file

Central Intelligence Agency

Washington, D.C. 20505

DIRECTORATE OF INTELLIGENCE

11 March 1986

Thailand's Foreign Debt Management: Frictions for US-Thai Relations? [redacted] 25X1

Summary

We believe Thailand can avoid a formal rescheduling of its $18.5 billion foreign debt over the next two to three years through a combination of continued budget austerity and refinancing of some of its short-term liabilities. If such measures are carried out, we expect the debt service ratio to rise only modestly from the record 35 percent registered in 1985 before beginning a gradual decline by the end of the decade. Nonetheless, the pressures on Prime Minister Prem's government will intensify as austerity continued export difficulties slow economic growth. [redacted] 25X1

As Bangkok struggles to curb its foreign borrowing and boost exports, we believe more friction is likely in US-Thai relations. Bangkok probably will urge Washington to keep US imports of Thai products high and to avoid competing in Thailand's traditional markets abroad. The US farm bill, in particular, probably will be a bone of contention in the coming year. Continued economic difficulties, moreover, could affect other areas

---

This memorandum was prepared by [redacted] Office of East Asian Analysis. 25X1
Information available as of 11 March 1986 was used in its preparation. Comments and queries are welcome and may be directed to the Chief, Indochina, Thailand, Malaysia Branch, Southeast Asia Division, OEA, [redacted] 25X1 25X1

EA M 86-20027

[redacted] [redacted] 25X1

Page Denied

Sanitized Copy Approved for Release 2011/03/24 : CIA-RDP86T01017R000605780001-4

[redacted] 25X1

of the bilateral relationship, such as cooperation on security or refugee matters. [redacted] 25X1

Debt Management Difficulties

Although international financial analysts believe that Thailand's foreign debt remains moderate compared with that of many LDCs, the Prem government over the past two years has become increasingly worried that the country's debt service payments (principal and interest) are growing substantially faster than its capacity to meet them. These payments have grown from about $2 billion annually in the early 1980s to $3.2 billion in 1985, when they represented 35 percent of export earnings for goods and services--up sharply from the 1980 debt service ratio.[1] In the same period, Thailand's foreign debt has grown an average of 18 percent per year, rising from $9.7 billion in 1980 to $18.5 billion last year.[2] [redacted] 25X1

An export slowdown has made Thailand's debt service more of a burden. Export growth has declined from 20 to 25 percent annually during the 1970s, to an average of 2.5 percent per year since 1980, as higher oil prices, depressed international commodities markets, and growing protectionism have combined to weaken import demand in Thailand's overseas markets. These factors also have caused the country terms of trade[3] to decline by over a fifth since 1980, compounding the strain on its balance of payments. At the same time, moreover, the domestic savings rate has declined as consumption has outstripped income growth, and foreign loans have been used increasingly to finance current consumption rather than for investment. (See appendix and table 2 for further information on Thailand's foreign debt and balance of payments.) [redacted] 25X1

---

[1] The debt service ratio is the ratio of principal and interest due on a country's foreign debt in a given year to exports of goods and services for that year. Short-term principal repayments are excluded. [redacted] 25X1

[2] Thailand in 1984 ranked 14th among the world's top LDC debtors, with its foreign debt substantially below that of the other ASEAN nations. In terms of its debt service ratio, however--32 percent in 1984--it ranked second to the Philippines' 49 percent and well above Indonesia, South Korea, and Malaysia, which had debt service ratios of 24, 21, and 12 percent, respectively. Nonetheless, Thailand's debt service ratio remains far lower than the 60-percent level of the Philippines when that country's debt crisis began to unfold in 1983. [redacted] 25X1

[3] A country's terms of trade is the ratio of an index of its export prices to an index of its import prices. The concept is a measure of the relative purchasing power of the country's exports. [redacted] 25X1

[redacted] 25X1

Sanitized Copy Approved for Release 2011/03/24 : CIA-RDP86T01017R000605780001-4

[redacted] 25X1

Bangkok Reacts

Concerned that continued growth of the debt service ratio could jeopardize Thailand's good international credit rating--and its long-term economic prospects--Prime Minister Prem's government as early as 1984 began taking steps to curb external borrowing and to improve the balance of payments. Bangkok cut public-sector foreign borrowing--which accounts for about half of total foreign debt--from $2-3 billion per year in the early 1980s to about $1.6 billion in 1985, and recently lowered its 1986 borrowing ceiling to $1 billion. In late 1984 it devalued and floated its currency, launched an export drive, and stepped up basic economic reforms--such as tighter regulation of the financial sector--to boost domestic savings and investment. In addition, Bangkok last year undertook a five-year, $1.9 billion, debt-refinancing plan[4] to lower interest costs and avoid a bunching of repayments over the next two years. Although the refinancing plan--which covers 10 percent of total foreign debt at the end of 1985--initially was limited to public enterprise debt, it now includes government debt as well. [redacted] 25X1

Prime Minister Prem, in our view, probably will face intense pressure as debt management considerations continue to limit the government's range of economic policy options, leaving him with few choices but continued austerity. There is little that Bangkok can do to boost exports in the current world trade environment--although it undoubtedly will fight to protect Thai exports from further cuts because of import barriers in overseas markets. [redacted] 25X1

As a result, we expect Prem to stick with his unpopular austerity program for the near term, even if a recent reshuffle of some of his cabinet ministers fails to soothe public discontent over his government's economic policies or to quiet squabbling within his coalition. We believe Finance Minister Sommai--the architect of Bangkok's austerity program--is unlikely to be ousted because he retains the support of Prem and the palace, and is an apolitical appointee. Even if Prem replaced him, moreover, [redacted] 25X1
[redacted] Prem's other economic advisers advocate similar policies. If 25X1
anything, they will probably urge the government to adopt additional belt-tightening measures over the next two to three years--a course they would be supported in by the IMF, according to the US Embassy. [redacted] 25X1

In addition, Bangkok will probably try to find other methods of raising revenue. For example, the cabinet recently approved a hotly debated tax-restructuring program that is intended to boost government receipts by increasing taxes on interest income, diesel fuel, and registration of certain vehicles. We believe that Bangkok may also launch a new offensive to promote foreign investment and tourism. [redacted] 25X1

In our opinion, the Prem government will consider additional politically controversial reforms to reduce Thailand's need to borrow abroad and to boost export earnings. These may include measures to reduce the budget deficit--for example, by

---

[4] Bangkok last year refinanced $300 million with the help of an IMF standby arrangement. The government plans to restructure an additional $700 million this year, and $300 million per year from 1987-89. [redacted] 25X1

[redacted] 25X1

[redacted] 25X1

cutting subsidies to the state enterprise sector, broadening the tax base, and improving tax collection--making local capital markets more efficient, and improving agricultural productivity.[5] If fully implemented, we believe these measures--advocated by the World Bank--probably would help to prevent a recurrence of Thailand's debt management difficulties. However, progress probably will be slow because of stiff opposition from influential interest groups. For example, efforts to privatize some state enterprises--such as the Communications Authority of Thailand--have stalled because Bangkok is reluctant to provoke powerful unions--or the military officers who sit on boards of directors. [redacted] 25X1

The Political Spillover

As Prem and the technocrats try to push ahead with financial austerity, we believe the opposition Thai Nation Party (TNP)--and Prem's chief political rival, General Arthit--probably will increase their pressure on the government. This would add to the strain on Prem's coalition, which is fraying as a result of intense bickering within the Social Action Party--the coalition's largest faction--over the party's responsibilities for executing unpopular economic measures. [redacted] 25X1 With limited budget resources for agricultural price support programs, however, we believe there is little that Prem or his government can do in the short run to ease the farmers' plight [redacted] 25X1

We believe that Bangkok's initiatives to curb military spending could lead to more frictions between the military and civilians. [redacted] 25X1 [redacted] 25X1 technocrats who are calling for cuts in military spending, especially for items requiring foreign exchange outlays. As a result, we believe the $300 million purchase of 12 US-made F-16s will once again to become a matter of public debate as the government looks for additional ways to alleviate its debt service burden. If Arthit maintains his opposition to delaying or scrapping delivery of the planes, the issue also could deepen splits within the military and lead to more political turmoil. [redacted] 25X1

---

[5] Reducing the budget deficit--$1.9 billion last year--could lead to a drop in private as well as government borrowing abroad if fewer private-sector borrowers were "crowded out" of domestic capital markets. A reduction in real interest rates--among the highest in the world--also would decrease the incentive among many Thai borrowers to seek cheaper loans abroad. [redacted] 25X1

[redacted] 25X1

[redacted] 25X1

Sanitized Copy Approved for Release 2011/03/24 : CIA-RDP86T01017R000605780001-4

[redacted] 25X1

Our Baseline Estimate

If Prem remains in office through the end of his term in 1987, we believe his government's economic policies--especially the austerity budget and more realistic exchange rate policy--together with the refinancing plan will allow Thailand to avoid a formal rescheduling of its foreign debt during the next two to three years. The country's foreign exchange reserves of $1.9 billion at the end of 1985[7] --about 2 month's import coverage--are comfortable, and it retains access to foreign credit on favorable terms [redacted] 25X1

Unless there is a major export setback because of a severe global recession or an upsurge in protectionism in Thailand's major overseas markets, we believe the debt service ratio will probably rise no more than 3 or 4 percentage points--to 38 or 39 percent--before beginning a gradual decline by the end of the decade. We estimate that foreign debt service payments will grow at only 6 percent per year through the late 1980s--about half the annual rate of increase during the first half of the decade--based on our assumption of new public sector foreign borrowing of about $1 billion annually, a slight contraction of private sector foreign debt, and export growth averaging at least 4 percent per year. [redacted] 25X1

If we are wrong, we believe that the most likely cause would be if Prem is turned out of office and his successor abandons the current government's conservative financial management. A less likely cause, in our opinion, would be either a marked softening of the austerity program if the Prem government gives into demands from interest groups in business or the military to ease up, or an abrupt withdrawal of Thailand's commercial lines of credit if, for example, a series of violent coup attempts made foreign bankers cautious. [redacted] 25X1

In our judgment, Prem and his economic team can probably stay the course until 1987, despite their troubles. However, we believe Prem's chances of remaining in office over the next 12 months will erode unless he takes some action to shore up his political position. Although he has done little to this end since last September's coup attempt, we believe his options consist of:

- Calling for early parliamentary elections--which do not have to be held until 1987-- to renew his mandate from the legislature.

- Making further cosmetic changes in the cabinet to defuse criticism of his economic ministers.

[redacted] 25X1

---

[7] This figure represents gross official reserves. Net reserves are substantially lower. For example, net official reserves (official reserves less IMF drawings) plus net unofficial reserves (net commercial bank assets) amounted to about $800 million at the end of 1985. [redacted] 25X1

[redacted] 25X1

[redacted] 25X1

Although we expect Prem to stick with his current policies, the pressures to back off from austerity seem certain to become more intense as Bangkok's debt management measures combine with weak export markets to rein in the domestic economy. We believe the government's austerity policies probably will restrain growth to about 3.5 percent this year--almost 50 percent below the average annual growth rates of the last decade--with only a marginal improvement in 1986 and 1987 if international commodities prices remain weak. The slow growth in store this year represents a further decline from 1985's growth rate of 4 percent--already the lowest in 20 years. Moreover, with annual population growth of about 1.8 percent, per capita incomes will expand even more slowly. [redacted] 25X1

Implications for US-Thai Relations

We are certain, in any case, that the bilateral relationship will face a bumpier road as Bangkok struggles to curb its foreign borrowing and improve the balance of payments. We believe Bangkok probably will ask Washington for increased security assistance to partly compensate for its own budget austerity. It also is likely to request better financial terms on the F-16 deal, and already has begun sounding out US officials, according to the Embassy. In addition, Bangkok is certain to press Washington to keep US markets open to Thai products. [redacted] 25X1

We believe the recently enacted US farm bill, in particular, will be a bone of contention in the coming year. According to the US Embassy, the Thai are concerned about the prospect that their foreign exchange earnings from agricultural exports such as rice--Thailand's leading merchandise export--will suffer if US grain exporters take advantage of the bill's export promotion provisions to increase sales in Thailand's traditional overseas markets. We believe such a setback to Thai exports would aggravate Bangkok's debt management problems and probably would leave Prem with little choice but to bow to demands from farmers, exporters, and members of his cabinet to retaliate against imports of US agricultural products such as soybeans and cotton. [redacted] 25X1

In the worst circumstances we can imagine, continued economic difficulties could lead to more political turmoil and open the way for a less pro-US leadership in Bangkok, especially if the Thai perceive US trade restrictions as a significant cause of their current problems. In that case, Bangkok might become less cooperative on narcotics or refugee matters, or seek to lessen its dependence on the bilateral security relationship. Moreover, a rescheduling could pose substantial hardships for US banks which have extended credit to Thailand. [redacted] 25X1

[redacted] 25X1

Sanitized Copy Approved for Release 2011/03/24 : CIA-RDP86T01017R000605780001-4

[redacted] 25X1

Appendix A

Estimating Thailand's Foreign Debt

Estimates of Thailand's external debt by international financial analysts at the end of 1985 ranged from $15.7 to $18.5 billion. The difference, we believe, is largely a function of poor data on private sector debt. Based on these figures, the debt service ratio ranges from 28 to 35 percent. We have used the higher figures [redacted] 25X1 because we believe that Thailand's private sector debt is generally underreported. [redacted] 25X1

Table 1: Thailand's Foreign Debt
Yearend 1985
(Estimated, US $ billion)

Total Debt	$18.5 b
By source:	
Official	8.8
Short term	0.9
Medium & long term	7.8
Private	9.7
Short term	3.6
Medium & long term	6.1

[redacted] 25X1

[redacted] 25X1

25X1

Table 2: Balance of Payments Summary
(Million US $)

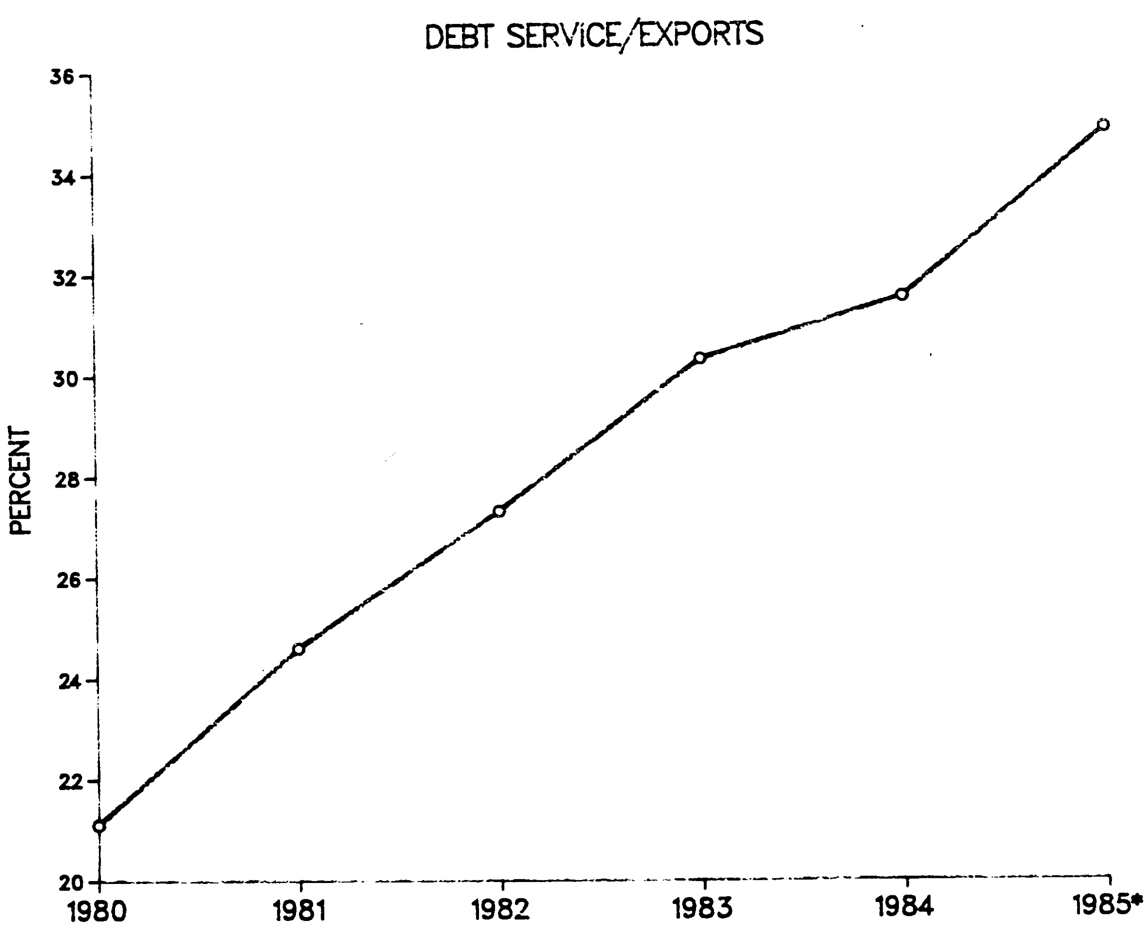
	1980	1981	1982	1983	1984	1985*
CURRENT ACCOUNT	-2070	-2569	-1006	-2874	-2108	-1700
Merchandise trade	-1903	-3022	-1571	-4092	-2862	-2700
Exports, f.o.b.	6449	6902	6835	6308	7338	6900
Imports, c.i.f.	-8352	-9924	-8406	-10,400	-10,200	-9600
Services & transfers (net)	-167	453	565	1218	754	1000
Of which: Interest payments	-964	-1471	-1563	-1475	-1769	-1760
Capital account	2044	2479	1443	2126	2562	1600
Of which: Direct investment	187	288	188	348	406	325
Errors and omissions	-180	133	-521	587	62	620
Overall balance	-206	43	-84	-161	516	520

*1985 figures are estimated.

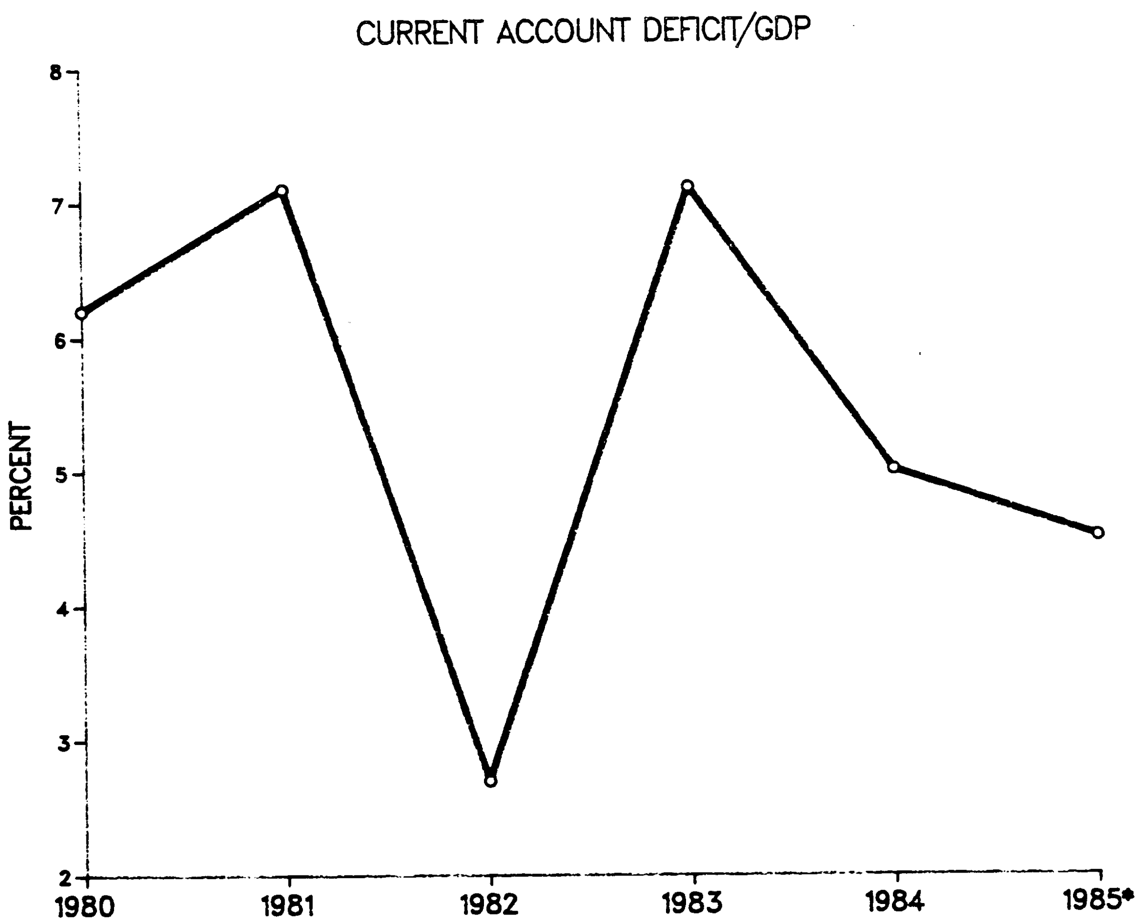
25X1

25X1

Selected Measures of Thailand's Foreign Debt



25X1



* 1985 FIGURES ARE ESTIMATED

25X1

[redacted] 25X1

SUBJECT: Thailand's Foreign Debt Management: Frictions for US-Thai Relations? [redacted] 25X1

Distribution:
Original - OEA/SEA/ITM
1 - Richard Childress, NSC
1 - Byron Jackson, Commerce
1 - Linda Droker, Commerce
1 - Charles Salmon, State
1 - Janet Malkemas, State
1 - Cora Foley, State
1 - Alan Kitchens, State
1 - Alice Straub, State
1 - Tom Forbord, State
1 - Jack Sheerin, State
1 - Lt. Col. William Wise, Pentagon
1 - Richard Rice, Pentagon
1 - [redacted] NSA 25X1
1 - [redacted] DIA
1 - [redacted] DIA
1 - Doug Mulholland, Treasury
1 - Bob Anderson, Treasury
1 - Lincoln Bloomfield, ISA
1 - Greg Moulton, USTR
1 - Melissa Coyle, USTR
1 - [redacted] FBIS 25X1
1 - [redacted] OCR
1 - DDO/EA [redacted] (5C18) 25X1
1 - NIO/EA (7E62)
1 - NIO/ECON (7E48)
1 - [redacted] NIC/Analytical Group (7E47) 25X1
1 - C/DO/PPS (3D01)
1 - [redacted] ANIO/Econ (7E48) 25X1
1 - C/OEA/SEAD
1 - DC/OEA/SEAD
1 - OEA/SEA/IB
1 - OEA/NEA (4G43)
1 - OEA/CH (4G20)
1 - D/OEA (4F18)
1 - OEA/Research Director (4G48)
1 - C/PES/DDI (7F24)
1 - C/EA/RR (5D10)
1 - CPAS/ILS (7G15)
5 - CPAS/IMC/CB (7G07)
1 - DDI/OCR/EA/A (1H18)
1 - DDI (7E44)
1 - PDB Staff (7F30)

[redacted] 25X1

[redacted] 25X1

1 - Senior Review Panel (5G00)

[redacted] 25X1

[redacted] 25X1

Sanitized Copy Approved for Release 2011/03/24 : CIA-RDP86T01017R000605780001-4