Board Meeting of July 9, 1998
Statement by Andrei Bugrov

Thailand: Country Assistance Strategy

We believe that the present CAS for Thailand is a document of high quality and that it correctly addresses the major issues pertaining to the assistance to the country needs in order to overcome its current distress and resume economic growth. We are pleased to see that this CAS is a product of close collaboration between the Bank and the Government of Thailand and of consultation with a broad range of other stakeholders. While supporting major elements of the CAS and the proposed Bank strategy, we would nevertheless like to raise a few issues.

1. Parts I and II of the CAS document contain an in-depth analysis of the causes of the current crisis differentiated by key sectors and describe the formidable tasks the Thai Government is confronted with in order to revitalize its economy. While the major points are well addressed, we believe that the above analysis still lacks clarity in addressing the fundamental issues that are at the core of the present crisis -- which indeed have relevance for other countries in similar situation. In particular, we do not perceive a clear-cut assessment of the macroeconomic policy before the crisis, especially with regard to the appropriateness of maintaining the fixed exchange rate regime, and liberalized capital accounts coupled with lax supervision of financial institutions. Paragraph 4 criticizes the Government for failing to take appropriate corrective steps despite speculative attacks on the fixed exchange rate in early 1997. What was the IMF assessment of the financial situation of the Thai economy at that time and what were the recommendations with regard to the exchange rate? What would have been, in the Bank’s view, the appropriate corrective actions, perhaps an earlier devaluation? Does this sentence have relevance to the situation where some other countries are praised by the Fund for maintaining the exchange rate stability at any price?

2. We are grateful to the Staff for the frank and realistic assessment of the current economic as well as social and political situation in Thailand. Especially worrisome is the fact that economic activity is caught in a vicious circle (described in paragraph 19) that reminds us of the Keynesian deflationary liquidity trap. We agree that renewing competitiveness of the economy is the key to breaking this cycle and for reviving growth. At the same time, implementing the four sets of measures that address the fundamental structural issues related to competitiveness will require large private and public investments. The
policies summarized under “Improving Governance” and “Sharing Growth and Ensuring Quality of Life” also seem to be an indispensable part of the economic recovery program. With respect to the latter, we may anticipate that it may contain some popular measures which would assist in protecting the vulnerable, redress the balance between the rich and the poor, develop the social security system, etc. At the same time, Chapter B (“Risks”) of Part IV mentions “a widely shared consensus that a period of austerity and painful economic reform is an inevitable precondition for economic recovery.” The question arises: what is the balance between “ensuring quality of life” and “austerity and pain” in the reform package financed by the Bank?

All structural reforms as described in Part II seem to us a bit ambitious in view of the continuing deep recession, current priorities of the short-term stabilization program and large external financing requirements caused by a continuing outflow of capital. A major share of the funds to be provided by the Bank will be used for BOP support. What will be the source of these funds necessary in order to finance the resolution of these complex structural issues? A better prioritization and concentration on the most realistic goals achievable in the short-run would be a more practical way of approaching these issues.

3. Chapter III describes the history of the World Bank assistance to Thailand and lessons to be learned from Bank involvement. We feel some uneasiness with respect to the fact that despite a well-developed and long-standing relationship with the member country, the Bank overlooked certain fundamental weaknesses in the economy that brought about a disruption in development on an unprecedented scale. Surprising is also the Bank’s reaction to the initial signs of the crisis which were readily apparent in the summer of 1996. According to the OED Country Assistance Note, “...the Bank staff became conscious of the difficulties faced by Thailand in the summer 1996. An internal memorandum noted that the rapid increase in unhedged short-term external liabilities raised concerns about the fragility of the financial system. It stressed the decline in exports of labor intensive goods and expressed doubts about the sustainability of the large external deficit -- these concerns were not, however, reflected in the economic memorandum issued on December 13, which projected an annual 7 percent growth of real GDP for the 1996-98 period.” We believe that these lessons should be adequately accounted for in the future work in Thailand and in ongoing working programs elsewhere.

4. We can support the size and composition of the lending program. We can also basically support alternative lending scenarios and program triggers. But one item in the triggers leading to a low case scenario causes some concern, namely the “lack of commitment to liberalizing the investment regime because of the backlash against globalization.” This item is also mentioned below as “risk of rising xenophobia and a cultural backlash against globalization.” We believe that the degree of openness of Thailand’s economy is quite high, especially with respect to the foreign investment regime. The lack of appropriate prudential regulations and excessive reliance on short-term capital inflows may have been among the reasons for the current crisis. We do not fully understand why it is important for the Bank “not to be seen

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1 Thailand: Country Assistance Note, p 12
as pursuing the interests of foreign investors” if they can provide capital and knowledge for reviving growth. This trigger or risk factor needs further explanations or should be reformulated in more precise terms.

5. Finally, let us hope that the people and the Government of Thailand will manage to overcome the current crisis with minimal pain and start a new phase of development which will enable everyone to share in the fruits of growth and ensure better quality of life for all.