Chapter 7

Fiscal Issues in Thailand: Assessment on the Impact of Stimulus, Fiscal Tranparency and Fiscal Risk

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CHAPTER 7

Fiscal Issues in Thailand: Assessment on the Impact of Stimulus, Fiscal Transparency and Fiscal Risk

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Sound fundamentals, quick and forceful policy responses, including fiscal stimulus, contributed to Thailand's economic recovery in the aftermath of the crisis. As the economy is recovering, the near-term challenge is to identify, communicate and begin to implement fiscal exit strategies from policy support. Moreover, fiscal policies in the Asian economies can "simultaneously" help strengthen their future growth potential. This paper reviews the impact of the recent global financial crisis for fiscal policy and identifies lessons for designing and implementing strategies for exit from fiscal policy support in the case of Thailand.

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EXECUTIVE SUMMARY

The Thai economy was affected by the Global Financial Crisis (GFC) through shocks to value chain (trade channel) and financial channel. Contraction in global demand led to declines in export, manufacturing production and capital utilization accordingly, which then led to declining in the country's consumption and investment. On the other hand, interest rate gap between Thailand and advanced economy became widening caused massive capital inflows and Baht appreciation, which brought about the severe impact to labour intensive production sectors of the country, while the sectors with high import content benefited from this incident. Baht had appreciated by 10% against the US Dollar in 2010.

Regarding the fiscal position of the country before and after the GFC, it is obvious that the automatic stabilizer worked effectively as the government revenue declined significantly in 2009 and surged again in 2010 after the economics recovered. However, it can be seen that the fiscal position is deficit together with an upward trend of the public debt as the government have adopted various fiscal stimulus to counter impacts of global crises. The fiscal stimulus packages have included short-term expenditure measures namely Stimulus Package 1 (SP1) which amounted THB116.7 Billions aiming to reduce impact of the GFC, long-term investment plan (Stimulus Package 2 (SP2)) which amounted THB 1.43 Trillion aiming to improve the country's competitiveness, and tax measures. In 2009, the Thai government imposed -5.6% budget deficits to GDP due to these measures.

The impacts of fiscal stimulus and monetary policies have been measured. It was found that the SP1 could affect the real GDP 0.9% additional growth, while the tax measures could cause 0.06% additional growth. On the other hand, as the SP2 is a multi-year investment program, it was estimated that disbursements of the program could bring about 1.5% additional growth in 2010, 1.2% in 2011 and 1.1% in 2012. Moreover, in this paper, it is noticed that simultaneous fiscal stimulus in Asia could also contribute to additional real GDP growth of the Thai economy. It is found that the

Asian stimulus brought about 0.9% additional growth in 2009 and 0.3% additional growth in 2010.

To maintain the fiscal sustainability of the country, the Thai Ministry of Finance (MOF) and the Bureau of Budget (BOB) have signed a MOU to recover balance of budget by using fiscal policies and budget management tools within 5 years or 2015 which leads to MOF strategic plan to revise government expenditure (expenditure control) and revenues (revenue collection efficiencies and introduction of new tax measures) to respond to that obligation. Currently, due to higher revenue collection efficiencies, stable economic growth assumptions and direction to control its expenditures, it is expected that the Thai government can resume budget balance within 2015.

Regarding the fiscal transparency and management of future fiscal risk issues, from the IMF assessment, it is reported that Thailand has met the requirements of the fiscal transparency code. However, there are risks from political and fiscal management rules that might cause some delays or impossibilities of some investment expenditures and the impacts of the fiscal stimulus. On the other hand, management of future long term risk has been made. The contingent liabilities from both explicit and implicit commitment and guarantees such as the Social Security Fund and Universal Health Care Program have realized. Many risk management measures have been proposed and adopted to reduce or prevent those future liabilities.

1. Introduction

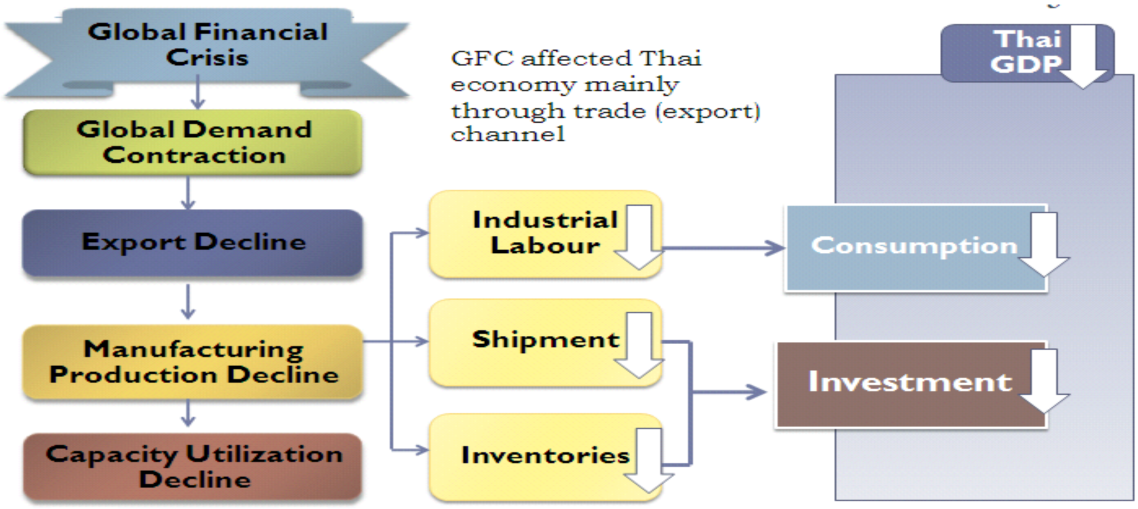
It is widely recognised that 1997 was an important year in the history of Asia. The turmoil that rocked Asia's currencies in 1997 was the world's third major currency crisis of the 1990s. Its forerunners were the crisis in the European Monetary System in 1992-93 and the Mexican peso crisis in 1994-95. Even so, the Asian financial crisis can be traced to a set of interrelated problems. Thus there is not a single rescue package to resolve it.

Interestingly, while the issues have changed in the intervening 10 years, yet Asia remains no less central to the world economy now than it was then. Currently we welcome 2007 with a look back to 1997, particularly focusing on how much things have changed since 1997. Having rebounded from the 1997 crisis, we find that in most cases, crisis-hit countries have taken a 180-degree turn over the past decade. We have experienced current account surpluses replacing deficits, international foreign reserves on the rise, currencies under pressure to appreciate instead of depreciate, and foreign capital continuing to flow in rather than fluxing out.

Turning to the remarkable year of 2008 Global financial crisis, whereas advanced economies experiencing a larger—and likely long lasting—deterioration, emerging economies also Thailand experienced less severe impact of the crisis. In this light, sound fundamentals and quick and forceful policy responses, particularly fiscal stimulus, contributed to economic recovery in Thailand in the aftermath of the crisis. Figure 1 explains transmission mechanism of 2008-2009 Global financial crisis to the Thai economy, while table 1 exhibits indicators of the shocks to the mechanism.

For macroeconomic perspectives, though the Thai real GDP was sharp declined in 2008Q4 – 2009Q3, the rebound from the global financial crisis was experienced then gave way to slower growth in the second and third quarters of 2010 (see Figure 2 and 3). GDP returned to pre-crisis levels following four quarters of strong growth. Without the tailwinds of the rebound, growth turned negative (qoq), but the economy performed better than expected. In the 2010Q2, higher-than-expected domestic and foreign consumption led to growth in manufacturing—negative GDP growth (qoq) was mainly due to the political turmoil, which caused tourism to plummet. Tourists returned in the third quarter, partly offsetting lower foreign and domestic consumption (the latter due to lower rural incomes as agriculture contracted sharply because of dry weather conditions earlier in the year). Going forward, growth is expected to pick up modestly driven by solid domestic demand supported by accommodative fiscal and monetary policies.

Figure 1. Transmission Mechanism of 2008-2009 Global Financial Crisis to the Thai Economy



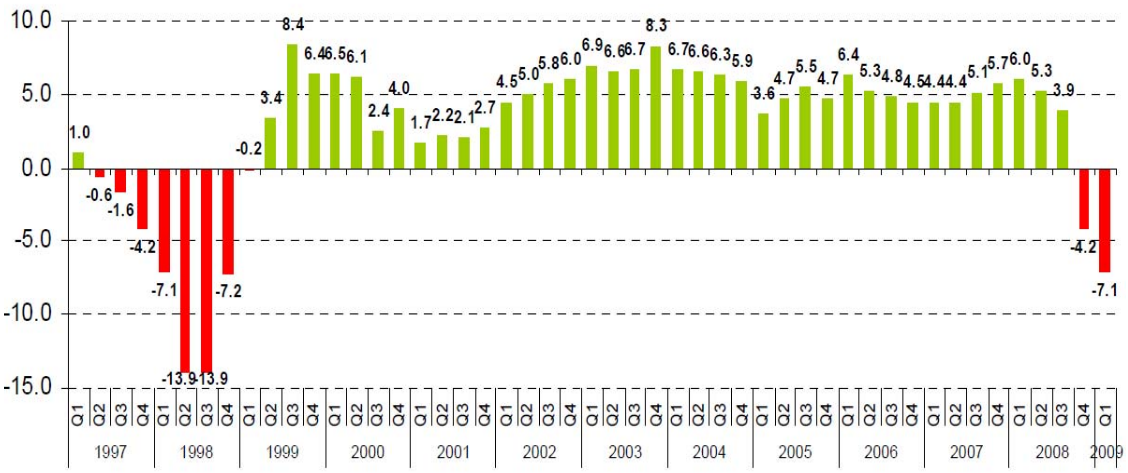
Source: FPRI (2011).

Table 1. Indicators of Value Chain Shocks (Shocks to Trade Channel) during the Global Financial Crisis

Indicators (%YoY)	Q1 2008	Q2 2008	Q3 2008	Q4 2008	Q1 2009
1. Exports of Industrial Products	13.4	16.5	9.0	-16.7	-18.8
2. Production of Industrial Products	11.6	9.4	5.9	-9.7	-25.0
3. Capital Utilization (Level)	67.5	63.7	62.7	56.5	50.0
4. Industrial Labour Utilization	2.3	-1.8	0.2	-4.4	-8.5
5. Shipment of Industrial Products	12.0	11.6	3.5	-11.2	-22.0
6. Stock of Industrial Inventories	-1.3	-3.6	9.1	12.0	9.5

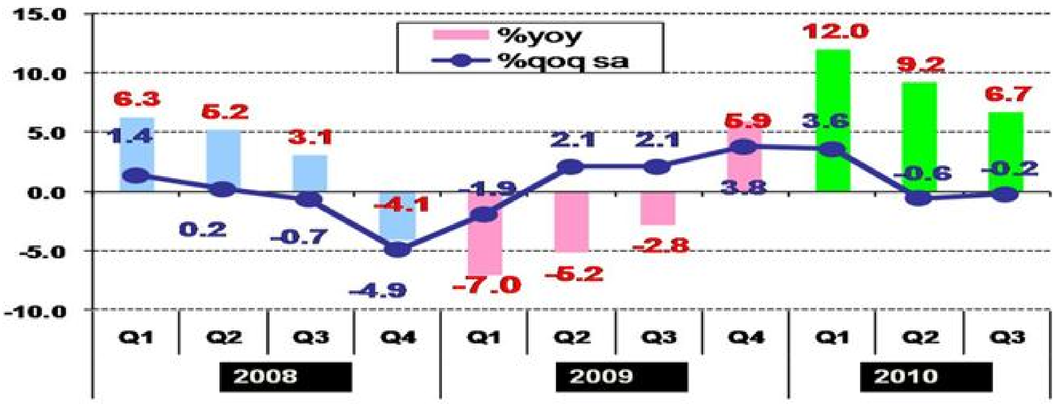
Source: Fiscal Policy Office (2010).

Figure 2. Thailand’s Real GDP Growth (1997-2009q1)



Source: FPO and FPRI (2010).

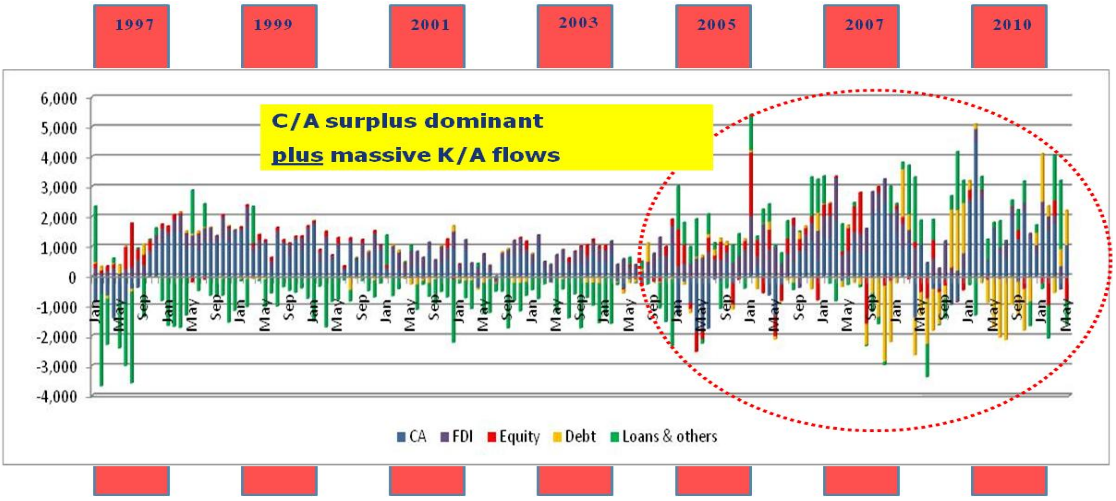
Figure 3. Thailand’s Real GDP Growth (2008 - 2010)



Source: FPO and FPRI (2011).

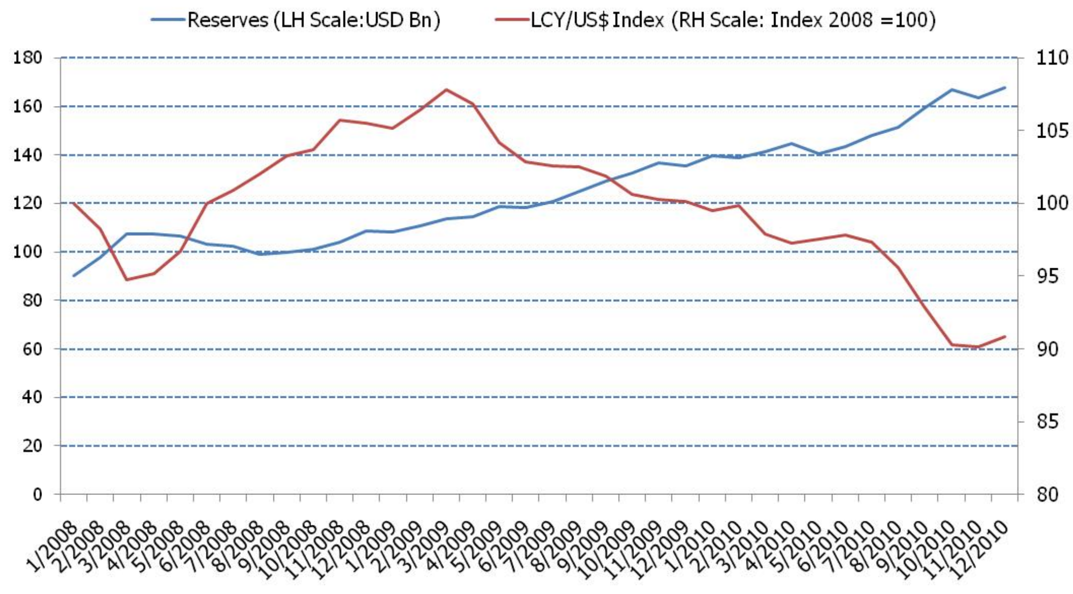
Focusing on the impact of global financial crisis both financial sector and real sector, these outcomes can be described as follows. As interest rate differentials with advanced economies started widening in the first half of 2010, capital flows from advanced to emerging economies have accelerated. Thailand had bucked this trend through June because of the political situation, which increased near-term risk perceptions of foreign investors (Figure 4) However, the resolution of the immediate political turmoil and Thailand‘s favorable growth outlook has led to a resumption of substantial foreign capital inflows.

Figure 4. Thailand's Capital Flows (1997 - 2010)



Source: BOT and FPRI calculation (2011).

Figure 5. Thailand's Foreign Exchange Reserves an Exchange Rate (2008 - 2010)



Source: CEIC and FPRI calculation (2011).

According to the Fiscal Policy Research Institute's (FPRI) exchange rate monitoring system, the positive capital flows from the current account and particularly portfolio channels have been observed (see Figure 4). This means the baht appreciated about 10 % against the US dollar in 2010 (see Figure 5). As a result of sterilized interventions to slow down the pace of exchange rate appreciation, foreign exchange reserves rose by USD 23.6 billion between January and November, reaching a record high. Reserves are equivalent to 11 months of trailing imports, nearly five times the sum of short-term debt and principal repayments due in 2011, and amount to about three-fourths of the country's gross external liabilities. On all three metrics, reserves are the largest in developing East Asia except China.

For the impact on real sector, the global financial crisis seriously hurt consumption, investment, and employment. The financial turmoil, via the negative wealth effect, has weakened consumer demand around the world, especially in the U.S. economy. In addition to the decrease in consumer demand, U.S. is the important trading partner of many countries. As the U.S. economy went downturn, many countries have gone through export deterioration.

Table 2. The FPRI Estimation on Effect of Baht Appreciation on Disaggregate Real Sector

Change in Exchange Rate	-12.00%
Change in Total Cap Return	-6.37%

	Key Ratios			Cost
	Wage / VA	CapReturn / VA	Export / Total Revenue	Capital Return
Agri	42.83%	57.17%	7.37%	-0.9%
Mining & Quarrying	17.71%	82.29%	20.00%	-4.7%
Food Manufacturing	43.16%	56.84%	31.26%	-21.1%
Textile Industry	61.66%	38.34%	30.29%	-17.6%
Saw Mills & Wood Products	63.13%	36.87%	48.42%	-21.4%
Paper & Printing	44.07%	55.93%	21.62%	4.3%
Rubber, Chem, and Petroluem	40.81%	59.19%	40.57%	-0.8%
Non-Metallic Product	44.04%	55.96%	41.11%	-23.6%
Metal, Metal Products and Machinery	47.02%	52.98%	55.34%	-14.8%
Automobile	46.08%	53.92%	14.47%	1.7%
Other Manufacturing	58.72%	41.28%	46.92%	-20.2%
Public Utility	29.47%	70.53%	3.02%	-0.4%
Construction	47.06%	52.94%	1.47%	9.7%
Trade	51.25%	48.75%	0.94%	-0.5%
Services	55.59%	44.41%	5.86%	-1.1%
Transport & Commu	36.73%	63.27%	19.55%	-10.6%
Other Services	47.32%	52.68%	62.07%	-28.0%

Source: FPRI (2007 and 2010).

Moreover, the FPRI has constructed a model to assess the impact of a sharp appreciation of the baht on the real sector. It is estimated that a 12% appreciation of the baht decreases the profit (total capital return) of the real sector by about 6.4%. Upon disaggregating the real sector, results show that the labour intensive sectors (i.e., agriculture, food manufacturing, and textile, etc.) tend to be adversely affected by a change in the exchange rate (see Table 2). On the other hand, “high-import content” sectors, such as paper and printing, automobile, and construction, tend to benefit from baht appreciation. This demonstrates that the baht appreciation is a two-sided coin. It benefits exporters with a high volume of imports and a low volume of exports, e.g., electricity plants and iron industry, because most of their revenues are in local currency, while their import costs are lowered. On the other hand, exporters with high levels of exports and low levels of imports, such as textiles, agriculture, and tourism, will lose their advantages.

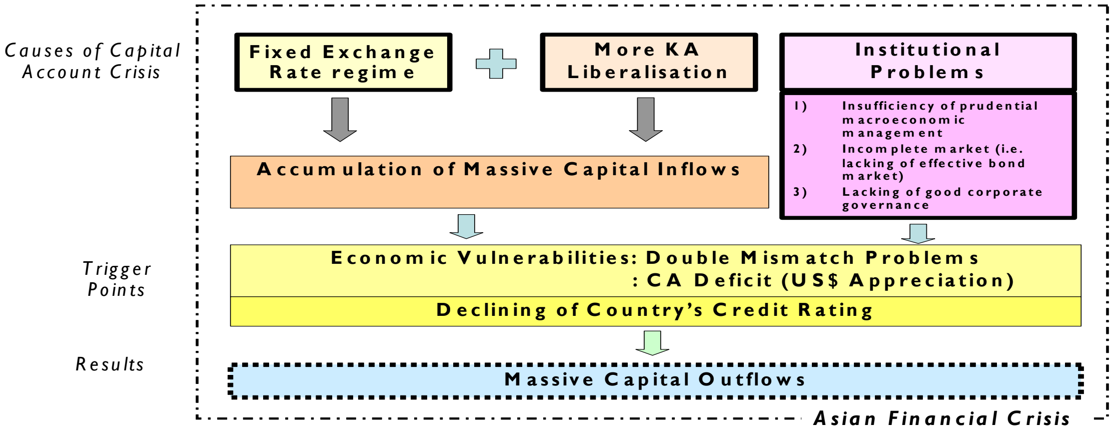
After the introduction of the Global financial crisis and the Thai economy, accordingly, this paper is structured as follows. Section 2 reviews the fiscal position both before and after the global financial crisis. Section 3 emphasises the impact of stimulus package, exit strategy and identification of future fiscal and macroeconomic risk. It highlights the near-term challenge of navigating the exit strategies in the case of Thailand. Finally, Section 4 provides fiscal transparency and anticipating policy for future crisis.

2. Fiscal Position-Before and After the Global Financial Crisis

2.1. The Conduct of Fiscal Policy during the Asian Financial Crisis 1997 - 1998

During the Asian financial crisis in 1997 – 1998, the conventional explanation laid on weak macroeconomic fundamentals that produce current account deficit, barely fits the Asian scenario. With the combination of fixed exchange rate regime and the high degree of capital liberalization, the Thai economy had become vulnerable to two major crisis-causes; current account deficit and double mismatch problems – currency and maturity mismatches. Thus, the Asian financial crisis was exemplified by massive capital inflows accumulated for years and sudden massive outflows in a short period of time, together with the lack of sufficient risk management system at the national and regional levels. The nature of Asian financial crisis is explained in Figure 6.

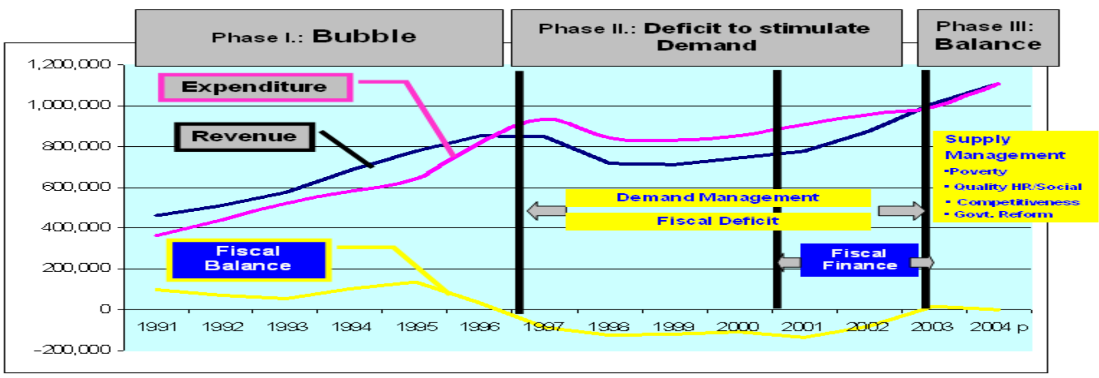
Figure 6. Nature of 1997 Asian Financial Crisis



Source: FPRI (2007).

To deal with the crisis, people's confidence and financial stability must be restored, along with economic sustainability. The conduct of fiscal policy was introduced to cope with the mentioned objectives. According to the International Monetary Fund (IMF), an increase in VAT rate and the reduction of current government expenditure were suggested as tightening fiscal policies. Nonetheless, Thailand's conduct of fiscal policy shifted from budget balance/ surplus towards more supportive stance through provision of temporary demand stimulus. After imposing the tight fiscal policy at the early stage of crisis management, the government refused to increase the VAT, but rather stimulated the domestic demand as well as introduced the fiscal finance policy as an alternative channel of micro credits. Thailand's fiscal policy and development phases are presented in Figure 7.

Figure 7. Thailand's Fiscal Policy and Development Phases



Source: FPRI (2007).

The fiscal finance was a part of the demand management of the dual tracks policy that ensured balanced growth between exports and domestic demand. In this connection, governments have attempted to strengthen different layers of the domestic economy, comprising the grass-roots economy, small and medium sized enterprises (SMEs) and large-scale business establishments [3]. In addition, the establishment of TAMC House for civil services and reduction of real estate transfer fee were aimed to stimulate the real estate sector. On the external front, the government intended to expand export bases via FTA. On the whole, the government restored the fiscal sustainability plan with the objective to create the country's fiscal discipline (targeted fiscal balance in 2005). Consequently, the dual-tracks policy paid off. The economy recovered quickly and the fiscal balance returned to a position in 2004. The last phase of fiscal-policy conduct then introduced the supply management concerning poverty reduction, human capital and competitiveness improvement, including the government structural reforms.

2.2. Fiscal Stimulus in 2008 - 2009

In 2008, the global financial crisis started with the subprime crisis in U.S. that influenced economy-wide to the financial system. The effect has spread worldwide to other regions in the global economy through the financial securities called CDOs and CDSs. The major cause of the crisis basically came from the lack of confidence among financial institutions that led to liquidity crunch in the system. Credit lines for business sector slowed down and the interbank lending procedure became stricter. Therefore, the liquidity crisis has emerged and increasingly affected the real sectors; production and export. In sum, the direct impacts were created through financial markets while the indirect impacts hit real sector via the channel of international trade.

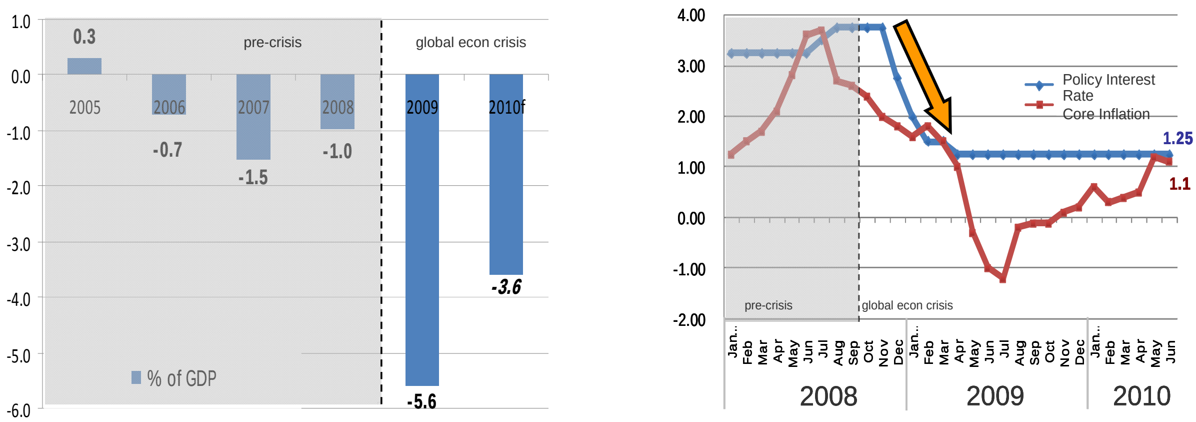
In the case of Thailand, the nature of the current crisis is different from the Asian financial crisis in 1997. Since Thailand's financial products and market are still in the developing phase, the effect from the crisis most likely struck the real sectors. It led to

[3] For example, the government has established a revolving village fund and a People's Bank Programme to provide micro-credit to promote economic prosperity at the grass-roots level. For SMEs, the government introduced new tax schemes for SMEs as an incentive for their investment. The SME Development Bank was also established to provide financial and advisory services to SMEs. Large-scale enterprises are being strengthened through the Thai Asset Management Corporation (TAMC), which has facilitated the debt and corporate restructuring for large corporations.

a decrease in export, and then production, along with an increase in local unemployment. In addition, as a level of income declined, the domestic expenditure dropped as well as consumption and investment. Nonetheless, the nature of current crisis was different from the one of Asian financial crisis since Thailand's financial sector was still strong with a high ratio of fund to total assets and a low proportion of NPLs. As a result, a challenge to the government was to solve the problem in the real sector, especially the export industry, and the problem of income reduction.

The Thai government has imposed three types of policy to rebuild confidence, gain economic recovery, and stimulate new economic growth. First, two phases of stimulus package, with the combination of tax measures, are implemented at different periods of time. Second, the quasi fiscal policy is implemented as a fast-track policy to create liquidity for business sector. Lastly, the monetary policy is introduced as another tool to stimulate the economic growth. Figure 8 shows that, in 2009, the government ran 5.6% budget deficit to GDP while the Bank of Thailand has reduced policy interest rate (RP 1 day) from 3.75% to 1.25%.

Figure 8. Government Budget and Interest Rate Policy Trends



Source: Fiscal Policy Office, Ministry of Finance.

In 2009, the fiscal stimulus packages were introduced to alleviate the impact of this global financial crisis and to help Thais from the economic recession. The Thai government has imposed two phases of the stimulus packages in accordance with an implementing period. The first stimulus package (SP1) is a set of instant measures under the purpose of economic recovery. The eighteen fiscal projects are implemented with the funding of THB 280 billions. The combination of fiscal projects is (1) Approximately THB 117 billions is funded from non-budgetary expenditures of the fiscal year 2009, (2) THB 124 billions is served for the price guarantee of agricultural products, (3) THB 40 billions is for the tax measures. Four economic engines are taken into consideration to setup the fiscal projects: consumption management, an increase in government investment and expenditures, private investment, and export and tourism supports. Table 3 demonstrates the related fiscal projects in Thailand's first stimulus package.

Table 3. Fiscal Projects in the First Stimulus Package

1. Domestic consumption stimulus	**2. Government investment and expenditure**
• THB 2000 cash hand-out for those earning < THB 15,000 per month • 5 public service subsidies program to lower costs of living for 6 months (5x6 subsidies) • Special prices for consumption commodities (Blue flag scheme) • Small reservoir construction • Old-age pension at THB 500/ month • Agriculture price guarantee	• 15-year free education • Training for unemployed workers • Sufficient economy fund • Irrigation project • Dust free road • Housing for junior police officers • Health station improvement
3. Private investment supports	**4. Export and tourism supports**
• Promotions of SMEs • Tax reduction for property trading • Credit guarantee for SMEs • Tax reduction for SMEs and Small and Community enterprises • Tax exemption from debt restructuring	• Risk management for exporters • National confidence restoration • Tourism promotion • Exemption of visa and landing fees • Tax deduction for seminar expenditure

Source: *http://www.chuaichart.com*

After the implementation of the SP1, the economy has continued recovering. Next step is to aim improvement of the country's competitiveness. The stimulus package 2 has a medium-to long-term goal to achieve economic growth by stimulating local employment and private investment. The target is to improve Thailand's competitiveness through fiscal liquidity, high-social-and-economic-return projects, and confidence buildup for crowding-in private investment. The detail of stimulus package 2 will be shortly described in the next section. Together with the stimulus packages, the mixture of tax measures is imposed to achieve the economic growth. Table 4 demonstrates the tax measures.

Table 4. Tax Measure Mixture for Economic Stimulus

Property tax	• Tax exemption for new housing with 2009 with the equivalent of paid amount, but not higher than THB 300,000, • Maintain the right of tax deduction for loan interest, not more than THB100,000, • Decrease specific business tax rate from 3.3% to 0.11, ended in March 2010, • Decrease administrative fee from 2% to 0.01%, ended in June 2010
SME tax	• Expand the minimum baseline of income for 0.5% tax calculation from THB 60,000 to THB 1,000,000 (or 9,700,000 companies)
Small and community enterprise tax	• Increase the ceiling of income base for tax exemption from THB 1.2 million to THB 1.8 million in 2009-10 (or 58,000 enterprises nationwide)
Tourist tax	• Corporate companies or partnerships can earn the tax deduction at double value of real payment for a company's local seminar or training in the accounting year of 2009.
Venture capital tax	• Extend the period of corporate registration of venture capital until 31 December 2011, • Relax the requirement for SMEs investment in the venture capital that must be at least 20% of the 1st year registered capital
Tax on financial institutions	• Exemption of tax relating debt restructuring - Income tax exemption for borrowers - Corporate tax exemption for lenders (financial institutions)
Tax on company limited	4 Exemption of tax relating business transfer (before 31 December 2009) for public company and company limited i.e., VAT, specific business tax, stamp duty, other fees on registration and legal transaction

Source: Fiscal Policy Office, Thailand.

As stated before, to create liquidity for the business sector, the quasi fiscal policy is implemented as a fast-track policy through the government's financial institutions. Table 5 shows the amount of stimulus package through each government bank.

Table 5. Stimulus Quasi Fiscal Package

Unit: THB Million

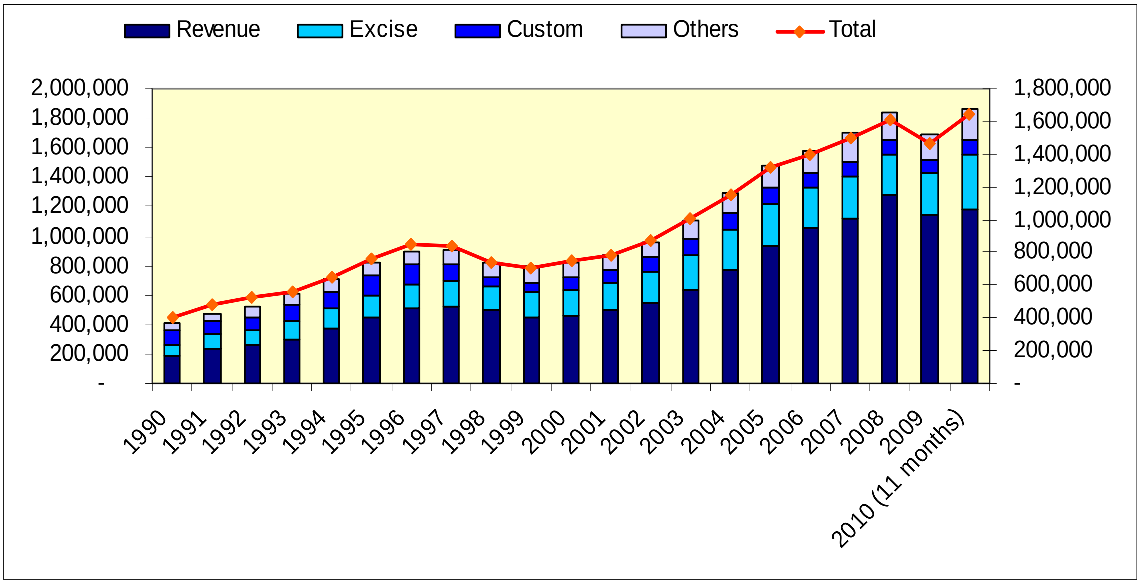
	Former Credit Target	Increased Credit Target	New Credit Target
Bank for Agriculture and Agricultural Co-Operatives	323,000	147,000	470,000
Savings Bank	162,600	80,000	242,600
Housing Bank	73,500	26,500	100,000
SME Bank	26,000	17,500	43,500
EXIM Bank	19,700	17,500	37,200
Islamic Bank of Thailand	20,700	13,000	33,700
Total	**625,500**	**301,500**	**927,000**

Source: Fiscal Policy Office, Ministry of Finance.

2.3. Contents of Fiscal Position

Putting together all economic stimulus plans of Thailand, the government's fiscal position must be investigated. In the past two decades, the government revenue has constantly grown, especially the revenue from corporate tax and value-added tax (VAT). This indicates a strong foundation of the Thai economy. At the same time, the revenue from the Excise Department has also increased, especially from excise fuel and automobile taxes; however, it is still at a smaller proportion of the total revenue. According to the fiscal policy office's report, the revenue collection in the third quarter of 2010 is amounting to THB 448 billion, or expanding by 15.5 % per year. This results in an increase in total government revenue throughout the third quarter of 2010 to THB 1,678.9 billion, exceeding the original revenue target by THB 328.9 billion. Comparatively to the same period of the 2009 fiscal year, it increased by 19 %. Figure 9 shows the combination of sources of government revenue.

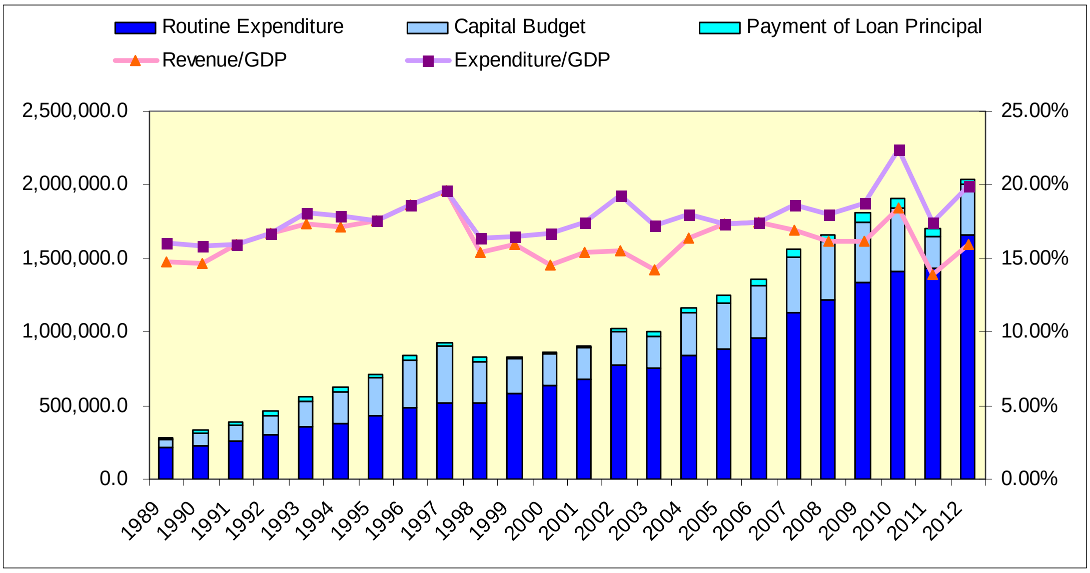
Figure 9. Thailand's Government Revenue



Source: Fiscal Policy Office, Ministry of Finance.

Considering the Thai government expenditure, the structure of budget expenditure is set under three major accounts in the fiscal year of 2010; routine expenditure, capital budget, payment of loan principals. The routine expenditure and capital budget compose of salary budget, operation budget, investment budget, subsidy budget, and others. Otherwise, the non-budgetary public expenditure is set for supporting the Thai economy in the period of economic recovery, the so-called "Strong Thailand (TKK) Program 2009 - 2012". Figure X.5 demonstrates a proportion of government expenditure. The routine expenditure has been a large proportion of the government expenditure for the past twenty years while the capital budget tends to increase overtime. Nevertheless, the projection says that the capital budget of the budgetary public expenditure would shrink down in the fiscal year of 2011. Taking a look at the ratio of revenue to GDP and expenditure to GDP, it shows that the ratio of revenue to GDP has always stayed lower than the one of expenditure to GDP since the Asian financial crisis in 1997.

Figure 10. Thailand's Government Expenditure



Source: Fiscal Policy Office, Ministry of Finance.

Turning to the non-budgetary government expenditure, the so-called "Strong Thailand 2012 (TKK) Program," as stated before, the purpose of the TKK Program is to create medium and long term stimulus package for economic recovery. The main objective is to encourage and build up Thailand's economic capability and competitiveness in order to survive the global economic crisis and to achieve superior position in the world economy. Economic indicators show that, up until present, the fiscal policies continue to support the Thai economy as evidenced by an increase in public expenditures. In September 2010, the budget disbursement accounted for THB 192.7 billion, resulting in the disbursement of Fiscal Year 2010; October 2009 – September 2010, of THB 1,784.4 billion [4]. This amount is composed of THB 1,627.9 billion of the 2010 fiscal year budget expenditure; or equivalent of 95.8% of disbursement, and THB 156.5 billion of the carryover budget expenditure. In addition to the budgetary expenditure, the disbursement of Thailand's stimulus package 2; the Strong Thailand 2012 Program, is at THB 18.7 billion in September 2010. Therefore, the accumulative disbursement is THB 234.4 billion or 67.7 % of the approved budgetary framework of THB 350 billion. The criteria of project selection are set and

[4] Monthly Economic Report (September and the 3rd quarter of 2010), Fiscal Policy Office, Ministry of Finance.

the TKK projects are categorized into 3 groups in accordance with the readiness of each project: (1) fast-track group, (2) medium-track group, and (3) slow-track group. The fast-track group composes of the TKK potential projects that are ready and possibly implemented since the end of 2009 and within 2010. The medium-track group includes the TKK projects that will be ready to implement in the 2010 Fiscal Year. The last group, the slow-track group, refers to the TKK projects that have the least readiness and will be ready to implement in the Fiscal Year of 2011.

Table 5 shows the list of TKK potential projects categorized by the government's objectives emphasizing on how to make the Thai economy stronger. The detailed progress of Thailand's stimulus package 2; the Strong Thailand 2012 (TKK), is also presented here. According to Table 5, the grand total amount of disbursed investment is THB 237,062 million from the total budgetary framework of THB 349,976 million, or 67.7 % of grand total disbursement. The three major objectives, determined by the amount of budget frameworks, are prioritized as (1) Create job and improve quality of life, (2) Basic public service development, and (3) Food and energy security. The funding amount of budget framework indicates that the government's policy emphasizes on their role to create job and improve quality of life during the crisis and after its hit. The rate of disbursed investment in the job creation and quality of life improvement; 78.7 %, is quite successful comparatively to other objectives. The second best rate lays on the TKK funding for creative economy, under the objective of creating new economic revenue. The disbursement rate under the objective of food and energy security is the third on the rank, which most of the amount spent on water resource management. Considering the rate of disbursement, it can be concluded that the government has tried to restore a basic foundation that directly affects people's standard of living. At the same time, it has aimed to improve both human capital and infrastructures e.g., logistics and transportation as the factors that encourage the country's efficiency and competitiveness.

Table 6. Progress of the Strong Thailand 2012 Project (TKK)

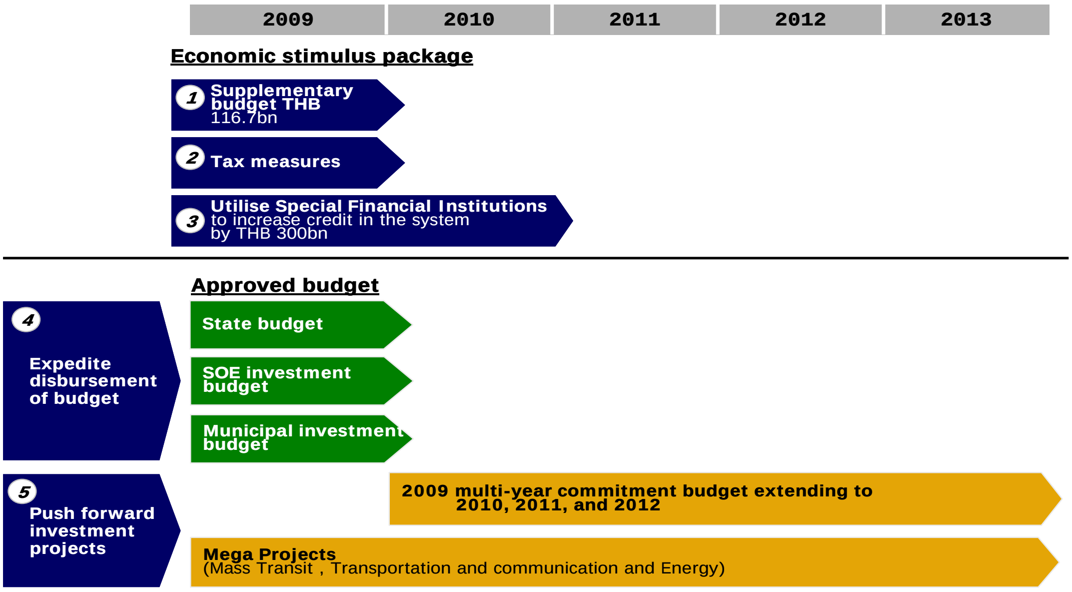
Objective/Sector	Budget Framework	2010			Disbursed investment	
		Aug	Sept	Oct	Amount	Disbursed rate (%)
1. Food and energy security	**59,503**	**3,347**	**3,717**	**894**	**38,218**	**64.23**
1.1 Water resource management	59,503	3,347	3,717	894	38,218	64.23
2. Basic public service development	**74,781**	**2,166**	**3,068**	**319**	**44,338**	**59.29**
2.1 Logistics and transportation	46,587	1,632	2,036	180	38,219	82.04
2.2 Energy	174	0	0	0	0	0.00
2.3 Communication	0	0	0	0	0	0.00
2.4 Tourism infrastructure development	3,282	2	29	0	575	17.5
2.5 Public health infrastructure development	14,692	123	374	94	851	5.8
2.6 Social welfare	9,173	358	475	44	3,851	42.0
2.7 Science and technology	185	7	28	0	178	96.4
2.8 Environment	689	45	126	1	664	96.3
3. Create tourism potential	**5,394**	**196**	**250**	**45**	**1,822**	**33.8**
3.1 Tourism development	5,394	196	250	45	1,822	33.8
4. Create new economic revenue	**1,331**	**163**	**230**	**75**	**945**	**71.0**
4.1 Creative economy	1,331	163	230	75	945	71.0
5. Develop education quality	**51,981**	**3,881**	**4,700**	**431**	**26,857**	**51.7**
5.1 Education	51,997	3,881	4,700	431	26,857	51.7
6. Develop public health quality	**1,928**	**14**	**111**	**6**	**332**	**17.2**
6.1 Public health personal development	1,928	14	111	6	332	17.2
7. Create job and improve quality of life	**106,542**	**5,481**	**6,316**	**756**	**83,872**	**78.7**
7.1 Community development	106,542	5,481	6,316	756	83,872	78.7
8. Government policies	**40,000**	**0**	**157**	**0**	**39,513**	**98.8**
8.1 Income support	40,000	0	157	0	39,513	98.8
Total	**341,476**	**15,247**	**18,550**	**2,525**	**235,897**	**69.1**
Expenditure under emergency circumstances	8,500	793	124	136	1,165	13.7
Grand total	**349,976**	**16,040**	**18,675**	**2,661**	**237,062**	**67.7**

Source: PDMO, Ministry of Finance (as of 2010).

The expected plan of government spendings in accordance with the stimulus packages is presented in Figure 11. The first economic stimulus package in 2009 includes spendings via supplementary budget, tax measures, and special financial institutions utilization under a purpose of increasing credit in the financial system. The disbursement of budget was expedited through three approved budgets; state budget, state of enterprise budget, and municipal investment budget. The purpose of the first stimulus package (SP1) aims to recover the economy at an immediate pace through the government expenditure for stimulating private consumption as well as to alleviate the effects of economic recession from the global financial crisis in 2008 with the reduction of unemployment.

Additionally, a longer-term stimulus package was proposed to restore the economy and to strengthen Thailand's capability by upgrading the standard of living along with competitiveness. The 2009 multiyear commitment budget was then extended for another three years from 2010-2012; the so-called stimulus package 2 (SP2). The goal of SP2 is to promote higher level of investment as another engine for economic growth. With the strong Thailand operative plan (SP2), not only the economic growth and higher employment will be stimulated, an enormous investment volume will be created. Hence, the government directly aims to make Thailand stronger on both consumer and producer sides. Together with the two stimulus packages, the government is pushing forward investment projects for Thailand's infrastructure development. The mega projects include mass transits, public transportations, communication, and energy. All mega projects are to facilitate local business transactions, reduce transaction costs, and lift up Thais' standard of living.

Figure 11. Government Spending Plan



Source: FPRI (2009).

Refer to the above mentioned multiyear commitment on stimulus packages, Table 6 shows the government expenditure on the stimulus package as a percentage of GDP. The government budget will be increasing for the next two years as well as the ratio of state enterprise additional income. However, the additional demand for SP2 investment tends to decrease overtime, which implies that the SP2 is aimed to be a high-impact 3 years stimulus package and the need of funding will be consistently lower. Consequently, the government burden is concluded on the last row of Table 7. It indicates that the Thai government will potentially experience increasing fiscal burden for the next 3 years, especially double burden during the overlapping period of 2010 and 2011, or after a certain period of progressive disbursement.

Table 7. Government's Fiscal Expenditure Plan on Stimulus Package 2 (SP2)

Unit: % of GDP

	2009 – 2010	2011	2012
Government Budget	2.23%	4.23%	4.74%
SOE Additional Income	0.11%	0.67%	0.69%
SP2 Additional Demand for Investment	0.46%	0.44%	0.39%
Others	0.13%	1.17%	1.78%
Government Burden	1.80%	3.43%	3.61%

Source: FPRI (20010).

2.4. Projection 2011 and Debt Status

The expected plan of government incomes and expenditure in fiscal year 2010 are presented in Table 7 and 8. The fiscal year 2010 fiscal deficit was much smaller than primarily feared when the budget was proposed. The budget for fiscal year 2010 was prepared at the trench of the global financial crisis in February 2009 and anticipated only 1.35 trillion baht in revenues. Thanks to Thailand's fiscal rule, on-budget expenditures were severely constrained and even including the off-budget Thai Khem Kaeng (TKK) stimulus program, the government was authorised to spend 2.06 trillion baht (or about 6 % more than in fiscal year 2009). In addition, thanks to the economic recovery and difficulties in disbursing public investment projects, revenues have come at 1.65 trillion baht or 10 % higher than the original estimates and expenditures (including TKK) at 1.98 trillion baht, resulting in a modest deficit of 1.9 % of GDP and a stable debt-to-GDP ratio (see Figure 12).

One issue need to be highlighted that the political unrest during April and May, as well as the continued deadlock over Map Ta Put in the case of PTT, led to delays in implementation of investment projects from both SOEs and central government agencies. A secondary factor accounting for lower public investment was the reduction in SOEs' investment budget for fiscal year 2010 compared to the previous year. In the second quarter of 2010, investment spending from SOEs (including PTT) declined by 31.7 % year-on-year or 16.8 % of total investment budget.

Table 8. Projected Government Income in Fiscal Year 2010

Unit: THB Million

Source of Revenue	Amount	%
1. The Revenue Department	**1,305,600**	**79.1**
1.1 Personal income tax	217,000	13.2
1.2 Corporate income tax	430,200	26.1
1.3 Petroleum income tax	536,800	32.5
2. The Excise Department	**387,100**	**23.5**
2.1 Tax on petroleum and petroleum products	152,000	9.2
2.2 Motor-vehicle tax	66,100	4
3. The Customs Department	**88,400**	**5.4**
3.1 Import duties	86,000	5.2
3.2 Export duties	100	0
3.3 Others	2,300	0.1
Total revenue from 3 Departments	**1,781,100**	**107.9**
SOEs	84,400	5.1
Others	93,000	5.6
Total revenue (gross)	**1,958,500**	**118.7**
Allocation of VAT to Local Administrative Organization	70,500	4.3
Total revenue (net)	**1,650,000**	**100.0**

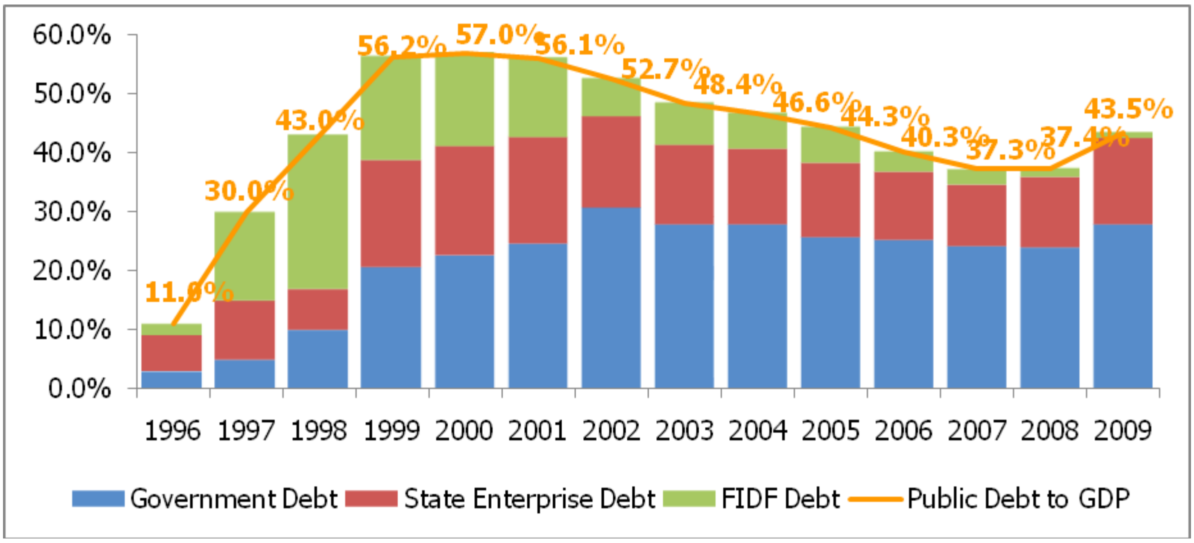
Source: Fiscal Policy Office, Ministry of Finance.

Table 9. Projected Government Expenditure in Fiscal Year 2010

Unit: million Baht	Fiscal year 2009	Fiscal year 2010		Fiscal Year 2011 (f)
		3Q actual disbursement	Forecasted (e)	
1.Government Expenditures	**1,931,629**	**1,503,263**	**1,989,985**	**2,100,063-2,126,157**
1.1Budgetary Expenditures	**1,917,129**	**1,338,964**	**1,765,638**	**2,048,159**
(1) Current expenditures	1,507,894	1,066,313	1,437,700	1,677,064
(2) Capital expenditures	282,969	140,705	177,300	248,036
(3) Carry-over expenditures	126,266	131,946	150,638	123,059
Current Fiscal year (1)+(2)	1,790,862	1,207,018	1,615,000	1,925,100
Disbursement to total budget (%)	91.8%	71.0%	95.0%	93.0%
(from Budgetary framework)	1,951,700	1,700,000	1,700,000	2,070,000
1.2 Non-budgetary expenditures (TKK Project)	**14,500**	**164,299**	**217,226**	**51,904 - 77,998**
2. Local Authorities Expenditures	**276,269**	**196,123**	**291,110**	**311,850**
3. SOE Investment Expenditures	**263,829**	**171,997**	**228,376**	**257,418**
4.Public Sector Expenditures (1+2+3)	**2,471,726**	**1,871,383**	**2,509,471**	**2,669,331 - 2,695,425**

Source: Fiscal Policy Office, Ministry of Finance.

Figure 12. Thailand's Public Debt to GDP (1996 – 2009)



Source: Fiscal Policy Office, Ministry of Finance.

With the space provided by better-than-expected fiscal outcomes in fiscal year 2010 and persistent concerns about the sustainability of growth, fiscal policy will remain expansionary in fiscal year 2011. Some new social policy initiatives originally included as part of the stimulus package have now become permanent and others have been introduced. These include a new agricultural price insurance scheme, a pension to the elderly not covered by social security, education subsidies and a debt refinancing scheme. These programs have now been integrated in the THB 2.07 trillion (20.4 % of projected GDP) budget for fiscal year 2011 (October 2010 – September 2011). Moreover, the government is trying to boost public investments. Accordingly, the capital budget was increased, and implementation of the off-budget stimulus plan, while winding down, will continue. The capital budget will return to normal levels (as a % of the overall budget), representing 16.6 % of overall expenditures, up from 12.6 % in FY 2010 (see Table 8). The investment budget of SOEs will increase by 23 % from the previous year. As a result of the increase in on-budget expenditures and the wind-down of the off-budget expenditures, overall expenditures are expected to come at 19.8 % of GDP and the deficit is projected at 3.2 % of GDP, up from 1.9 % of GDP in fiscal year 2010.

As economic recovery resulting in improving revenue collection, TKK financing is planned to move to on-budget rather than borrowing. Source of finance to TKK program in fiscal year 2011 is largely from budget and undisbursed budget allocation under Emergency decree (THB 350 billion). Foreign borrowings from World Bank, ADB and JICA are expected to be able to disburse within fiscal year 2011 with the approved loan amounts to THB 48 billion (USD 1.6 billion).

3. The Impact of Stimulus Package, Exit Strategy and Identification of Future Fiscal and Macroeconomic Risk

3.1. Effectiveness of Fiscal Stimulus

Since Thailand's stimulus packages are implemented at the two different periods of time, the effects of each package will be discussed separately.

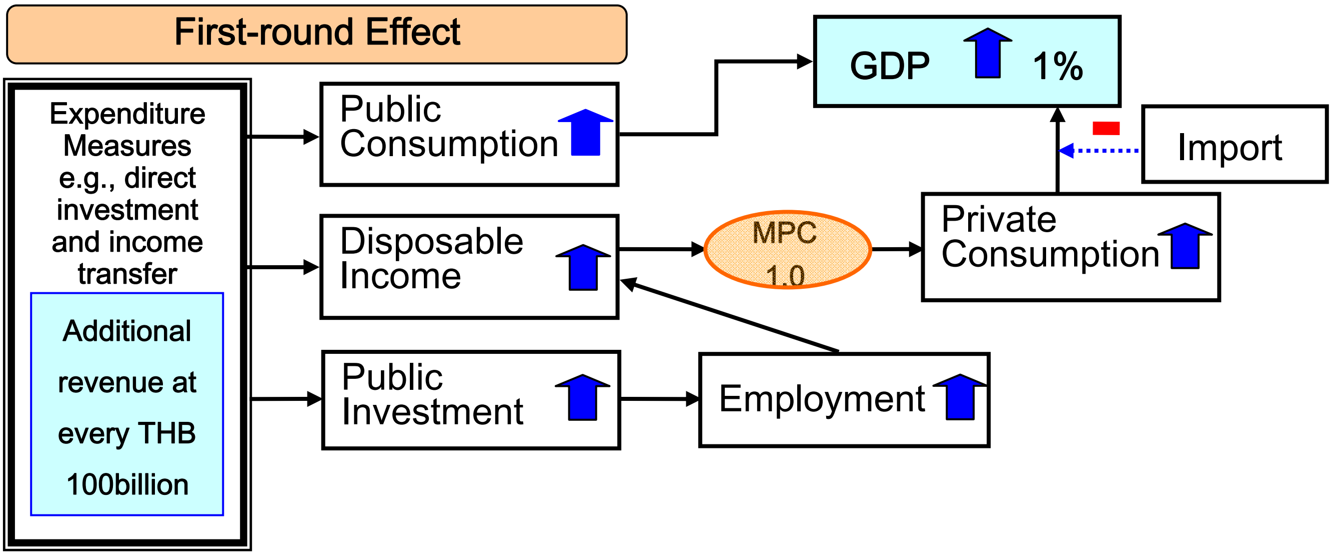
3.1.1. Stimulus Package 1 (SP1)

The aim of stimulus package 1 is to alleviate effects of the global financial crisis (subprime crisis) at a sudden pace. The Thai government implemented the fiscal package consisting of government expenditure, tax, and credit from SFI measures. The transmission mechanisms are described in Figure 13, Figure 14, and Figure 15.

The first round effect of SP 1 reflects good economic recovery and stimulus through the government expenditure. Theoretically, marginal propensity to consume (MPC) is a factor that determines an effect of fiscal measure. Since the target group is the poor, who has higher MPC than the rich does, the government expenditure measure, composing of income transfer and lowering costs of living, should effectively stimulate the economy. Jobs were created through public investment. People's disposable income increased due to income transfer and reduction of living costs. Private consumption climbed up along with public consumption; therefore, the rise of national GDP.

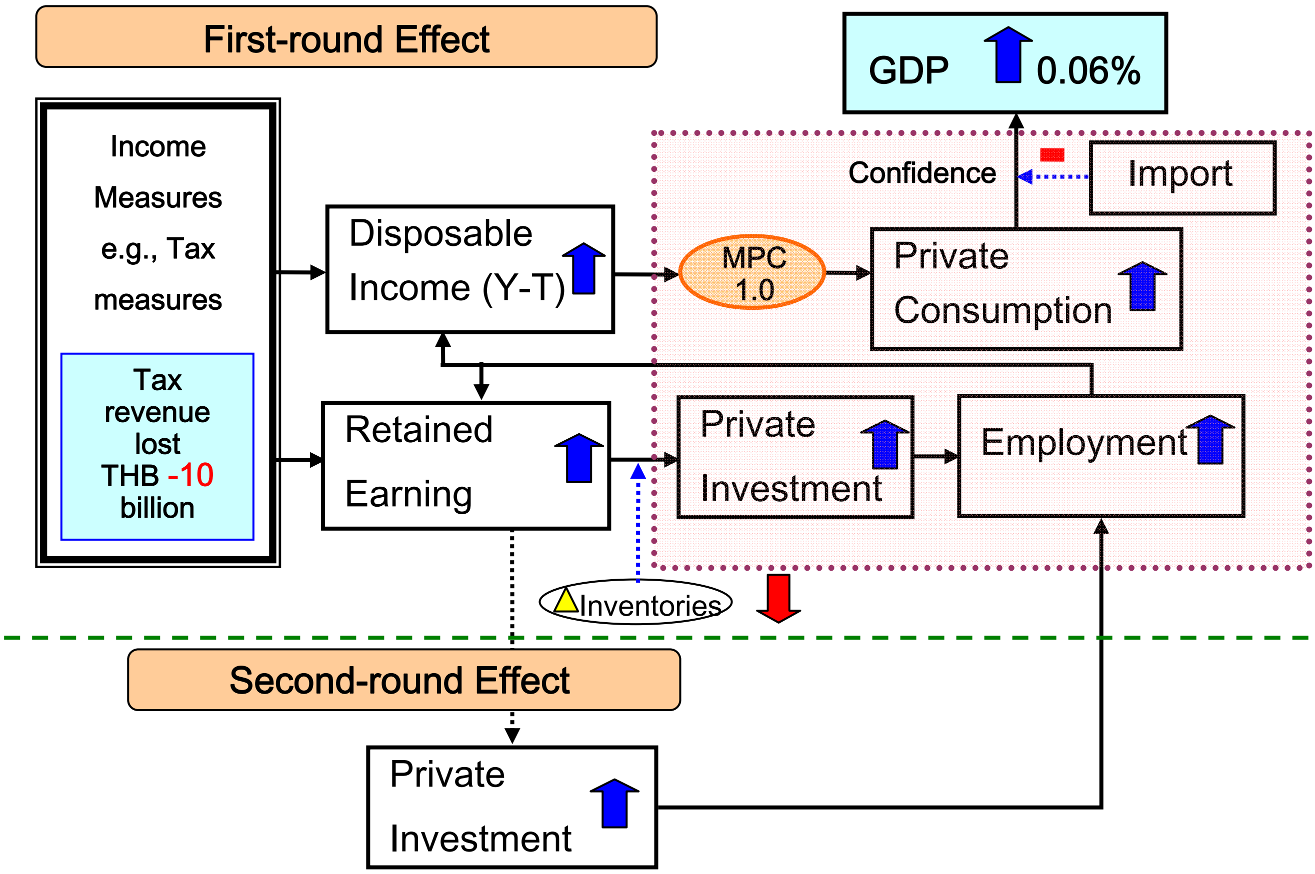
The impact of SP trough out the economy can be summarized in Figure 13, Figure 14, and Figure 15 whereas Figure 16 presents the total effect of SP1 on GDP growth.

Figure 13. Transmission Mechanism of Stimulus Package 1 (SP1)



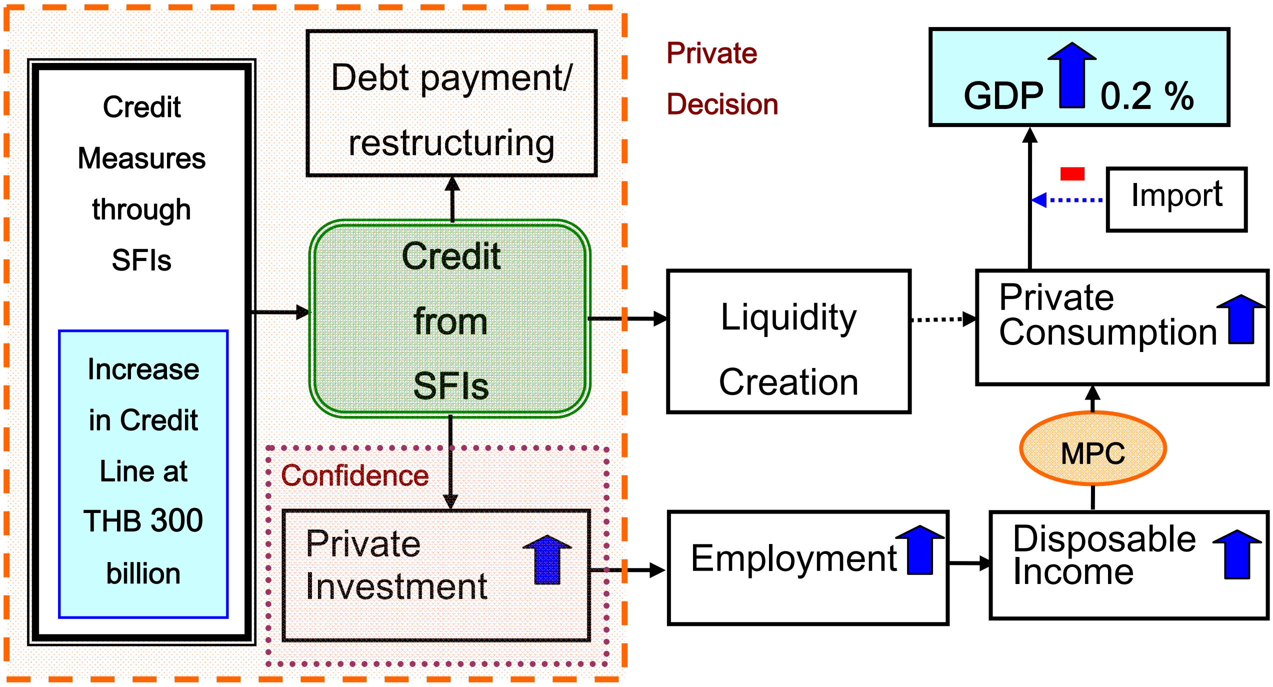
Source: Fiscal Policy Office, Ministry of Finance, Thailand.

Figure 14. Transmission Mechanism of Tax Measures



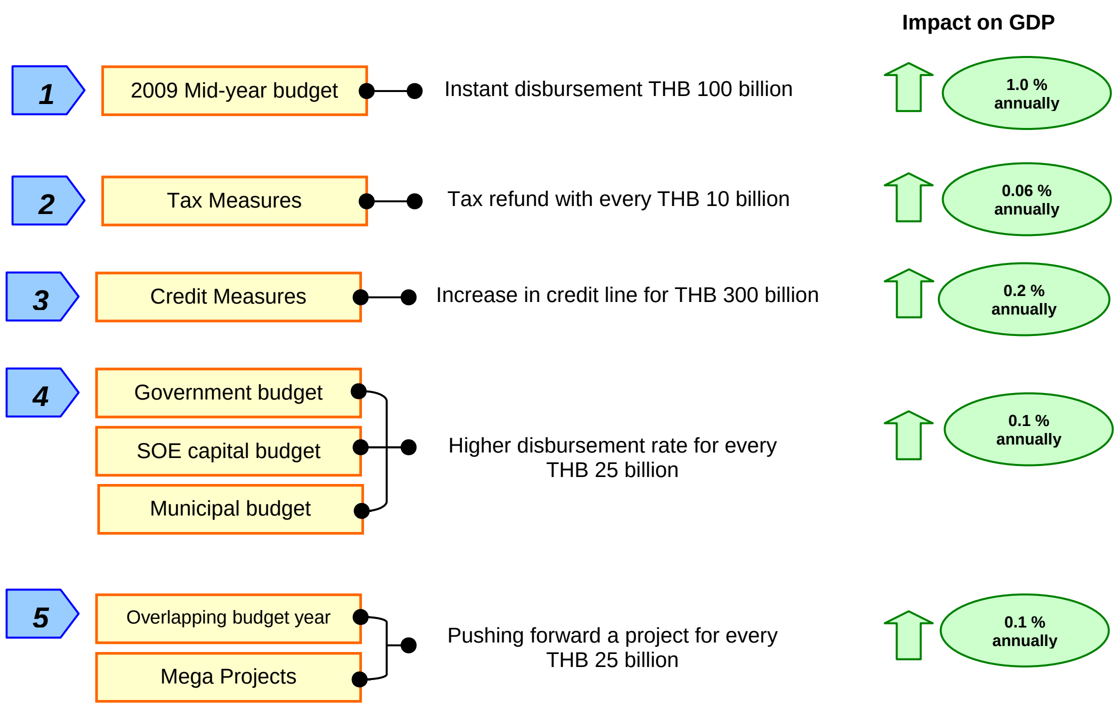
Source: Fiscal Policy Office, Ministry of Finance, Thailand.

Figure 15. Transmission Mechanism of Credit Measure through SFIs



Source: Fiscal Policy Office, Ministry of Finance, Thailand.

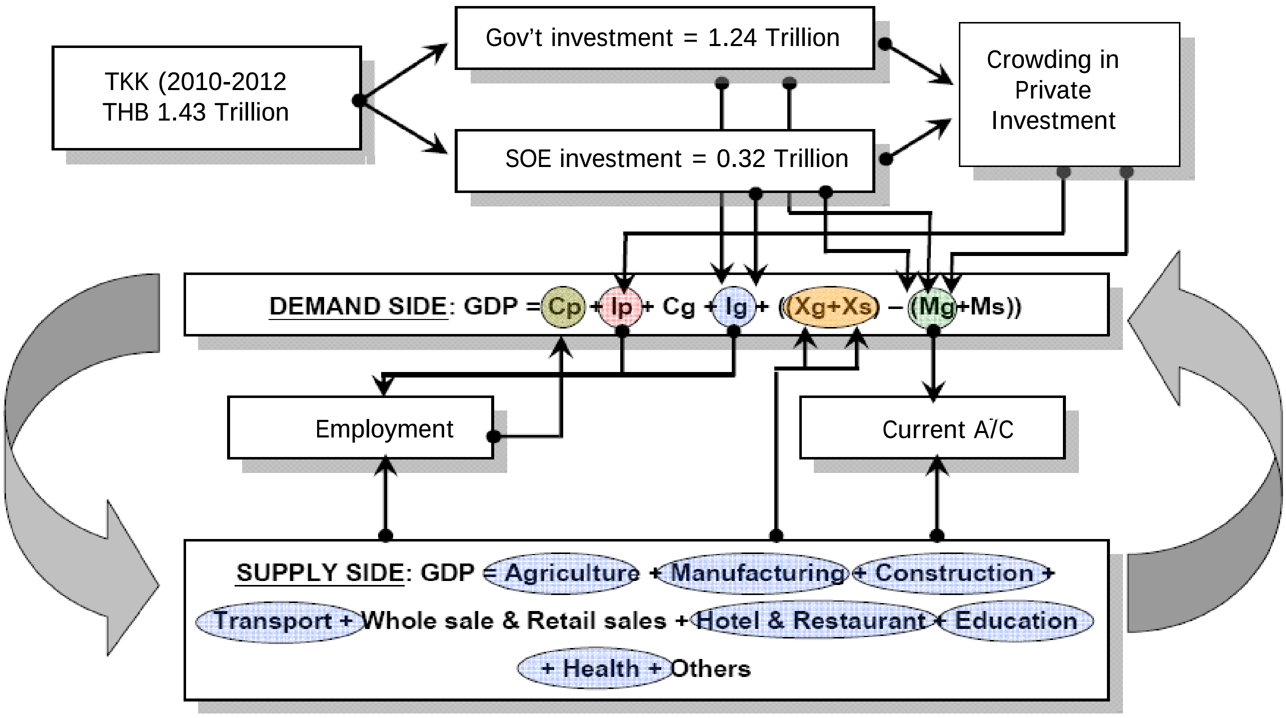
Figure 16. Total Effect of the Fast-track Stimulus Package (SP1) on GDP Growth



Source: Fiscal Policy Office, Ministry of Finance, Thailand.

3.1.2. Stimulus Package 2 (SP 2)

Figure 17. Transmission Mechanism: SP2 to GDP

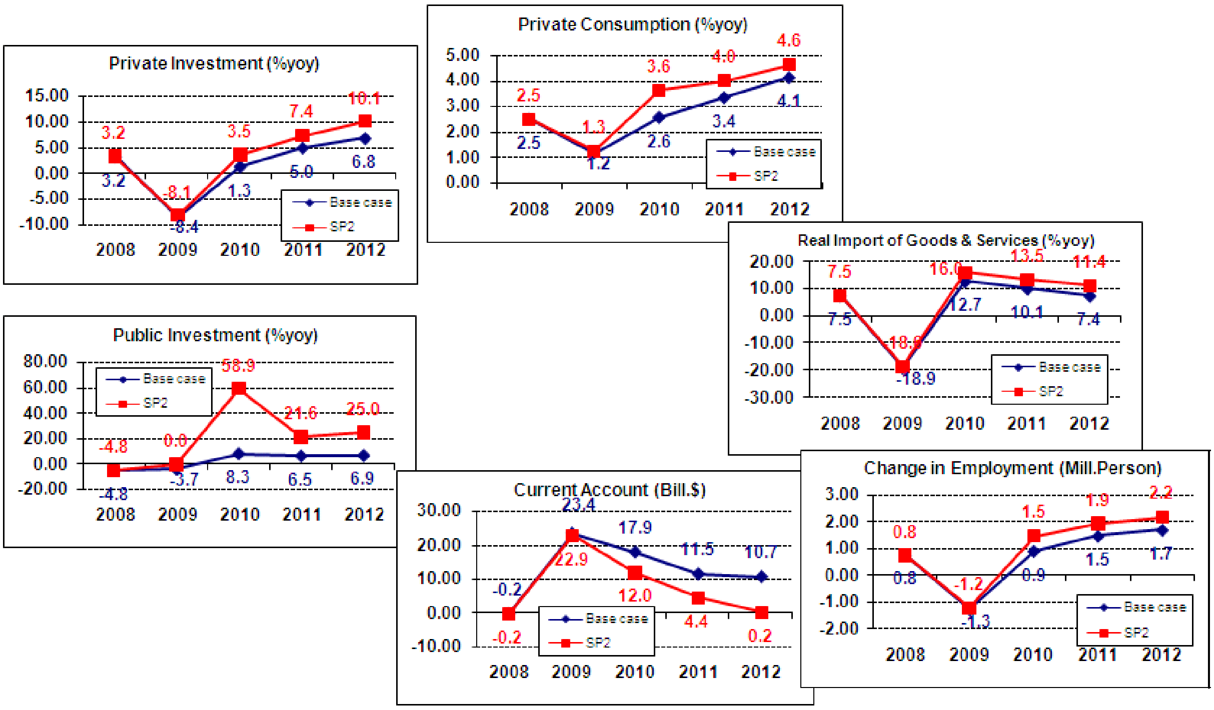


Source: Fiscal Policy Office, Ministry of Finance, Thailand.

Figure 17 presents the transmission mechanism of SP2 (TKK) to Thailand's economy. In this light, FPRI has estimated the impact of SP2 to the Thai economy through various channels which summarized in Figure 18. The TKK stimulus package contributed modestly to the public investment growth in 2010, but most disbursements have been for consumption expenditures. The total approved budget for TKK was THB 350 billion, of which THB 301 billion was approved for projects under seven areas16 and the remainder was allocated to the agricultural insurance scheme and the central fund. As of September 2010, the disbursement rate stood at 67 % (234 billion baht). Actual investment spending was approximately 40 % of the total disbursement. In the first nine months (October 2009-June 2010), actual investment spending from budget, carry-over and SOEs (excluding TKK investments) contracted by 16.2 % from the same period of last year. Including TKK investments, nominal public investment increased by 8 %, suggesting that TKK not only compensated a reduction of capital budget, but also contributed to public investment growth.

Moreover, TKK will continually expect to contribute to public investment growth in fiscal 2011. Although the capital budget and SOEs investment budget in fiscal year 2011 will return to their pre-crisis levels, TKK will also continue its role in contributing to the growth on public investment. The remainder of the TKK budget available to spend in fiscal year 2011 is THB 125 billion out of the THB 350 billion borrowing authorization under the Emergency Decree. Taking the fact that investment to consumption expenditures ratio is 60:40, the TKK budget is expected to be THB 68 billion assuming a high disbursement rate. In addition, fiscal year 2011 the capital budget will increase to THB 344 billion. Assuming a 75 % disbursement rate (consistent with historical average), the estimated actual spending from the capital budget is expected to be 258 billion baht. Thus, public investment from budget and TKK in fiscal year 2011 is expected to come in at approximately 326 billion baht, representing an 11 % increase from the previous year.

Figure 18. Estimated Impact of SP2 to GDP



Source: Fiscal Policy Office, Ministry of Finance, Thailand.

Thailand is not the only country in the region that impose fiscal stimulus package, but many countries in Asia also moving in the same direction (see Table 10). Regarding this, the FPRI has constructed a model to investigate impact of “Asia’s simultaneous fiscal stimulus” to Thai economy via the FPRI World Macro Model. As a result, the model indicates that Thailand’s GDP growth in 2009 and 2010 have been contributed by the “Asia’s simultaneous fiscal stimulus” by 0.9 and 0.3 % respectively (see Figure 19). This means that Asia’s simultaneous fiscal stimulus is important to the recovery of Asia aftermath of the 2008 Crisis.

Table 10. Fiscal Stimulus Packages in Selected Asia- Pacific Countries

Country	Date of Announcement	Amount (USD Billion)
China	9-Nov-08	585.7
	12-Jan-09	0.1
	21-Jan-09	0.1
Japan	1-Aug-08	120.0
	1-Oct-08	
	1-Feb-09	
	1-Apr-09	101.0
Korea	13-Dec-08	26.0
	1-Jan-09	37.0
	23-Mar-09	20.0
Thailand	1-Jan-09	3.3
	1-Jun-09	41.9
Malaysia	1-Nov-08	2.0
	1-Mar-09	16.4
Philippines	1-Jan-09	7.0
Singapore	22-Jan-09	13.8
Indonesia	1-Jan-09	6.6
	1-Aug-09	6.1
Vietnam	1-Dec-08	1.0
	1-Mar-09	17.7

Source: Global Financial Crisis: Analyst and Policy Implications, Congressional Research Service, World Bank, Reuters and FPRI’s calculation.

Turning to the issue of automatic stabilizer, what would happen to Thailand unless the fiscal stimulus packages? The operation of automatic stabilizers exacerbated the fiscal impact of the crisis in Thailand, though their impact was smaller than in advanced economies. In Thailand, the fiscal impact of automatic stabilizers was about 1 % of GDP (see Table 11 and Table 12), lower than their impact in advanced economies (close to 2 % in the advanced G-20), where governments are larger, and a greater share of spending is directly linked to the economic cycle.

Table 11. Impacts of Automatic Stabilizer vs. Discretionary Fiscal Policy - Estimation of Stimulus Package I (SP1) Impact to the Thai Economy

	2009	
	Base Case	**Effect to the Macroeconomics**
Real GDP Growth	-2.5%	+0.9%
-Real Gross Consumption	3.0%	+1.5%
-Private Sector	1.2%	+0.8%
-Government Sector	13.0%	+5.5%
-Real Gross Investment	-2.9%	+1.1%
-Private Sector	-6.1%	0.1%
-Government Sector	7.0%	2.2%
-Real Net import	-25.2%	+0.1%
Value of Import (USD.)	-33.2%	+0.1%
Current Account Balance	USD 24.7 Bil	USD -0.2 Bil.
Employment (Persons)	37,260,456	37,471,290

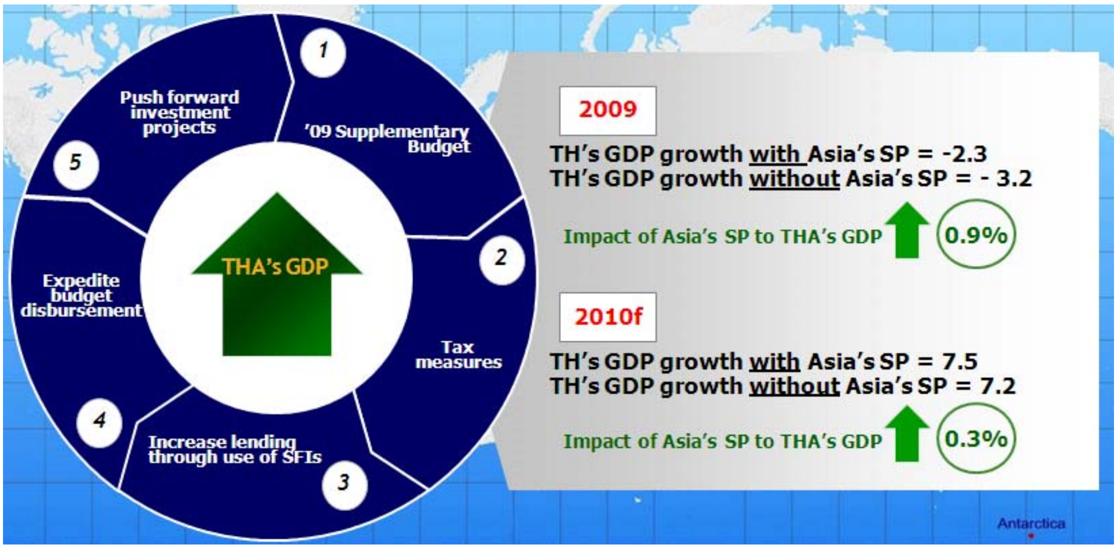
Source: Fiscal Policy Research Institute Foundation, Thailand.

Table 12. Impacts of Automatic Stabilizer vs. Discretionary Fiscal Policy - Estimation of Stimulus Package II (SP2) Impact to the Thai Economy

	2010	2011	2012
Estimation of Money to be injected in SP2 (Mil. Baht)	465,347	456,074	531,175
Base Case			
-Economic growth rate (% per annum)	2.5	4.0	4.5
-Real Private Investment Growth Rate (% per annum)	1.3	5.0	6.8
-Real Private Consumption Growth Rate (% per annum)	2.6	3.4	4.1
-Employment Creation (Mil. Persons)	0.9	1.5	1.7
-Real Import Value Growth Rate (% per annum)	12.7	10.1	7.4
-Current Account (Mil. USD.)	17.93	11.49	10.70
-Current Account to GDP Ratio (%)	7.3	4.3	3.7
SP2 Case			
-Economic growth rate (% per annum)	4.1	5.2	5.5
-Real Private Investment Growth Rate (% per annum)	3.5	7.4	10.1
-Real Private Consumption Growth Rate (% per annum)	3.6	4.0	4.6
-Employment Creation (Mil. Persons)	1.5	1.9	2.2
-Real Import Value Growth Rate (% per annum)	16.0	13.5	11.4
-Current Account (Mil. USD.)	11.99	4.43	0.20
-Current Account to GDP Ratio (%)	4.8	1.6	0.1
Change			
-Economic growth rate (% per annum)	1.5	1.2	1.1
-Real Private Investment Growth Rate (% per annum)	2.2	2.4	3.3
-Real Private Consumption Growth Rate (% per annum)	1.1	0.7	0.5
-Employment Creation (Mil. Persons)	0.6	0.5	0.5
-Real Import Value Growth Rate (% per annum)	3.2	3.4	3.9
-Current Account (Mil. USD.)	-5.9	-7.1	-10.5
-Current Account to GDP Ratio (%)	-2.5	-2.7	-3.7

Source: Fiscal Policy Research Institute Foundation, Thailand.

Figure 19. Estimated Impact of "Asia's Simultaneous Fiscal Stimulus" to Thai Economy



Source: Fiscal Policy Office, Ministry of Finance, Thailand.

3.2. Fiscal Sustainability

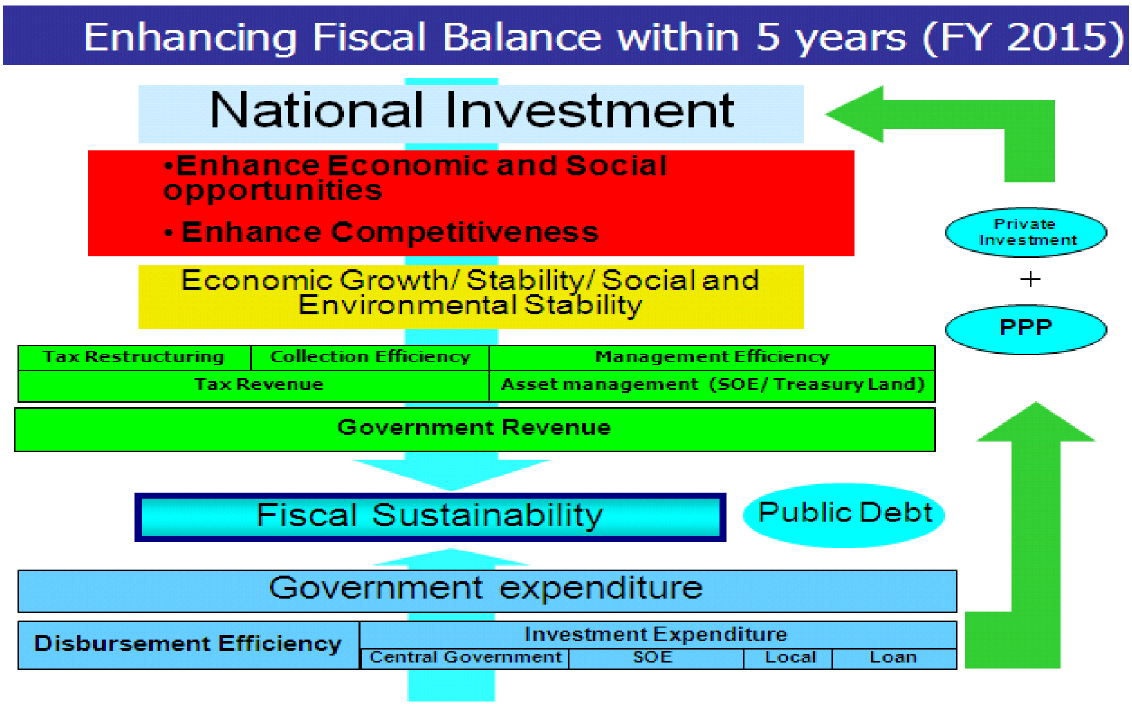
As the economy is recovering, the near-term challenge is to identify, communicate and begin to implement fiscal exit strategies from policy support. We hence are entering an exciting new era of strong economic growth with stability. As abovementioned, fiscal policies in the Asian economies can "simultaneously" help strengthen their future growth potential. Therefore, the transformation of the economy after the Global financial crisis once we are moving towards the exit strategies in the years to come are worthy of careful study. It is important that the exit strategies aim at not only rolling back many of the fiscal stimulus measures, but also at establishing the foundations for strong, sustainable and balanced growth and at lowering public debt to create fiscal space for counter-cyclical fiscal policy responses to future shocks. It is desirable that fiscal exit strategies be transparent, comprehensive, and communicated clearly, with the goal of implementing them within a clearly-specified timeframe (IMF (2009)).

With the recovery of economic activity being more entrenched in Asia, including Thailand, many countries have already started a gradual exit from policy support in 2010, although in some cases, this may be postponed to 2011. This policy response reflects a stronger than anticipated economic rebound, but also the need to manage risks to public debt sustainability, especially in some countries experiencing aging-related spending pressures.

Comparing to its regional peers, withdrawing policy stimulus is estimated to result in structural improvements in Malaysia and Singapore, in 2010, with small continued fiscal stimulus in Thailand. The move of TKK investment projects on budget represents the government‘s exit strategy from fiscal stimulus.

Concerning fiscal sustainability, The Ministry of Finance and the Bureau of Budget signed a Memorandum of Understanding agreeing which reflecting the MOF Strategic Plan (2011-2016) that agreement has been made to restore balance of budget within 5 years by using fiscal policies and budget management tools, which cover both revenue and expenditure tools. Implementation details are under discussion among concerned agencies within MOF and BOB. Briefing of Ministry of Finance’s Strategic Plan can be seen in Figure 20.

Figure 20. Ministry of Finance’s Strategies Towards Fiscal Balance within 5 Years



Source: Fiscal Policy Research Institute Foundation, Thailand.

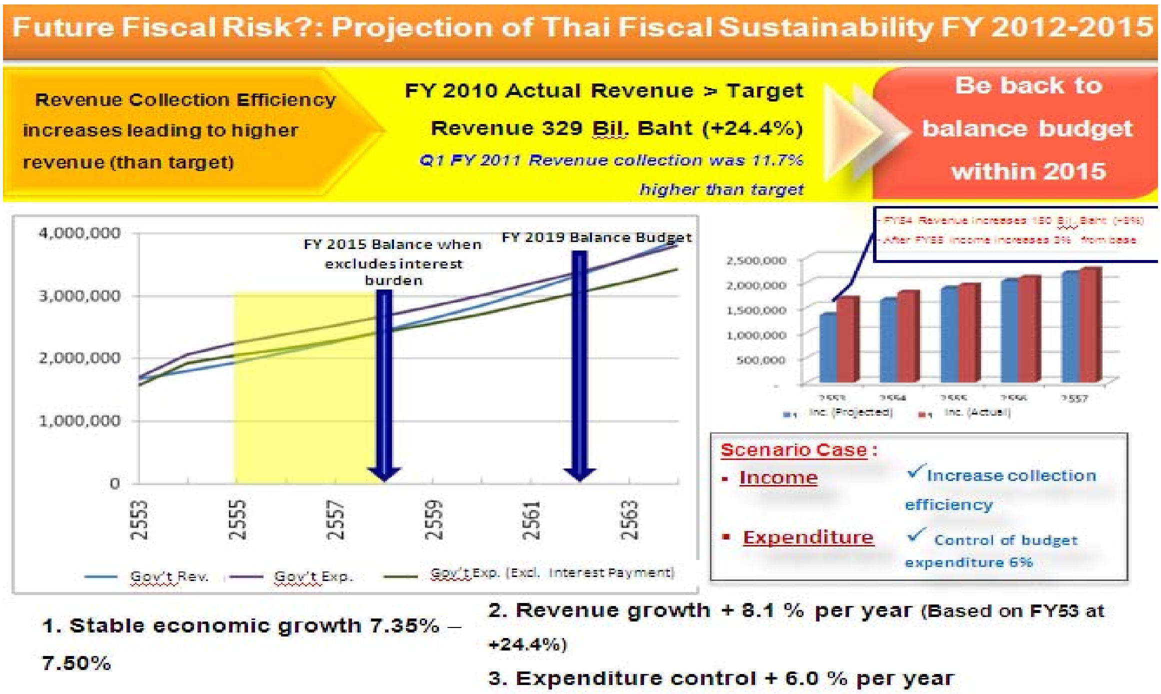
Focusing on fiscal sustainability, since Thailand's long track record of fiscal prudence underpins the projection that deficits will enter a declining path in fiscal year 2012. This assumption is supported by the Thai Government's consistent pursuit of a conservative fiscal stance of low budget deficits or surpluses. Since 2002, budget deficits were no more than 2 % of GDP and the primary balance was in surplus twice between 2005 and 2008. More concretely as earlier, the government has introduced a plan to achieve a primary surplus within five years (see Figure 21).

Projection of Thai fiscal sustainability has been done to achieve the target in fiscal year 2015 under the assumptions that (1) stable economic growth 7.35- 7.5%, (2) Revenue growth of 8.1% per year and lastly (3) expenditure controlled to be not exceeding 6 % per year. Among the 3 assumption, the last one on the expenditure is rather challenging as the current expenditure is about 12% per year. This means the crucial task for Thailand as there is a clear need to create fiscal space to address developmental challenges (meeting infrastructure needs and/or reducing poverty) while undertaking fiscal adjustment.

To achieve a medium-term reduction in the deficit, the government is considering measures on both the revenue as well as the expenditure side as presented in Figure 21. On revenue side, MOF is studying the possibility to amend the Treasury Reserves Act to receive interest earning from Treasury Reserves, held at the Bank of Thailand. The Treasury Reserves Act of 1948 mandates that Treasury reserves be held in unremunerated accounts at the Bank of Thailand. Currently, the amount of reserves is around THB 400 billion. On the expenditure side, current expenditures have been growing significantly over time. The ratio of current expenditures to revenues has been increasing steadily over the past three years, and in fiscal year 2011 it is for the first time expected to exceed 100 %, suggesting that the capital budget must be entirely debt-financed. Around 35 % of total current expenditure is allocated for civil service salaries and Civil Service Medical Benefit Plan (CSMBS). However, actual disbursement on the CSMBS always exceeds its budget allocation, on average by 27 %. Therefore, the government is looking at measures to improve the management of the CSMBS and reduce its burden on the budget. For example, it is considering allowing members to receive care in private hospitals. Finally, the government has been looking into options to reduce the burden of interest payments on debt of the Financial Institution Development Fund (FIDF).

It is evidence that fiscal space needs to be created to help address development challenges such as meeting infrastructure needs and alleviating poverty or to allow for counter-cyclical responses to future shocks. Hence, when implementing their exit strategies, countries should thus avoid public investment cuts as a quick fix to achieve budget targets. Growth-enhancing structural reforms, which can stimulate private infrastructure investment, should also be a part of countries' fiscal exit strategies, as they could help sustain growth potential while easing the fiscal burden. Furthermore, enhancing fiscal institutions, medium-term budget frameworks and fiscal rules would be important in implementing fiscal goals. In addition, revenue-based fiscal consolidation would be important in Thailand, where governments are relatively small and the efficiency of tax collection is low. In view of these considerations, exit strategies would need to be supported by revenue enhancing measures and reorientation of spending priorities.

Figure 21. Projection of Thai Fiscal Sustainability



Source: Fiscal Policy Research Institute Foundation (2011).

Even with recent fiscal expansions, fiscal positions remain relatively sound, having benefited from years of prudence. However, under conservative assumptions of only partial fiscal consolidation, Thailand‘s public debt-to-GDP ratio does not exceed 46 % of GDP and ratios start to decline (albeit slowly) in 2015. After an initial spike due to the substantial financing needs that arise from the fiscal stimulus, debt ratios resume their downward trend. The debt-to-GDP ratio is expected to be approximately 45 % of GDP by 2020 following a peak of 46.6 % in 2014. The slow decline under the baseline arises from conservative assumptions on fiscal balances, which remain lower than their post-financial crisis average throughout the projection period. Debt projections are substantially lower compared to April 2009, indicating the magnitude of the recovery.

Public debt sustainability continues to be resilient to worse-than-expected outcomes in 2011-2012, but a permanent shock to growth could lead to an upward path of public debt. The contingent liability shock is the most severe, leading the debt-to-GDP ratio to peak at 55 %, but favourable debt dynamics lead to a declining debt path. The greatest risks to debt sustainability come from protracted growth slowdown and lack of fiscal consolidation following the resumption of growth. If primary deficits remain at 1.5 % of GDP—high for historical standards but almost 1 percentage point of GDP below fiscal year 2009 levels—the debt-to-GDP ratio would remain on a rising trend in the longer term and would exceed 50 % by the end of the projection period. The scenario with permanently low growth also leads to rapidly increasing debt ratios. This emphasizes the importance of taking advantage of the crisis to enhance competitiveness and ensure a return to sustainable growth.

4. Fiscal Transparency and Anticipating Policy for Future Crisis

4.1. Fiscal Transparency

Thailand has followed IMF’s Code of Good Practices on Fiscal Transparency by actively strengthening its fiscal management in 4 areas of transparency. Referring to

IMF's previous assessment[5], it is said that Thailand has met the requirements of the fiscal transparency code in many respects and exceeded them in a few cases. Achievements can be summarized as follows:

Fiscal Transparency Aspects	***Achievements***	***IMF Assessment***
1. Clarity of roles and responsibilities • The government sector should be distinguished from the rest of the public sector and from the rest of the economy • There should be a clear and open legal, regulatory, and administrative framework for fiscal management.	• The fiscal powers of the executive, legislative, and judicial branches of government are set out in the 2007 Constitution. • Many attempts have been made regarding decentralization. • The legal framework underlying public finance is broadly sound. This includes public debt management framework and state-owned enterprise management. • A more transparent and effective performance management framework has been developed, including specification of outputs and Key Performance Indicators.	Thailand largely achieved in this category. • Announced limits on debt and interest payments reflect commitment to fiscal prudence. • However, some large state-owned financial and non-financial enterprises conduct substantial quasi-fiscal activities.
2. Public Availability of Information • **The public should be provided with comprehensive information on past, current, and projected fiscal activity and on major fiscal risks.** • Fiscal information should be presented in a way that facilitates policy analysis and promotes accountability. • A commitment should be made to the timely publication of fiscal information.	• Reports of all fiscal information are designed and transparent. Those include government revenue, expenditure, disbursement progress, public debt and debt issuance plan. • Economic data (real sector, monetary, fiscal and debt data) and government policies are publicly reported regularly through the Internet (www.mof.go.th, www.bot.or.th, www.nesdb.go.th and www.bb.go.th) and press releases. • Consolidation of fiscal account is an ongoing process. The Ministry of Finance has strengthened its capacity and capability in data collection and analysis for the entire public sector using the IMF's GFS framework. Consolidated central government position is reported to the public monthly. Consolidated public sector position is reported to the public on a quarterly basis. • Accrual accounting and the GFMIS have been introduced in most of the central government, improving quality and timeliness of data. • Multi-year commitments are	Thailand largely achieved in this category. Information on revenue is not as much as budget's. There is no information on civil service pensions published together with the overall fiscal documents. However, the information can be achieved in individual agency (Social Security Office) Balance Sheets in their Annual Reports. Not much information on local authority is provided. The only information on Local Authorities in the central government budget is transfers to them. There are no hidden deficits or debts that are not shown in the data.

[5] International Monetary Fund, "Thailand: Report on Observance of Standards and Codes—Fiscal Transparency Module," IMF Country Report No. 09/250, August 2009.

Fiscal Transparency Aspects	*Achievements*	*IMF Assessment*
	presented in the budget documents • The budget documents report extensively on SOEs.	
3. Open Budget Preparation, Execution, and Reporting • Budget preparation should follow an established timetable and be guided by policy well-defined macroeconomic and fiscal objectives. • There should be clear procedures for budget execution, monitoring, and reporting	• The budget process is well specified, linked to the strategic policy priorities of government and is based on a sound macro-fiscal framework. • Multi-year departmental estimates are used for budget requests. • Budget documents provide extensive fiscal information. Overall information can be retrieved from website, while detailed information can be requested from authorities. • The 2007 Constitution requires development of a new Public Finance Act with further improvements in budget management and presentation.	Thailand largely achieved in this category. Well organized budget process. More than adequate time for Parliamentary consideration. There is no fiscal sensitivity analysis in the budget documents.
4. Assurances of Integrity • **Fiscal data should meet accepted data quality standards.** • Fiscal activities should be subject to effective internal oversight and safeguards. • Fiscal information should be externally scrutinized.	• Public Service Accounts are being introduced to record the cost of Quasi-Fiscal Activities in SOEs and SFIs • Public sector activities including standards of behavior for public servants, employment procedures and conditions, procurement, sale and rent of public assets are opened to public through electronic systems. In the revenue departments, computerization and electronic filing have enhanced monitoring and have reduced the scope for abuse. • The Ministry of Finance sets a consistent standard for government accounting and has been strengthening its accounting principle • The MOF authorizes the Bank of Thailand to inspect all public financial institutions. • The National Counter-Corruption Commission and the Office of Auditor General provide important independent checks on the integrity of public finances.	Thailand largely achieved in this category.

4.2. Management of Future Liabilities

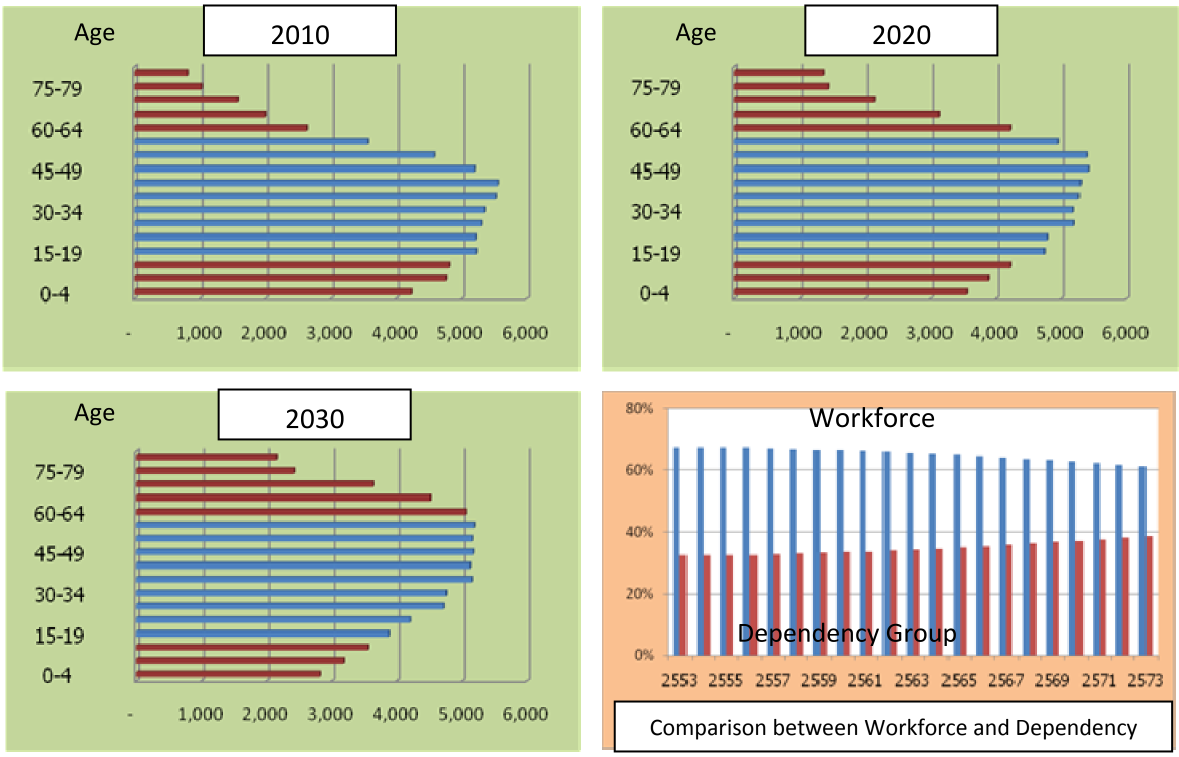
Future liabilities can arise from 2 sources: temporary policy; and permanent policies. Regarding the temporary policies, the risk lies in the fiscal rules that have been set to maintain fiscal sustainability namely fiscal debt management act (B.E. 2548)[6] and the fiscal sustainability conditions[7]. Even, the Thai ministry of finance has been empowered the executive decree to secure extra loans to carry out the programs; the necessity to raise loans might force the ministry of finance to violate the rules. The plan to find alternative sources of incomes; and decrease unnecessary expenditures are designed to manage this risk. However, other risk exists as fund securing under SP1 and SP2 are made through enactments of the loan acts which are needed to be approved by the parliament. Political instability might cause some delays or impossibilities in the investment plans.

Regarding future liabilities which may arise from the permanent policies such as social security and health care funds (social service policies), it has been recognized that both policies are future commitments and needed to manage to prevent any unexpected liabilities. Normally in both initiatives, threat to future liabilities comes from change in demographic trend. It can be seen from figures below that structure of Thai population is forecasted to gradually changing to old-age society due to significant improvement in health care system and decrease of mortality ratio. Hence, these lead to similar risks to both funds to face with higher expenditures for the old age benefit; and for treatments. Detailed-discussions regarding projections and risk managements of both funds are as follow.

[6] The Ministry of Finance can raise loans only for finance the budget deficits (when expenditure is larger than revenue), economics and social development, public debt restructuring and refinance. Under the condition of financing deficits, the loan amount is set to not exceeding 20% of annual budget plus addition budget of that fiscal year; or 80% of budget set to repay the principle in that fiscal year.

[7] Stock of public debt to GDP would not exceed 60%. Proportion of debt financing in the budget should not exceed 15%. Proportion of investment budget should be at least 25%.

Figure 22. Demographic Structures of Thailand in 2010, 2020 and 2030



Source: Fiscal Policy Research Institute Foundation (2011).

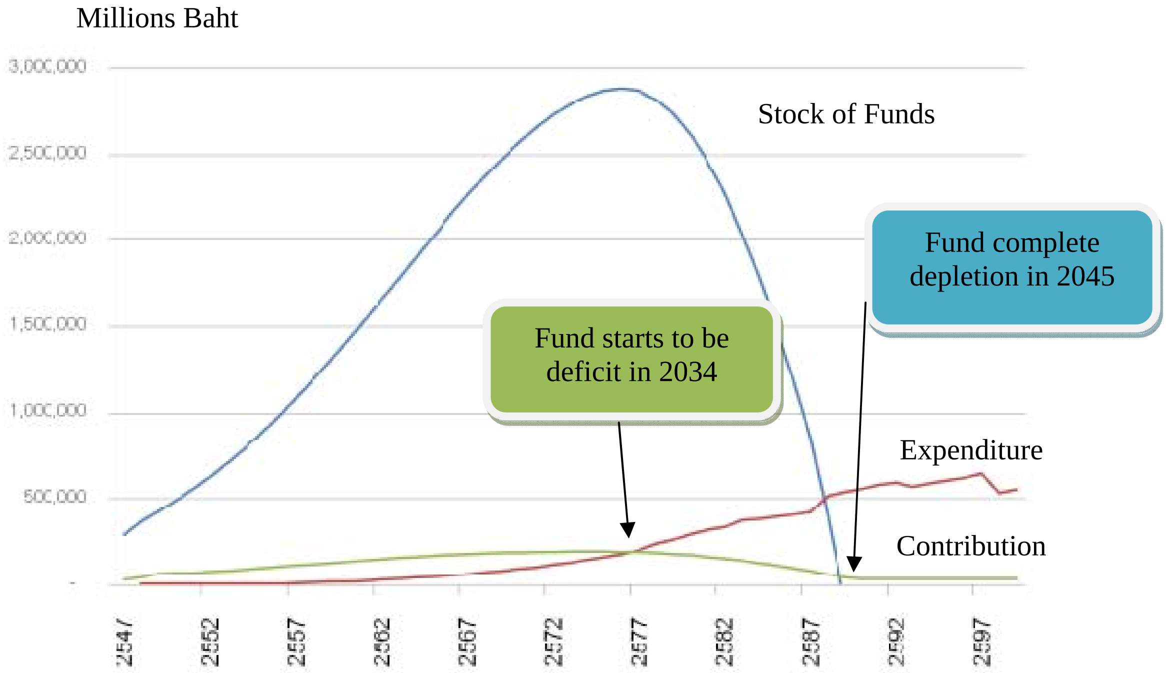
4.2.1 Social Security Fund (SSF)

The social security fund is comprised with 7 benefits which can be categorized into 2 groups of short term benefits (Death, Sickness, Maternity, Child cares, and Unemployment) and long term benefits (Old-age, and invalidity). Contributions of members to the fund are accounted and managed separately by type of the benefits (short-term and long-term). In FPRI 2003, it is found that both short-term and long-term benefit funds were managed and invested conservatively as the fund is under the board that invested mainly in the low risk & low return investments (such as government loans and bank deposits). The returns on investments of both funds were low. Together with threat from demographic change (lower contribution from decreasing workforce and higher expenditure from increasing of pensioners), it was forecasted in FPRI 2007 that the 2-benefit fund (old-age and invalidity) would first deficit in 2034 and the fund would completely deplete in 2045. As the fund was established by the law (Social Security Act B.E. 2533) and was explicitly guaranteed by that law, after the fund depletes, it is expected that the Thai government has to use its budget to support the pensioners from 2045-2128. However, the contributions (receipt) and expenditure of the 4 benefit fund (Death, Sickness, Maternity, and Child cares) and unemployment funds were expected to go well as the usage is small and the service packages are well-designed to well-controlled of the expenditures.

This forecast and similar studies are well-known and the Thai government already set many measures to tackle and lessen this burden. The measures include:

1. Changes of contribution rate: Increase of contribution rate from all parties (employer, employee and government) can prolong the solvency. It is also proposed that if the rate was high enough, the fund will go to sustainable state. (It was 9% each from all parties in FPRI 2007). Currently, the Social Security Office (SSO) has proposed to slightly increase the contribution rate from employer and employee.
2. Change of investment options: Currently the proportion between low risk and high risk investment choices of the SSO is 83:17, while the requirement by law is 60:40. Many studies includes ILO's and FPRI's suggested that if the investment option leans more to higher risk options, the solvency of the fund would be prolonged. Currently, the SSO has employed professionals to conduct its investment under the supervisors of the SSO board.

Figure 23. Projection of the Sustainability of the 2-Benefit Fund (Old Age and Invalidity) of the Social Security Office.



Source: Fiscal Policy Research Institute Foundation (2007).

4.2.2 Universal Health Care Program (UC)

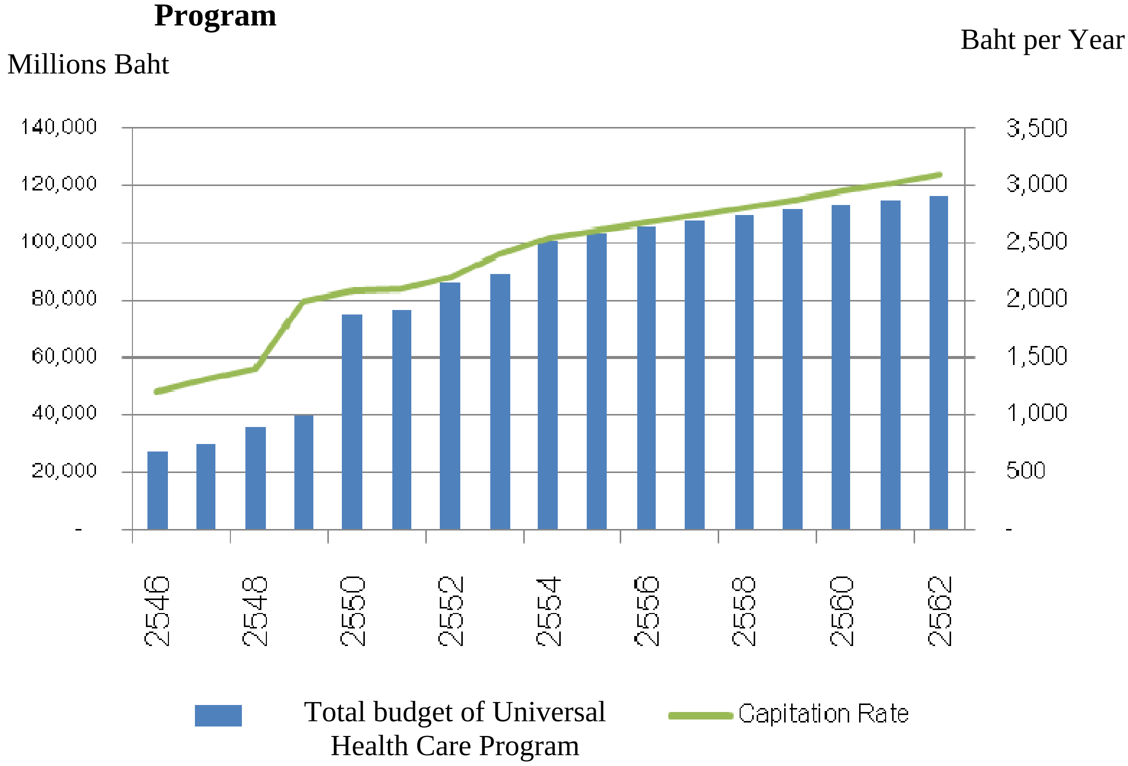
Thailand has achieved universal healthcare coverage (UC) by October 2001. The system employs a low cost capitation model with the benefit package that is quite generous and comprehensive. It is financed by the government budget (general tax revenue). The government has adopted the capitation payment method for purchasing cares from public and private service providers[8]. The capitation ratio in each fiscal year was calculated based on the data sets concerning costs of care, probabilities of morbidity, and choices of care of the Thai population in the National Statistical Office's Health and Welfare Survey (HWS), and Socio-economic Survey (SES), as well as the reports from the social insurance schemes. The National Health security Office (NHSO), which is an agency appointed by the government to manage the system, will propose the capitation based on its calculation and methodology to the Bureau of Budget (BOB) for cabinet approval. However, the capitation will be altered up to

[8] There are 3 types of service providers in this scheme: (1) The public service providers under the ministry of public health (2) The public service provider under other government agencies (the medical schools) and (3) The private service providers.

negotiation between the NHSO and the BOB, which is normally smaller than the rate that the NHSO proposed. The capitation rate has increased in each year due to increasing in treatment price and related stuffs. In Grenville and Wangcharoenrung (2003), it was evaluated that no contingent liabilities would occur to the government from the operation of the program in the future.

Even the budget under this program is expected to increase in each year due to price changes and coverage expansion, it depends on the capitation, which is up to negotiation between the NHSO and the BOB that is, in turn, the government can control the size and burden that it would bear.

Figure 24. Forecast of Budget and Capitation of the Universal Health Care Program



Source: Fiscal Policy Research Institute Foundation (2011).

4.3. Trend of Thailand Fiscal Policy

In conclusion, it is obvious that Thailand has applied counter-cyclical fiscal policy in managing its economy. Past experiences in 1997-1998 Asian crisis and 2008-2009 Global Financial Crisis (GFC) have proved it. Such trend does not change at all. On the other hand, successes in using the counter-cyclical fiscal policies to handle its economy during the crisis time have assured the government in doing so.

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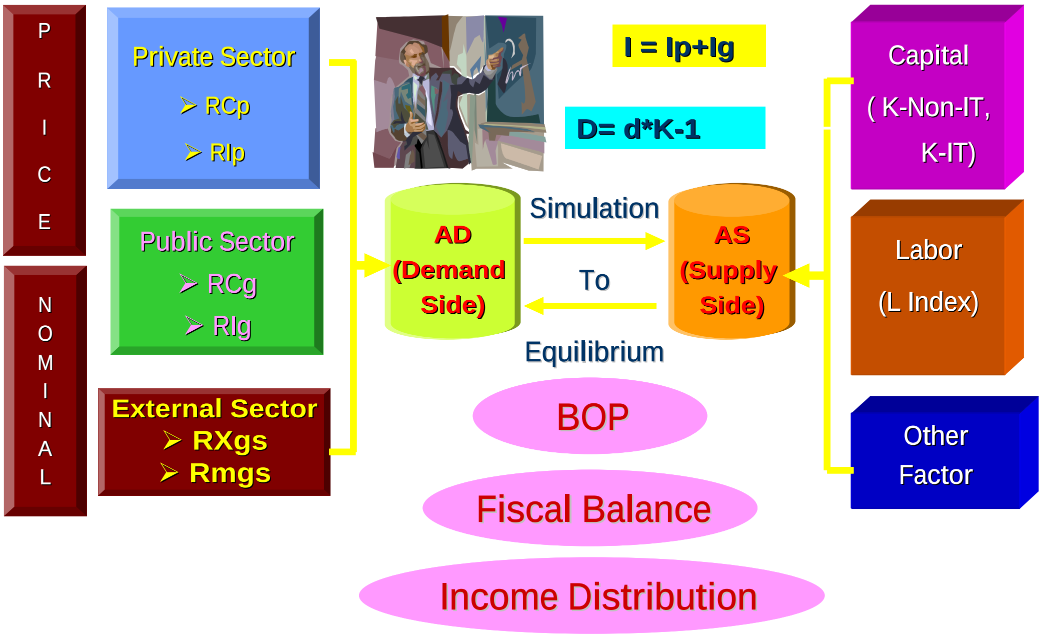
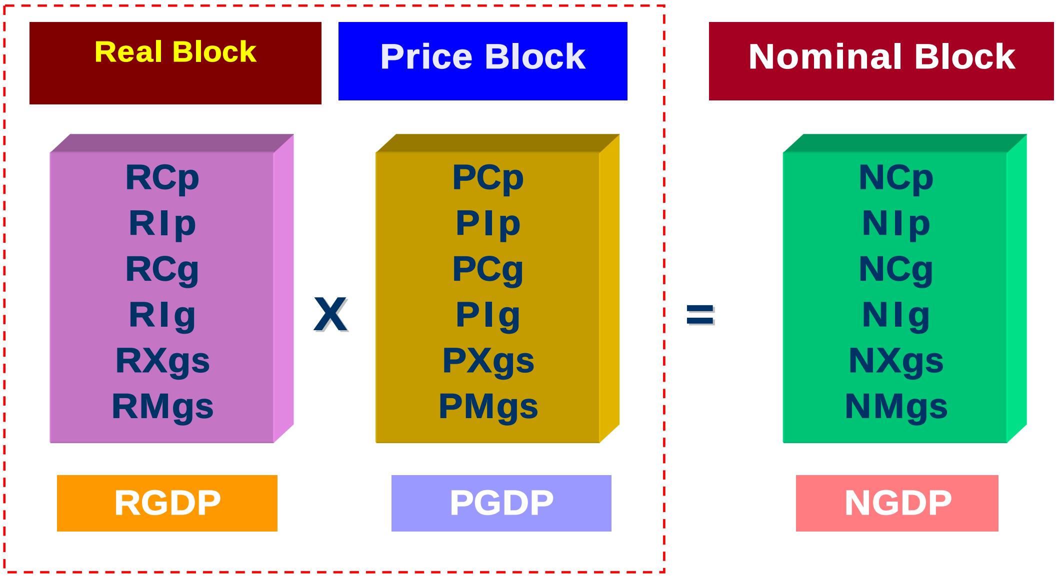
APPENDIX

A. The FPRI Macroeconomic Model (Non-linear model)



➢ **Aggregate Demand**



➢ Aggregate Supply

Cobb Douglas Production Function

$$Y = f(K,L) = aK^{\alpha}L^{\beta}$$

Assumption: constant return to scale

$$(\alpha+\beta=1)$$

B. Assumptions for Projections of the Thai Social Security Fund (2-Benefit Fund)'s Financial Sustainability

Labour Assumptions

- Birth rate is 1.5% in 2007 and declining to 1.27% in 2020
- Mortality rate varies by age
- Proportion of labour in formal sector to total population increases from 12% in 2007 to 24% in 2032 due to various economics and education policies
- Labour starts to work when he ages 15
- Salary increases 5% annually

Investment Assumptions

- Return on high risk investment was 6%, while return on low risk investment was 3%
- Contribution conditions remain the same through out the projection (Employer 5%, employee 5%, and government 2.5% of employee's salary, which is capped not to exceed 15,000 baht per month
- Investment proportion between high risk and low risk option changes from 17:83 to 40:60 within 15 years from 2007

Source: FPRI (2007).