 added). Three kinds of poverty measures are reported here: poverty incidence or the head-count ratio which shows the percentage of the poor in the total population, poverty gap ratio which shows the extent to which the actual income of the poor had fallen below the poverty threshold relative to that poverty line, and the severity of poverty index which shows how serious and how concerned the society is towards the existing poverty by giving more weight to income movement among the poor.

(Table 2 about here)

In general, the lower these indices are the better in terms of poverty alleviation. On the Head-Count ratio or the percentage of the poor in total population, it may be seen that the percentage of the poor in Thailand had fallen from 32.6 per cent in 1988 to 11.4 per cent in 1996 before rising to 12.9 per cent in 1998 mainly as a result of the economic crisis. Professor Kakwani had estimated the trend of this poverty improvement and predicted that had it not been for the crisis, the poverty incidence for the whole kingdom in 1998 would have fallen to only 10.8 per cent. The fact that the actual poverty incidence in 1998 was 12.9 per cent means that the impact of the crisis had caused the poverty incidence to increase about 19.7 per cent. In terms of the number of the poor during crisis, the last column in Table 3 shows that, without the crisis, the expected number of the poor would be 6.4 million. The fact that the actual number of the poor was 7.9 million means that there was a 22.3 per cent increase in the number of the poor between 1996 and 1998 (about 1.5 million people).

Somchai and Jiraporn (2001) provided additional information on poverty incidence in 1999 and 2000. In 1999, the NSO conducted a special socio-economic survey for smaller sample size throughout the country (about half the size of 1998) in order to check and monitor the seriousness of the crisis on income and expenditure. The results had shown that although the average poverty line for 1999 was lower at 881 baht per person per month (due mainly to lower prices), the loss of income during the year caused the incidence of poverty to increase to 14.6 per cent. By the end of 1999, the employment situation in Thailand had improved, and large amount of public

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4 Information on poverty incidence (and income distribution) from 1988 to 1998 was obtained from Kakwani and Medhi (1996) and NESDB (1999), whereas the additional information of the same for 1999 and 2000 was obtained from Somchai and Jiraporn (2001).

5 The Head-Count Ratio (HCR) is defined as HCR = q/n where q = number of population having income below the poverty line, z; and n = total number of population or income-receiving units. The Poverty-Gap Ratio (PGap) is defined as PGap = HCR \cdot IGap where the Income-Gap Ratio (IGap) is equal to \([z - y^*]/z\) where z is the poverty line, and y* the average income of the poor. This ratio measures the extent to which the poor is far away from poverty threshold. Any transfer from the poor to the rich, while the HCR may remain unchanged would still the IGap.. This shows the proportion of total income or resources necessary to bring every unit below poverty line up to the poverty line. The Severity of poverty index is the same as the Foster-Greer-Thorbecke Index (FGT) which is defined as FGT = \(1/n \sum_i \left[(z - y_i)/z \right]^\alpha\) where y’ is the income of the poor individual, i, and \(\alpha\) is a parameter that measures how sensitive the index is to transfer among the poor units. When \(\alpha = 0\), FGT becomes HCR; and when \(\alpha = 1\), FGT become IGap. The \(\alpha\) value used in this study is 2.
spending had begun to show its multiplier effect, resulting in the proportion of the poor falling to 14.2 per cent in 2000.

It is useful to discuss the distribution of income in the country as well when the issues of poverty is considered. Income inequality can be considered as relative poverty. It is often believed that the distribution of income of a country could become more unequal in the early phase of its economic development but will improve once a certain development level is reached. This is the famous ‘Kuznets Curve Theorem’ which relates the economic development of a country with increasing income inequality (as measured by the Gini index, for example) to produce an inverted U-shaped curve. The income distribution of Thailand exhibited the rising part of the Kuznets curve from the beginning of its modern economic development until 1992 when the Gini index reached the highest point of income inequality and began to fall after that. As shown in Table 3, the Gini index for 1992 was estimated at 0.536, falling to 0.521 in 1994 and 0.516 in 1996 and 0.509 in 1998. In 1999, however, the Gini index had increased to 0.531 or an increase of about 4.3 per cent. In 2000, as the employment situations improved, the distribution of income also improved, and the Gini index for 2000 fell slightly to 0.525.

Also in Table 3 the income share of the overall population was divided in to 5 equal groups or quintiles, ranging from the poorest group (Quintile1) to the richest group (Quintile5). It may be noted that between 1998 and 1999, the income positions of all quintiles except the richest one had deteriorated. This is sufficient to explain the increase in the Gini index between these two periods as shown earlier. In 2000, the income position of the poorest quintile improved slightly while that of the richest quintile fell slightly, but overall the income distribution in the post-crisis period is still very unequal. In the last column of Table 4 we can see the ratio of the richest quintile (Quintile5) and the poorest quintile (Quintile1). The larger of this ratio shows the more unequal distribution of income. Not surprisingly, this ratio for 1999 of 15.2 is the highest.

To conclude, the economic development of Thailand since the First Plan in 1961 had raised the welfare of the Thai people through an increase in their real income during the last three and a half decades. This increase in real income directly reduces poverty across the board in Thailand. However, the distribution of income became more unequal in the early periods of development, reaching the deepest inequality in 1992 before worsened again as a result of economic crisis in 1997. In 1998 when the crisis reached its lowest point, poverty reversed in declining trend and became higher, while the income inequality also reversed itself equalising trend and became more unequal again. The economic crisis of 1997 had indeed created enormous havoc in the normal life of the Thai people. It is an economic event that will forever etched itself in the Thai economic history. We need to know the causes of this crisis and must do our best to avoid it in the future.

3. The 1997 Economic Crisis and Policy Responses

3.1 Causes of Economic Crisis
On looking back, the new economic development in Thailand that started in earnest in 1988 with the establishment of the new government under General Chartichai Choonhavan had created a situation that an economic crisis of some sort could not be averted. It was the crisis that Thailand ‘has to have’. Why? This is because everyone was carried away by the euphoria of economic success and prosperity. Short-term and long-term foreign capital kept pouring in, adding to the economic bubble that was already forming. There is no shortage of analysis on the causes of the Thai currency turned financial and economic crisis. In my own analysis (Medhi 2001a), I have pointed out six factors that led to the crisis, namely financial sector mismanagement, high current account deficit, high domestic interest rate and uncontrolled capital inflows, the rigidity of exchange rate, lack of economic leadership from political leaders, and the decline in export performance.

1. Financial-sector mismanagement. Many banks and financial companies lent excessively, and imprudently, made possible by abundant and cheap foreign sources of money. Much of the loans were spent in the non-productive property and stock markets. The existing state philosophy protected public financial institutions at all costs, creating a grave moral hazard.

2. Current account deficit. Thailand had spent beyond its means; it had to borrow from the savings of other countries to finance its investment and consumption. This overspending became chronic and reached a level thought to be unsustainable (more than 8 percent of GDP in mid-1997), creating uncertainty in its ability to maintain the fixed rate of the baht.

3. High domestic interest rate and uncontrolled capital inflows. High interest rates in the domestic market and low interest rates in overseas markets induced uncontrollable inflows of foreign capital. An excess inflow of foreign capital pressured the local currency to appreciate; subsequently, baht appreciation hurt Thai export performance.

4. Rigidity of the exchange rate. Thailand attempted to practice the so-called impossible trinity, the combination of a fixed exchange rate, freedom from capital controls, and freedom from interest rate control. This was abandoned when the U.S. dollar appreciated in early 1997 as the baht became overvalued and subsequently devalued.

5. Lack of economic leadership from political leaders. Before flotation of the baht, political leaders were kept out of the decision-making process concerning the use of reserves to defend the baht. The existing system had not required close supervision or consultation of top leaders of the country, and leaders were informed after foreign reserves were depleted.

6. Decline in export performance. Increasing costs in the production of Thai exports eroded the price competitiveness that Thailand had over other competitors, especially China. The slowdown in world demand of Thai exports also contributed to the decline in export performance, although the overvalued baht was another factor. With a high current account deficit, the poor export performance in 1996 and early 1997 severely hurt the Thai economy.

3.2 Policy Approaches to Economic Crisis

When Thailand turned to Japan and the IMF for help after the meltdown of its currency in July 1997, it had less than 3 billion US dollars left in its foreign reserve.

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6 As shown in Footnote 1.
More than 30 billion US dollars were lost in the defence of the baht. Japan and the IMF together had managed to raise 17.2 billion US dollars rescue package for Thailand. This package had come with the usual IMF conditionalities. First, the IMF had asked the Thai government to spend less, which had turned out to be a bad advice because the economy contracted further with this drastic cut in public spending. The basis for that advice by the IMF, however, was the fear that the losses from the bail-out of the commercial banks and finance companies would require the government to use enormous amount of public funds to payback to the Financial Institution Development Fund (FIDF), a unit under the Bank of Thailand, which provided the bail-out money in the first place. The government needed all the public savings it could get, and that included the increase of the Value-Added Tax (VAT) from 7 to 10 per cent. This latter measure was also another bad advice because it had caused further contraction, created tax evasion, and hurt the majority of workers and other fixed income and self-employed people.

Other than these two fiscal measures, the other measures were followed by the Thai authority with a better result. First of all, the currency was already floated (devalued), so this part of conditionalities was met. Next, the mismanagement of the financial sector which was at the heart of the problems was tackled immediately and forcefully. Through special legal power, the Thai monetary authority suspended more than half of the finance companies and eventually seized control of almost all of them. A special institution called the Financial Sector Restructuring Authority (FRA) was established to auction off the assets of these failed financial institutions to pay back the debts to the government. The Bank of Thailand also ordered the remaining financial institutions to increase their capital bases, and establish more stringent controls over their loans. In order to help them recapitalise their capital bases, the majority control of foreign financial institutions was allowed. The government also provided public funding for those banks who were having problems with the recapitalisation requirement and would like the government to help in exchange for some public control on the management and operation of those banks. These stringent recapitalisation plans by the Thai government were often criticised for being too stringent, but the government was quite adamant in its intention to enforce these accepted international standards for the future of Thai banking institutions.

On monetary policy, the Bank of Thailand had kept a watchful eye over the fluctuation in the exchange rate. Domestic interests were kept high when the baht was weak, and low when the baht was strong. Domestic money supply was also under close scrutiny by the Bank of Thailand so that the appropriate rate of monetary expansion is maintained to reduce the pressure of inflation. The government had succeeded in cutting its budget to the point that a fiscal surplus for the fiscal year 1997 was achieved, but later the IMF had agreed to allow larger and larger fiscal deficits so that the public sector could usher in the economic recovery and to help provide social assistance to the public (social safety net and social investment programs).

Perhaps one earlier good news was the good performance in the external sector where exports had increased while imports had plummeted. The positive change in the external sector was so quick and drastic that the current account had turned into surplus within a few months after the crisis broke. From October 1997 onward the current account of Thailand remains in surplus. At the end of July 1999, this surplus
amounted to more than 1.2 billion US dollars. This had positive effects upon the external confidence on the Thai economy as shown by the continued improvement in the exchange rate of the baht since February 1998.

It was earlier expected that the economy would bottom out before the end of 1998, and earlier signs in both the domestic sector (low inflation rate, falling interest rates) and the external sector (stable exchange rate and slowdown in capital outflows) but this was not so. To succeed in stimulating the economy quickly, the commercial banks must be able to start lending quickly. At first these banks were not able to do so because of tight money situation. But when the liquidity was eased and the interest rate was brought down, commercial bank lending was still slow. Most local banks were burdened with large numbers of non-performing loans (NPLs), and the corporate debt restructuring between these banks and their debtors was not very successful at first. The bankruptcy law that existed at the time of the crisis was inadequate to cope with the situation where debtors and creditors need to negotiate about their debt settlement quickly and move on. The attempt by the government to enact a new bankruptcy law was faced with strong resistance from the Thai political community, particularly in the Senate. It took the government several months to pass this new law, with several compromises. This was one of the reasons the new bankruptcy law was not very effective in changing the behaviour and practices of Thai debtors. As a result of recapitalisation push of many commercial banks, the liquidity situations became loose again, but commercial banks still refused to lend for fear of NPLs.

3.3 Some Macroeconomic Results

(a) GDP Growth

As can be seen from the Chart 2, the economy was growing at the rate of about 4.7 per cent during the last quarter of 1996. During the first half of 1997, the economy began to falter through stagnant export, with the GDP growth less than 2 per cent at the end of the second quarter of 1997. Then the crisis struck. The growth rate of GDP during the last quarter of 1997 was minus 4.6 per cent. The economy was already in recession. The economy continued to contract throughout 1998, and reached the bottom during the second quarter of 1998. It then began a slow climb back, achieving the positive growth rate for the first time since the crisis broke during the second quarter of 1999 (with the GDP growth rate of just 0.1 per cent). The growth hit the highest rate in the post-crisis period at 7.5 per cent during the third quarter of 2000 then became more laboured through the remainder of 2000 and 2001 due to the slowdown in the world economy. As shown in Chart 1, the growth of the Thai economy during the third quarter of 2001 was estimated at 1.5 per cent. 7

Chart 2: Growth Rate of GDP, 1995 to 2001

7 The latest statistics from the NESDB which became available in early July 2002 has shown that the GDP growth rate for Thailand during the first quarter of 2002 was estimated at 3.9 per cent. See NESDB (2002).
(b) Production and Trade

The production situations before and after the crisis are divided into two parts, agricultural production and manufacturing production. With the overall crop production in 1995 set at 100, the index for 1996 and 1997 were 106.1 and 110.9, respectively. It may be seen that the crop production index for 1998 was 109.1, only a slight, almost imperceptible, decline from 1997 level. A simple interpretation of this phenomenon is that the crisis had little impact on the crop production of the country. Indeed the relative crop production levels of 1999 and 2000 continued to grow strongly with the respective indices of 115.3 and 121.7 for 1999 and 2000. The depreciation of the baht had made the agricultural commodities of Thailand cheaper in the eyes of foreigners, and the demand for them had subsequently increased.8

Chart 3: Industrial Growth and Capacity Utilisation

The situation was different with regards to manufacturing production. The total index of manufacturing production declined from 107.1 in 1997 (with the index for 1995=100) to 96.5 in 1998. However, the manufacturing production picked up quickly in 1999, with the index of 108.6, and in 2000 with the index of 112.1. Again,

8 It should be noted, however, that the increase in agricultural section is in terms of volume, not value. In fact, with the price of agricultural commodities generally lower in 1998 and 1999, the earning from agricultural exports of Thailand in 1999 and 2000 actually declined despite a larger volume of production and sales.
the massive devaluation of the Thai currency explains a lot of this increase through production for export. The value of exports in 1996 in dollar terms was lower than that of 1995. This was one of the reasons that brought about the crisis as mentioned earlier. In 1997, the export earning in dollar terms improved slightly but fell again in 1998. It was not until 2000 when the value of export in dollar terms had increased noticeably. Thailand has to sell a lot more in volume terms to receive the same amount of earning compared to the situation before the crisis.

Even before the crisis, there was an excess capacity in the manufacturing sector of Thailand. Chart 3 shows that in 1995, two years before the crisis, the industrial capacity utilisation was estimated at 77.4 per cent. This fell to 72.5 per cent in 1996. The economic shocks at the end of 1997 hit the industrial sector hard as the rate of capacity utilisation dropped to 64.8 per cent in 1997 and hit the bottom at 52.8 per cent in 1998 before increase slightly to 61.2 in 1999. Regrettably, the industrial capacity utilisation during the last two years do not show much improvement at all. In fact, the latest figure for September 2001 only shows the rate of capacity utilisation of only 52.8 per cent, the same level as at the bottom of recession.

(e) Consumption

The crisis had brought about fear of uncertain future among the people resulting in their witholding the purchase of unnecessary items and/or increase saving. This has a deleterious effect on expansion of the economy. The Composite Private Consumption Index shows a decline from 101.4 in 1997 to 95.4 in 1998 (with 1995=100). Typically private consumption was slower in comparison with the manufacturing production in their response to economic change. In the short-run, many people would find it difficult to cut consumption quickly, and they are likely to try to maintain their consumption patterns as long as they could. If the economic downturn continues, these people have no choice but to slow down their consumption also, and in reverse, would not adjust quickly to the return of economic normalcy. This phenomenon is very clear when we compare the Composite Consumption Index with the Manufacturing Production Index. Whereas the manufacturing activities showed a strong recovery in 1999, the Consumption Index was still at 96.9 in 1999. Even in 2000, the Consumption Index was only 100.2, only slightly higher than the starting period in 1995. Domestic aggregate demand will need to go up much higher if the economy is to maintain a much higher rate of growth than now.

Chart 4: Household Consumption Expenditure Growth
The price level in Thailand rose quickly after the crisis struck at the end of 1997, especially food price. Not that food was scarce, but the increase in the demand for food as a natural response to a crisis had bid up the food price. The food price index was highest in 1998 (137.9 compared to 125.9 in 1997) representing the rate of increase in the price level of 9.5 per cent. In 1999, however, the food price had come down. Meanwhile the non-food items whose supply was plentiful as a result of excess production capacity did not increase much in price. It, therefore, acted to pull down the overall price inflation in the economy. The core consumer price inflation (calculated from the index excluding the raw food and energy items) for the periods 1997 to 2000 stood at 4.7, 7.2, 0.02, and 0.7 per cent, respectively for 1997 to 2000. Even in the second quarter of 2001, the core consumer price inflation was only less than 1.5 per cent. This low inflation helped economic recovery and cushioned the plight of poor families and families of laid-off workers as well. The change in the price level using GDP deflator shows similar result as the change in consumer price index.

**Chart 5: Growth Rate of GDP Deflator**

Source: NESDB (2001)

### 3.4 Social Welfare Effects and Policy Responses

There are at least three ways that the life and well being the Thai people could be affected by the crisis. One way is for the crisis to hurt the private business causing losses which could lead to the companies shedding their workers or employees. The loss of employment is a major source of adverse outcome of the crisis. The second way is for the crisis to cause a slowdown in economic activities causing a drop in income of the self-employed like the farmers, and a cut in wage or salary of those who remain in employment. But while these two ways cause the negative effects on the people, the government or the state could intervene to help by providing social assistance through its social spending such as on health, education, or other welfare. In this section we will discuss these three ways in which the life and welfare of the Thai people are affected by the crisis.

#### (a) Employment and Unemployment
This crisis has hurt many people in different sectors differently. In the public sector, public servants who are normally paid less than their counterparts in the private sector may lose some of the fringe benefits that come with the jobs such as medical allowances, supplementary salaries based on special qualifications or entertainment expenses due to government budget cuts, but their job security has remained intact. The long-standing policy of the government to freeze the size of the public officials by allowing no more than a 2 per cent increase in the existing workforce annually actually helps those who remained in the jobs because the government does not need to incur heavy additional costs to look after new officials.

The situation is different for private sector workers, the professional and business people are those who were most adversely affected by the current economic crisis because the economic slowdown has translated into less economic activities and income. Those who had foreign-denominated debt without appropriate hedging had suffered immensely from the rapid depreciation of the baht. The wage and salary workers are also affected by job losses. These people may benefit from availability of credits but only through the regeneration of jobs and employment by the professional and business people. Lack of unemployment benefits in the Thai social security system makes these workers very vulnerable to hardship. Some may have to find a new job completely in order to survive, and a majority of these unemployed wage and salary workers may have to depend on their families at least in the short-run until business activities improve, or a new job is found. Wage workers who came from the countryside may choose to return to the rural areas where family supports are still available.

Farmers may be the only group of people who could benefit from this crisis. Assuming that their production inputs are mainly land and labour which have little import contents, their products would be in greater demand through a depreciated exchange rate (as is actually the case with regard to the production and exports of high-quality rice). However, they could not escape the impact of inflation brought about by the increase in the costs of production of other necessary household goods and services. Moreover, the burden of the farm sector in the rural areas in looking after members of the families who had gone to work in cities but returned home after job losses could put a great deal of pressure on these farmers who are generally the least well off in the society.

The analysis in this paper is based on the Labour Force Survey which have been compiled by the National Statistical Office (NSO) since 1963. The NSO presently conducts four rounds of the survey for the whole kingdom each year; the first round is scheduled in February to capture the data on the non-agricultural season; the second round is normally held in May when new graduates finish their schooling and join the workforce; the third round is held in September – during the peak agricultural season; and – starting from 1998 – the fourth round of survey has been conducted in November as well so as to better capture the changes in the data. One should note that the patterns of employment of many Thai workers often exhibit high degrees of underemployment, shifting, or seasonal employment from circular migration (especially between rural and urban areas during the dry and wet season). In addition, due to the lack of unemployment insurance facilities, poor workers have to try to find new odd jobs as soon as they lost their old jobs. This type of employment pattern is difficult to assess.
Since a large proportion of the population is working in the agricultural sector, unemployment usually increases during dry season and falls during wet season. In order to accurately analyse unemployment data, this seasonal effect must be taken into consideration. A recent study by Nanak Kakwani (1999) has attempted to do that. He had used the employment trends of the periods before the crisis to project the employment and unemployment situations in the crisis period (the first quarter of 1998). The difference between this projected figure and the actual figure is an estimation of the effects of the crisis. As it turned out, the estimated unemployed persons as a direct result of the economic crisis numbered about 810,000 – much lower than the often quoted number of between 1.5 to 2 million persons. The study also found that the effect of the crisis on total unemployment was statistically insignificant. This may infer that the nature of the crisis was cyclical and not structural.

A new study by Behrman, Deolalikar, and Tinakorn (2001) presented several interesting findings on the overall labour market effects in Thailand. Some of their findings are:

(1) The pre-/post- crisis comparison indicates that there were not only significant downward quantity adjustments in employment, but also in hours worked and in shifts from wage to non-wage employment.

(2) The post-crisis average real wage rate did not decline compared to pre-crisis levels (except for some rounds). Actually, post-crisis average real wage rates exceeded pre-crisis real wage rate due to a combination of reduced hours worked for fixed (monthly/weekly) pay workers and some movements from wage to non-wage employment by previously lower wage workers.

(3) Wage labour earnings in Thailand decline only by about –7.6 per cent in 1998, which was less than the decline of –10.0 per cent in GDP. Workers in other Asian countries were not as lucky, since wage labour earnings declined nearly three times as much as GDP in Indonesia and Korea.

(4) Previous studies on the labour market outcomes in Thailand and other East Asian economies confound changes in hours worked in their measures of changes in real wage rate and hence can be misleading with regard to price or wage effects (aggregation problems).

(5) Wage flexibility in Thai labour markets are not as high as those in some low-income countries (e.g. Indonesia) where post-crisis unemployment change was minimal.

According to the LFS data, unemployment began to surge dramatically in the first quarter of 1998 (dry season) from 0.9 per cent of the current labour force to 4.8 per cent of the labour force. Unemployment remained high for several quarters and peaked at 5.6 per cent in May 1999 before declining to 3 per cent in August 1999. A recent data shows that unemployment rates are between the 2.5 per cent - 3.5 per cent range, which are still higher than the pre-crisis level (between 1 per cent - 2 per cent
range). In October 2001, about one million people are reported to be unemployed (3.2 per cent of the current labour force).

There are several policies which have existed in Thailand prior to the crisis such as policies on minimum wages which is set according to regional labour market conditions, severance payments, social security, and labour unions. However, some these policies are not strictly adhered to or do not cover the majority of workers, and hence are not as effective as they should be. Take minimum wage for example, LFS Data shows that approximately 30 per cent of all wage employees in the Thailand earn wages that were below the minimum wage. Therefore, further expansion of public works programs could be the principal vehicle for temporarily strengthening social safety nets; as public works programs which guarantees at least the minimum wage rate is attractive to these poor workers.

**Chart 6: Employment and Unemployment Rates in Thailand, 1996 to 2001**

![Chart 6](chart6.png)


There are several measures that the government could undertake in order to prevent future negative impacts on the labour market. These include prioritising human resource development, synchronising between technology-intensive industries and labour-intensive industries, introducing more employment options (alternative employment industries and SMEs), enhance social security and unemployment/severance benefits, and improve law and policy enforcement against misuse of labour (exploitation of children, women, and migrant labourers).

**(b) Individual income and its distribution**

Overall changes in individual income and its distribution are already discussed to in Section 2 above. This section will take a detailed look at the sources of income of Thai households during the crisis. Statistics from the NSO have shown that the average monthly household income steadily increased from 1,928 baht in 1975/76 to
10,779 baht in 1996, one year before the crisis. Despite the start of the crisis in July 1997, the average income of Thai households was found to increase to 12,492 baht in 1998, and indeed to 12,729 baht in 1999. This can be seen as a delayed effect of the economic crisis. But more accurately, however, this could be interpreted to mean that there are both gainers and losers in the first two years of the economic crisis, and it appears that the average income of households did not fall until the year 2000. This is also a problem of distribution, or rather, maldistribution of income. On the expenditure side, the household expenditure did fall slightly between 1998 and 1999. At least the anxiety and apprehension of the crisis was shown here among the average Thai households. By 2000, the cut in home consumption was very clear. This is a natural response to hard time.

The NSO data also show a clear trend of modernisation of the Thai economy where the importance of money income increases, and that of income-in-kind decreased, where the non-food expenditure increased against food expenditure, and where income from wage and salaries had shown an increased importance. On the distribution of income, income inequality in Thailand reached the peak in 1993, then fell continuously until the depth of the crisis in 1998, then increased in 1999. With the economic situation improved in 2000, the inequality also slightly declined. The regional inequality is less than national inequality because a national inequality as a result of the combination of a rich region, say, Bangkok, and a poor region, say, the Northeast, would be certain to stretch the income distribution further, causing greater inequality.

It is possible that the crisis still bring about the increase in average household income as was the case in Thailand, but this is possible because the income distribution has become more skewed, and it was the income position of the rich that makes up to the increased in the average income of the overall households. It is sufficient to say here that future income policy should not address only absolute poverty problems, but relative poverty problems as well. Otherwise, the situation that we saw in Thailand in 1998 and 1999 could happen again, that is the average income has shown an increase while the majority of the population is genuinely suffering from economic hardship through job losses and the fall in income and earning.

(c) The Role of State in Providing Social Assistance: Health, Education, and others

There were many government spending programs which target at alleviating negative social impacts resulting from the crisis. The previous government of Mr. Chuan Leekpai used part of the normal government budget to assist and resolve problems experienced by the poor (simply defined as people whose income are lower than 10,000 baht per year). The other part of the funding came from loans from foreign governments and organisations:

(1) The Social Investment Project (SIP) from the World bank and the Japan Bank for International Co-operation (JBIC) totalling 21,689 million baht. Through this government loan program, the Government Savings Bank

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9 Since 1988, the government has instructed the NSO to conduct this SES every two years. The SES in 1999 was a special survey that the government asked the NSO to carry out in order to find out the impact of the economic crisis.
distributed and lent out money to local authorities and organisations in order to enhance their residents’ economic positions.

(2) Loans from the Asian Development Bank (ADB) under the Social Sector Program Loan of approximately 7,800 million baht. This fund was mainly used to alleviate the negative impacts experienced by the newly unemployed and the disadvantaged people in the society.

(3) Loans from the World Bank and the JBIC to help increase growth-induced government spending. This package which was announced in March 1999 amounted to some 53 million baht, and was commonly referred to as ‘the Miyazawa fiscal stimulus package’ or ‘the Miyazawa Plan’ following the name of the Japanese Minister of Finance who provided a large portion of funding for this social assistance program. The policy started hiring people in April 1999. It generated short-term employment for low-skilled workers in the rural areas in the rehabilitation of water supply, irrigation, and other public work.

(4) Measures to encourage rural and society development. The budget for this program was 4,272 million baht, and the funding came from existing SAL loan (no additional borrowing necessary).

To sum up, after two years of conservative, market-driven, policy packages, the Thai economic began to show sign of recovery. This was helped also by various state-directed policy packages, for example, two major economic stimulus packages by the government, one in March 1999 and the other in August 1999, and heavy doses of tax cuts and increased public spending. In early September 1999 when the Thai government was preparing its 8th and last Letter of Intent to the IMF, the economy had clearly shown strong signs of recovery. The manufacturing production index had shown continuous positive increase, whereas the private investment index had stopped its decline. The household consumption has also begun to increase, thanks to stable price level, cuts in income and sales taxes, increase public spending, and so on. The growth rate of GDP was 4.6 per cent in 1999 and 4.6 per cent in 2000. The current account remained in surplus, while the balance of payments also turned to surplus one year after the massive outflows of capital which precipitated the crisis. Employment started to increase as the production in the real sector began to come to life again.

But as the economy had shown signs of responding to the government’s medicine at the end of 1999, the government itself appeared to have run out of its own gas. It was ineffective in tackling the two stickiest problems, the continued high level of NPLs and the stagnant real estate sector. The unresolved NPL problems had caused a failure in commercial bank credit expansion. The rising oil price in 2000 compared to two years earlier, had dampened the GDP growth. The export was growing well in 2000, but that was partly because the baht had become weaker. Toward to end of the year, the US economy began to slow down, whereas the Japanese economy continued its depressed state. The prospects of the Thai economy at the end of 2000, therefore, was not very promising. Coupled with popular political campaigns of the new political party, the Thai Rak Thai (TRT), the government under the Democrat Party became unpopular, and lost the election to the Thai Rak Thai at the general election in early 2001.

The events surrounding the victory of the TRT Party and the subsequent assumption of power of Mr Thaksin Shinawatra as the current prime minister of Thailand were very interesting. The new constitution promulgated in October 1997 was already in force which had given a kind of political transparency that hitherto unexperienced in Thailand, such as strict rules against vote buying, separation of legislative power from executive power, creation of various legal bodies to counter the political influence of politicians and bureaucrats, and so on. As a successful businessman who has made a fortune in telecommunications, Mr. Thaksin was financially secure to make deal with old- and new-styles local politicians to lend their support for his eventual prime ministership. At the same time, Mr. Thaksin needed to seek the support of modern businessmen, many of whom were counted among those who were laden with NPLs but whom political, social, and economic influences were large. He also had the support of many technocrats and business associates who could provide the necessary political manpower to run a modern government. Despite the shaky start due to the impending case against him in the Constitution Court for his indictment for the concealment of his assets (which could cost him the prime ministership if found guilty), Mr. Thaksin won his case and thus could concentrate on implementing his election promises.

These election promises were no small matters. It is true that Mr. Thaksin has the capability to be prime minister and head of progressive government, but there is no denial that his Party overwhelmingly won the election because of these election promises. Once in power, he must fulfil his party’s election promises which became guidelines for his development policies. In the context of appropriate governance, he has to do two things at the same time, that is to continue to maintain and speed up the economic recovery and to implement policies that essentially bestow social welfare or social well-being to a certain target group of people, mainly farmers and the people in the countryside.

In February 2001, Mr. Thaksin announced his government’s policies to the Parliament. In his policy statements, Mr. Thaksin introduced several ‘urgent’ policies aiming at improving the living standards of the people. Nine of his urgent policies are shown in Box 2. How good are these policies? Will they be able to generate necessary growth and provide specific welfare to the people at the same time? Are there better alternatives to these policies which are conditioned by election promises. Is Mr. Thaksin different from, and better than other prime ministers before him? These are some of the questions that many will raise while evaluating the success or failure of his policies. Let us take a look at some of his policies referred to above.

(a) The National AMC Policy and the Solution to NPL Problems

It was mentioned earlier that one of the two stickiest problems facing Thai government during economic crisis was the problems of NPLs. The last government under Mr. Chuan Leekpai attempted to solve the problem by recapitalising banks and finance companies. The Government, with the advice from the Financial Restructuring Advisory Committee, the Ministry of Finance (MOF), and the Bank of Thailand, implemented the August 14th 1998 Recapitalisation Scheme promising to provide matching Tier 1 capital for Thai financial institutions that can find funding from strategic partners. The scheme also offers to provide Tier 2 capital to financial institutions in percentage terms of their credit extension and debt restructuring. At the
end, only about one-third of the 300,000 million baht pledged for this program was actually used, indicating that there were some concerns among the private banks about government intervention if they enter the program, especially the Tier 1 Scheme which the MOF has the right to appoint a representative(s) in the Boards of participating financial institutions, and reserves the right to change the existing management team if it sees fit.

The establishment of a national asset management corporation (AMC) was one of the Thaksin’s government brainchild. The government proposed to establish a central, government-run organisation to take over the NPLs and facilitate a quick debt restructuring to strengthen the real sectors and the service sectors, with the hope to kick start the economy. This idea of the nationalisation of bad loans differs from the Chuan government’s policy of encouraging banks and financial institutions to set up private AMCs to manage their own NPLs.

The Thailand Asset Management Corporation (TAMC) intends to restructure a substantial amount (500,000 million baht) of NPLs by the end of 2002. All NPLs are expected to be resolved in two years’ time (by the end of 2003). The TAMC will continue to monitor the performance of the restructured loans for another 3 years. By the end of 2006, all the process is expected to be concluded – 3 years earlier than originally expected. It was reported that the TAMC will initially focus on big debtors so as to stimulate the economy, then it will turn to smaller debtors – some of which can be grouped up and managed by professional asset managers.  

The TAMC not only sets ambitious goals for itself, but it also sets equally demanding goals for the state-owned banks who act as its asset managers, for the management of the NPL pools. State-owned banks are responsible for managing the single creditor loans which they originated and are given nine months to finalise all deals (until September 2002). Debtors normally propose debt restructuring plans with a certain percentage of haircuts. So far the TAMC has approved an average of 10-20 per cent haircut (or debt reduction).

How does TAMC work? The TAMC was set up in June 2001 after the enactment of the TAMC Act. Its current Board consist of a banker, a representative from the Federation of Thai Industries, a representative from the Board of Trade of Thailand, and nine technocrats/bureaucrats. The assets which were transferred are divided into two types: state-owned (state banks and AMCs) and private-owned.(private banks and AMCs). Only private-owned AMCs, not state-owned AMCs, are allowed to be the lead creditor in multi-creditor debt restructuring negotiations.

According to the gain/loss sharing scheme between the TAMC and the financial institutions (Articles 47 - 52), the financial institutions would shoulder the first 20 per cent loss, while the next 20 per cent loss would be split equally between the TAMC.

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10 It has been observed, however, that NPLs that have not been settled one way or another now, almost 5 years after the meltdown, are probably beyond any resurrection now, and are probably better off liquidated. Dr. Ammar Siamwalla, for example, believed that by the time the TAMC was set up much of the damage to the economy and therefore to asset values had already occurred. The firms and assets that could be kept intact had already gone through either the Corporate Debt Restructuring Advisory Committee (CDRAC) process or the bankruptcy courts. The assets that remained would only command break-up values. See Ammar (2001).
and the financial institutions. The TAMC will be responsible for all losses over the 40 per cent threshold. If the overall results turn out positive, the first 20 per cent of the gains would be shared equally between the TAMC and the originating financial institutions. Gains above 20 per cent will go to the financial institutions (but not to exceed the difference between the accounting value of the asset and the transfer price). Any extraordinary gains belongs to the TAMC.

As the initial investment is paid out of the FIDF (which receives regular funding from the banks) and the day-to-day operations are funded by the interest income from debtors, the present government is not burdened with an upfront payments. As for the payment for the NPLs transferred, this government has arranged for the TAMC to pay the financial institutions in the form of promissory notes (P/N) which has a 10-year maturity. How will the TAMC finance the P/N repayment with cash in ten years’ time is not this government’s problem – the government in power in the year 2011 will have to figure that out. TAMC encourages financial institutions to extend additional credit to debtors by promising that any new financing that they provided would receive a senior debt status (that is, they would get their money back before other original creditors).

The government also introduced a new ‘matching fund’ concept whereby a Fund can choose to invest in companies which has been restructured by the TAMC. The first Fund was established in April 2002 with joint funding from Ceberus (an international asset management firm) and Krung Thai Bank and the Industrial Finance Corporation of Thailand (or IFCT, both of which are state-owned financial institutions). Minimum investment in each debtor company is set at 5 million USD. The government stressed that the primary intention of the matching fund must not be to purchase assets from the debtor companies, but should be to restructure the companies. A few other Funds have expressed interests in joining this Matching Fund program.

Since October 2001, the TAMC has accepted multiple lots of loans (around 4,600 accounts) from state-owned financial institutions and private financial institutions, with book value totalling almost 700,000 million baht – significantly lower than their original target of 1,100,000 million baht. In the TAMC’s latest progress announcement as of March 31st, 2002, it reported a completion of 100,216 million baht (177 cases) of debt restructuring, up 100 per cent from its previous announcement three weeks earlier (50,133 million baht). Of this number, 55.4 per cent are cases with multiple creditors (67 cases), 37.1 per cent of the cases are in the property sector, 26.8 per cent are in the industrial sector, and 15.4 per cent are in the service sector.

Even though the overall restructuring figures for the TAMC seems impressive, some felt that the core of the problem has not been resolved. There were speculations that a majority of the 50,083 million baht of NPLs restructured in the last three weeks of March 2002 are single creditor loans (previously originated by government-owned banks) which are much easier to resolve compared to multi-creditor loans. Since the TAMC only employs less than 100 full-time staff, one might question whether it is possible to conduct a thorough analysis of each debtors’ financial status prior to executing these restructuring deals. Many believe that these doubts are not unfounded. In addition, it is suspected that many of the restructuring deals were back-end loaded, namely, debtors only need to pay a small amount up-front and agree to
pay the rest of the money later on, usually in several payments. It remains to be seen whether or not these debt repayments actually materialise.

Another point of concern for the private banks is the fact that the TAMC prohibits state-owned AMCs from being the lead creditor in multi-creditor debt restructuring negotiations. This means that private banks have to shoulder some additional burden of managing the whole restructuring negotiations, even if their total lending is small relative to other state-owned creditors. The gain (or loss) sharing is scheduled in year 5 and 10, but the expenses incurred as a result of these asset management activities go straight into the banks’ profit and loss account every year. It is not surprising, therefore, that many banks reluctant in becoming lead creditors. Moreover, it is speculated that the TMC, in an attempt to meet their ambitious target, was directly negotiating several restructuring deals with the debtors – without notifying the creditor banks as previously agreed. The creditor banks, especially private banks which are more concerned about the terms of the restructuring and the resulting haircuts, disapprove of this practice. As a result, there is an increased tension among the parties involved.

A major criticism of the TMC law is that the TMC committee is given too much power and there is no oversight of the committee.11 The committee has the power to authorise and approve all kinds of debt and business restructuring, asset sales, and liquidation of debtors, as long as they have acted in a “careful and professional manner” – which is sometimes difficult to assess. The TMC Committee, managing director, and other officials are well protected by professional immunity as specified in Article 28. They shall not be held responsible for their activities, if they have acted in a careful and professional manner. However, this immunity provision would not apply if they violate the law, are dishonest or guilty of gross negligence.

In spite of the summary powers of the TAMCs and the opportunity to clean up their balance sheets, many banks were not too enthusiastic about the scheme and tried to speed up their restructuring efforts and finalise the deals prior to the cut-off date (transfer date) in order to reduce the amount of NPLs which needs to be transferred to the TMC. The value of loans transferred from private banks fell short of expectations, which many observers put down to fears that the TMC will go soft on well-connected debtors. Besides, Thailand’s privacy laws makes it impossible for outsiders to evaluate the TMC’s degree of toughness on each debtor. At present, there are approximately 12 per cent of NPL in the banking system. NPL re-entry are occurring every month – but not at a worrying rate.

To conclude, the existing bad loans problems in Thailand are beyond the point where the work of TAMC could make any real difference. The greatest worry now is that if the TMC performs badly, either unprofessionally through irregular practices, or does not protect public interest well enough, then it is the taxpayers who will

11 See, *Bangkok Post*, November 25, 2001. On the power of the TMC, Dr. Ammar Siamwalla (2000) also noted that the TMC was not unlike the FRA in its role as an asset disposal unit. But whereas the FRA was in charge of disposing of financial institutions’ assets, with its buyers still having to go collect on the loans given to the debtors, TMC will itself directly deal with the debtors, in many cases, if not in most, actually foreclosing on properties. Consequently, unlike the FRA, a key feature of the TMC law is to empower it to grab these assets. Actually, there is nothing wrong with this as long as TMC is doing its jobs openly, professionally and accountably.
eventually pay for the past and present mistakes of those who are now handling the country’s NPLs.

(b) ‘30-baht’ Health Care Scheme

Another ambitious Thaksin Government policy is to provide universal health services and facilities, capping each hospital visit at 30 baht, in order to reduce the overall cost to the country and the people in acquiring health care. This is part of the long-term government plans to reform the health service system to provide health benefits comparable to those of the social security system to all Thai citizens for free or for a small co-payment. It is considering the possibility of merging all public health benefit programs into single or dual health funds. The Universal Health Care Coverage also allows private health care providers to participate in the program, with the hope that their participation would give more choices to the people and increase the quality and efficiency of the system. The government proclaimed that since April 1st, 2002, all Thai people have been guaranteed equal access to a nationally acceptable standard of health care.

The Scheme works this way. All Thais over 13 years of age who do not currently receive other forms of government-assisted health insurance12 are entitled to join this ‘30-baht’ program in which they are (supposed to) be able to get most kinds of medical treatment while paying only 30 baht each time. Those citizens who are not government servants or employees who are already covered by the government medical expenditure scheme, and private workers who are not covered by private insurance, and poor citizens who are provided with free medical care cards, will be given ‘Gold Cards’ to receive comprehensive medical services for a charge of 30 baht (less than 70 US cents) each time. The government will pay 1,252 baht for each person registered at a particular hospital (whether public or private). The program covers necessary vaccinations, medical treatments, (except for the kidney dialysis which is extremely expensive), pregnancy care and delivery, and dental care. In December 2001, the Public Health Ministry has extended its 30-baht health care scheme to cover anti-retroviral drugs for HIV/AIDS. In the early stages, the scheme would cover 6,000 – 7,000 AIDS sufferers. A Committee would work out a budget management plan and criteria for deciding who should get the drugs. However, provincial committees may decide to give different rates of budget to the contracting unit for primary care for each population group in the areas depending on the health conditions of each group. The ministry said its budget on AIDS would be increased to more than 1 billion baht, of which 42 per cent would go on prevention, 39 per cent on treatment, and the rest on information and research.

This is one of the most popular public programs under the new government. The idea of providing universal health services for a very nominal fee (almost free) is a good one, especially for the poor. But the actual practices or implementation of this policy of this government have several flaws. The followings are some of the flaws:

- This 30-baht Scheme does not target the poor only but applies to everyone who is not public servants, workers who enrolled in social security scheme, and those Free Medical Card holders. This wastes resources, creates moral hazard for the

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12 Such as the Social Welfare Scheme for the poor, Voluntary Health Card Scheme, Civil Servant Medical Benefit Scheme, Social Security Scheme.
overutilisation of health services, and disturbs good practices of both the patients and health providers.

- The present health care services system in Thailand is already functioning well, or at least not functioning too badly. The public hospitals or health clinics already charge reasonable fees for various medical services commensurate with the true costs of treatments. Those with ability to pay can go to private health care services; low-income households can buy low-cost health insurance cards; poor households can apply for Free Medical Service Cards; and so on. There are better ways in which to use several billion baht of government budget to provide health services for those who need them most.

- The 30-baht Scheme affects the behaviour of both the patients and health providers in a certain way. For example, as the first receiving hospital has to take care of the patient throughout the treatment episode, if expensive specialised services in other hospitals are need, the first receiving hospital may be reluctant to refer its patient there for fear of having to bear additional burden of costs. The cost comparison between different medical schemes may disrupt normal behaviour that is not efficient.

- There is a natural constraint to the provision of medical services under this 30-baht Scheme. Limited supply of medical services under low price will eventually bring about rationing and queuing of those services. Indeed, because of the possibility of the system correcting itself through service rationing and queuing, the state can even set the price lower than 30 baht per visit.

- It is obvious that the government recognises the political popularity of this policy, and is willing to go through with it. But eventually the welfare of the whole population could be adversely affected by this market-distorted policy than is helped by it.

(c) The Village and Urban Revolving Fund

Another election promise which has become one of the earliest implemented policies of the Thaksin government is the establishment of the One-Million Baht Village and Urban Revolving Fund. Every village in the whole kingdom was promised one million baht each from the Thaksin government as a loan to that village to use in a project or activity that generates income, employment and better livelihood for that village. This loan will remain in the village without having to return to the government unless it is clear that the village administrators were not able to make the proper use of it. This loan could be further lent out to households or individuals in the village for investment purposes. This loan can also be combined with another village-based policy called ‘One Village One Product’ which is the government policy to encourage village or group of villages to develop at least one local product based on traditional indigenous expertise and local know-how that can be sold or marketed in larger markets outside that village (even nationally or internationally). The government is further prepared to provide additional assistance in terms of appropriate modern technology and new management techniques to market such local products.

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13 The government often cited that it got the idea from Oita, Japan, which started off as a very poor village but later became a national success story following the implementation of the ‘One Village One Product’ project.
from the village to domestic and international outlets through a national or international retail network or through its internet website.

The government believes that the overall economy would gain momentum through increase in investments and local spending. By early March 2002, 71,578 villages and urban communities were set up to receive one million baht each. This accounts for 95.6 per cent of the government’s target of 74,881 accounts. At present, the Department of Community Development in the Ministry of Interior is responsible for monitoring and measuring the performance of this program. Some feel that this arrangement is inadequate as it is suspected that some village fund do not have sufficient planning and monitoring for credit extensions, allowing locals to borrow to buy luxury items such as mobile phones, motorcycles, or even use the money to gamble. Moreover, the low interest rate (1 per cent) of the VURF is also very attractive and has caused some villagers to churn away from their village’s own savings co-operative. If this practice continues, the local savings co-operative may have to wind down its operations, and it would be quite difficult to rebuild it again once the VURF Scheme is phased out in 2004.

The government would also like to see this VURF as part of the Sufficiency Economy where each community at the grassroots level produces for personal consumption first and then sells excess production to augment their income at the family level. Villagers are encouraged to join together in conducting economic activities at the community level, accelerate the development of small- and medium-scale entrepreneurs, provide access to domestic and overseas markets in order to systematically strengthen the income creation process for the people.

This program limits each individual borrowing to 20,000 baht and the amount must be paid back in one year’s time. Once a village distributed all of its one million baht to the local borrowers, additional lending is prohibited until the Fund receives at least 20 per cent of the total debt repayment. Interest level is not specified by the government, the local Fund Council can determine the appropriate interest applicable to different types of loans depending on the loan’s objectives and repayment schedule.

In March 2002, Dr. Chalongphob Sussankarn, the President of Thailand Development Research Institute (TDRI), the country’s well known think tank, commented that the government’s ‘grass-root funding program’ is theoretically beneficial, but is facing several obstacles in practice because it cannot encourage the grass-root population to lead the economic recovery process. In addition, the system is not exactly market-driven and hence may lead to business failures that could bring about another problem at the national level. Since most of the lower income population in Thailand has limited purchasing power and significant income inequality, the funding from the government has to pass through the same old political-business groups. As a result, it might not yield the right ingredients for success, similar to what has happened in the past where the government introduced several unsuccessful projects in the rural areas. Therefore, adequate performance measurement and continuous monitoring should be emphasised in order to ensure the effectiveness of these programs. A strong, independent, and transparent local committee is also a crucial factor. Dr. Chalongphob also believed that since the problem of the country is structural, not lack

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14 See Krungthep Turakij, March 25, 2002 (in Thai).
of demand, boosting state expenditure to boost household income might not be an ideal solution during the economic crisis such as this one. The country needs structural change, in terms of infrastructure and means of production, to make it more competitive internationally. This is a factor which Dr. Chalongpob feels the government is lacking.

Mr. Paiboon Wattanasiritham, a well known leader in non-governmental organisations, also has a mixed view on this VURF program. On its positive side, this program, if well managed, could create a structural change in the local economy and may lead to numerous job creation and strengthen the local community, both socially and economically. On its negative side, this program could create ‘bubble’ at the grassroots level due to huge economic stimulus (similar to the bubbles at the national level during the pre-crisis period where foreign capital inflows were very high). The people who receive easy money may not be careful in spending it. Moreover, the scheme could weaken the local community, making it accustomed to seeking help from outside rather than build a strong internal network. Finally, treating money, not people, as the most essential ingredient of development is inappropriate.

It is difficult to evaluate the effectiveness of this program at this stage. Village leaders themselves certainly are in favour of this program, and are thankful to the Thaksin government for it. But, again, to provide monetary assistance to all villages across the board without checking their needs and conditions can waste a great deal of resources. A recent World Bank Report (World Bank, 2001) suggested that block grants and other anti-poverty interventions targeted to the poorest villages are likely to be a better use of public funds than universally distributed programs, at least from an equity perspective. But if one sees this program as a fulfilment of an election promise, then, there is no much room for analytical debate.

(d) Debt Moratorium to Small Farmers

The Government has also initiated a policy to immediately grant a grace period for individual small farmers for both interest and principle payments for 3 years, to relieve their debt burden as a part of a comprehensive reform of the traditional farm economy to be more viable and self-sustaining in the long term. The ideas of giving or granting debt rescheduling or even debt forgiveness to small farmers have existed for a long time and in all governments, but thus far no government was bold enough to implement it.

The government provides two options for the farmers. The first option is the 3-year pure debt moratorium where the government will pay the interests for loans of all farmers who choose this option. The second option is the debt reduction program where the Bank of Agriculture and Agricultural Cooperatives (BAAC) will reduce the interest rates charged on loans to farmers. The reduction would depend on the credit status of the farmers. Credit status which are considered above-average are divided into 3 levels – excellent, very good, and good. ‘Excellent’ borrowers would receive higher interest cuts than ‘good’ borrowers. By September 2001, 95 per cent of the eligible farmers have joined the program. About 1.1 million farmers opted for pure debt moratorium option, while around 1 million farmers chose to join the debt reduction program.

15 Ibid.
There are concerns that the moral hazard problem, already reflected in the large number of strategic NPLs in the country, would spread to the grass-root level as well. Imagine a case where two farmers borrow the same amount of money from the government’s bank. Farmer A is a good farmer who is diligent and disciplined. He uses his loan well and is able to recoup his investment within the stipulated period of time, pays his debt to the government’s bank, and makes plans for his agricultural improvement and expansion. Farmer B is opposite. He uses his loan badly, spending it on consumer goods rather than on investment. When the time comes to pay back the debt, he is unable to do so. Now the government comes out with a policy to help Farmer B while Farmer A receives nothing from the government. This not only distorts good economic decision making and destroy good ‘debt culture’, it has the effect of rewarding the indigent and punishing the diligent. This is not saying that all indebted farmers are indigent—some indeed are afflicted by natural and market calamities, but the incentive packages should help both farmers equally. If Farmer B is to receive assistance from the state, similar assistance should also be made available to Farmer A. This is the basic idea that should govern the way the government gives a debt amnesty to small farmers. It does not seem that this idea lies beneath the debt moratorium policy of the current government.

(e) The People’s Bank

Actually this idea was already conceived by the previous government but it did not have the opportunity to operate it. When the new government came into power, this idea was independently developed and expanded. In an effort to ensure better and improved access to banking facilities and resources for low income citizens to enhance their capacity to increase their income from self-employment, and eventually reduce their dependence on organised and punitive money market sources, the government’s ‘People’s Bank’ program commenced its operation on June 25, 2001.

It is very easy to become a member of this program, one only needs to have a contactable address and a determination to start self-employment, plus a savings deposit account at the Government Savings Bank (GSB). Apart from requesting for loans to facilitate self-employment, members can use all types of deposit services of the bank and can also receive regular employment training and advice. The GSB will consider each loan application after the deposit account has already been opened for two months, and will determine the appropriate amount of loan. The loans can be used as working capital in self-employment, to repay (employment-related) personal debts incurred elsewhere, or for use in necessary day-to-day expenditures; on the condition that borrowers are credit worthy enough. At present, the first batch of loan to each person is limited to 30,000 baht (double from its original limit of 15,000 baht), while the second batch of loan has a higher cap of 50,000 baht – but this amount could be higher provided that there is adequate collateral. Interest to be charged on these loans is fixed at 1 per cent per month. Borrowers can repay both the principal and the interests on a monthly basis, with repayment terms varying from 13 to 37

16 This is different from Krung Thai Bank’s Community Bank Program which complements the government’s People’s Bank Program. KTB’s program focuses on customers with higher borrowing needs, especially startup manufacturers. The loan offers are up to 50,000 baht each, with up to 3 year repayment terms.
periods (months). Both personal guarantees and asset collaterals are accepted in this program.

As of February 15th, 2002, there were approximately 500,000 members in the program, of which approximately 70 per cent have submitted loan requests and 83 per cent of these loan requests have been approved – totalling around 4,000 million baht. Forty per cent of members are from the Central region, 29 per cent from the Northeastern region, 18 per cent from the Northern region, and 13 per cent from the Southern region. It is reported that approximately 3,000 new members are joining the program each month.

Despite the fact that the stated 1 per cent per month interest rate seems low, the principal that is used to calculate the interests does not reduce with each debt repayment. Therefore, the real interest that the borrowers have to pay is much higher than a simple 12 per cent per year. As it turns out, members who have borrowed from this program have to pay approximately 22 per cent effective interest per year. The People’s Bank argues that there is a need to charge high interest rate because the effective cost of the Bank in providing loans to the members is approximately 18 per cent per year, as it has to incur large expenses in hiring 500 new staff and motorcycles for use in collecting debts. In addition, the loans were granted to retail borrowers who are mostly considered to be in a high-risk category.

There are several problems encountered by program administrators. They include members who do not fully understand the Program’s criteria and conditions, do not have continuous savings stream, resulting in the lack of funds for future employment capital, cannot find acceptable collateral or guarantor, have too much debt ‘outside the system, do not have adequate planning on how to use the loans properly, or move their places of residence frequently, making it difficult for bank representatives to locate them. Despite these problems, however, it can be admitted that this People’s Bank is a great help to the poor or near-poor. Without state intervention, poor borrowers with little or no collaterals would have little chance of borrow from commercial banks. So, this intervention is to supplement normal functioning of the market rather than to add obstacles to it.

5. Summary, Conclusions and Policy Implications

This paper has tried to address the issues of the dichotomy or trade-off between economic growth and promotion of social welfare in the context of the development of Thailand in the last 40 years or so, and the outcome of the economic crisis that struck the country in 1997. The main argument is that the Thai government has adopted free-market approach to economic development with the private sector playing the leading role in private investment and the public sector providing institutional and infrastructure support. This development approach has been beneficial to Thailand and its people in the past 40 years, as can be seen by the rapid rate of economic growth, the rate of increase of household and individual income, and the subsequent reduction in poverty. As poverty reduction is a direct consequent of economic growth, the government was under no pressure to institute specific anti-poverty policies that directly attack remaining poverty. The 1997 economic crisis has reversed the trend of poverty decline, as well as slowed improvement in income inequality, making the government more conscious about the effects of economic
growth and its impacts on social welfare. The development policies of the current
government in Thailand have taken into account various measures to increase social
welfare of the Thai people. However, many of these policies measures are inefficient
and wasteful as they distort the working mechanisms of the market. It is still
important that the government maintains satisfactory economic growth through good
macroeconomic management, and use public resources more efficiently by the better
targeting of the poor and the better delivery system of public expenditure.

This paper also discussed how the crisis started in Thailand and how the government
had dealt with the most severe economic problems in its recorded history. It has
looked at some of the more important macroeconomic indicators that show the state of
the economy such as the growth in GDP, the production conditions in both
agricultural and manufacturing sectors, the household consumption levels, the price
levels, and so on, and at the impact of the crisis on the welfare or well-being of the
people. Foremost in the government’s concern is the employment and unemployment
situations facing the Thai households during and after the depth of the crisis. It is
obvious that welfare and well-being of most Thai people have declined, although the
severity of the problem had not gone beyond its worse expectation. There are several
explanations for this resiliency in the life of the Thai people. One is the existence of
the family ties that bind members together in time of trouble and crisis. The other is
the reasonable public policy to help the public in needs. However, there is a danger in
trying to raise welfare of the people through inefficient economic means. This wastes
resources and may not achieve the twin goals of reasonable rate of economic growth
and satisfactory level of social welfare.

The economic crisis of 1997 has taught the Thais many lessons. One is not to get
carried away by the appearance of rapid economic growth, and the other is not live
beyond one’s means. The new Philosophy of Sufficiency Economy which stresses
moderation, constant awareness and adjustment to surrounding environment, and
careful management of risk has become a guiding principle of present and future
development of Thailand. However, there is still much to do in reducing the
remaining poverty and income inequality. This is the main tasks that any government
in Thailand will have to tackle.

The present government of Thailand under the leadership of Mr. Thaksin Shinawatra
came into power with enormous political support from the Thai population. This
makes it easier for him to carry out economic policies that continue to get the Thai
economy out of recession and strengthen its macroeconomy. Despite the earlier
perception that his government was inward-looking and anti-foreigners, the true
nature of this government is very much outward-looking and market-oriented. 17 This
is good and should help future economic position of Thailand. However, this
government is laden with several election promises to undertake several welfare-
oriented policies that are very costly, inefficient, and unlikely to fulfil the objectives
of raising the welfare of the people in the long run. The creation of huge public debts
to finance these policies can become the Achilles’ Heel of this government. In the
final analysis, it is always proper to refer to the Philosophy of Sufficiency Economy to
find an answer to development policies that give balance between sustainable
economic growth and adequate social welfare and protection.

17 On the analysis of foreign economic policy of the new government, see Medhi (2001b).
References


Bank of Thailand (various years), Economic and Financial Statistics.


_______(various years) National Income of Thailand.

National Statistical Office (NSO), (various years), Labour Force Surveys (LFS).
_______(various years) Socio-Economic Surveys (SES).


Box 1: The Philosophy of Sufficiency Economy: Thailand’s New Guiding Development Principle

The economic crisis of 1997 affects everyone in Thailand even His Majesty the King. Seeing many of his subjects suffering from the pain of economic crisis, he gave his kind words of advice that Thai people should change the economic philosophy of their livelihood so as to be able to cope with present economic adversity and withstand future economic insecurity. His Majesty’s words has become known as the Philosophy of Sufficiency Economy, and has been used as the guiding principle for the drafting of the current 9th National Economic and Social Development Plan.

This philosophical statement can be summed in just one paragraph, in Thai, and the following is the translation from that paragraph:

- Sufficiency Economy is a philosophy that guides the livelihood and behaviour of people at all levels, from family to community to the country, on matters concerning national development and administration so that the ‘middle way’ is observed, especially economic development that keeps up with the world of globalisation. Sufficiency means moderation, reasonableness, including the need to build reasonable immunity system against any shocks from the outside as well as from the inside. In so doing, one must rely on intelligence, attentiveness and extreme care to use all kinds of knowledge in making plan and in carrying out every step of its implementation. And at the same time we must build up the spiritual foundation of all people in the nation, especially state officials, scholars, and business people of all levels, to be conscious of moral integrity and honesty, and to strive for appropriate wisdom to live the life with forbearance, diligence, self-awareness, intelligence, and attentiveness, so as to maintain the balance and readiness to better cope with rapid physical, social, environmental and cultural changes from the outside world.

In essence, His Majesty’s philosophy could be interpreted to include three major elements: (1) moderation in consumption; (2) capability of self reliance; and (3) immunity against external shocks. This philosophy does not reject the force of globalisation but supports the need to live and cope with it.
Box 2: Urgent Policies of the New Government of Mr Thaksin Shinawatra

(1) Immediately grant a grace period for both interest and principle payments for 3 years for individual small farmers to relieve their debt burden as part of a comprehensive reform of the traditional farm economy to be more viable and self sustaining in the long term.

(2) Establishment of the Village and Urban Revolving Fund, funded with one million baht each as a loan facility available for individuals and households of each community to borrow for local investment and supplementary vocations. Concurrently, the Government will promote a "One Village One Product" project to enable each community to develop and market its own local product or products based on traditional indigenous expertise and local know-how. The Government is further prepared to provide additional assistance in terms of appropriate modern technology and new management techniques to market such local products from the village to domestic and international outlets through a national or international retail network or through the internet.

(3) Establish a People’s Bank to ensure better and improved access to banking facilities and resources for low income citizens to enhance their capacity to increasing their income from self employment and thus reduce their dependence on organised and punitive money market sources.

(4) Establish the Bank for Small-and Medium-sized Enterprise in order to promote existing and increasing the number of entrepreneurs in a systematic manner with a view to expanding the national productivity base, increasing additional employment opportunity and creating income, promoting exports, and serving as the mainstay for future national economic growth and stability.

(5) Establish a National Asset Management Corporation in order to comprehensively solve the problem of Non-Performing Loans (NPLs) in the commercial banking system swiftly, systematically, comprehensively and to enable the financial system to resume their normal credit functions.

(6) Utilise State Enterprise as key vehicle to mobilise domestic resources from Thai investors to promote revitalisation and development of the Thai economy through selling shares of incorporating a holding company incorporated by grouping a number of state enterprises with strong income potentials employing professional management and free from political interference as one alternative and listing of individual state enterprise directly in the Stock Market of Thailand at the appropriate time as another alternative.

(7) Provide universal health insurance with a view to reducing the overall cost to the country and the people in acquiring health-care capping each hospital visit at 30 baht. All Thai people will be guaranteed that equal access to a nationally acceptable standard of health care.

(8) Accelerate efforts to establish drug rehabilitation centres concurrently with implementing effective drug suppression and prevention measures.

(9) Encourage full and open public participation in the prevention and suppression of corruption.

Source: Prime Minister’s Statement to the Parliament on 26 February 2001.
### Table 1: Household Income and Poverty Incidence, 1962/63 to 2000

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<td>11.4</td>
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Sources: NSO, *Socioeconomic Surveys*, various years.
### Table 2: Incidence of Poverty, Whole Kingdom, New Series, 1988 to 1998.

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<th>Period</th>
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<th>Poverty gap ratio</th>
<th>Severity of poverty index</th>
<th>Number of poor in million</th>
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<td>1994</td>
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<th>Percentage change</th>
<th>Percentage of the poor</th>
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<td>1988-1990</td>
<td>-16.6</td>
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<td>14.1</td>
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<td>15.8</td>
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| Crisis index (for 1998) | 19.7  | 22.5  | 16.5  | 22.3  |
| Expected value (for 1998) | 10.8  | 2.6   | 1.0   | 6.4   |

**Additional information on poverty incidence**

| 1999   | 14.6 |
| 2000   | 14.2 |

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Table 3: The Distribution of Income in Thailand

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<th>Quintile2</th>
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<th>Quintile5</th>
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