



Introduction to Thailand Case Study and its Relevance to Lao P.D.R.

Financial Programming and Policies (PPP) Workshop
5 – 16 May 2014, Vangvieng, Lao P.D.R.

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Bank of Thailand



Agenda

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Pre-Crisis Background

2

Causes of Thailand Financial Crisis in 1997

3

Relevance of Thailand Crisis for Lao P.D.R.

4

Topics The Course will Cover

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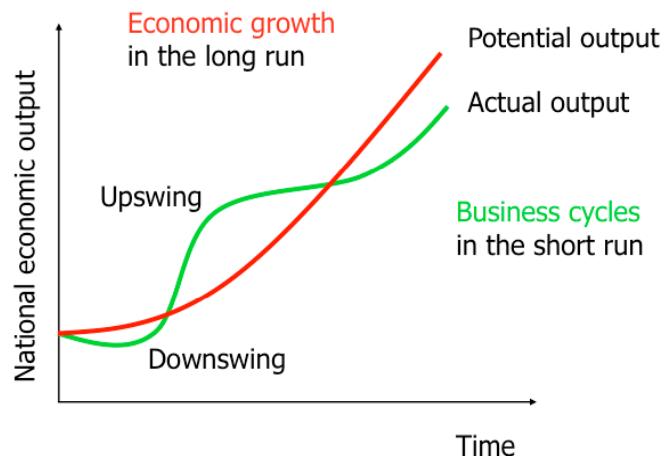
Thailand's Economic Conditions Pre-1997 : Changing from domestically oriented to Int'l connected

- The BOOM of Foreign Direct Investment (FDI)
- Export-Led economy, mostly by the manufacturing sector
- Export destination was clustered around G3 economies, not well-diversified
- Introduction of “International Banking Facility” (IBF)
- Crawling pegged exchange rate with implicitly known moving band (± 0.20 from previous day)

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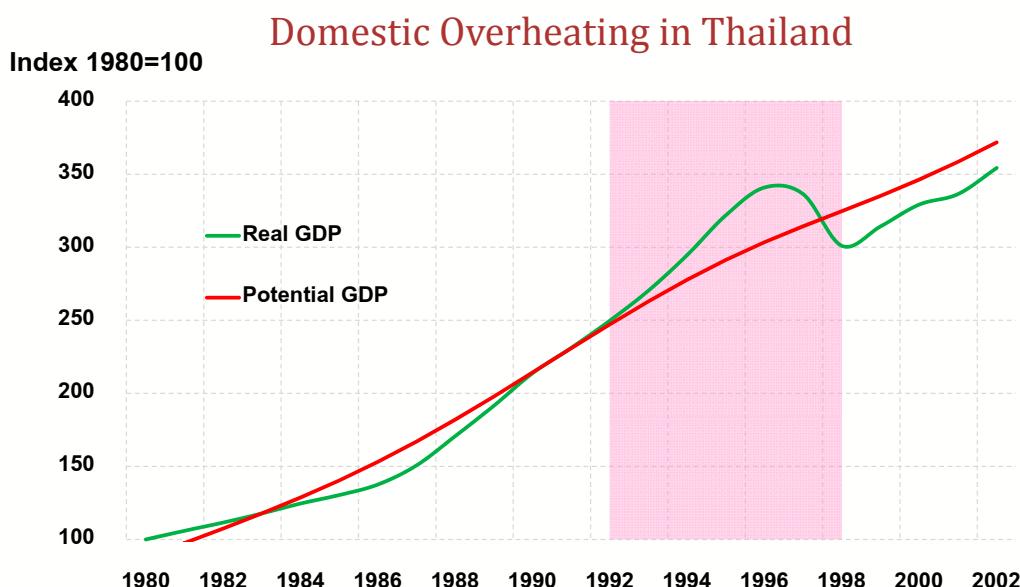
These Factors led to Economic Boom (overheat)

Domestic Overheating: Recap

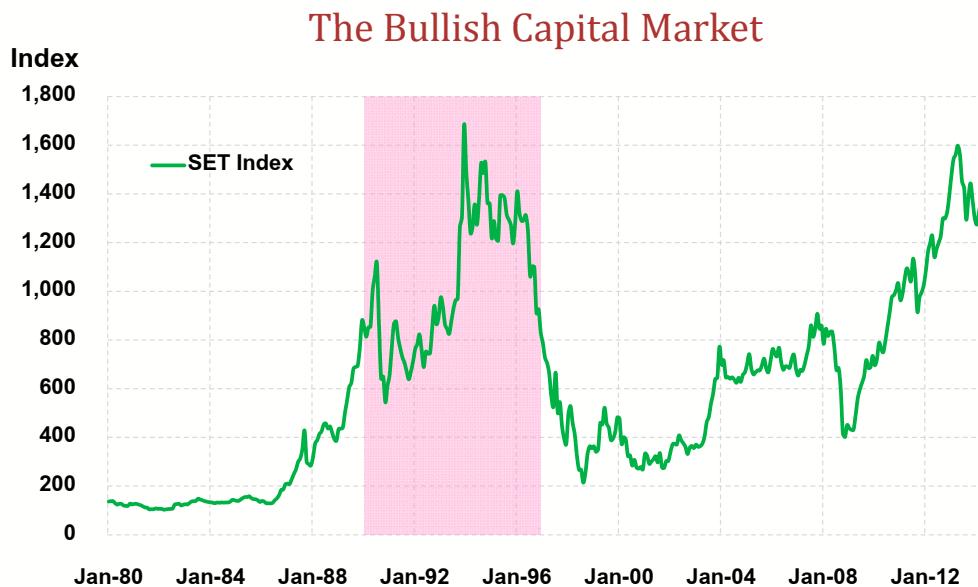


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Economic Growth Averaging 7.6% during 1977 – 1996



... and Contributed to Asset Price Bubbles

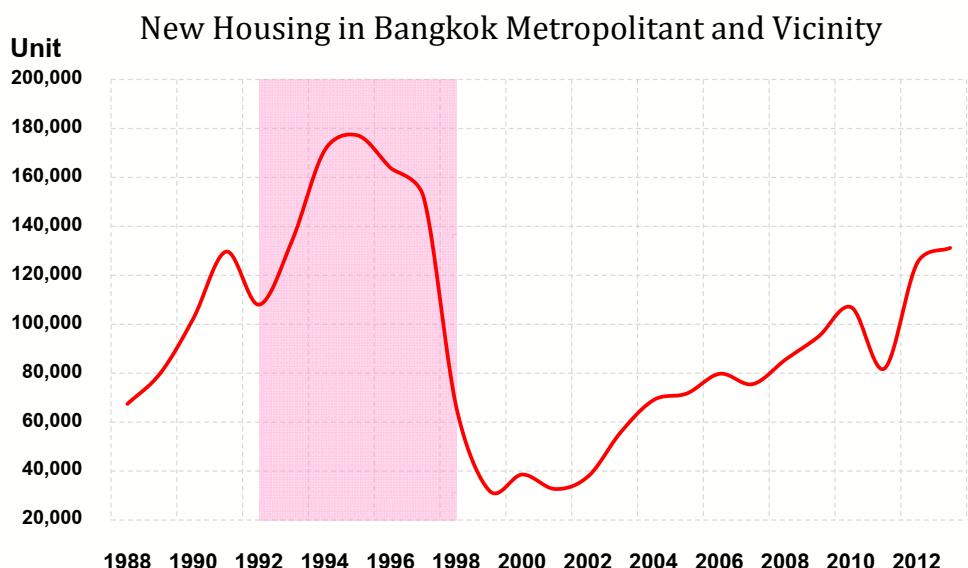


Source: The Stock Exchange of Thailand

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... and Contributed to Asset Price Bubbles

Real Estate Bubble



Source: Bank of Thailand

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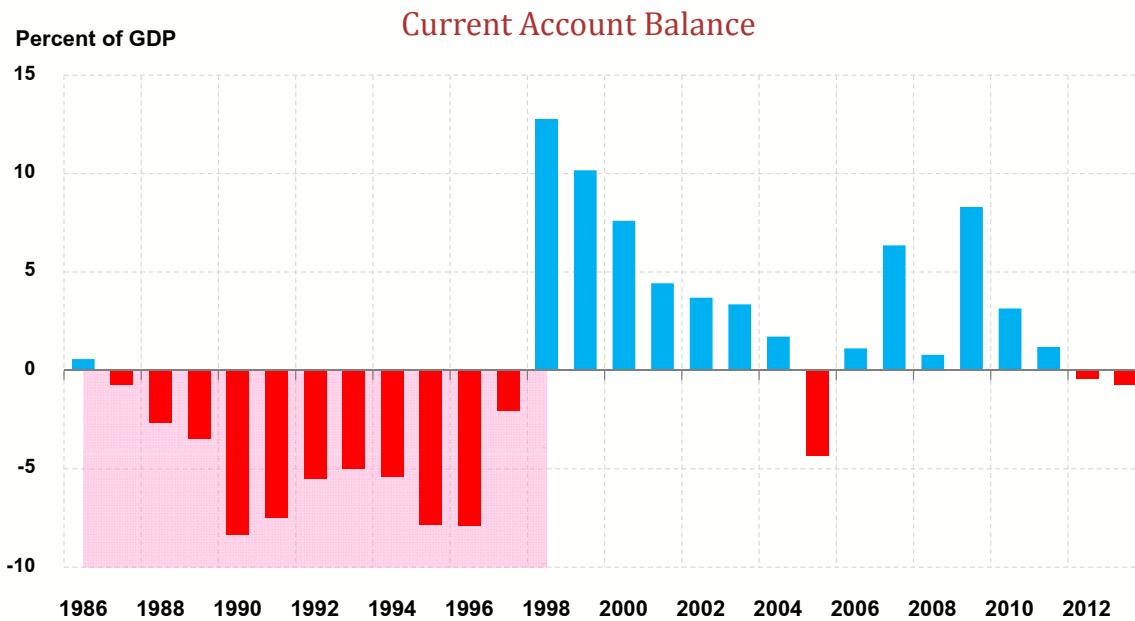
Topics The Course will Cover

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**Under the boom, vulnerabilities were accumulated
led by a number of factors**

- Persistently high current account deficits
- Financial and Capital account liberalization
- Weaknesses in the financial system
- Forbearance of supervisory authority
- Inappropriate macroeconomic policies
- Political instability

Persistently high current account deficits

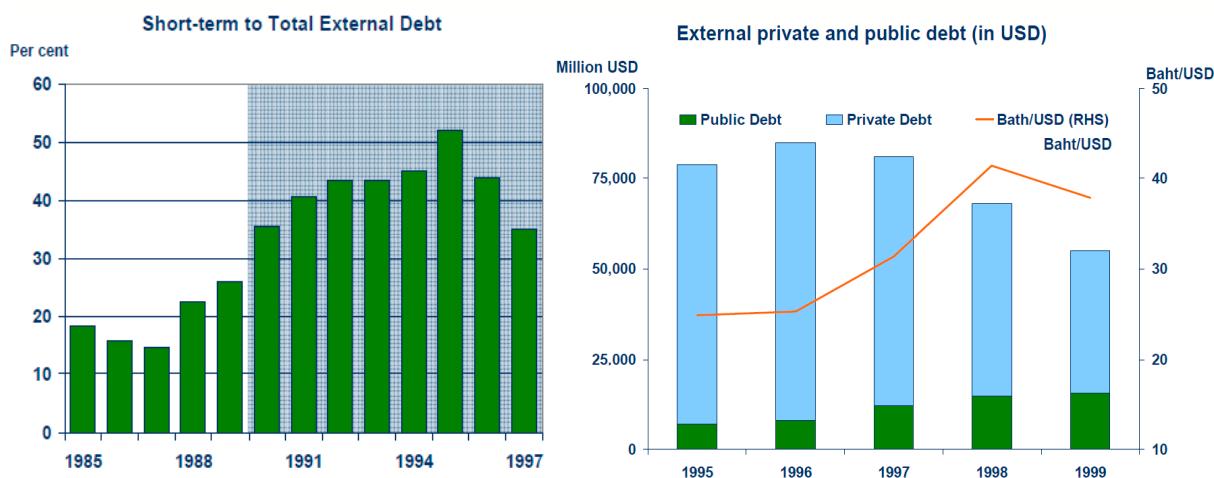


Source: IMF World Economic Outlook Database, April 2014

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Financial and Capital account liberalization

The BIBF, established in 1993, enhanced the capacity of Thai FIs in international banking business and facilitated foreign borrowing for domestic investment.



Boom in capital inflows denominated by short-term debt dominating

Foreign debt buildup followed. Most borrowing was private.

Source: Bank of Thailand

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Weaknesses in the financial system

- Weak governance at corporate firms and financial institutions
 - lending money recklessly without a prudent procedure of lending contraction and monitoring
- Large-scale maturity and currency mismatch on balance sheets
 - Relied on short-term borrowing in foreign currency but provided long-term loans in domestic currency

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Forbearance of supervisory authority

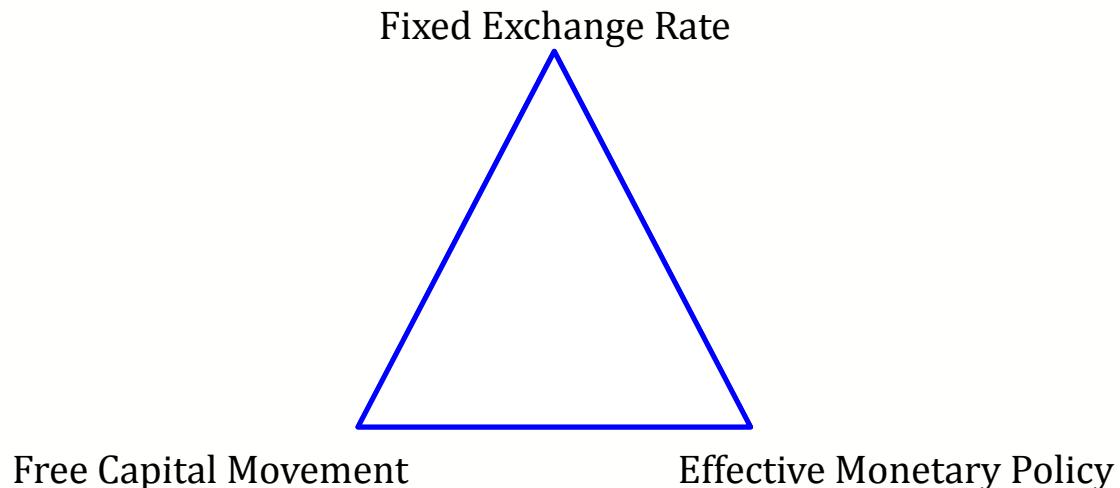
- A weak and under-supervised financial system
- Delayed policy responses to the mounting problems



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Inappropriate macroeconomic policies

The Impossible Trinity



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Political instability

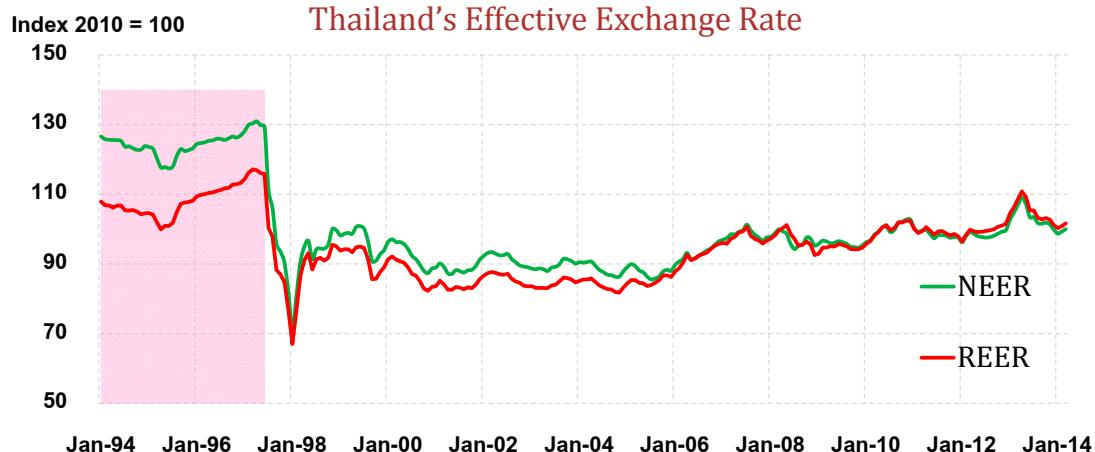
- Politics in transition period of “democracy” with instability: within 6 years before the crisis, Thailand had 4 governments, 10 finance ministers, and 4 BOT governors



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The trigger points

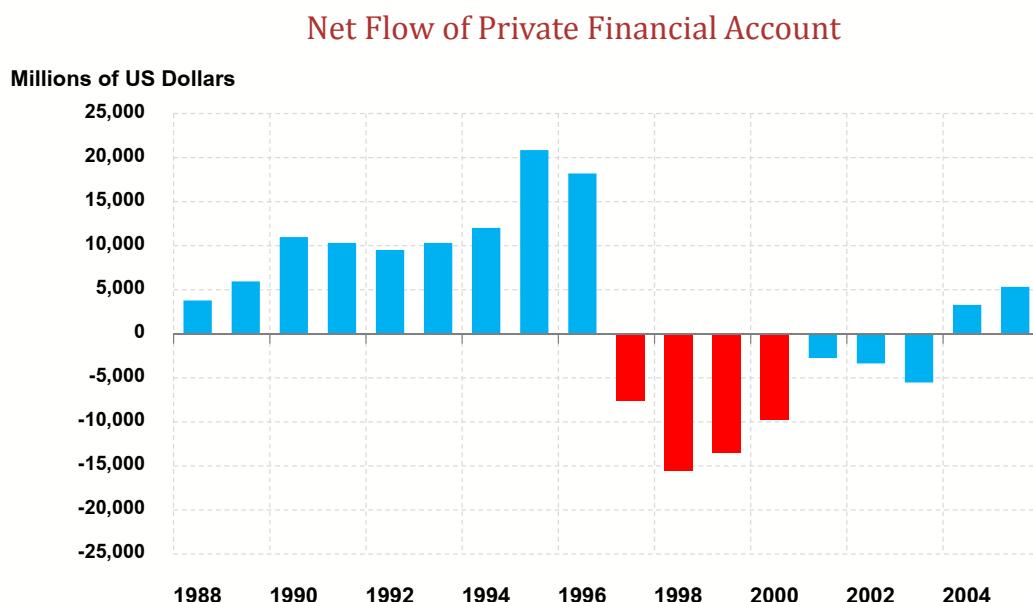
- Sharp fall in merchandise exports in 1996 due to
 - Fall of the world's demand of semiconductors which was one of the Thai major exports
 - China emerged as an intimidating competitor in international trade
 - the US dollar appreciated, Thailand became less competitive since baht was pegged to the US dollar



Source: BIS

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Investors' confidence waned as economic slowdown, leading to excessive capital reversal

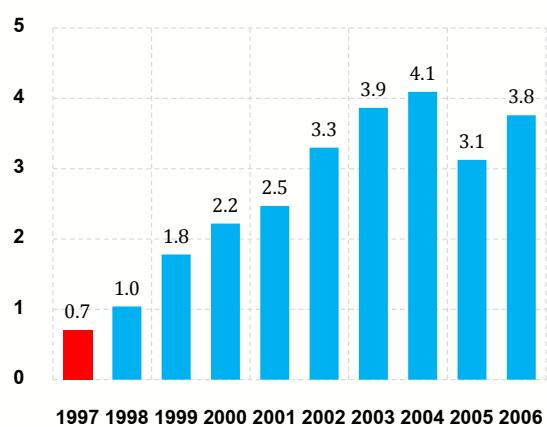


Source: Bank of Thailand

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Vulnerability to speculative attacks increased as reserves to short-term debt declined. Under attack, reserves fell precipitously, leading to the abandonment of the fixed parity.

International Reserves to Short-term Debt Ratio



Exchange Rate



Source: Bank of Thailand

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Asset price bubble burst and banks run



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Many businesses closed down and unemployment rose



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This was one of the worst in Thai economic history



Source: World Bank and Office of the National Economic and Social Development Board (NESDB)

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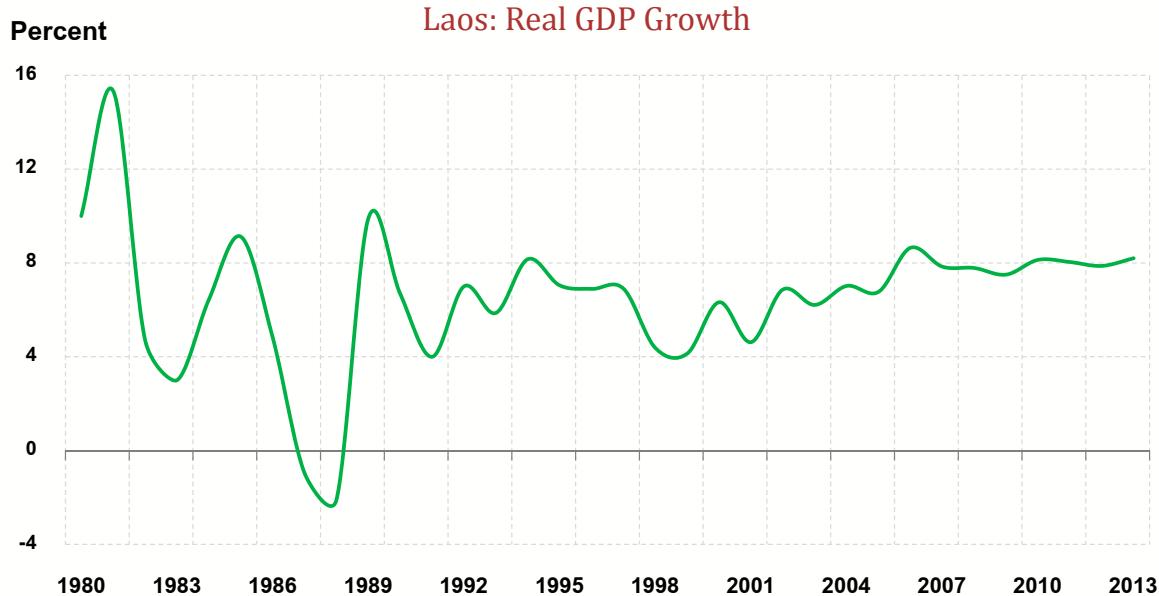
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Why the Thailand Crisis is still Relevant

- Thailand financial crisis appeared to be very similar to Mexican crisis of 1994-95.
- The crisis was built upon macroeconomic imbalances of the country, combined with faulty structure of financial sector.
- A similar type of financial crisis could happen to any country in the future.
- The global financial crisis is the most recent instance where element of the Thailand crisis resurfaced.

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Domestic overheating in Lao P.D.R. ?

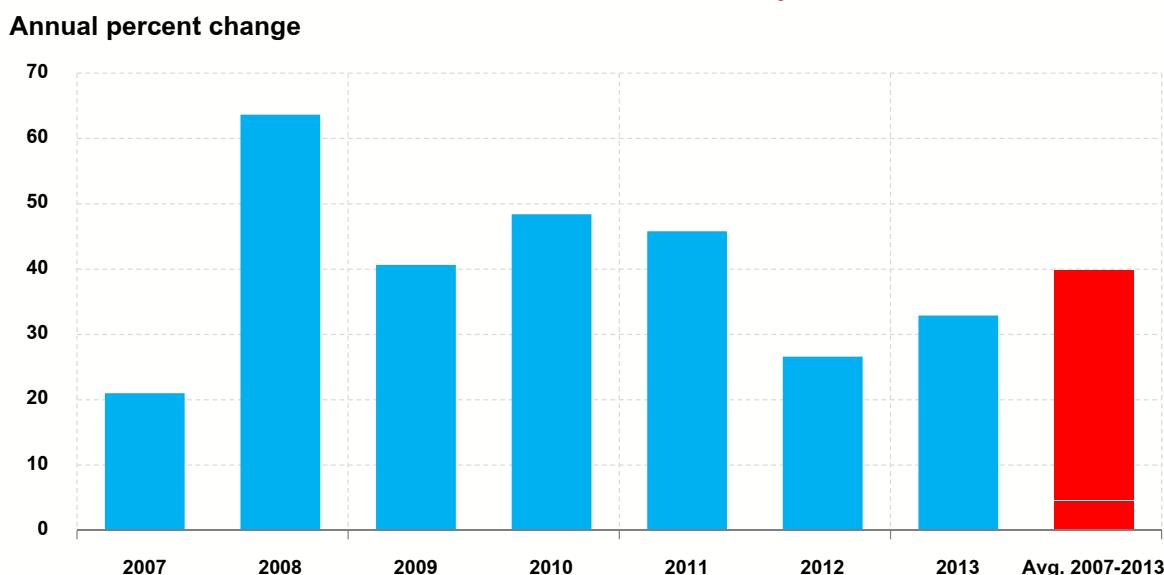


Source: IMF World Economic Outlook Database, April 2014

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Bank credit has expanded rapidly, raising concerns about domestic banking sector soundness

Laos: Credit to the Economy

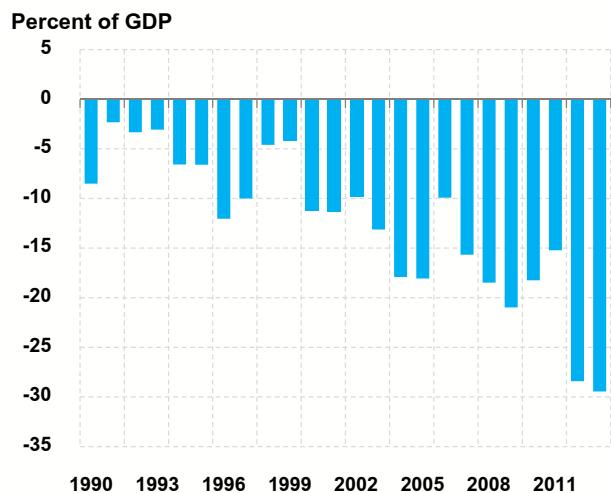


Source: Bank of Lao P.D.R. Annual Report and IMF Staff Report

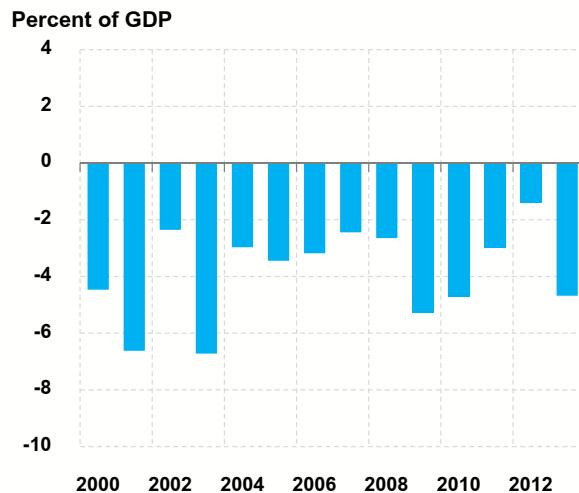
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Persistently twin deficits Is it going to be sustainable?

Laos: Current Account Balance



Laos: Fiscal Balance



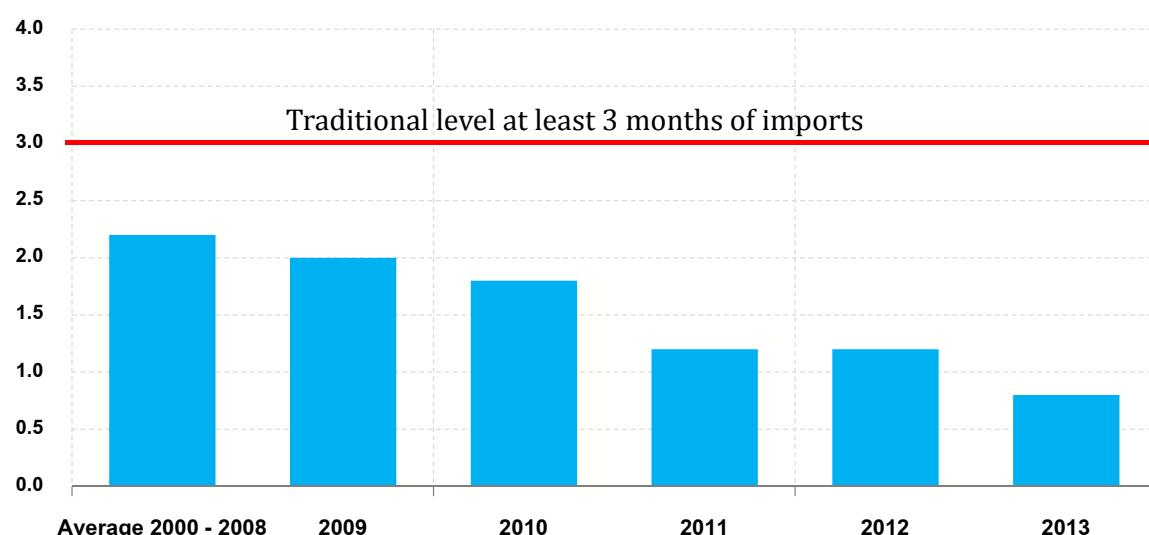
Source: IMF World Economic Outlook Database, April 2014

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International reserves may not offer adequate protection against adverse external shocks

In months of imports

Laos: International Reserves



Source: Lao P.D.R. – Staff Report for the 2013 Article IV Consultation

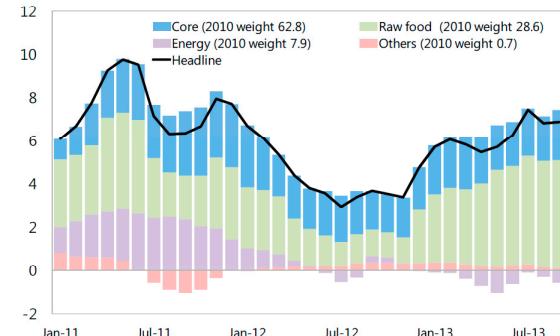
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Sharp real exchange rate appreciation, partly due to rising inflation, threatens country's competitiveness

Real Effective Exchange Rates 1/
(Index, March 2005=100)



Contribution to Headline Inflation 1/
(In percentage points)



Source: Lao P.D.R. – Staff Report for the 2013 Article IV Consultation

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Topics the course will cover

- Real sector
- External sector
- Fiscal sector
- Monetary sector

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Real sector – key issues

- Understanding the system of national accounts
- Measuring real GDP
- Generating GDP projections using production and expenditure approach and reconciling those
- Analyzing GDP trends and its components

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External sector – key issues

- Understanding the current account balance
- Discussing the role of real exchange rate for the current account
- Analyzing linkages between real sector and current account

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Fiscal sector – key issues

- Understanding the basic principles of fiscal accounting
- Generating budget projections, i.e. revenue, expenditure and financing projections
- Discussing fiscal policy options for addressing the crisis
- Generating public debt projections

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Monetary sector – key issues

- Understanding the monetary accounts and its linkages to other sectors
- Discussing monetary policy options to address the crisis, especially exchange rate options