Thailand's recession: "Emerging economies" dragged into global downturn

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The Thai government of Prime Minister Yingluck Shinawatra this month downgraded the country's expected growth rate for 2013, from the previous range of 4.2 to 5.2 percent to 3.8 to 4.3 percent.

The slashing of the National Economic and Social Development Board's (NESDB) forecast for economic growth, which had been 6.4 percent in 2012, followed data that showed that gross domestic product (GDP) unexpectedly contracted 0.3 percent in the June quarter. This followed a 1.7 percent fall in the first quarter, indicating a recession.

These are the first two consecutive quarters of negative growth in Thailand since the initial phase of the global financial crisis, when the economy contracted by 5 percent in the final quarter of 2008 and 2.5 percent in the first quarter of 2009.

Officials and economic commentators attributed the recession to weaker domestic demand, slowing exports and the government's failure to implement a promised 2 trillion baht infrastructure program. The NESDB downgraded export growth predictions from 7.6 to 5 percent.

Within two days of the announcement, the Thai currency, the baht, dropped to its lowest level in three years, 32.12 to the US dollar. Thailand's current account has dramatically changed from a surplus of $US1.3 billion in the first quarter of 2013 to a deficit of $5.1 billion in the second quarter.

Thai officials rushed to issue reassurances. Bank of Thailand (BOT) governor Prasarn Trairatvorakul said the overall economic condition of Thailand was "still OK." Deputy Prime Minister and Finance Minister Kittiratt Na-Ranong claimed that seasonal factors were responsible for much of the decline.

In reality, the dramatic turnaround in Thailand is the product of global economic developments engulfing the "emerging economies."

Thai exports, particularly motor vehicles, electronics, electrical equipment and rice, account for two thirds of its GDP. The country's main trading partners are Japan (which takes 10 percent of exports and provides 20 percent of imports), China (12 and 15 percent respectively), the European Union, the United States and Malaysia.

Stagnation in the US, recession in Europe and the slowdown in China have already impacted on exports. Even the weak growth predictions of 3 to 4 percent for Thailand this year are based on an unlikely recovery in export earnings in the second half of this year.

Thailand and other so-called emerging economies are being hit by the quantitative easing policies of the central banks in the US and Europe that has poured billions into the international financial markets. According to International Monetary Fund chief Christine Lagarde, $1.1 trillion of net inflows has flooded into "emerging" equity markets and government bonds, driving up the value of local currencies.

This influx provided easy credit for private and government borrowing and, to a lesser extent, increased foreign direct investment. Foreign investors currently hold 20 percent of Thailand's government debt, about 50 percent of Malaysia's and over 30 percent of Indonesia's.

Now the decline in export markets, combined with the US Federal Reserve's signals that it will taper off its quantitative easing policy, has seen speculative capital move out almost as fast as it moved in. Among the first casualties were the inflated currencies. The baht has declined 2.3 percent so far, but may fall further. The Indian rupee is already down 16 percent and Indonesia's rupiah 5.5 percent.

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Equity markets have also suffered. Over the past month, foreign investors have withdrawn $1.04 billion from Thailand. Foreign direct investment is also down compared to other South East Asian economies. In 2011, Thailand was a net exporter of capital, mainly for intraregional investment.

The capital outflow has strained financial systems. As in Malaysia and Singapore, household debt has risen sharply in Thailand, reaching 8.97 trillion baht ($282 billion) in March. This represents 77.5 percent of GDP, up from 55 percent in 2007. Households are now spending an average of 34 percent of income on loan repayments. The need to attract capital has meant that the BOT has not been able to lower interest rates to stimulate growth.

The country's budget is also under pressure. Public debt grew by 47.93 billion baht in June, to 5.22 trillion baht, or 44.27 percent of GDP. Yingluck's 2 trillion baht infrastructure program depends on parliament passing a bill to allow the sum to be borrowed over seven years, a proposal expected to cause conflict in ruling circles.

The government is also under fire from big business over its rice pledging scheme, which pays rice farmers 15,000 baht a tonne. The idea was to increase farm incomes to stimulate the economy and shore up the electoral base of the ruling Puea Thai party. But the plan has proved a disaster, forcing high-priced Thai rice out of much of the international market and costing $15 billion this year, or 4 percent of GDP.

The deteriorating economic situation will only exacerbate tensions within the ruling class, between the traditional establishment centred on the monarchy, military and state apparatus and the wing led by Yingluck's brother, exiled premier Thaksin Shinawatra, who was ousted in the 2006 military coup.

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