INSTITUTE OF CURRENT WORLD AFFAIRS

JEF-25
Thailand's Balance of
Payments: The Long View

150 Soi 20 Sukhumvit Road
Bangkok 11, Thailand
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Mr. Richard H. Nolte
Institute of Current World Affairs
535 Fifth Avenue
New York, New York

Dear Mr. Nolte:

For some time now I have been preparing my observations on the long-range prospects for Thailand in light of the recent changes in peninsular Southeast Asia. Part of this project involved a look at economic prospects, and the more I looked, the more fascinated I became by what I uncovered. Hence I have put together the following essay on Thailand's economic relations with the rest of the world. My impression from looking at the kingdom's economic history is that many current observers do not appreciate the major shift now taking place in Thailand's economic relations with the rest of the world and how this will work itself out in the balance of payments -- hence the apocalyptic headlines a few samples of which follow. As is usually the case, these apparently economic shifts are grounded in factors going far beyond economics. A while back I got a letter from someone (he shall remain nameless) advising me to the effect that my participation in a certain endeavor would be pointless, since the endeavor had to do with economic development and, as a student of politics, I could have nothing to contribute. I hope what follows may serve in some small way as a counterexample to this unfortunately widespread view.

Let me conclude this introductory note by apologizing in advance for the voluminous tables and graphs in the following pages. I want to demonstrate that national character and the political relations between groups in society show up markedly in the balance of payments, and this has required a lot of numbers.

Sincerely,

Jeffrey Race

Investment falls to critical level

Jeffrey Race is an Institute Fellow studying how the institutions of the past influence people's behavior toward one another today. His current area of interest is Southeast Asia.

For the first time in its history, the Kingdom of Thailand is planning to go into the world's commercial capital markets to finance the deficit in its balance of payments. Concurrently, foreign investment is sharply off, while the price of imported oil continues to rise. These developments, and others in the political sphere, suggest the wisdom of a hard look at Thailand's balance of payments history, in order to get a perspective on the changes now taking place.

Such a hard look reveals that important long-run economic, political, and demographic trends are just now beginning to make themselves felt in the balance of payments. The convergence of these trends will move the kingdom away from its previously atypical foreign reserve position, toward one more closely approximating that of Third World countries in its per capita income range. Several policy implications ensue from these long-term trends. If the current elections lead to an effective government, there should be no problem in responding to them. Thailand's economy still retains enormous vitality vis-a-vis the rest of the world. Thailand was, for example, one of the few oil importers to increase its reserves during 1974. The present transition appears to have drawn the attention it has not because the economic future appears so bleak (it doesn't), but because Thailand's economic past has been so favorable. Recent alarmist headlines would be hard for the leaders of many other countries to understand: they would be delighted to occupy the economic position which Thailand will enjoy even after completing the transition now taking place. The fact is that both Thai leaders and the Thai people have been spoiled by their extraordinary economic history.

Peculiarities of History

The first phase of Thailand's recorded history of external transactions began in the middle of the nineteenth century, roughly with the Bowring Treaty of 1855 between England and Thailand which opened Thailand to foreign trade. Figure 1 below illustrates that the kingdom's trade account (except for temporary distortions introduced by World War II) showed an ever more favorable balance for the entire century 1850-1950. This favorable trade balance was due to some peculiar

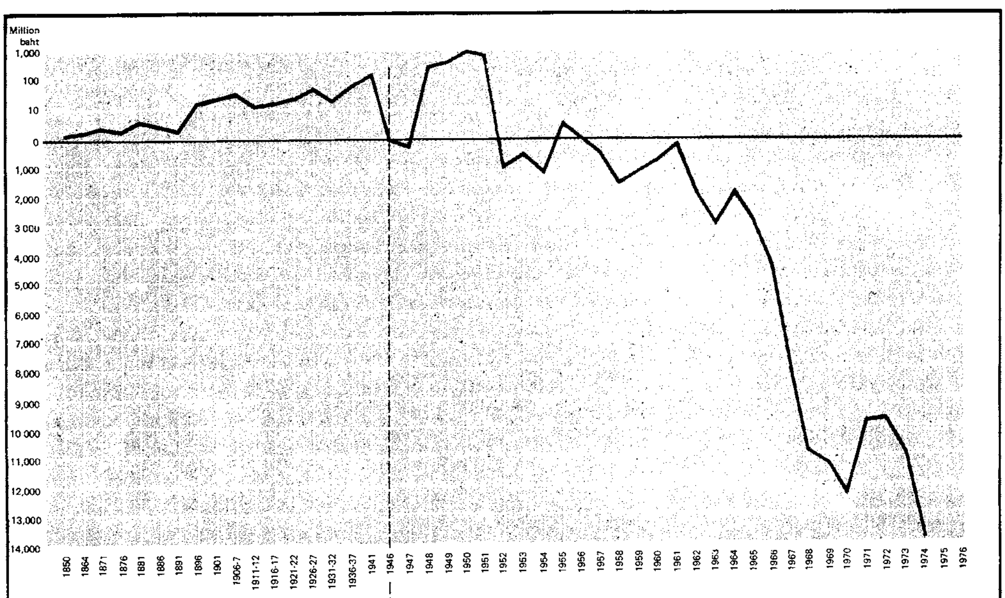


Figure 1: Thailand's Historical Balance of Trade Position (1850-1974)

accidents of history. A favorable resource endowment, principally of tin and teak, assisted on the export side. But much of the export income was from sales of rice. It is a strange fact that in the whole world there were (and are) few exporters of rice. Though the cereal is one of the major staples of mankind, even now less than 5% of world production is traded in international markets. Thailand, the US, and China dominate this world trade, with Thailand's share being about 15% in the 1969-1974 period. Before World War II Burma, Thailand, Indochina (i.e. South Vietnam) and the US were the dominant countries. Note that three of these four lay in peninsular Southeast Asia.

Table 1: Yield of Cleaned Rice in Pounds per Acre in Differing Degrees of Latitude, North and South of the Equator (1940's-50's)

Latitude 0 *to* 10°	*Latitude* 11 *to* 20°	*Lattiude* 21 *to* 30°	*Latitude over* 30°
ASIA:			
Malaya .. 1 100	Burma 850	India .. 700	Iraq .. 850
Ceylon .. 750	Indo-China 850	Pakistan 650	Korea .. 1,700
Indonesia 1,000	Thailand 750	China .. 1,600	Iran .. 950
	Philippines 600		Turkey 2,200
	Formosa 1,600		Japan .. 2,150
			Manchuria 1,200
EUROPE:			
			Italy .. 2,800
			Yugoslavia 1,200
			Bulgaria 1,500
			Spain .. 3,250
			France.. 1,500
			Greece.. 2,200
AFRICA & OCEANIA:			
Belgian Congo 600	French W. Africa 450	Egypt .. 2,300	Australia 3,250
Sierra Leone 700	Madagascar 850		
Tanganyika 500	Fiji .. 1,400		
NORTH & CENTRAL AMERICA:			
Costa Rica 750	British West Indies 1,750	Cuba .. 850	United States 1,650
Panama .. 750	Dominican Republic 850	Mexico 1,200	
	El Salvador 750		
	Honduras 750		
	Nicaragua 750		
	Guatamala 700		
SOUTH AMERICA:			
Columbia 700	Peru .. 2,250	Brazil .. 950	Chili .. 1,650
British Guiana 1,400		Paraguay 1,450	Uruguay 2,150
Surinam .. 2,550		Argentina 1,900	

Source: D. H. Grist, *Rice*, Third Edition. London, Longmans, 1959, Table 23

Note: The unusually high yields for a given latitude in South America are probably due to atypical soil conditions.

Thailand has never belonged to this select club of rice exporters because of phenomenal yields. As Table 1 reveals, around the World War II period, Thai yields were among the lowest for the latitude 11° to 20°. (Table 1 also shows that it is important to control for latitude in comparing yields, for rice is biologically a temperate crop. Its widespread culture in the tropics is due to another strange characteristic of Oryza: its ability to grow in flooded conditions.)

Thai yields are still among the lowest in the region, a fact about which we shall have more to say presently. Nevertheless, as Tables 2 and 3 show, the kingdom has managed to stay near the top of the world rice trade for many decades, despite the rise and fall of competitors. In fact, Table 3 shows something even more remarkable: Thailand is a major rice exporter despite having the lowest yields per hectare of all the major rice-exporting countries!

How is this possible? Part of the answer appeared more than two decades ago

Table 2: Pre-War and Post-War Sources of Rice Exports (thousands of metric tons)

Exporter	*Average* 1937–39	*Percentage of world total*	1958	*Percentage of world total*
Burma	2,966	38·3	1,410·2	22·0
Thailand	1,386	18·0	1,143·1	17·8
Indo-China	1,225	15·8	392·2	6·1
Formosa	638	8·2	179·3	2·7
Pakistan	279	3·6	1·7	—
U.S.A.	122	1·6	585·5	9·1
Italy	136	1·8	183·0	2·9
Egypt	101	1·3	360·1	5·6
Iran	54	0·7	1·3	—
British Guiana	15	0·2	18·0	0·3
Australia	13	0·2	44·4	0·7
Ecuador	10	0·1	27·5	0·4
Madagascar	8	0·1	58·2	0·9
Spain	—	—	97·0	1·6
China	9	0·1	1,213·2	18·9
Others	772	10·0	702·3	11·0
Total	7,734		6,417·0	

Source: D. H. Grist, *Rice*, Third Edition. London, Longmans, 1959, Table 25

in a journal article appropriately titled, "The Indochinese Peninsula: A Demographic Anomaly." Its author concluded that in the great river basins of peninsular Southeast Asia, namely the Irrawaddy, the Chao Phya, and the Mekong, population densities were abnormally low because political stability was so late in arriving. Hence a second historical accident: the ecological carrying capacity of the Chao Phya basin is much higher than its population, leaving room for an exportable rice surplus even with primitive technology.

But this is only half the story, for there need be no surplus at all if rice farmers grow only their subsistence requirements, or keep their surplus for themselves. A third historical accident is thus that ancient Siam had a closed political system under an absolute monarchy which permitted elites to extract a surplus

Table 3
Major Producers and Exporters of Rice in Recent Years

Country	Average Paddy Production 1968-1973 (million metric tons)	Average Rice Exports 1969-1974 (million metric tons)	Yield(metric tons paddy/ha)	Percent of Production Exported	Exports as Percent of World Trade
China	102.12	2.47	.32	3.7	27.5
USA	4.09	1.75	.48	65.7	19.4
Thailand	13.19	1.29	.19	15.0	15.2
Japan	16.47	.48	.60	4.5	5.3
Egypt	2.51	.47	.51	28.8	5.2
Pakistan	3.75	.43	.24	17.7	4.8
All other exporters		2.13	--	--	22.6

Total traded rice 9.02 million metric tons of total world production of approximately 200 million tons

Source: FAO *Production Yearbook* Note: Calculated at 65% conversion rate paddy to rice and send it abroad. While students of the subject (including myself) are still struggling to understand exactly how this took place, the fact remains that Thai elites were coherent enough on their own, and strong enough vis-a-vis the farmers, to bring this trick off. It need not always be so. As one economist has shown for Vietnam in the late 1940's and early 1950's, production stayed up but the Vietminh rebel movement was able to prevent the cities from collecting it and sending part abroad. Instead farmers consumed their surplus, invested it on their own account, or used it to support the rebellion.

In summary, then, there was a strong surplus on the trade account for a century, and a net inflow on capital account. These positive balances were more than adequate to cover deficits on services, dividends, and unrequited transfers abroad. What happened to the resulting surplus? Because of the silver standard in use until 1902, much of it went into the import of bullion which served to expand the domestic specie, both a currency and a store of wealth which could be (and was) exported when necessary. In the first decade of the twentieth century the system was altered to a gold-exchange standard, stabilizing the baht at a new rate to gold and greatly expanding the use of paper currency, issued against sterling balances held by the Treasury.

The extremely conservative nature of national finances during this period is illustrated by the 100% foreign exchange backing of the currency, and rising Treasury balances abroad. In effect, then, Thailand was a net lender to the rest of the world, which reinforces our point about the strength of Thai elites, who could instead have used these sums for the development of the countryside. There was no lack of proposals for development projects, but many economically justifiable ones were turned down due to the preference of the national leadership for holding official Thai wealth abroad as liquid balances rather than as domestically productive capital investments.

Sharp drop in reserves —Boonchu

The Shift to Domestic Development

Figure 1 also illustrates a second phase in Thailand's balance of payments history, from 1951 to 1965. During the immediate post-war years imports were artificially held down to restore the foreign exchange position eroded by the forced acceptance of now-worthless yen claims on Japan, and the freezing of Thai sterling balances in London. Through the use of multiple exchange rates and other strong policies, Thai reserves went in only five years from less than 10% of notes in circulation to about 100% by 1951, thus reverting to the extremely conservative pattern which had obtained during the previous century.

At this time a significant shift began to take place in the structure of exchange flows. After a strong surplus in 1951 due to war-induced peaks in rubber and tin prices, the trade account moved into a gradually increasing deficit, as the government increased expenditures on defense and domestic development. These deficits were covered by a continued inflow on capital account, and by an emerging surplus on services and unrequited transfers.

Thus for some fifteen years the kingdom was moving toward a pattern of foreign exchange flows much closer to that of a typical country with a percapita income of one hundred dollars or so a year: a balance of trade deficit, financed in part by capital inflows (loans and direct investment) which were a claim on future income to be generated out of the investments so financed. Of continued note during this period was the steady, predictable surplus of rice for export despite government policies like the rice export tax which strongly shifted the domestic terms of trade against the agricultural sector. In other words, Thailand's irrepressible farmers continued largely without complaint their earlier sturdy contribution to the kingdom's foreign exchange holdings.

Lightning Strikes Again: Another Historical Accident

This shift toward normalcy by world standards was aborted with the start of serious American military operations in nearby Vietnam. The economics of military technology are such that land-based air forces are much cheaper than sea-based forces, and the US urgently needed a secure land mass from which to attack Vietnam. It was willing to pay handsome rents, and it did. While there had been resource transfers to Thailand since the early 1950's as part of America's anti-communist containment plan in Asia, the numbers began to pick up significantly in 1962 with the beginning of base construction, and really took off in 1965 as military operations commenced from Thai territory. As Table 6, further on, reveals, in this environment foreign investment (after a lag of three years) picked up substantially too. Thailand was obviously "safe" under the US umbrella; there was plenty of foreign exchange to repatriate capital, dividends, interest and royalties; and the generals, partly for the reasons spelled out in my letter JEF-22, had the domestic situation firmly under control.

Figure 2 plots the special inflows received from the US because of the kingdom's favored geographic position in America's world plans. The years of sharpest rise were 1965-1968, with the flows peaking in the latter year at about $300 million, staying near $250 million through 1973, and dropping sharply thereafter.

Warning of 'severe' inflation

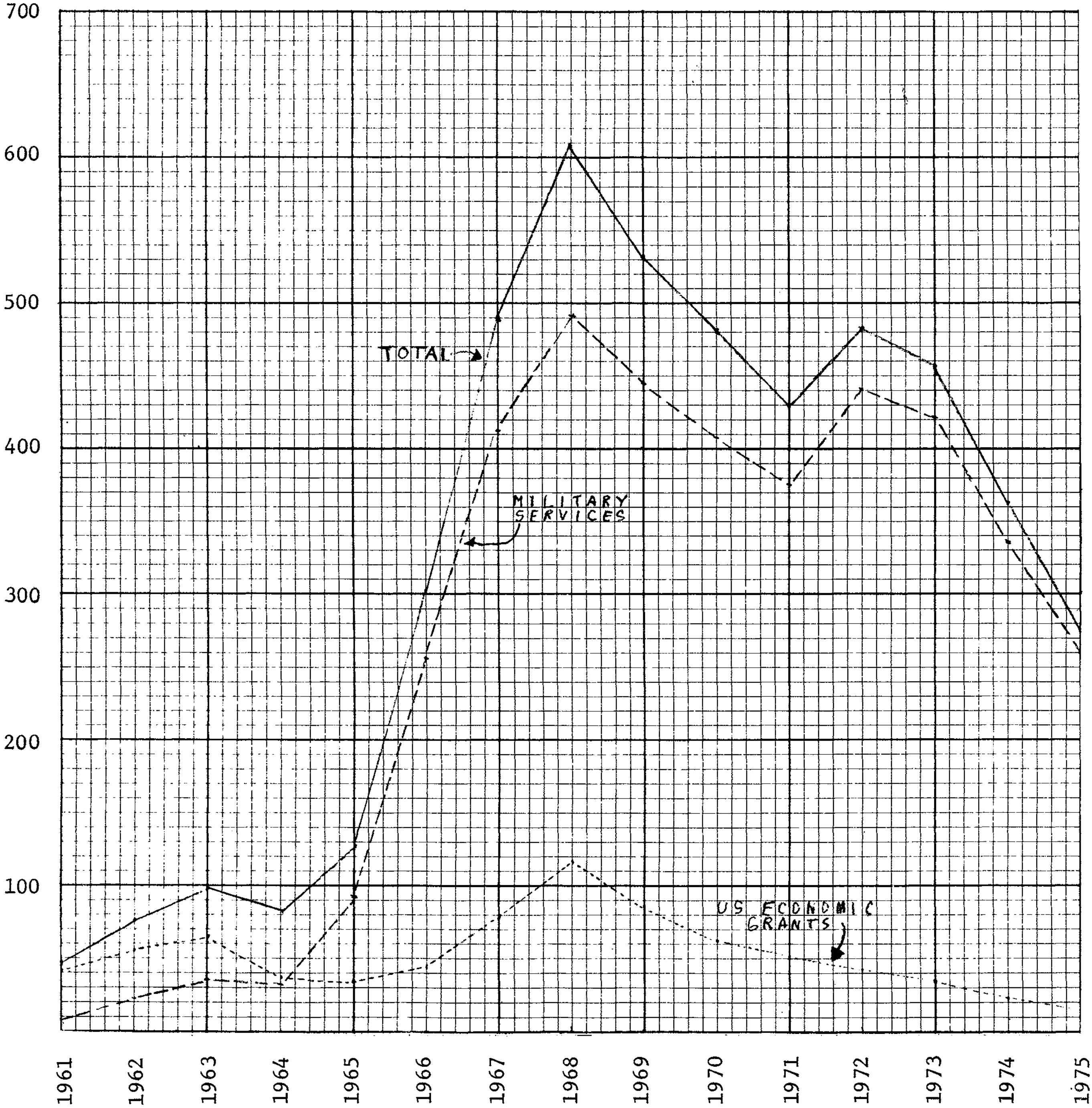
THE National Economic and Social Development Board (NESDB) yesterday warned of possible severe inflation in 1976 but predicted that income distribution and production would tend to improve from 1975.

The economic study group of the NESDB which made the analysis [illegible]d predictions [illegible]he country's [illegible]

According to Bank of Thailand estimates, about 10% of US military spending in Thailand went out of the country as imports directly required by the US itself. (Of course, much more foreign exchange was actually lost from imports induced by the higher domestic incomes, but we will get to that in a moment.) Thus of the 40 billion baht listed in the national accounts as "military service" income from 1961 to 1975, Thailand received a net inflow of foreign exchange of about $1.8 billion. Taking into account US economic grants as well, we can say that more than $2 billion was transferred to the kingdom in this way.

How was this foreign exchange utilized? Was it frittered away on high living? Some of it certainly was, but a surprising amount was invested. Even more surprising, this investment was not just by the Bangkok industrialist set, but by the lowly farmer too. And, these investments clearly show up in the kingdom's increased foreign earning capacity.

Figure 2: Special Inflows from the United States
(millions of baht)



Source: Compiled from Bank of Thailand *Monthly Bulletin* ฿100 million = $5 million

These conclusions are supported by Tables 4 and 5. Table 4 attempts to portray how much of the foreign exchange increment went into consumption and how much into investment, by showing how much of the total change in a given import category is accounted for by the change between 1965 and 1968, when inflows rose rapidly. The year 1972 is chosen since it is the last full year before the oil crisis distorted secular price comparisons; 1962 was an ordinary year a decade before. Assuming roughly constant growth patterns, we can say that any accounting category not affected by the inflow should show a ratio of 3 to 10, or .3. On the other hand those categories of imports sensitive to the inflow of dollars should show a figure higher than .3 during these years of rapid increase in incomes and foreign exchange holdings.

Table 4: Sensitivity of Imports to Foreign Exchange Inflow

Import Category	Imports (million baht) 1962	1965	1968	1972	Absolute Change 65-68	62-72	Ratio of Change 1965-68 to 1962-72
Consumer non-durable goods	2850	2920	3440	3290	520	440	1.20
Consumer durable goods	3670	4160	5320	5725	1160	2055	.56
Intermediate products and raw materials chiefly for consumer goods	1300	2120	3210	5880	1090	4580	.24
Intermediate products and raw materials chiefly for capital goods	660	1080	1880	3250	800	2590	.31
Capital goods	3250	4775	8340	9780	3565	3560	.54
Note: The items showing the largest changes in this category were: fertilizer and pesticides (.41); tractors (1.0); machinery (.51); and scientific equipment (.53).							
Vehicles & parts	1020	1450	2770	2210	1320	1190	1.10
Fuel & lubricants	1220	1350	2000	3120	650	1900	.34

Source: Compiled from Bank of Thailand *Monthly Bulletin*

Note: Does not include bullion, "miscellaneous" or military imports

Perhaps predictably, the most sensitive category was consumer non-durable goods, with a sensitivity ratio of 1.2. However, the absolute increase was not large, and in fact this category dropped from two-fifths of imports to one-fifth by 1972. The next most sensitive item was vehicles and parts, including passenger cars, trucks and buses, and predominantly the latter two. The sensitivity ratio of 1.1, and the absolute increment of 1.3 billion baht, indicates a substantial investment in transport capability. Consumer durables show a ratio of .56 on an absolute increment of 1.19 billion baht. The major item, however, is capital goods imports, with an index of .54 and an absolute increment of 3.565 billion baht.

Table 5 shows that the heavy investment during these years showed up strongly both in the agricultural and the industrial sectors. Agricultural exports showed the biggest absolute increase during the decade 1962-1972, while industrial exports showed the biggest percentage increase, starting from a smaller baseline amount. The actual impact on industrial development during these years is in fact understated, since the development strategy at that time was import substitution, rather than export promotion. The result was a shift in the composition of imports, though there was also an increase in exports. As the strategy altered to one of export promotion, the industrial export earnings figure rose dramatically after 1972.

Table 5: Growth of Exports 1962-1972

Classification (see note below)	Exports (billions of baht) 1962	1972	Factor of Increase
Constants	6.86	7.33	1.07
Mining	.72	2.57	3.57
Agriculture, marine, forestry	1.68	7.18	4.26
Industrial	.07	.72	10.03
Processed agricultural	---	.28	n/a
Other	.75	4.13	5.50

Source: Compiled from Bank of Thailand *Monthly Bulletin*

Note: These categories do not use the aggregate classifications employed by the Bank of Thailand but were computed, I feel more usefully, as follows: Constants: rice, rubber, teak, cattle, eggs, hides and skins, feathers, castor seed, kapok seed, ground nuts, sesame, seedlac and sticklac, tamarind, salt, kapok fiber, yang wood, vegetable cake. Mining: tin, fluorite, tungsten, antimony, other slag, precious stones. Agriculture, marine, forestry: maize, tapioca, jute and kenaf, shrimp, tobacco leaves, sugar, mung bean, sorghum, cotton seed, soybean, cotton, molasses. Industrial: cement, petroleum products, gunny bags. Other: a residual category employed in the Bank's reports, consisting of items too small to report individually, and not otherwise described.

Overall, then, more than half the increment to external flows from the historical accident of the Vietnam War went into productive investment and into a buildup of liquid foreign reserves, following the traditional preference of Thai financial elites for holding large official balances of foreign currency. As is apparent from the bottom half of Table 6, the bizarre result of this preference is that if the kingdom had gone into liquidation at any time during the past decade, except for a few months in 1971, foreign reserves would have been more than adequate to cover all outstanding debt, public and private, short term and long term. Consequently, with a per capita income of some $250 per year (1973), Thailand continued to be a net lender to the rich countries of the world, just as it always had been.

Table 6: Balance of Payments and

Balance of Payments (millions of baht)	1962	1963	1964	1965
Balance of trade	-1962.6	-3117.0	-1960.6	-2556.3
Services	508.4	686.2	732.6	1443.8
(of which military)	(204.6)	(361.1)	(438.7)	(922.1)
Unrequited transfers	910.9	1138.2	775.1	796.4
Capital movements	1495.8	1645.0	1643.6	1665.3
(of which direct investment)	(156.0)	(346.8)	(374.2)	(870.3)
Allocation of SDR	---	---	---	---
Errors and omissions	342.4	596.3	239.6	635.8
Overall balance	1294.4	948.7	1430.3	1985.0
External Assets and Liabilities (millions of dollars)				
Total foreign reserves	494.9	540.5	609.6	705.0
Total foreign liabilities	na	na	na	403.0
Private sector	na	na	na	150.0
Public sector	na	na	na	253.0

Source: Bank of Thailand

Conclusion: The Patterns of the Past

Five factors stand out in Thai history as responsible for the kingdom's unusual balance of payments situation.

1. A natural resource endowment. To some extent the inflows from abroad have arisen from nature's gifts, principally of tin and teak.

2. The kingdom's irrepressible agriculturists. Year after year, Thai rice farmers have produced an exportable surplus. After a long period of stagnation, yields began an unspectacular increase about 1961. Nevertheless much of the increment to output in the past came from increases in cultivated area. While the output increases have never been remarkable in themselves, they are spectacular in view of the government's long history of anti-agriculture policies, ranging from the rice export tax to the fertilizer import monopoly (not to mention sheer neglect). Despite being ripped off by the government and the urban worker, the rice farmer has kept on doing his thing, acquiescing quietly in having his surplus taken away from him. But that he is capable of doing better and knows how to is also apparent from the truly spectacular growth in production of export crops which haven't been subject to price controls: maize, soybeans, kenaf, sugar and tapioca.

3. A peculiar demographic situation. The historical accident of underpopulation

External Assets and Liabilities

1966	1967	1968	1969	1970	1971	1972	1973	1974	1975[e]
-4479.4	-8150.2	-10640.0	-11297.7	-12244.8	-9935.0	-8884.6	-10802.4	-13856.2	-18395.0
4105.9	5913.1	6148.5	5954.4	6036.2	5404.1	6583.1	6836.4	8087.7	5815.0
(2589.1)	(4109.2)	(4917.8)	(4445.7)	(4192.1)	(3788.7)	(4413.2)	(4210.3)	(3443.4)	(2600.0)
969.9	1198.2	1547.5	1187.2	1011.7	904.1	1238.8	2968.8	5499.9	3310.0
1518.8	2250.1	2444.0	2897.6	2462.7	1736.2	3643.2	2282.5	6708.2	5045.0
(570.6)	(894.4)	(1239.7)	(1057.5)	(890.5)	(808.4)	(1427.1)	(1604.9)	(2766.3)	(1720.0)
---	---	---	---	---	298.2	320.7	---	---	---
1195.2	101.8	959.1	344.7	82.2	1257.2	1090.2	-421.1	1572.2	1431.0
3304.4	1313.0	449.1	-913.8	-2652.0	-335.2	3991.4	864.2	8012.0	-2794.0
863.8	916.4	938.0	894.0	766.5	777.0	968.8	1082.0	1564.0	1372.0
438.1	509.2	572.4	664.3	754.9	796.8	914.2	910.9	1177.5	1365.1
170.2	229.4	273.4	342.9	406.9	428.8	507.7	451.8	649.2	728.3
267.9	279.8	299.0	321.4	348.0	368.0	407.2	459.1	528.3	636.8

e = estimated   na = not available

(due apparently to unsettled political conditions a millenium or more ago) has meant that the kingdom can have an exportable rice surplus despite appallingly low yields.

4. <u>A strategic geographic location</u>. By another accident of history, the kingdom's location near Vietnam permitted it to earn roughly two billion dollars from the export of anti-communism.

5. <u>The tight control by political elites</u>. Thailand's government until 1973 was one of the political mysteries of Asia. While it was an autocracy, it was hardly an oppressive one; and while Bangkok elites clearly exploited their country cousins, the latter hardly complained. It was the smiling complaisance of the Thai which permitted the whole system to continue. The result of this unusual state of affairs was that the kingdom's elites maintained their dominance against competing domestic groups, particularly the farmers, which clearly showed up in the balance of payments and external reserves. For example, having (for more than a century) a foreign reserve equal to 100% of the money supply was unusual for a Third World country, and highly appealing to foreign investors and creditors and their domestic partners, but it had real costs for the rural Thai.

This is because the alternative use of these resources, for domestic development, would have had a much higher rate of return than the 3.5% to 7% in fact achieved by leaving part of the reserves in gold and part to draw interest in Western capital markets. Consider, for example, the effect of converting one-half of the kingdom's one billion dollars in reserves at the end of 1973 into domestically productive assets. At that time reserves were drawing about 7% abroad. We can use a conservative rule-of-thumb figure of 15% as the payback rate for investment in agricultural facilities. (Thailand has one of the poorest irrigation infrastructures in the region.) There would thus have been an increment of at least 8% of $500 million, or $40 million per year, to national income. But more importantly, there would have been an increment of $75 million per year to the rice farmers who benefitted. Alternatively, if the investible increment of reserves had been put into an expansion of primary education facilities, where rates of return are estimated to be about 25%, the increment to national income would have been $90 million. Viewed from a distributive angle instead, there would have been an increment of $125 million per year flowing to the poorest segment of the population rather than the Bank of Thailand. It is obvious from these figures which groups historically have not had much influence in the management of foreign reserves.

If these are the special historical factors in Thailand's heretofore healthy foreign reserve position, what were they not? It seems fair to say that industrial discipline and a compulsive attitude toward work were not responsible. Thai have traditionally resisted with great stubbornness a move into trades and into factories, so much so that kings in past reigns had to import millions of Chinese laborers because of this obsession of Thai to remain in the agricultural sector where, it is only proper to note, they have distinguished themselves with the resources available.

The purpose of this observation is not to make an invidious comparison, only to spur an appreciation of the genuine strengths and weaknesses of the kingdom. Thai are not Japanese, with their compulsive and disciplined work habits and their phenomenal savings rates, and they have no intention of becoming Japanese, which is one of the reasons for increasing Thai-Japanese domestic conflict in recent years, as Japanese investors, managers and supervisors have become more prominent in the economy. Thus a development strategy which emphasizes the kingdom's comparative advantage in agriculture, and the preference of its people for life in this sector, capitalizes on a native strength, while on the contrary one which attempts to pit unwilling Thai against the factory workers of Hong Kong, Tokyo, Taiwan, or Singapore is swimming against a rather brisk historical current.

A second apposite observation is that Thailand's impressive foreign reserve position and her equally impressive growth rate in recent years have not been particularly due to the wisdom of those guiding her economic path, but rather to their prudence in handling assets which came their way for reasons largely beyond their control and, in some cases, perhaps beyond their understanding. We might draw a contrast with Singapore in the last ten years, or Japan in the last hundred. Both are island nations without natural resources to speak of. And yet, what they have achieved by careful planning, sound management, and disciplined use of their natural strengths, is remarkable. Thai leaders have never achieved such feats, for the simple reason that they have never had to --- yet.

And the Patterns of the Future?

What are the prospects for each of these five special historical factors?

The first, a natural resource endowment, shows promise in the aggregate only of improving as new discoveries are made of oil and gas offshore, of potash in the Northeast, of zinc in the North, and of new technologies for exploiting the long-known tin resources of the South.

The second, the vigor with which Thai farmers ply their profession, similarly shows no sign of abating, as production continues to increase in all major commodities, even the rice sector.

However the third, fourth, and fifth are each changing in the opposite direction.

The third, historic underpopulation, is now ending, symbolized by the exhaustion of new cultivable land. Henceforth exportable rice surpluses must come from intensification and increased yields, not extensification and bringing new land (forests!) under the plow. In fact, the imperative for new rice technology is even more demanding, for economists and political scientists have shown from studies of Vietnam that the closing of the land frontier in 1930 in the Mekong Delta, the continuation of static rice technology, and population growth, was the explosive combination which led to the successful peasant rebellion later known as the Vietnam War.

If the third factor has slowly come to an end over the last several years, the fourth factor suddenly terminated on April 30, 1975. Until that date Thailand was selling anti-communism into a monopsonistic market, but now that the only buyer has lost interest, the kingdom's strategic location has lost its economic value. Thailand can no longer expect 200 million dollars a year in base rents, and in fact these flows will largely cease in 1976.

Finally, the monopoly on politics by a tightly-knit group in Bangkok has been irreversibly broken by the revolution of October 1973. One of the consequences of this development is that farmers have spoken out, demanding an end to the exploitation they have suffered for a century or more, and which was in part responsible for the healthy exports of rice. This shift in the political relationship of Bangkok to the farmers was symbolized by the first-ever farmers' demonstration in the capital in March 1974, and by continued agitation since for institutional reforms in the rural sector. No longer are Thai farmers going to be content to do their duty for rewards meager in this life and doubtful in the next.

Consequently there will have to be an adjustment, but from a very abnormal baseline toward a new position more closely approximating that of similarly endowed countries elsewhere in the world. The long-term shifts just now making themselves felt will force political and economic leaders to make overdue domestic reforms which will have a significant payoff but for which there has previously been little impetus. In this perspective, then, the current alarm is not warranted, but what is warranted is a serious consideration of the historical roots of Thailand's special balance of payments situation, and a new strategy to build on the remaining strengths and to compensate for new weaknesses. The underlying basis of the economy is still as strong as it was historically, though due to the oil crisis not

Table 7 Terms of Trade (1958 = 100)	
1957	94.4
1958	100.0
1959	107.3
1960	108.7
1961	104.3
1962	109.2
1963	108.6
1964	109.3
1965	110.1
1966	115.9
1967	115.7
1968	121.4
1969	128.3
1970	112.5
1971	102.2
1972	101.5
1973	136.5^{e}
1974	113.8^{e}
1975	103.7^{e}

Source: Bank of Thailand

e = estimated

as strong as it has been earlier in the preceding decade. As Table 7 shows, the most recent terms of trade are still higher than those of the late 1950's, during which time the kingdom was nevertheless able to maintain heavy foreign reserves. More recently, in mid-1975, foreign reserves equalled 100% of the domestic money supply -- notes and demand deposits.

Short Term Prospects

The immediate prospect is for a continued serious trade deficit. During earlier periods in Thai history, imports fell automatically with a fall in exports due to the tight linkage to the international economy provided by the silver and gold-exchange standards. This automatic mechanism has been greatly weakened by the international financial system which has grown up since World War II, and, domestically, by the growth of the banking system and accompanying credit availability. Furthermore for domestic political reasons the present budget is highly inflationary (a 12 billion baht deficit) and this will increase imports rather than decrease them as the reduced foreign exchange availability would dictate.

One possibility now being discussed in Bangkok, particularly in view of the recent strong appreciation of the US dollar to which the baht is tied, is a devaluation of the currency, possibly back to the old rate of 20.825 to the dollar which applied until the July 15, 1973 revaluation.

Furthermore, since reserves probably will not be permitted to drop below $1 billion, the prospect is for greatly increased borrowing abroad, and commercial borrowing at that. This unprecedented development has been viewed with some alarm in local business circles. While it is a historic departure from Thai practice of financing development out of grants and current income, it is nevertheless borrowing to increase domestic productivity and foreign earning capacity, not to finance current consumption as in some countries. Businessmen ought to be the first to realize that it is good practice to borrow at fixed rates against a set of technologies whose rate of return is higher than the borrowing rate.

The Long Term

The most important implication of the change in three of the historic factors in the kingdom's happy foreign exchange position is that Thai leaders are going to have to work harder and do better managing the economy, a point which the most recent World Bank country report makes in its own way. There should be no problem of bureaucratic capacity here, for observers agree that professionalism in this sphere has been increasing ever since the early 1950's. Furthermore, the country's leaders meet this challenge with more than a billion dollars in reserves, saved up (irrationally, perhaps) over the past century. Finally, the fact that the agricultural sector has been able to do so well, for so long, with such abysmally low yields and such contrary policies, argues that there are few practical limits to what could be done if the country's leaders set their minds to modernizing agriculture. The last decade's performance in the industrial sector has also been impressive, though there are limitations here, which the country's leaders would be well advised to heed, in terms of the stability of international markets, the receptivity of Thai to a factory life, and the much higher capital intensities required for employment creation in the industrial as compared to the agricultural sector.

However an important question at this point is whether the elections now scheduled for April 4 will permit formation of a government that can make the hard but necessary decisions on resource allocations. Some critics assert that the kingdom has been marking time during the past two years, allegedly proving that Thailand cannot "afford democracy." As readers of my JEF-22 already know, I take the contrary view that many necessary and important measures have been adopted during the past two years, most significant among them being the opening up of the political system itself. Such critics may yet be vindicated, though, if the present 50-party system fails to resolve itself into something more reasonable. If foreign investment fails to pick up due to continued domestic instability, and possibly to a perceived foreign threat as well, there will be adverse employment consequences down the line. Yet, the Philippines and Indonesia show that a country can live (though not happily) with desperately high levels of unemployment and with declining real wages.

A second major long-term implication is that henceforth Thailand's "balance sheet" as portrayed in the bottom half of Table 6 will look much different from that of the past. This is a consequence of the political changes of 1973, as a result of which the kingdom's poor (which is to say, largely its rural people) will no longer permit reserves they helped to earn to sit in the Bank of Thailand's accounts with the Bank of England, the Federal Reserve Bank of New York, and the international capital markets. This will require borrowing a great deal of money, and hence 1975 will probably have been the last year in which foreign reserves equal or exceed total external borrowing of all types and maturities.

From a narrow bookkeeping viewpoint, then, the kingdom's creditworthiness will decline. From a broader point of view, however, it means that future commitments will be covered not by cash in the bank now, but by the future income streams generated by those commitments. This is probably the only realistic viewpoint, for the whole meaning of development in the modern world is converting treasure into productive assets. It has taken a domestic revolution finally to convince the kingdom's leaders to do just that.

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Later this year Jeffrey Race will be completing his fellowship with the Institute. He plans to remain in Asia for a period of time before returning to the U.S., working further on the subjects explored in his Newsletters: regional political, military and economic developments; evaluation of new agricultural and industrial technologies; development, improvement, and effective management of institutions. Dr. Race is now considering employment opportunities in these or related areas, either in the U.S. or in Asia. He can be reached at 20 Chester Street, Somerville, Mass. until June 1; thereafter at PO Box 2, Rangsit, Thailand.

R.H. Nolte
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535 Fifth Avenue, New York, N.Y. 10017