2 Tailand

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2.1 Introduction

The Kingdom of Thailand is the only country in Southeast Asia that never colonized by a Western power. Thailand covers 514,000 square kilometers on the western side of the Indo-Chinese Peninsula. It faces the Andaman Sea and Myanmar to the west, Laos and Cambodia to the north and east and Malaysia to the South. Thailand has a humid, tropical climate, and is hot all year round. Summer is from March to May with average temperatures around 93ºF (34ºC), but the temperature can reach over 105ºF (40ºC) for extended periods. Summer monsoons begin as the warm humid air masses flow towards the north from the Indian Ocean. The monsoons end in the fall when the wind reverses direction with the dry southwesterlies. The rainy season, with periods of sunshine, lasts from June to September, with temperatures ranging from 80ºF to 89ºF (27ºC to 32ºC). The amount of rainfall varies with topography. The northeast receives the least rain, while the south is flooded during the summer months. The best time to visit Thailand is during the cool season, from October though February, when it is not as humid as during the summer and rainy seasons. The average temperature is around 65ºF to 89ºF (18ºC to 32ºC). During this season, it can be very chilly in the north, with temperatures dropping to 44ºF (7ºC) at night.

Over the years, Thailand has attracted many immigrants. The people of Thailand share a rich ethnic diversity consisting of Thai, Mon, Khmer, Laotian, Chinese, Malay, Persian and Indian descendants. The great majority of those people are Thai (89% of the population), and the largest minority are the Chinese. The Thai group is divided into four branches: the Central Thai (36% of the population), the Thai-Lao (32%), the Northern Thai (8%), and the Southern Thai (8%).

The official language of Thailand is Thai, but Chinese, Malay, and English are also spoken. The language spoken by almost all people in Thailand has four main dialects. The Central Thai dialect is the official language and is taught in the schools. Many people in Thailand speak the Central Thai dialect in addition to their own regional or ethnic dialect. Many people also speak Malay or Chinese. English is taught in many schools and is often used in business and government affairs.

The Thai economy is based on free enterprise, in which businesses operate largely free of government control. About 65 percent of the nation's workers make their living by farming or fishing, and only about 10 percent work in manufacturing. However, manufactured goods contribute more to the national income than agricultural products do. Government, education, trade, transportation, and other service industries employ large numbers of people in Thailand. Other Thai people work in construction and mining. Forestry, especially the harvesting of teak, was formerly important to Thailand's economy. But the government banned logging in 1988 because too many trees had been removed.

More than 60 percent of Thailand's labor force is employed in agriculture. Until the onset of the economic crisis in 1997, the manufacturing sector was outstripping agriculture in relative importance. But throughout 1997 and 1998 agriculture has been the only high-performing sector in the economy. Rice is the country's most important crop. Thailand is a major exporter in the world rice market. Other agricultural commodities produced in significant amounts include fish and fishery products, tapioca, rubber, corn, and sugar. Exports of processed foods such as canned tuna, pineapples, and frozen shrimp have risen dramatically. Farmland makes up about 45 percent of the nation's land. Farms in Thailand average about 10 acres (4 hectares), and about 75 percent of the farmers own their land.

Manufacturing first gained importance in Thailand in the 1970's, when the Thai government began expanding industries that would increase international trade, particularly with Japan. Thailand's main manufactured products include automobiles, cement, clothing, electronic goods, food products, plastics, and textiles. Fishing has always been a mainstay of the Thai economy. Many farmers raise fish in ponds. Commercial fisheries in the south and southeast fish are trawling. Fisheries also raise shrimp and other shellfish for sale worldwide.

Thailand is a constitutional monarchy, a form of government in which the constitution limits the power of the king or queen. The nation's Constitution provides for a monarch, a prime minister, and a legislature called the National Assembly. The monarch has an advisory role as head of state, and the prime minister heads the government. The National Assembly consists of the House of Representatives with 500 members and the Senate with 200 members. The House members are elected by the people of Thailand. House members serve four-year terms. The senators are also elected by the people of Thailand. Senators serve six-year terms. The House of Representatives selects the prime minister, who is then formally appointed by the monarch. The prime minister selects the Cabinet. The maximum number of Cabinet members is 48. Thailand is divided into more than 70 provinces. The provinces are subdivided into more than 600 districts. Each province has a governor, and every district has a district officer. These officials are appointed by the minister of the interior. Thai villages range in size from a few hundred to a few thousand people.

Thai law requires children to attend school from age 7 to 14. The government provides free public education, but some students attend private schools. Only a small percentage of Thai students continue schooling beyond the required years. Thailand has 15 universities, several large institutes of technology, dozens of teachers' colleges, and numerous vocational colleges. Almost all of Thailand's adult population can read and write.

2.2 Overview of Fiscal Position

Before the financial crisis, manufacturing led the growth of the Thai economy. There is a real compound annual growth rate of 9.6 percent between 1986 and 1996. Relatively abundant and inexpensive labor and natural resources, fiscal conservatism, open foreign investment policies, and encouragement of the private sector underlay the economic success in the years up to 1997. The Asian financial crisis began in Thailand with the floating of the bath in July 1997, has created uncertainty and difficulties for Thailand's economy.

Thailand suffered a sharp economic downturn with the combination of currency and financial crises in 1997 as a result of the unsuccessful defense of the currency and the weak banking system. The economy has been weaker than anticipated, with a decline in real GDP of 0.6 and –10.8 percent in 1997 and 1998 respectively. For 2000 as a whole, the Thai economy grew by 4.3 percent, with moderate expansion in investments and economic activities, compared with 4.2 percent in 1999.

The Asian financial crisis began in Thailand with the floating of the bath in July 1997, has created uncertainty and difficulties for Thailand's economy. After years of impressive economic growth, averaging 9.4 percent for the decade up to 1996, the Thai economy contracted during 1998, and recovery in 1999 will be modest at best. The economic recovery from the economic downturn depends on restructuring the financial sector, attracting foreign investment, and increasing exports of manufactured goods. The Thai have focused on restructuring the financial sector and stimulating domestic demand. Continued liquidity problems plague the real sector, and the Thai government aimed for a budget deficit through increased spending on economic stimulus projects. The Thai government expects improved macro-economic fundamentals to translate into renewed growth and a modest rise in the GDP.

A loan program arranged through the IMF in August 1997 helped Thailand begin restructuring its economy and financial sector. The government closed or took over insolvent institutions and tightened provisioning requirements for banks. The crisis and subsequent restructuring opened the way for increased foreign participation in the financial sector, and foreign banks now own controlling interests in four Thai commercial banks. Legal reforms focused on the financial sector continue. Throughout, Thailand has favour a market-oriented private sector-led approach to restructuring the financial sector. These important measures notwithstanding, the slow pace of economic restructures raises concerns about the sustainability of recovery.

The Thai government welcomes foreign investment, and investors who are willing to meet certain requirements regarding local content or ownership can apply for special investment privileges through the Board of Investment (BOI). To attract additional foreign investment, the Thai government has proposed changes in the investment law. Machinery and parts, electronic integrated circuits, chemicals, crude oil and fuels, and iron and steel are Thailand's principal imports. As much of this import volume fed the manufacturing and export cycle, import levels have decreased dramatically during 1997-1998.

Problems of infrastructure, evident before the financial crisis, will constrain future growth. Telecommunications, roadways, electricity generation, and ports showed increasing strain and bottlenecks during the period of sustained economic growth. Thailand's growing shortage of engineers and skilled technical personnel threatens its future technological creativity and productivity. The rise in per capita income is not equal across occupations or regions of the country. Most of the additional income has gone to those participating in the manufacturing and services sectors if the modern economy. Farmers and fishermen, who still comprise the majority of the working population, have been left behind

The Thai taxation system has undergone significant revision since 1992, when a value added tax (VAT) system was introduced to replace a multi-tiered business tax system. The VAT rate was raised from to 10 percent in 1997 but lowered temporarily back to 7 percent in March 1999 to stimulate consumption; the rate is scheduled to revert to 10 percent on September 30, 2001. Exemptions in place for low revenue businesses were expanded in March 1999. Exporters are "zero rated" under the VAT system but must file returns and apply for rebated. The corporate tax rate is currently 30 percent of net profits for all firms.

Table 2.1 Recent macroeconomic Indicators (1994-2000)

	1994	1995	1996	1997	1998	1999	2000
GDP (Growth rate)	8.8	8.7	6.4	0.6	-10.8	4.2	4.3
Population (million)	59.1	59.5	60.1	60.8	61.5	61.7	61.9
Inflation	5.0	5.8	5.9	5.6	8.1	0.3	1.6
Government Budgetary Balance (In percent of GDP)	1.8	2.7	2.3	-0.7	-2.5	-2.9	-2.4
Export Value (% change)	21.3	24.3	-1.8	3.7	-6.8	7.4	19.6
Import Value (% change)	17.6	31.5	0.6	-13.4	-33.8	16.9	31.3
Current A/C Balance*	-7.8	-13.2	-14.4	-3.1	14.3	12.5	9.2
Current A/C Balance (In percent of GDP)	-5.4	-7.9	-8.1	-0.9	12.8	10.2	7.5
Balance of Payments*	4.2	7.2	2.2	-10.6	1.7	4.6	-2.0
Debt service ratio	11.7	11.4	12.3	15.7	21.4	19.4	15.4

Remark: * In billions of US$
Source: Bank of Thailand

2.3. 1 Brief Review of Economic Activity

A. International Environment

Thailand followed the pattern of economic development in East Asia, moving from an import-substitution strategy to export-oriented industrialization. Beginning in the 1950s, for 30 years the government promoted and protected key local industries to supply a growing domestic market. Leading industries were nurtured by high tariff protection and close ties with the military and bureaucracy.

The second global oil shock of 1979 prompted the introduction of policies to promote the growth of manufactured exports. The recession of the early 1980s forced the government to adopt a strategy of export-oriented industrialization. Conditions the World Bank and the IMF imposed on the Thai government in exchange for aid in reducing its foreign debt put more pressure on the government to increase exports. These policy changes, which stimulated rapid industrialization through foreign investment, were partially responsible for the boom. Other external factors included: the drive by developed countries, especially Japan, to shift their factories to Southeast Asia to lower their production costs; remittances from construction workers in the Middle East; and the growth of tourism, which is now the kingdom's biggest foreign-exchange earner.

Thailand's trade balance returned to positive territory in the year 1998, but this resulted from a collapse of imports rather than a surge of export goods. In the year 2000 Thailand's exports grew by 27.1 percent, with a total volume of Bath 2,733.3 billion. This growth can be attributed to the high rate of world economic expansion, the continuous high growth rates of major industrialized countries, while the Asian economies slowly picked up following the economic crisis. Therefore, both the world trade and Thailand's trade expanded significantly. At the same time, the Bath tended to weaken, thus increasing the competitiveness of Thai products. Exports that enjoyed high growth included computers and accessories, integrated circuits, garments, vehicles and parts, plastic pellets, radio television sets and components, canned seafood, and gems and jewellery. The US remained Thailand's most important export market, followed by ASEAN, the EU and Japan respectively.

Imports in the year 2000 grew at bath 2,513.5 billion, a 39.6 percent increase over the previous year's figures, bath 1,800.1 billion or 7.3 percent. This is in line with growth in exports, which necessitated greater imports of capital goods and raw materials. In addition, the prospect of a stronger economy in the year 2000 stimulated the import of more consumer goods. Most importantly, the substantial rise in the price of oil led to an increase of about 70 percent for oil imports. Imports with the highest value in the year 2000 were electrical machinery and components, integrated circuits, crude oil, industrial machinery, chemicals, computers and parts, iron and steel, metal products, and gems. The largest source of imports was Japan, followed by ASEAN, the US and the EU respectively.

The key factors which has accelerated the export are part of the speeding up of export promotion including the investment from foreign investors and the support from the parent company in seeking the new markets for their subsidiaries, especially in the electrical appliances sector.

In the year 2000 Thailand recorded a trade surplus of bath 219.9 billion, down from a surplus of bath 349.9 billion in 1999. This decline was caused by the large difference between growths of imports and exports. Although the net service increased from that of the previous year, nevertheless it caused the current account surplus to drop to bath 373.9 billion, compared with bath 469.9 billion in 1999.

Capital outflow started since 1998, running continuously up to the end of 2000. The major cause was the low domestic interest rate, giving a wide discrepancy between domestic and foreign interest rates. Then the economic and political uncertainties in the year 2000 and the weakening of the bath helped worsen the outflow. As a result balance of payments showed a deficit in the year 2000 of around bath 58.4 billion, compared with a surplus of bath 172.7 billion in 1999.

From 1984 to 1997 the bath was pegged to basket of currencies of Thailand's major trading partners, with the dollar representing the largest share. The exchange rate averaged 25 bath to dollar during that period. Following the depletion of Thailand's foreign exchange reserves in an unsuccessful attempt to defend the peg, the currency was allowed to float in July 1997 and depreciated to below 50 bath per dollar by January 1998. On January 12, 1998, the bath hit a record low of Bt 56.45/US dollar, and from July 1997 to February 1998 it lost more than 50% of its value against the US dollar. As reform measures and IMF support took hold, the bath stabilized and has traded in the 36 to 44 bath per dollar range since March 1998. The value of bath suffered a continuous decline against the US dollar throughout the year 2000, from bath 37.46 to the dollar to bath 44.72.

The huge inflow of net foreign direct investment in 1997 and 1998, during which Thailand faced with the economic crisis, was an extraordinary event never happened before in Thailand. It happened that since Thailand changed its currency exchange system to a managed float regime on 2 July 1997, foreign investment expanded more than one fold, whereas the economy shrank steadily. The inflow of net foreign direct investment rose by 65.4% and 35.2% in 1997 and 1998 respectively. The large FDI flows in 1998 and 1999 were mostly for recapitalization of the Thai corporate sector rather than greenfield investments. Thailand continues to attract substantial FDI. At the same time, the sectoral composition of net FDI flows changed substantially. Services, electrical appliances, machinery and transport equipment, and chemicals all gained, while the trade sector received less than 10 percent of the 1999 flows.

The excess of domestic investment over local saving was reflected in unsustainably large current account deficits, mostly financed by foreign borrowing. By the mid-1990s nearly half of foreign debt was short-term. Moreover, insufficient investment was directed into higher-technology manufacturing, apart from the fast-growing vehicle and component sector, maintaining the reliance on low-value labour-intensive industries such as textiles and plastics. Much responsibility for the resource misallocation lay with the inadequately supervised financial sector, which is currently undergoing major restructuring. Most finance companies, responsible for much of the excessive lending, have been closed or merged, and several banks have been sold to majority foreign partners.

By the end of 2000, Thailand's outstanding foreign debts increase to US$ 79.7 billion, down from US$ 95.2 billion in 1999. Non-bank private sector debt declined to US$ 33.6 billion while that of the banking sector dropped to US$ 12.1 billion. Public sector external debt declined slightly to US$ 33.9 billion, partly due to the prepayment of state enterprises.

B. Domestic Environment

The real economic growth increases from about 6 percent per year in 1976-1985 to above 8 percent in 1986-1995. At its peak in 1988-1990, growth averaged 12 percent per year. The financial and currency crisis in mid-1997 had a severe impact on the Thai economy. After experiencing a real compound annual growth rate of over 9 percent between 1986 and 1996, real GDP contracted by 0.6 percent in 1997 and –10.2 percent in 1998. Real GDP increased by 4.2 percent and 4.3 percent in 1999 and 2000 respectively.

While the economy stabilized by late 1998, the real economy did not respond, and the focus turned to stimulating domestic demand. Government measures to resolve the crisis have since significantly improved the macroeconomic setting and outlook. Fiscal policy played a significant role in stimulation the economy, as reflected by the fiscal deficit. The government ran fiscal deficits (after years of balanced or surplus budgets. In March and August 1999 the government announced additional stimulus programs to create jobs, increase government purchases of goods and services, lower taxes and industrial energy costs, and promote investment. The economy responded to these stimulus programs with moderate improvements in most indicators from the first quarter of 1999. The government is financing the program through domestic bond sales, as well as foreign debt and grant assistance. The government recognizes the important role of foreign investment and in the year 2000 introduced new incentives designed to make Thailand a more attractive destination for direct foreign investment.

Following a year of relatively high inflation of 8.1 percent in 1998, the price was remarkably stable in 1999. Despite upward pressure from rising oil prices in the world market, inflation was contained at 0.3 percent for the year, the lowest level since Thailand started compiling the index more than 50 years ago. The exchange rate and most commodity prices (aside from oil) remained stable, while domestic demand recovery did not generate upward pressure on prices. However, declining as a result of the fiscal stimulus measures including the VAT rate reduction, and reduction of prices of electricity and cooking gas which became effective since 1 April 1999. Inflation rose only moderately from 0.3 percent in 1999 to 1.6 percent in 2000 despite the sharp rises in oil import prices and the weaker bath.

The major factor affecting domestic demand and private consumption in particular, was the high oil price. Disappointing performances in the stock market also weakened consumer confidence while private investments remained low as there was substantial excess productive capacity except for some export-related industries. Meanwhile, fiscal stimulus was limited by concerns over public debt burden. Several structural weaknesses made the economy particularly vulnerable to a loss of investor confidence, as in 1997. The excess of domestic investment over local saving was reflected in unsustainably large current deficits. For the year 2000 as a whole, passenger car sales and motorcycle sales, which are the usual indicators of private consumption, rose by 24.3 and by 34.1 percent respectively, compared with 44.1 and 21.0 percent in 1999.

Private investment recovery started in 1999. In 2000, its growth was 14.2 percent, compared to a contraction of 5.0 percent in 1999. Machinery and equipment investments continued to grow especially in export-oriented industries such as integrated circuits, jewellery, and electrical appliances. Domestic commercial car sales and import of capital goods (at constant prices) rose significantly by 18.2 and 21.3 percent, respectively. Meanwhile, private construction which dropped 23.5 percent in 1999, showed a sign of leveling out.

2.4 Fiscal Position

2.4.1 Government Expenditure

The government expenditure increased to bath 853.2 billion, up from the previous year by 2.4 percent. The increased expenditure was mainly allocated for current expenditure (except for salaries and wages) such as interest payments and purchases of goods and services, which rose by 22.8 and 8.4 percent, respectively. Capital expenditure experienced a significant decline from the previous year by 15.0 percent.

In the year 2000, the fiscal policy aimed to stimulate the economy under the government budget deficit policy of bath 106 billion. Throughout the year, the government showed a cash deficit of bath 106 billion, down from the previous year by bath 13.6 billion. This lower government deficit together with the decline in disbursement from state enterprises, investment budget, however, resulted in contraction of fiscal impulse, which is measured by a smaller public sector deficit than the previous year.

Table 2.2 National Government Actual Expenditure 1/

(Millions of Bath)

Items	1996	1997	1998	1999	2000
Total expenditure	819,083	931,705	842,861	833,064	853,193
Current expenditure	499,284	512,482	567,062	605,602	659,742
(% change)	14.8	2.6	10.7	6.8	8.9
Wages and salaries	245,629	266,924	284,915	298,701	307,114
Expenditure on goods and services	179,348	167,463	161,072	143,776	155,783
Interest payments	9,164	15,582	18,766	48,799	59,946
Subsidies and current transfers	65,143	62,513	102,309	114,326	136,899
Capital expenditure	319,799	419,223	275,799	227,462	193,451
(% change)	54.0	31.1	-34.2	-17.5	-15.0

Remark: 1/ Representing only actual expenditures as appropriated in the National Government Budget and excluding those financed by external loans and grants.

Source: Bank of Thailand

Table 2.3 National Government Actual Expenditures by Major Economic and Functional Classification

(Millions of Bath)

Items	1996	1997	1998	1999	2000
Total expenditure	819,083	931,705	842,861	833,064	853,184
Economic classification:					
Current	499,284	512,482	567,062	605,602	659,733
Capital	319,799	419,223	275,799	227,462	193,451
Major functional classification:					
Economic services	254,925	308,249	214,325	199,826	191,499
Social services	322,513	363,640	381,282	371,503	382,830
Defense	100,220	98,172	86,133	74,809	71,268
General administration and Services	93,750	100,379	92,547	93,312	97,778
Unallocable items	47,675	61,265	68,574	93,614	109,809

Source: Comptroller-General's Department

: Bank of Thailand

2.4.2 Public Borrowing

In 1998, the government began to absorb the losses of the fund with the first of medium-and long-term bond issues. Interest on the bonds would be paid through the central budget, while principal would be met through central bank profits and proceeds from the privatization of state enterprises and intervened financial institutions. The bond issues helped to dramatically lower financing costs for the fund, which had previously relied on costly short-term borrowing from the money market to raise funds for its liquidity support to financial

The government launched an economic stimulus package in 1998. The expenditure measures placed priority on creating employment and increasing incomes for those severely affected by the crisis in both rural and urban areas. These expenditure measures were financed by external borrowing which did not require Parliamentary approval. The objective was to spend the money quickly to stimulate the economy through job creation and productive investments while at the same time cushioning the poor from the crisis and creating a foundation for the future competitiveness. As a result, foreign debt has increased considerably in the past three years, the result of borrowing by the government to fund stimulus and reform programmes from agencies.

Table 2.4 National Government Finance

(Millions of Bath)

Items	1996	1997	1998	1999	2000
Revenue1/ (+)	853,201	847,696	717,779	713,079	746,817
Expenditure (-)	819,083	931,705	842,861	833,023	853,193
Budgetary deficit (-) or surplus (+)	34,118	-84,009	-125,082	-119,944	-106,376
Non-budgetary deficit (-) or Surplus (+)	9,185	12,958	-4,210	-34,418	-1,815
Cash deficit (-) or surplus (+)	43,303	-71,051	-129,292	-154,362	-108,191
Financing:					
Net domestic borrowings (+):	-25,123	-16,357	-3,018	84,754	48,967
Bank of Thailand	2,054	-5,277	2,548	15,565	-22,925
Commercial Banks	-21,320	-966	-1,635	16,629	40,743
Government Saving Bank	-3,570	-8,200	-3000	13,239	-5,371
Others	-2,287	-1,884	-931	37,563	36,520
Net foreign borrowings (+)	-3,665	-3,761	-4,403	50,636	16,134
Government Bond for FIDF, Fin. Inst.	-	-	400,000	-	44,808
Lending to FIDF, Fin. Inst.	-	-	-400,000	-	-44,808
Use of Treasury cash balances (+)	-14,515	91,169	136,713	-214,780	43,090

Remark: 1/ Excluding grant.
Source: 1. Comptroller-General's Department
: 2. Bank of Thailand

2.4.3 Aggregate Tax Revenue

The aggregate tax revenue increased up to bath 746.8 billion, or 4.7 percent from the previous year, partly due to the corporate tax which increased by 39.4 percent. The marked increase in corporate income tax was due to the improved economy of the year 1999 compared with the significant contraction of the year 1998, and some businesses such as exports and commerce were able to make more profits. In addition, higher revenue was collected from both import duties and VAT (despite the deduction of VAT from 10 percent to 7 percent as of 1 April 1999). Nevertheless, personal income tax still contracted as a result of the sharp declining deposit interest rates. Additionally specific business tax declined considerably as a result of the measures to restore real estate sector and the decline in lending interest rates.

Table 2.5 National Government Actual Revenue Classified by Major Sources

(Millions of Bath)

Items	1996	1997	1998	1999	2000
Taxation	785,797	762,286	633,599	632,626	679,017
Income taxes	281,528	276,365	213,435	205,007	243,493
Personal	107,727	111,682	123,058	91,925	90,541
Corporation	170,178	159,717	85,114	101,941	142,097
Petroleum	3,623	4,966	5,263	11,141	10,855
Indirect taxes	504,269	485,921	420,164	427,619	435,524
Import duties	121,783	94,813	60,928	73,355	85,081
Export duties	9	14	18	68	88
Business tax	520	394	451	95	152
Value added tax	180,911	185,942	176,392	157,721	154,181
Selective sales tax	173,737	175,159	158,908	167,986	165,316
Fiscal monopolies	4,027	12,133	8,906	14,995	14,696
Royalties	5,056	6,471	8,771	7,601	12,186
Licenses & fees	2,084	2,808	1,248	1,168	1,550
Other taxes	16,142	8,187	4,542	4,630	2,274
Sales and charges	8,626	8,710	9,422	25,598	10,403
State enterprises contribute & Dividends	45,697	57,694	35,846	37,806	34,471
Miscellaneous revenue and income	13,081	19,006	38,913	17,049	22,925
Total revenue	853,201	847,696	717,780	713,079	746,816

Source: 1. Comptroller-General's Department
2. Bank of Thailand

Figure 2.1 Tax Revenue Components

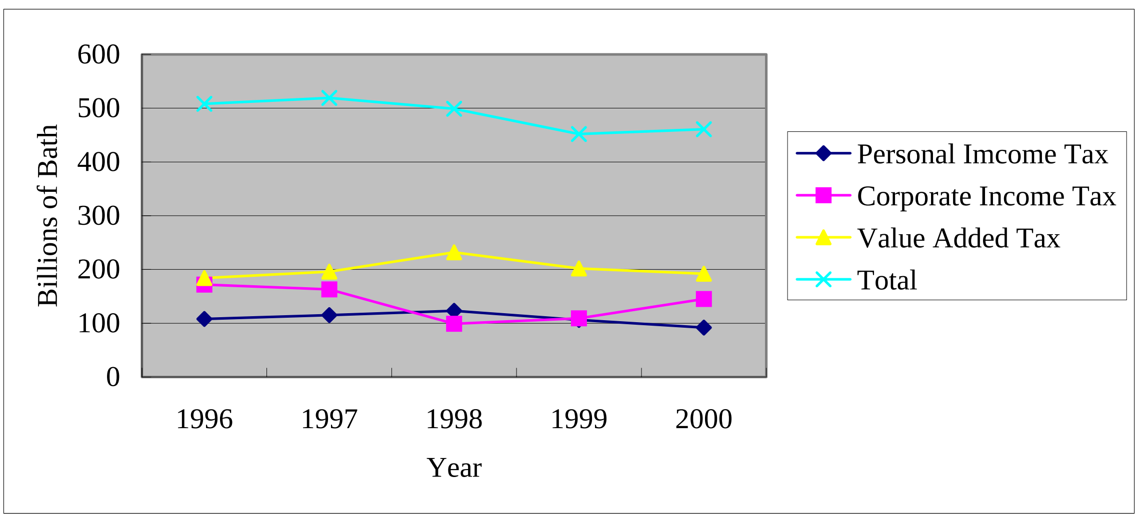
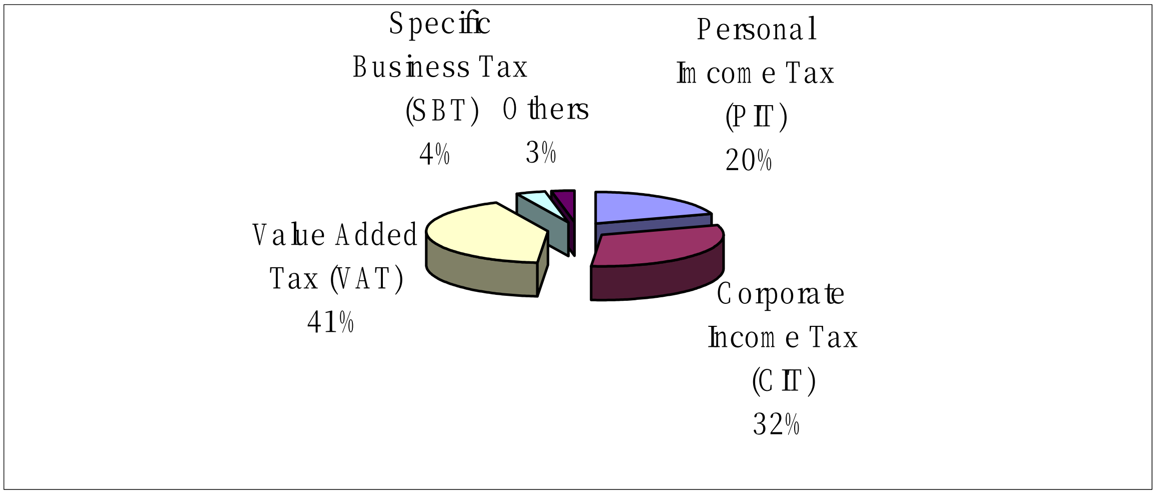


Figure 2.2 Tax Revenue Collected by the Revenue Department Fiscal Year 2000



2.5 Technical Assistance in Fiscal Affairs

The World Bank began lending to Thailand in 1950, a year after the country became a member in 1949. In subsequent years through June 1999, Thailand requested and received approximately US$8.0 billion in loan or credit assistance for over 130 operations.

After the crisis, the Bank worked closely with the Government to design and implement measures for recovery. The Bank is supporting the Government's ambitious program to reform the public sector through improved performance-based resource management, better service delivery, and greater accountability and transparency. One instrument which supports the Government's initiative is the Bank's Public Finance Review, which analyzes weaknesses in the management of public expenditures, public debt, contingent liabilities, and other fiscal risks. The Bank is also working with the Thai government on a US$400 million **Public Sector Reform Loan**, which is scheduled for presentation to the Bank's Board in mid-October 1999. The loan will assist the government in areas such as civil service reform, fiscal decentralization, and tax administration.

In May 1999, the Cabinet passes a Public Sector Management Reform Program, which outlines the Government's vision for institutional change. The program is designed to achieve three main objectives:

- Improve resource management by creating incentives for budget and civil service agencies to focus on outcomes and improving performance and effectiveness in the management of financial and human resources.
- Enhance service delivery by restructuring the way government delivers its services, through outsourcing, restructuring or decentralizing government activities to enhance the responsive to communities.
- Promote accountability and transparency of government – restoring confidence in government by improving transparency in budgeting, refocusing the civil service toward client service, and establishing effective mechanisms to promote accountability and transparency.

The World Bank has supported the Government's reform program through technical assistance, knowledge sharing and financial support.

Key Public Sector Reform Areas

- Revenue management – improve taxpayer compliance; strengthen collection enforcement; and improve overall revenue management by developing strategic and business plans, identifying information technology priorities, and developing an integrated IT system.
- Expenditure management – improve strategic planning capability of ministries, implement performance budgeting, form resource agreements with performance targets in sector ministries, and incorporate budget evaluation and feedback into the budget cycle.
- Human resource management – develop new organizational structures and staffing profiles for ministries in line with redefined functional objectives; develop modern performance-based HRM systems for the civil service; and develop the framework for autonomous public organizations.
- Decentralization – devolve expenditure functions to local administrations, enhance local revenue collections, improve the intergovernmental transfer system and enhance accountability within local governments.
- Cross-Government accountability and transparency – work with the Office of the Prime Minister and OCSC to increase institutional accountability, enhance public access to government information; promote probity among civil servants; and enhance civil society participation.

2.5.1 Tax Policy

Thailand tax revenue has traditionally relied heavily on indirect taxes and corporation taxes. The revenue share from direct taxed is low about one-third of total revenues and is composed mostly of corporation taxes. Personal taxes are less significant. Substantial revenue comes from import duties and selective sales taxes, which tend to be more distortion than broader-based taxes like the value added tax (VAT). During the boom years, Thailand’s revenue collection systematically exceeded expectations without significant effort. Tax policy changes (such as broadening tax bases, reducing tax rates, etc.) will also be needed to enhance the productivity, efficiency, and equity of the tax system.

As part of the Public Sector Management Reform Program, the Revenue Department has launched a reform program that seeds to improve revenue collection and minimize tax evasion, and to achieve a more equitable distribution of the tax burden. These objectives will achieved by:

- Strengthen collection enforcement.

  The first priority is to accelerate efforts to collect current debts, and to develop debt collection strategies by debt category. Accurate and timely information about tax arrears will also be developed, as well as a debt case management application to improve controls over casework, and audit case selection methods. Collectible debt is expected to be reduced to a manageable level of no more than 5 % of total annual tax collections.

- Improve taxpayer compliance.

  Important steps taken so far include the establishment of the Large Business Tax Administration Office and designing an automated audit case selection system. Other critical tasks include:

  (i) developing and implementing a more comprehensive audit strategy
  (ii) improving the quality and availability of audit data
  (iii) unifying taxpayer identification numbers
  (iv) establishing a more streamlined and focused VAT refund control system and
  (v) coordination audit and delinquency collection.

- Enhance information technology as a means to strengthen management.
  The Revenue Department’s computer system lacks basic functionality to maintain taxpayer accounts, identify arrears, select quality audit cases, and provide timely management information. Efforts will be made to develop an operational, functional and integrated computer system and to align business and operational priorities with the envisaged developments in technology.

The recent developments

- Taxpayer compliance has improved.

For 2000, there are 324,000 registered VAT taxpayers, an 11% increase since 1998. Revenue collected from audit activities improved significantly. A national audit plan has been prepared with target audit revenue to be collected each month by each region.

- Tax collection enforcement has also been strengthened.

Total tax arrears have fallen from bath 98,000 million at end 1999 to 87,546 million bath at end 2000. Collectible debts at end 2000 were 25,905 million representing 5.6 percent of total tax collections for the year 2000 (bath 461,191 million). This is well below the benchmark target of 8 percent.

Tax arrears are divided into 4 main categories – collective, collection postponed (awaiting appeals and court decisions), uncollectible (in bankruptcy or awaiting write off), and debit account balances not yet due for payment. The Debt Collection Devision has reviewed the components of each of the categories, and has moved some of the components into different categories. For example, “unable to locate taxpayer” cases have been moved from the “uncollectible” to “collectible” category. This will take effect from October 1, 2000, and the immediate result will be that the collectible debt will increase from bath 25,905 million (5.6 percent of tax collections) to bath 34,078 million (7.4 percent of tax collections). Factors contributing to this improvement are the increased attention given by management to tax arrears, greater control over debt cases in the regions, and a reduction in the number of new debt cases raised by auditors.

With such a large number of debt cases and limited resources, it is important to give priority to the cases that are most likely to yield additional revenue. These are the newer, larger debts in the collectible category. However, the reasons why debts in other categories are increasing should also be explored, to minimize the number of debts where there are impediments to collection. Of particular concern is the growth in the number and value of cases delayed because of appeals and court decisions – the postponed category. There are currently 8,800 VAT debts under appeal – an increase of 4,200 debts from one year ago.

- The Revenue Department is completing its new strategic plan, which will extend from year 2001 to 2003. The Plan will incorporate critical success factors and key performance indicators, consistent with the Results Based Management approach. The Plan is based upon four objectives:

(i) collecting revenue more efficiently

- minimized the risk of losses by ensuring that revenue is collected from a range of different taxes across broad taxpayer bases. Policies aimed towards lower tax rates and larger taxpayer population are more equitable and sustainable.
- adjusted withholding tax system to cover all business in order to prevent tax evasion.
- investigated taxpayers who may have evaded tax. Such information to investigate may come from various sources such as written complaints, telephone calls, other governmental sectors and foreign tax administration

(ii) helping taxpayers meet their obligations under the self-assessment system

- telephone inquire systems and the Internet are being installed in order to provide better and more accessible information for taxpayers and the general public.
- introduced the face to face counseling system and gave some assistance and guidance to the taxpayers who cannot file the tax return properly due to lack of appropriate knowledge.
- published some publications of news bulletins on tax matters, internal procedures and regulations for both taxpayer's and official's use.
- developed the mutual understanding between taxpayers and the tax authorities and getting support and corporation of mass media for a better tax administration

(iii) strengthening compliance (control and enforcement)

- taxpayers can pay their taxes not only at the tax offices but also through the bank system. In this case, taxpayers do not have to go to tax collection offices, however, they can pay their taxes in time.
- introduced an Electronic filing system (Diskette filing system) to decrease taxpayers difficulties in filing their tax returns. Presently, this Electronic Filing System is used only for the filing of personal income tax returns. It is still not yet a full-scale system such as the transfer of information via telephone. In the near future, a full scale Electronic filing system will be implemented.
- improved the awareness of dead lines and importance of filing tax return and paying taxes on time.

(iv) developing, training and encouraging staff so that they can perform their work more effectively

- trained tax officials in various tax courses and computer courses including attained domestic and international tax seminar.

2.5.2 Budget and Public Expenditure Management

The Bureau of the Budget (BOB) is a key actor in building such a public expenditure management system in Thailand, with responsibility shared among the National Economic and Social Development Board (NESDB), the Ministry of Finance (MOF), and the Bank of Thailand (BOT).

Fiscal transparency is weak in Thailand. Fiscal planning is based on cash flows of a narrowly defined central government, off-budget operations dilute fiscal responsibility and accountability, fiscal risks arising from government's contingent liabilities are not considered properly, and lack of ministry and department level financial reporting hides the true cost of government policies and services. This lack of transparency distorts the prioritization and allocation of public resources, and diminishes accountability.

Enlargement of poverty alleviation programs and improved targeting will be critical to reduce the population of poor persons and to protect against periodic downswings in the economy. Although expenditures allocated to these programs are growing. The government should increase the use of geographical targeting and self-targeted programs in allocating resources to meet distributional objectives. Critical needs are to shift away from the current, equal distribution of resources across regions, and to define better criteria for allocating resources (e.g., on the basis of per capita income or regional poverty levels).

As part of the public Sector Management Reform Program, the Bureau of the Budget has launched a comprehensive budget modernization program that will reform Thailand's budget management so that it promotes better performance and transparency. Expenditure management reforms are underway to:

- Introducing performance-based budgeting.

  In the context of performance-based budgeting, the Bureau of the Budget defined a new flexibility and accountability framework for sector ministries, which will delegate more authority to these ministries in return for greater performance and reporting standards. Such a framework will improve the management of outputs and outcomes rather than control inputs. The Comptroller General's Department is concurrently identifying financial reporting requirements for ministries and departments, improving the government's accounting policies, and developing an integrated financial management system.
- Strengthen evaluation of sector policies and performance.

  In the new performance framework, as central agencies relinquish line-item control they will focus more on reviewing and evaluating the performance of ministries and departments and on analyzing whether their polices are consistent with the government's strategic priorities. A first step in this process is to coordinate evaluation and policy analysis among the Bureau of the Budget, the NESDB and line ministries.
- Improve fiscal transparency.

  The Bureau of the Budget and the Comptroller General's Department are developing a policy to improve fiscal transparency. And standards for reporting off-budget fiscal operations as part of budget documents and financial statements. The Bureau of the Budget and Public Debt Management Office are compiling information of contingent liabilities. A fiscal strategy extending over the general government financial position with a medium –term outlook will also be developed. Additional reforms are needed to manage fiscal risks within the budget process and to meet international public accounting standards.

The recent developments

A subcommittee chaired by the Deputy Minister of Finance has been established to recommend reforms to the existing Budget Procedures Act. Work has commenced on defining a legal framework within which performance-based budgeting will operate, which could include the preparation of a new Budget Act in the future.

- The Comptroller General's Department (CGD) has completed a set of high-level accounting guidelines (on assets, liabilities, revenues and expenditures together with reporting formats), which will establish standards for agency charts of account. The CGD is responsible for establishing the accounting standards which pilot agencies will observe in order to meet the financial management hurdles developed by the BOB.
- The Bureau of the Budget (BOB) has revised budget regulations to permit block granting. In the year 2001, the BOB has allocated block grants to two pilot agencies; the Provincial Hospitals Division of the Ministry of Public Health, and the Department of Commercial Registration in the Ministry of Commerce. In addition, BOB forward estimates for pilot agencies have been included in the budget Red Book for the first time.
- A Memorandum of Understanding (MOU) between the OCSC and the BOB on Performance Budgeting in the OCSC was signed in April 2000. This MOU is a prerequisite for developing a Resource Agreement that allows block granting. It is expected that the OCSC will be block granted in the year 2002.

2.5.3 Fiscal Federalism

Thailand is a unitary government that presently has a highly centralized fiscal system that grants limited local autonomy in terms of functions, area, staffing, funding and decision-making. The government has only recently begun implementing the decentralization reforms mandated by the new Constitution, Which include increasing the share of local government expenditures, assigning more revenue sources to local governments, revising the system of intergovernmental transfers to provide grants in a more transparent and predictable way, and promoting mechanisms for local accountability. Because most Thai local governments are weak in financial management, planning and service delivery, and generally lack adequate resources to deliver services effectively or to undertake needed capital projects, implementing the proposed program of decentralization reforms will require significant strengthening of local capabilities. As part of the Reform Program, the government is designing the decentralization framework for subsequent implementation. Decentralization reforms are underway to:

- Clearly definite central-local expenditure functions.

  Clarity in expenditure assignment is necessary to eliminate the overlapping functions performed by the central and local governments, and to improve expenditure effectiveness. The National Decentralization Act specifies a phased approach – spanning four years – to the devolution of administrative power to prepare central and local governments to assume their new roles.

- Devolve revenue authority.

  The proposed devolution of revenue authority is based on the goal that, by 2001, the share of local revenue relative to total government revenues (including intergovernmental transfers) will increase to 20 percent, largely by increasing transfers to local governments. Local revenue shares are expected to increase to 35 percent of total government revenues by 2006. International experience shows that decentralization can have negative effects – including overlapping expenditure provision and macro-instability – if financing precedes functional assignment of responsibilities. Equally important, the potential disincentive effects of large central transfers on local resource mobilization should be carefully considered.

- Improve local revenue mobilization.

  As additional responsibilities are devolved to local governments, they must improve their revenue mobilization both to assure fiscal sustainability and to promote local accountability. Options include introducing new taxes. Reforming existing taxes and enhancing collections from charges and fees. To meet the targets for 2006, local governments may need to double their own revenue collections (from 1.5 percent of GDP to 3 percent of GDP). In many countries around the world, property taxes, which are underutilized in Thailand, serve as an important local revenue source. Proposed property tax reforms could enhance local revenues, although establishing competent, local administration may be costly and require significant capacity building. Reforming the intergovernmental transfer system.

Thailand's intergovernmental transfer system is neither transparent nor stable. Over 70 percent of intergovernmental transfers (or subsidies) are allocated for specific investment projects. Reforms will reduce the reliance on specific project grants and increase reliance on general-purpose grants that are allocated according to transparent formula that address vertical imbalance and equalization objectives.

- Promote responsible local borrowing.

  While municipalities have the legal right to borrow, few do so because of limited resources and experience, and cumbersome approval processes by the Ministry of Interior. International experience has shown that macroeconomic fiscal imbalances can arise if local government borrowing is not managed carefully. Reforms underway include the development of the Regional Urban Development Fund as a mechanism to channel credit to viable projects managed by creditworthy local governments. Future reforms include potential aggregate limits on local indebtedness, local bankruptcy regulations and mechanisms for promoting responsible local borrowing.

- Enhance local accountability.

  Local accountability must be enhanced if decentralization is to succeed, and reforms must be introduced to strengthen local fiscal reporting and local revenue mobilization, and to engage civil society in local decision making and monitoring.

The recent developments

- The National Decentralization Act, which became effective in November 1999.

  The Act defines the roles and responsibilities of the National Decentralization Committee (NDC). The NDC was established in February 2000 and is located in the Office of the Permanent Secretary of the Prime Minister's Office. The Act also requires the NDC to prepare a **Plan to Decentralize Administrative Power to Local Authorities** and specific Action Plans within sectors.

2.5.4 Human Resource Management

Several key problems are linked to the under-performance of public administration. First, the role, organization, and processes of government are in need of serious overhaul to streamline procedures, eliminate duplicative structures, and shed and/or devolve activities inappropriate for central government administration. Second, the civil service is overstaffed and underpaid, resulting in difficulties in attracting, retaining and motivating good staff and, ultimately, in poor performance of basic government functions. Third, the current civil service's organizational culture, reinforced by cumbersome and antiquated regulations, does little to reward performance or service to citizens.

Effective civil service reform must focus on three important objectives:

(i) enhancing the quality of service through more effective performance

(ii) increasing the efficiency of government operations by reducing its cost

(iii) reducing the scope for corruption and political interference in civil service activities.

Several inter-related measures are proposed to achieve these reform goals. Delivering better services in a cost effective and equitable way will require enhancing the access, timeliness and quality of public services through outsourcing, restructuring or decentralizing activities and being more responsive to clients. Administrative renewal involves modernizing the role, organization, and processes of key line ministries to enhance their performance in delivering services. More efficient use of public resources requires streamlining procedures, eliminating duplicative structures, and devolving to local governments or outsourcing activities inappropriate for government involvement to the private sector.

As part of the Public Sector Management Reform Program, the Office of the Civil Service Commission has launched a program that will reform Thailand's human resource management so that it promotes better performance and transparency. Human resource management reforms are underway to:

- Develop detailed programs to align organizational structures of line ministries with their new functional objectives to achieve the optimal mix of government functions and most efficient processes and staffing allocations for effective policymaking and service.
- Match staffing profiles and numbers to the new functional requirements of the civil service and containing the cost o government through various mechanisms.
- Develop modern, performance-based human resource management systems for civil service. This may include an updating of out-of-date procedures, or the introduction of performance management through results-based human resource approaches that couple greater managerial discretion with performance incentives, and can include individual job description and classification systems, greater flexibility in employment system, performance appraisal and remuneration, career development and advancement, and disciplinary and complaint systems.
- Develop a well-motivated, politically neutral, cross-governmental senior cadre to lead civil service renewal program, which would build a professional class of higher civil servants.
- Develop a regulatory framework for autonomous public organizations (APOs)

The recent developments

- The World Bank and Japanese government joint to give the scholarship to the civil servants to study Master's Degree Program in Taxation Policy and Management in Japan for two years.
- A voluntary Early Retirement Plan (ERP) yielded the retirement 24,000 civil servants, teachers, police and military, with estimated budget savings of bath 8.4 billion over 10 years.
- In August 2000, the Cabinet approved the establishment of a Senior Executive Service (SES). Through the SES, the OCSC will develop a well-motivated, politically neutral, cross-governmental senior cadre to lead the civil service renewal program. Full implementation of an SES will require a new salary system. In its current form, the proposal does not envisage radical change (e.g. existing position holders will transfer

across to the SES, new open recruitment will apply only when these positions become vacant, and outside recruitment is not yet envisaged).

- The OCSC addressed several key, emerging issues in civil service management reform. The OCSC is proposing to develop a Human Resource Management Information System (HRMIS) that would be used by all ministries and agencies. Better personnel information (e.g. on location, personal profiles etc.) is a key aspect of a performance-based and more devolved Human Resource Management System.

2.6 Country-Specific Technical Assistance Requirements

2.6.1 Board of Investment Incentives

Collection of Corporate Income Tax ranks the third in amount of tax collected by the Revenue Department. It is recognized that this could be attributed to Board of Investment (BOI) granting exemption. This surmised in the following- ‘ exemption of a juristic company or partnership on the net profits derived from the promoted activity for a period prescribed by the Board; which shall not be less than three years but not more than eight years, from the date income is first derived from such activity’.

In the case where a loss has been incurred during the period receiving exemption, the promoted person shall be granted permission to deduct such annual loss from the net profits accrued after the expiration of the period of exemption. This period will not be more than five years from the expiry date and can be deducted from the net profits of any one of those chosen five years.

It can be seem that permission granted for the promoted activity from BOI is not making the needed assessments of the possible losses and gains incurred when granting permission for the exemption of corporate income tax. It cannot say that if this could in turn cause a fiscal burden on the government because it has no information for systematical measurement.

Given this, if we can obtain the necessary tools to establish a database for tax data collection that would enable us to assess and evaluate the promoted activity from the BOI It would provide us with the necessary data collection tool to manage and track specific data for example-domestic income, foreign income, and any expenditure such as labor figures and fluctuating business sectors. This data would facilitate other related areas and would assist in the making decision of both trade and investment which certainly will ensure us in the appropriated policy.

In addition, we will be able to use the database of information for comparative analysis, e.g. BOI and non-BOI. It would be the responsibility of the Regional Revenue Offices and Area Revenue Offices for the data collection and data-entry of the information collected from their respective areas. It is the Revenue Department’s aim to develop and train its human resources in computers and technology, to learn new methods and utilize the experiences of other further developed countries within the region.

2.6.2 Improving the effectiveness of collecting Excise Tax

In the past, the Excise Department has been modernizing its information system. Its modernization effort is focused on enhancing the transparency and efficiency of Excise Tax collection. The current modernization initiatives of modern information technology aimed in particular at extending the coverage of the existing computer systems, introducing the electronic data imaging and processing system for improving the effectiveness of Excise Tax collection and better understanding of macroeconomic factors that influence Excise Revenue.

The Excise Programs initiative will cover three components:

(i) modernization of Documentation and Information System

(ii) establishing new Computer Cabling System for Excise-Net
(iii) Excise Revenue Forecasting in Macro-economic Model.

The first two components are used for enhancing the Excise Tax collection. Their implementation requires an insight of excise operations and solid knowledge on excise activities, Therefore the implementation of the New integrated IT system with document image system will improve the performance of Excise Department. In addition to the last component, the Excise Department as well as other government tax collecting agencies have been under pressure to carry out the improvement of administrative performance. The better administrative performance will be focused on precise estimation on excise revenue with the adjustment of taxpayer behaviors, such as the change in oil price, GDP, inflation, interest rate and excise tax rate, lead to change in excise revenue in macro-economic model.

Therefore the Modernization of Documentation and Information System with establishing new Computer Cabling System for Excise-Net; and Excise Revenue Forecasting in Macro-economic Model are critical part of Excise Department reform. Such a system will be very important in helping the ED achieves the enhancing performance. In this regard, the Excise Department requires consulting services to develop the above modernization of documentation systems on Excise-Net and revenue forecasting in macro-economic model.

2.6.3 Taxation of Debt Instruments and Derivatives

The past two decades have seen what is described as a financial revolution however; financial regulations in Thailand do not seem to have kept pace with the development of existing instruments. Taxation on debt instruments is currently one of our concerns. It should not impede smooth and active trading of government and corporate bonds in order to ensure continued development of the market. While in the past, tax officials had no difficulty identifying certain income items such as interest or capital gains, considerable difficulties are arising in connection with new debt instruments. Ambiguity in both tax rules and policies would prevent fair competition among financial institutions, distort capital flow and impede market development. This it is crucial to clarify as well as rationalize applications of the existing tax legislation to ensue continued development of the domestic financial market.

At the same time, importance of rational taxation for derivatives instruments is increasingly recognized. Interest rate derivatives are needed to facilitate investment, dealing in and underwriting of long-term fixed income instruments such as government and corporate bonds. Before the government bond market started generating benchmark yield curve, currency and interest rate swap market has served as a market to offer implied benchmark yield for Thai bath interest rate. This market is expected to continue to be an important market and, requires appropriate taxation. An organized market for stock index options is expected to be introduced shortly by the Stock Exchange of Thailand. These instruments, especially designed to handle different kinds of risks, have been rapidly accepted in financial markets around the world, and it is notable that, in Thailand, a large number of private entrepreneurs or organizations are beginning to recognize the benefit such instruments will bring in handling their assets and liabilities. Due to the large volume issuance of government bonds since the crisis, commercial banks now take significant long positions in longer-term bonds. They need to be able to manage market and interest rate risks, especially given the current historically low interest rate.

This requirement aims to provide an analytical review of the present status of the Thai tax law system in relation to financial instruments with particular emphasis on debt and derivatives instruments. It will also equip the Revenue Department of the Ministry of Finance with analytical tools to make appropriate judgments and take definitive actions necessary for reforming the existing system. The overall objective of the consulting assignment is to assist the Thai tax authorities in their effort to:

(i) minimize the distortion in the system of debt instruments and derivatives taxation, so as to minimize tax arbitrage opportunities as well as the distortion in the flow of funds in relation to various types of debt instruments and derivatives;

(ii) reduce evasion of taxes and improve effectiveness of collection of taxed levied on debt instruments and derivatives; and

(iii) promote healthy development of the Thai financial market.

2.7 Conclusion: Where we stand and Where we go

Thailand has implemented several structural measures that address the underlying causes of the crisis in 1997. Manufacturing is no longer the largest sector in Thailand. Services replaced manufacturing as the largest contributor to growth, and attract a large proportion of foreign direct investments. However, there are risks that need to be managed well. The Thai recovery, as with the other East Asian countries, was led by exports. And now with the global downturn, export growth has lost its momentum significantly. External demand has softened at a time of weakening domestic demand. Domestic private investment and consumption growth fell. Recovery in business investment has been held back by the high level of distressed assets in the banking system, slow progress in corporate restructuring, and potential concern regarding the consistency of short-term policies with the medium-term goals.

The prospects for employment growth and poverty reduction are affected adversely by the slowdown. Until the onset of the crisis in 1997, high growth had created many employment opportunities, wages had increased rapidly and poverty had fallen. As a result of the crisis, more than one million Thais are still without a job and poverty incidence increased sharply.

The new government, with a strong electoral mandate, has introduced a number of pro-poor programs as part of the fiscal stimulus to support recovery. These include the village fund, health fund, debt suspension for farmers, as well as a fiscal stimulus reserve fund to be implemented if the expected pick up in external demand does not materialize. Debt restructuring could be accelerated through the formation of a national asset management company (TAMC). The stalled privatization of state owned enterprises is being revived. These are steps broadly in the right direction. The challenge is to ensure that these policy actions are consistent with the medium term objectives of (i) maintaining sound macroeconomic policies, (ii) developing a well balanced financial sector with a strong credit culture, (iii) enabling both public and private firms to become more competitive, and (iv) developing modern public sector institutions to improve efficiency, transparency, and competition. In addition, pressure for rapid reform must be balanced against the need for transparency and broader participation in government policy formulation.

The government has increased the size of the budget deficit. Public debt has increased three-fold compared to the pre-crisis levels, mostly due to costs arising from financial sector restructuring. The high level of public debt is comparable to the other countries in the region but is sustainable only of GDP growth remains at 4-5 percent per year, interest rates remain low and the surplus on the primary fiscal balance can gradually be increased. The recent slowdown in growth places a limit on the size of the fiscal stimulus.

The recently established Thai Asset Management Corporation could help boost financial restructuring. The design of the TAMC addressed well some of the incentive issues: NPLs will be acquired from both state and the private banks. Private banks would share gains and losses with the government on their transferred NPLs if recovery rates turn out to be different from initial transfer prices. The design and the special legal powers granted in the TAMC Act will speed up restructuring but implementation will be a challenge. The outcome of the TAMC will depend on the quality of its management, credibility in deal making, transparency and simplicity in restructuring guidelines for borrowers and guarantors, and the incentives for TAMC managers to maximize recoveries and minimize the cost to taxpayers.

Several measures have been announced to revive the privatization program, which is a good development. These include (i) government announcement that 18 state owned enterprises would be privatized by 2003; (ii) creation of a National Holding Company under which commercial state enterprises will be gathered; (iii) announcement of a schedule of Initial Public Offerings (IPOs) of state enterprises in the Thai stock market; and (iv) inclusion of Employee Share Ownership Programs (ESOP) in the IPO transactions. These announced measures, if properly implemented, would speed up privatization of large-scale enterprises, and could significantly deepen and strengthen the capital markets.

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