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Asia

Thailand's economy

The high cost of stability

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SINCE the coup d'état in May (http://www.economist.com/news/asia/21602759-sudden-move-army-brings-only-near-term-calm-path-throne) economists have been trying to figure what South-East Asia's second-biggest economy will do next. The data show that this year there will be hardly any growth at all. Spending is weak, investment down, trade and tourism shrinking. A drought is looming in the provinces and in Bangkok easy money has pushed the bourse nearly to an all-time-high. The optimists note that the coup has restored peace and order and things are already looking up. The pessimists see nothing but problems: a collapse in domestic demand, martial law, crippling uncertainty—about the army's ability to run the economy, among other things—and an imminent royal succession.

How much will Thailand's indebted households choose to spend against this background of artificial stability and longer-term uncertainty? TMB Bank plc, formerly known as Thai Military Bank, reckons the moment Thais will confidently dip into their spending money is just around the corner and that it will produce a "V-shaped" recovery. Economists at Siam Commercial Bank, the royal family's bank and bankers, also see a nice pick-up around the corner, with the economy returning to its potential of around 4.5% in 2015. And the Bank of

Thailand, the central bank, agrees that things will soon improve. Everybody hopes they are right.

Ask economists at the World Bank (which stopped lending to Thailand long ago because the country had become too rich) and the answer is different. This week, in the bank's luxe 30th-floor offices overlooking Bangkok, they told reporters that Thailand would remain the slowest-growing economy in South-East Asia till 2016 (see page 153, ff (http://www.worldbank.org/content/dam/Worldbank/document/EAP/region/eap-economic-update-october-2014.pdf) , of their report). They expect the economies of Thailand's neighbours to keep chugging along nicely: Myanmar at 8%-plus, Cambodia and Laos at 7%, and Indonesia, Malaysia and Vietnam all between 5% and 6%.

It surprises no one that Thailand's economy has performed poorly over the past year. The country has suffered six months of political agitation; the absence of a proper government capable of handling fiscal policy since the end of 2013, when the prime minister at the time, Yingluck Shinawatra, dissolved parliament; and then a military coup in May.

An empirical analysis (http://fivethirtyeight.com/datalab/how-thailands-coup-could-affect-its-economy/) of the impact of coups on other national economies shows that growth slows, on average, by 2.1 percentage points in the year of a coup, 1.3 and 0.2 in the first and second year after the coup. But in Thailand the idea that the recent coup might not be good for the economy simply does not arise. It tends to be pushed aside with references to the country's uniqueness—a kind of all-season pass familiar to authoritarians around the world. It is perhaps worth noting that, though the World Bank did not mention political risk explicitly, its predicted shortfall from Thailand's potential growth in the years from 2014 to 2016 roughly matches the estimated average annual negative shock on GDP that this analysis would attribute to the average coup. Paul Collier, a professor of economics at Oxford who has noted that coups "are not a cheap way of replacing a government (http://www.nytimes.com/2009/03/22/books/review/Roth-t.html?pagewanted=all&_r=0) ", calculates that the cumulative effect of a coup, tracked over several years, is to reduce incomes by 7%.

Consider the three main ways in which the Thai economy might get back on its feet—higher household spending, higher exports and a larger government deficit—and it becomes clear why the economy is unlikely to rebound like bouncy ball.

Consumer confidence has recovered somewhat but household spending is still weak. The Bank of Thailand's private consumption index fell in August. High household debt keeps individuals' disposable incomes low. Purchases of flats, houses, cars and consumer durables are being deferred. In many parts of the country the price of land has fallen. A long period of large increases in money supply has not led to the rapid increase in consumption and investment for which many had hoped. Instead much of the cash has been invested in financial assets, driving up Thailand's stockmarkets in the absence of improvements of earnings. No matter, it would seem. Against the evidence, most forecasters based in Thailand predict a solid recovery in household spending in 2015.

The next possible route is higher export growth. So far this year exports have been falling. A strong currency has not helped. Exporters have always struck deals with customs and port authorities to lower their costs—but since the coup and the coupmakers' anti-corruption drive, these have become uncertain. The main reason however that exports have not grown properly in recent years is a loss in Thailand's export-competitiveness. Unlike the tigers of East Asia or, more recently, Vietnam, Thailand has failed to invest in education such as it would need to produce higher-value goods for export. In sum, a self-sustaining export-led recovery is beyond the control of the Thai state—it relies on good times in China, Europe and America, Thailand's main export markets.

So as a third option, could the junta boost growth by increasing government spending dramatically? Thailand does have the fiscal headroom. But experience suggests that the effect of rapid increases in government spending will be slower than the authorities would like. In addition, all indications are that the cabinet will be very conservative when it comes to adjusting government expenditure. The core members of the Thai bureaucracy in charge of fiscal policy live in fear of spending the public's money. It has ever been the politicians who drive up expenditures, and they have been asked to leave the playing field. Another reason why it is hard to see a gaggle of senior Thai bureaucrats taking up the cause of stimulus spending and a greater deficit.

Like every government before theirs, the generals-turned-civilians (http://www.economist.com/blogs/banyan/2014/10/thailands-political-future) face two longstanding economic puzzles: How much to pay farmers for their rice; and how best to manage the exchange rate. They are unlikely to find solutions fundamentally different from those attempted by the elected government they ousted.

The Bank of Thailand and the finance ministry have tended to be very conservative and determined to hang on to the value of the baht. The last time a big depreciation was undertaken deliberately, in 1984, delivered explosive growth in income and exports. At that time a strong finance minister pushed it through against the advice of the central bank. When export growth slowed down to virtually zero, in 1996, the central bankers refused to depreciate. In the end the currency collapsed and Thailand's economy collapsed with it. It took years to bring the economy back to its pre-crisis level of activity. The country's income growth since the collapse has been among the lowest in Asia (http://www.economist.com/blogs/banyan/2014/06/thailands-military-coup) .

A significant depreciation of the baht surely would trigger another spurt in exports and tourism and raise the inflation rate somewhat. However the central bank thinks this would be the wrong approach. Rather than try for 5% growth they are following policies that are likely to result in 2% to 3% growth while trying to convince everyone that things will be better for other reasons. No one wants to risk questioning the authority of the central bank; instead any failure to grow can always be blamed on political uncertainty.

Finally, what to do with the price of rice? This is a regular issue in Thai politics. The question is whether city people should get cheaper food or the farmers should get higher incomes. The ousted government of Yingluck Shinawatra attempted to raise the market price of rice through government intervention. The only way they could manage this while exporting rice at the global price was by absorbing the loss as a subsidy. In a bid to dodge the blow they tried to corner the global market in the belief that then they could sell the rice at a higher price. When this ploy failed Ms Yingluck ended up with a large stockpile of rice and was found guilty of negligence by a national anti-graft commission for her role in the scheme. The junta has just sanctioned one-off payments of $1.2 billion to small rice farmers. It is yet to announce a policy going forward. Though its method of delivery may differ, the junta will have little option but follow the example of Ms Yingluck and pay off farmers in exchange for their political support.

The members of the triumphant mob that cheered the army to power are still enjoying their victory. Playing politics with the economy is an expensive business. The costs to Thailand's economy are still piling up. Compared with trend economic growth the cost will be perhaps $20 billion to $30 billion from 2014 to 2016, which makes it roughly equal in value to the wealth of the Thai monarchy. One can only hope the junta's upcoming performance is good enough to offset such a loss.