COUNTRY CONTEXT

A. INTRODUCTION

This document[1] provides a framework for a new and innovative Thailand-World Bank Group Partnership for FY03-05. Since the previous Country Assistance Strategy (CAS), formulated at the height of the economic and financial crisis in 1997-98, the relationship between Thailand and the World Bank Group has progressed from a borrower-lender relationship toward a true development partnership. Financial support does remain part of the relationship, especially for IFC and MIGA transactions, but the Bank's role has evolved more toward facilitating knowledge sharing and providing policy advice on medium-term structural issues. Building on this evolving approach, the Partnership proposed for FY03-05 focuses on diagnostic and monitoring work and a limited amount of implementation support for selected critical issues in Thailand's overall national development agenda.

B. RECENT POLITICAL DEVELOPMENTS

At the height of the economic and financial crisis in 1997, Thailand adopted a new Constitution, a landmark in the country's political history. Participatory and inclusive, the new Constitution is widely accepted as a "People's Constitution." It reflects the rise of civil society—a vocal middle class, a vigorous NGO community, and vibrant business interests—and it sets out a bold vision of Thailand's future, laying the foundation for a more open democratic society and serving as the impetus for major reforms. For the first time in Thai history, the Constitution establishes a judicial review process independent of executive branch control, enhancing the accountability of government and the protection of civil liberties. It provides a legal basis for broader public participation. It establishes constitutional mechanisms to promote accountability and transparency. It is also very specific about the rights, liberties, and welfare of the people—including gender equality, access to information, education and health, and environmental protection.

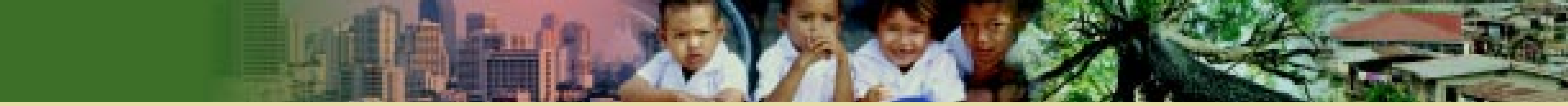
A new Government formed in 1997 made significant progress in advancing the constitutional agenda and restoring macroeconomic stability. Under the leadership of Democratic Party head Chuan Leekpai, governance reforms progressed with the establishment of independent watchdog institutions, including the National Counter-Corruption Commission, the National Election Commission, the State Audit Commission, the Administrative Court, and the Office of the Ombudsman. Furthering the constitutional goal on access to education, an Education Act granted all citizens the right to 12 years of free education. The Government also helped restore macroeconomic stability and embarked on a comprehensive structural reform program focused on the financial, corporate, and social sectors.

In the 2001 elections, the first under the provisions of the 1997 Constitution, the Thai Rak Thai Party, led by Thaksin Shinawatra, won a landslide victory. Thai Rak Thai won the election on a pro-poor, pro-rural, and pro-Thailand platform and formed a coalition government with 325 out of 500 seats in Parliament. The Government spent its first year in office putting into place its signature election programs, including more affordable healthcare, support for village funds to finance local projects, and a debt moratorium for farmers. The Government has also moved on the governance and public sector reform agenda, with a major restructuring of central government ministries in October 2002. It is now placing more emphasis on some of the other difficult structural reforms.

C. RECENT ECONOMIC DEVELOPMENTS

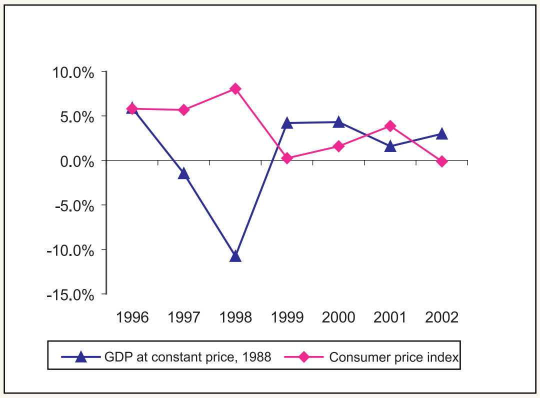
Thailand has made commendable progress since the crisis. Real GDP grew by an average of 3.6 percent a year during 1999-2001, and poverty came down to 13 percent in 2001, from a peak of 15.9 percent in 1999 (Box 1). Thailand has been highly effective in restoring macroeconomic stability, achieving low inflation, and reducing external vulnerability. Growth rebounded strongly in the first half of 2002. Estimated to reach about 4 percent for 2002, it is more than twice the 1.8 percent registered in 2001 and will return real GDP to its level before the crisis.

[1] In light of feedback received from the Thai Government and other stakeholders, this document will be called the "Thailand-World Bank Group Partnership for Development" instead of "Country Assistance Strategy" to reflect the changing nature of the Bank Group's engagement in Thailand.

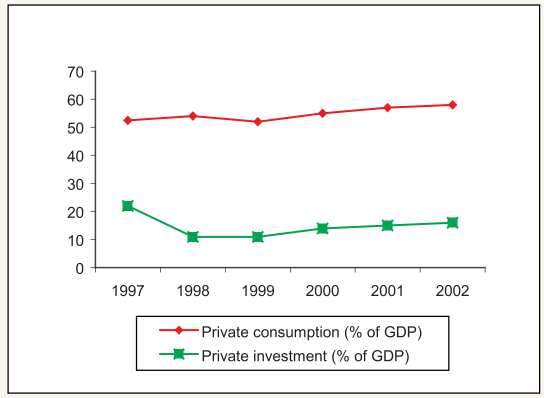


Box 1. Summary of Recent Economic Developments

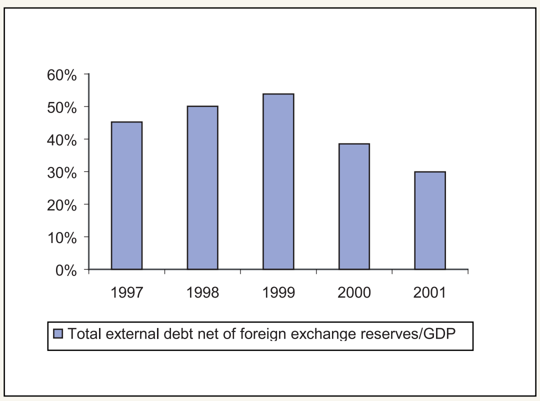
1. Growth recovery is strengthening



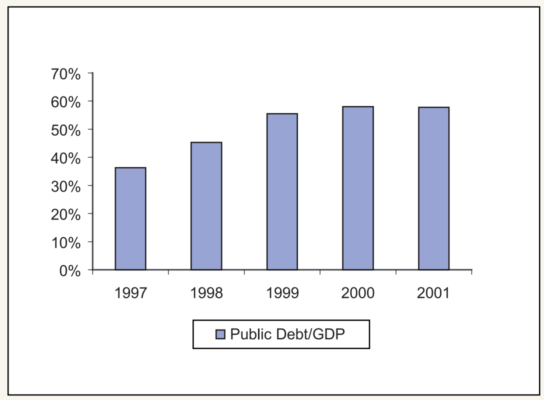
2. ... driven mainly by consumption.



3. External debt is falling ...



4. ... but public debt is rising.



Domestic consumption has been the main driver of growth. A significant fiscal stimulus program amounting to about 2 percent of GDP and rising consumer confidence have supported rural incomes and raised private consumption to over 58 percent of GDP. Private investment, after hitting a low of 11 percent of GDP in 1998, has risen gradually to reach 16 percent this year, but it remains below the average of about 20 percent for 1975-90. Further corporate and financial sector restructuring is still required, and capacity use, though improving in several sectors, remains low. Public investment as a share of GDP has been falling since 1996-97, as recurrent spending on social safety nets and financial restructuring increased.

Thailand has reduced external vulnerability by preserving its export market share and lowering its external debt. In sharp contrast to 2000, export volumes and export and tourism receipts grew in 2001, and total export receipts in 2002 are expected to be more than 20 percent higher than in 1998. Thailand has also generated annual current account surpluses of around 6 percent of GDP to repay debt and accumulate foreign reserves. External debt net of reserves, having come down from 50 percent of GDP in 1998 to 30 percent in 2001, is expected to decline further to around 20 percent of GDP by end-2002, outperforming other countries in the region.

However, public debt has increased, and the Government has initiated fiscal consolidation. The cumulative buildup of public spending and fiscal deficits boosted total public debt—mainly domestic debt—to 60 percent of GDP in 2002. Nearly two-thirds of the increase in spending stemmed from financial sector restructuring, with the rest from the costs of social safety nets, the deficits of non-financial state enterprises, and the fiscal stimulus package. As the Government's plans for fiscal consolidation are implemented, public debt is expected to stabilize but debt dynamics remain vulnerable to lower-than-expected growth, future fiscal policy, and state-owned enterprises' performance.

Corporate indebtedness has fallen but still remains high relative to other countries in the region. Corporate profitability remains weak, and the result is a rise in new and reentry non-performing loans at an annual rate of around 8 percent this year. Large banks are able to generate profits and fully provision, but others continue to be under-provisioned and under-capitalized.

Total factor productivity growth has begun to recover since the crisis. Although there is a cyclical component in this recovery, structural factors also account for this turnaround in productivity growth. Recent improvements in regulatory institutions and in the business environment contributed to it; this is evident from the fact that Thailand's global ranking on competitiveness rose in 2001 relative to 2000 and also from firm-level information, which suggests that the recovery is led by the more efficient outward-oriented manufacturing sector.

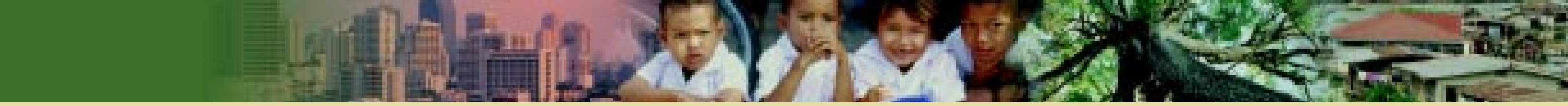
D. KEY POVERTY AND INEQUALITY TRENDS

Thailand made impressive gains in poverty reduction from the 1980s to the mid-1990s, but poverty increased with the crisis. Although high economic growth rates pulled the income poverty incidence down from 32.6 percent (17.9 million people) in 1988 to 11.4 percent in 1996 (6.8 million), the incidence of poverty increased sharply to 15.9 percent in 1999 (9.9 million people). Economic recovery since the crisis has reversed some of this increase, with income poverty declining to 13.0 percent (8.2 million people) in 2001. However, poverty incidence remains above pre-crisis levels, and a large share of the population is clustered around the official poverty line (Box 2).

Thailand's poor are concentrated in rural areas. Nine of every ten poor people reside in rural areas, and the rural Northeast region is home to two-thirds of Thailand's poor, with a poverty headcount of 28.1 percent in 2000. This severe regional bias is a product of Thailand's unequal growth pattern in the past. During 1987-96, Bangkok accounted for more than 52 percent of the rise in GDP, but only 11 percent of the increase in population. By contrast, the Northeast region accounted for only 11 percent of the increase in GDP but 32 percent of the increase in population.

Although income poverty declined over the last two decades, income inequality increased. Income inequality in Thailand rose between 1981 and 1999, with the share of income of the poorest quintile dropping from 5.4 percent to 3.9 percent, while the share of the richest quintile increased from 51.5 percent to 58.3 percent. The Gini coefficient of income inequality rose from 45.3 in 1981 to 52.5 in 2000. In the region, only Papua New Guinea, the Philippines, and Malaysia show higher inequality.

Poverty and inequality take on many shapes in Thailand. Lack of income is only one dimension of poverty and inequality, with lack of opportunity, empowerment, access to social services, and vulnerability being other equally important aspects.



The continued degradation of the environment and inadequate natural resource management deprive some of their sustainable livelihood. As described in the next section, these multi-dimensional aspects of poverty and inequality and measures to address them are a priority for Thailand's national agenda. They are also the focus of the Millennium Development Goals (MDGs), agreed on by the members of the United Nations (UN) "to create an environment—at the national and global levels alike—which is conducive to development and the elimination of poverty," and which Thailand intends to utilize to enhance outcomes- and impact-based management (Box 3).

Box 2. Poverty Measurement and Vulnerability

Thailand's poverty is measured on an income basis. The official poverty line in 2000 amounted to 882 Baht, or US$1.60 in 1993 Purchasing Power Parity (PPP). The income-based poverty headcount is 14.2 percent, while the alternative consumption-based indicator is 12.2 percent.

Poverty line for 2000	Consumption-based headcount (%)	Population below poverty line (millions)
PPP$1 a day	5.2	3.2
PPP$1.60 a day	12.2	8.9
PPP$2 a day	35.6	22.2

A large share of the population is clustered around the official poverty line. Raising the poverty line from PPP$1.60 a day to PPP$2 a day increases the poverty headcount from 12.2 percent to 35.6 percent and the number of poor from 8.9 to 22.2 million. No matter how the poverty line is set, poverty in Thailand remains predominantly rural, concentrated in the Northeast.

Regions	PPP$1 a day (%)		PPP$1.6 a day (%)		PPP$2 a day (%)	
	Headcount	Share of poor	Headcount	Share of poor	Headcount	Share of poor
Bangkok	0.1	0	0.3	0	1.2	0
Central	2	6	5	7	12	10
North	5	13	12	15	30	19
Northeast	14	69	28	67	50	59
South	6	11	11	10	26	12

E. THAILAND'S DEVELOPMENT CHALLENGES

To address the challenges of growth and poverty reduction, a comprehensive national development agenda is being developed around four pillars: Human and Social Capital, Competitiveness, Poverty and Inequality, and Natural Resources and Environment. Anchored in the 1997 Constitution, this national development agenda is in line with the broad objectives of the Ninth Economic and Social Development Plan (2002-06) and the national Poverty Reduction Strategy drafted in 2002. Consultations with the Government and other stakeholders reveal that sustained progress on these four pillars will also require improvements in governance, as clearly embodied in the Constitution, and that effective implementation of this agenda should help ensure that Thailand continues to reduce poverty, including in the Northeast.

Thailand's National Agenda

i) Human and Social Capital

The Human and Social Capital pillar is critical to realizing faster growth, better quality of life, and greater social cohesion and achieving the targets of the Ninth Plan and the MDGs. The Constitution contains explicit provisions for access to education and health services, as well as social protection for the vulnerable.

- ***Education***. Thailand is likely to achieve universal access to primary education as targeted in the MDGs. However, enrollment rates in higher education remain low at only 71 percent for secondary education and 25 percent for tertiary. The equity, efficiency, and quality of education also remain major issues. In 2001, Thailand was ranked 44th of 49 countries for its competitiveness in education, lower than other Asian countries such as Korea, Malaysia, and the Philippines.[2] Failure to address these issues could result in further deterioration in Thailand's competitive position over time, as well as increased tension as disparities grow. The Constitution and the 1999 Education Act are sweeping in their scope with respect to education. Their intent is to focus accountability at the local level (through the establishment of local education authorities and school boards), introduce more creativity and locally-driven innovation in curricula; move to a learner-centric teaching model; upgrade the quality of teachers; establish effective quality assurance; and enhance the use of technology. However, the envisaged administrative reforms have proven difficult to implement, and overall progress to date has been limited. Special emphasis should be placed on achieving universal secondary education; improving educational outcomes, including on such critical subjects as science and technology; enhancing educational standards; and establishing a quality assurance system. It will also be important to review carefully the balance between public and private provision of services, the adequacy and mix of public expenditures, financing issues, and other constraints to achieve higher enrollment.

- ***Health.*** Over the past 30 years, Thailand has achieved remarkable progress in basic healthcare, with significant declines in infant and maternal mortality, and is projected to meet the MDG goal of further reducing these mortality rates. Health financing reform remains a key priority. The public sector finances about half of all health expenditures, and about 75 percent of Thais have access to some form of health benefits. To help provide coverage for the quarter without access, the Government introduced the "30 baht per visit" health scheme in 2001, boosting utilization rates, but at a significant burden to the budget.[3] *HIV/AIDS constitutes an important challenge.* Although infection rates in brothel-based sex workers fell from 31 percent in 1994 to 18 percent by the end of the decade, the rate

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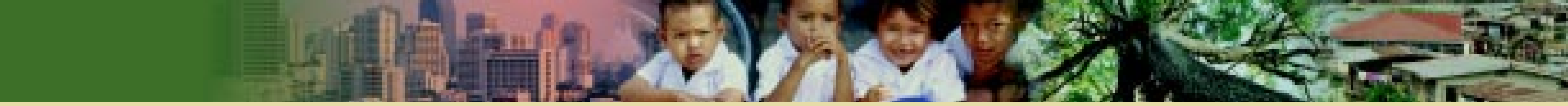
[2] Source: *World Competitiveness Yearbook 2001*, International Institute for Management Development. The criteria for competitiveness in education are comprised of i) total public expenditure on education, ii) pupil-teacher ratio (primary education), iii) pupil-teacher ratio (secondary education), iv) secondary school enrollment, v) higher education achievement, vi) education assessment, vii) educational system, viii) university education, ix) illiteracy of adult over 15 years, x) economic literacy, xi) education in finance, xii) qualified engineers, and xiii) knowledge transfer between companies and universities.

[3] Under the 30-baht health policy, all Thais are entitled to receive doctors visits at 30 baht per visit, including any medication prescribed. The policy does not cover procedures such as cosmetic surgery, fertility treatments, organ transplants, or treatment for HIV/AIDS (with the exception of treatment for opportunistic infections associated with HIV/AIDS).



of infections among women is increasing faster than among men, indicating that HIV/AIDS will be a health problem for adults and children outside the traditional higher-risk groups. Particular emphasis needs to be placed on sustaining condom use and launching an initiative to prevent infection by injecting drug users. Ensuring access to cost-effective treatment also remains a priority.

- *Social protection.* Thailand's long-trusted mechanism of community and family-based social protection was tested during the economic and financial crisis, and many Thais at the fringes of the economy were left without resources to sustain themselves. The main challenge is to put in place formal social protection mechanisms without displacing these informal mechanisms that underpin social cohesion. The main components of Thailand's social protection strategy include labor market policies and programs, social insurance, and social assistance. The first two are oriented toward those in the formal sector, and coverage has been expanded significantly. For example, the old-age pension system introduced in 1998 now covers an estimated 5.7 million workers, and a formal unemployment benefits scheme is planned. Social assistance schemes are targeted toward only the vulnerable—women, children, the elderly poor, and the handicapped. However, implementation has been difficult, with wide gaps in coverage and equity. For example, enterprises with fewer than 10 employees account for more than 40 percent of non-government wage employment but are not covered by any occupational safety and health legislation. Unpaid family workers and informal sector workers are especially vulnerable, as protection under current laws is limited—this is a gender issue, as 75 percent of the unpaid workers and 80 percent of the informal workers are women. Less than 15 percent of the elderly poor receive social assistance benefits targeted at the elderly, and only half the recipients of the student loan program come from the bottom three income quintiles. Overall public spending favors richer over poorer provinces, and the efficiency of many programs remains problematic, with significant overlaps.

ii) Competitiveness

Competitiveness, critical to sustaining higher growth in Thailand, is a high priority for the current administration. The Government has established a National Competitiveness Committee, and its competitiveness strategy seeks to balance the successful East Asian formula of fiscal discipline, openness to trade and investment, and export orientation with a renewed focus on domestic capacity and linkages with domestic firms, including small and medium size and rural enterprises.

- *Economic management.* In addition to maintaining sound macroeconomic management, Thailand needs a business environment conducive to innovation, entrepreneurship, and competition on a level playing field. This requires improvements in its trade, competition, and investment regimes. While Thailand is a relatively open economy, it intends to further liberalize its trade regime under commitments to the ASEAN Free Trade Agreement (AFTA) and its numerous bilateral preferential trade agreements. Improving the transparency and efficiency of customs administration as part of the Master Plan for Administrative Reform of the Customs Department is also important. While the new Competition Law improves the overall competition regime, the institutional capacity to enforce the law needs to be strengthened along with public awareness of the rights provided to consumers by the law. Thailand has been successful in attracting foreign direct investment (FDI) in some sectors, particularly electronics and automotive, but efforts now need to be focused on maximizing the linkages between those investments and the domestic economy and integrating FDI more clearly into the overall competitiveness strategy. In large part, this means shifting the strategy of the Board of Investment from attracting fixed capital investment through granting discretionary tax incentives to focusing on the enabling environment, including the quality of local suppliers, human capital, infrastructure, and services.

- ***Financial and corporate sector development and legal reform.*** The 1997 crisis caused an enormous loss for the Thai economy—with non-performing loans (NPLs) peaking at 48 percent of total loans and total costs to taxpayers estimated at over US$33 billion, or 27 percent of 2001 GDP. There has been a gradual shift toward greater market discipline of banks and firms and toward a more balanced financial system, with capital markets, institutional investors, and non-bank financial institutions playing a more equal role, reducing the concentration of risk in banks and loans. These gradual changes will spread risks, reduce the likelihood of asset bubbles, and better allocate funding to the most productive uses. Although the direction for reform is clear, the speed of implementation has been mixed, in part due to concerns about re-pricing and reallocating assets while the economy is still recovering from the crisis. Further structural reforms should provide competitive incentives which reward restructuring, re-capitalization, disclosure, good corporate governance, and risk-based pricing. A stronger legal regime, especially in terms of economic laws and streamlined judicial procedures, would build confidence that disputes will be resolved expeditiously. Full implementation of international accounting standards and prudential regulations would attract capital into banks and firms, while tax changes would promote mergers and better allocation of risk through securitization and derivatives transactions. Finally, a measured transition to a limited deposit insurance program would reduce the moral hazard from a bank-dominated system with a high proportion of non-performing loans and blanket deposit insurance.

- ***Infrastructure.*** Although the private sector has a sizable involvement in infrastructure, state investments dominate. Markets are not yet open for effective private participation and competition, and inadequate economic regulations continue to hinder private participation. In addition, poor infrastructure in remote regions—particularly for transport—has raised logistical costs and constrained rural business opportunities. The Government has begun to address these structural weaknesses. A master plan adopted in 1999 aims to separate the policy, regulatory, management, and operating functions of the infrastructure sub-sectors (including transport, telecommunications, energy, and utilities). The reform effort culminated in major realignments of state agencies in 2002. The Government also intends to establish an independent regulatory regime in each sub-sector. The goals are to improve governance, promote private participation in telecommunications and utilities, strengthen multi-modal transport linkages, and improve road and waterway accessibility in remote regions. Thailand must continue to implement this ambitious agenda, as well as focus on state enterprise reform and capacity building for regulatory agencies and new line ministries.

- ***Knowledge economy and innovation.*** While Thailand's rapid economic growth in the years preceding the crisis was driven largely by capital accumulation, policymakers understand that future growth will depend largely on productivity gains—increasing the capabilities of firms to innovate and the skills of Thailand's workforce to produce higher value products. While Thailand enjoys important assets, such as economic openness, relatively flexible labor policies, a substantial presence of multinationals, and rich local wisdom and culture, the challenges are substantial. Thai firms face a bureaucratic public service and a system of public institutions and research universities that are seen as unresponsive to market needs. In addition, Thailand produces a small number of engineers and scientists relative to regional competitors. This contributed to research and development spending of just 0.13 percent of GDP in 1997, half the level of Malaysia, and just one-twentieth the level of Korea. Corporate governance practices have been slow to evolve, with minority shareholders not empowered to play a strategic oversight role. Perhaps more importantly, a lack of inter-firm collaboration, alliances, mergers and knowledge sharing has prevented an effective response to the pressing quality and cost standards that characterize high-value opportunities. The Thai Government, like Korea, Singapore, Malaysia, and several others, sees ICT as an entryway to a vision of a knowledge-based society, and substantial research supports this view. However, without rapid progress in building core skills and improving the business environment, firms will have neither the capabilities nor the incentive to actually leverage ICT. Without parallel reforms in telecommunications policy, large gaps in information access between rural and urban Thais, larger and smaller firms, is likely to persist. Given the complex, cross-cutting agenda which by its nature requires public-private partnership to be successful, the immediate challenge is to establish the leadership and governance framework that can help prioritize reforms and facilitate partnerships across government, civil society, and the private sector.

- ***Strategic thrusts for the real sectors.*** The Government's competitiveness strategy emphasizes sectors in which the country is perceived to have a comparative advantage: agriculture and agro-processing, textiles and fashion, tourism, software, and automotive. The Government is also stressing the importance of shifting the competitive paradigm in agriculture, industry, and services toward value creation, product differentiation, customization, market positioning, and cluster development. Greater understanding of sectoral conditions and opportunities—including supply chain linkages, technological capabilities, and clusters—can enhance Thailand's competitiveness, but it will also be important that the Government avoid the temptation of "picking winners" and continue to maintain a "level playing field" for all enterprises, domestic and foreign. Successful promotion of small and medium size enterprises (SMEs)—which account for more than 94 percent of firms, half of industrial employment, and the majority of service employment—will also require that the underlying structural weaknesses facing SMEs, including human capital, technological, and regulatory issues, be effectively addressed along with their financing constraints.

iii) Poverty and Inequality

Reducing poverty and inequality remains central to the Government's national agenda. Poverty and inequality feature prominently in the Ninth Plan and the national Poverty Reduction Strategy, which recognize that improvements in human and social capital, enhanced competitiveness and growth, and progress on the environment are all critical to poverty reduction, as captured by the MDGs.

- ***Understanding poverty.*** In the post-crisis environment, the problem of poverty has taken on new characteristics, and better understanding of poverty dynamics and the changing profile of the poor is needed to strengthen the foundation for anti-poverty strategies in Thailand. The Government has been enhancing the poverty database, which can greatly assist in analyzing poverty and the impact of public programs and policies. Important initiatives are developing a national poverty map, improving the socio-economic survey, and establishing a poverty monitoring system. Further work is needed to improve the gender disaggregation of poverty data and to develop an understanding of the links between gender equality and poverty reduction. It will also be important to look more broadly at the range and quality of data currently collected and at its adequacy in relation to the overall growth and poverty reduction challenge.

- ***Balanced development.*** Thailand has not made progress in lowering inequality. Income inequality is increasing, and regional inequality remains high. The mean per capita income in Bangkok is more than four times that of the Northeast. To address these issues, the Ninth Plan emphasizes sustainable and balanced rural and urban development. It focuses on empowering community organizations and civil society, decentralizing decision-making power and resources, promoting gender equality, developing border provinces as economic gateways, and providing greater access to sources of information and knowledge for outlying regions. Such measures will need to be accompanied by a significant reallocation and improved targeting of government expenditures. Because education has the highest explanatory power in accounting for interpersonal and regional variations in income and inequality, lowering inequality will require addressing educational access and quality.

- ***Targeted programs.*** Thailand has a large number of anti-poverty programs in place, and the Government recently introduced additional programs, such as the three-year debt moratorium for farmers and the village fund program. If well-targeted and effectively implemented, these programs can be an important supplement to broader strategies for growth and poverty reduction. However, better data, monitoring, and evaluation will be needed.

iv) Natural Resources and the Environment

Management of natural resources and the environment, overlooked during the high growth years, will need to become a higher priority. Consultations with stakeholders have consistently identified natural resources and the environment as requiring urgent attention. Continuing environmental degradation, likely to aggravate conflicts over the use of natural resources, could undermine Thailand's social cohesion.

- ***Improving environmental quality.*** Thailand's economic expansion has been accompanied by significant environmental costs. Rapid expansion of industry and increasing population, especially in urban areas, has rapidly increased the levels of pollution (solid and hazardous waste, air, noise, and water). Fine particles in Bangkok's air exceed standards by 2.5 times, and river water in the central, southern, and eastern regions is of poor quality. The resulting risks to human health are high. Thailand needs to focus on more effective enforcement of environmental laws; stronger institutional capacity, both national and local; and increased investments in pollution prevention and control, with private sector participation.

- ***Sustaining natural resources.*** Land conversion, slash-and-burn agriculture, and intense exploitation of water have led to rapid deterioration of natural resources. Forest cover fell drastically from 53 percent in 1961 to 25 percent in 1998, and over-harvesting of marine fisheries has reduced fishing yields by 90 percent. Of particular concern is water scarcity, which occurs against a backdrop of low availability, high pollution, and increasing per capita consumption. Thailand ranks the lowest in Asia for annual per capita water availability, but it ranks 14th in the world in industrial organic water pollution. To better balance conservation and exploitation of natural resources, the Government recently established a new Ministry of Natural Resources and Environment. The Ministry's immediate challenges are to ensure an integrated approach to sustainable resource management, eliminate harmful subsidies (such as excessive use of pesticides and over-fishing), and assist in the capacity building of local institutions and communities. As the Constitution grants local ownership of environment and natural resources and promotes community involvement in their management, appropriate incentives (such as land tenure, water rights, village forest management) and capacity building are needed to create opportunities for communities to partner with local governments to find solutions.

- ***Environmental commons.*** Thailand is a signatory to many international and regional treaties, such as the Montreal and Kyoto Protocols and the Regional

Haze Action Plan. It also shares the biologically rich Mekong River with Cambodia, China, Lao PDR, Myanmar, and Vietnam. It therefore has an intrinsic interest in participating in regional and global initiatives. Going forward, the challenge will be to deepen regional cooperation and to partner with neighboring countries on initiatives such as the integrated management of the Mekong River.

v) Governance

Progress on governance is recognized as critical for achieving sustained progress under the four pillars of the development agenda. Progress on governance is required at all levels: the public and private sectors, and civil society.

- ***Effectiveness of national public sector institutions.*** The crisis highlighted concerns about the performance of the public sector, whose role, organization, and processes need an overhaul. The Thai civil service has been overstaffed and underpaid, and the organizational culture has not rewarded performance or service. Expenditure management has been characterized by weak linkages among planning, budgeting, and sectoral policy; lack of medium-term fiscal planning; and weak monitoring and evaluation of expenditures. To address these issues, Thailand developed a Public Sector Management Reform Plan in 1999. Government commitment in this area is high, as witnessed by the recent passage of two public sector reform laws—the Public Administration Act and the Ministerial Restructuring Act—and the impending passage of the Budget Procedures Act, Financial Management and Accounting Act, and Public Debt Management Act. Together, these laws provide a significant opportunity to improve public sector performance. The success of reforms will hinge upon the details of their implementation, particularly on the careful coordination of expenditures and decentralization.

- ***Local government and decentralization.*** Thailand is a highly centralized country. In 2001, the central government spent 91 percent of total expenditures and collected 97 percent of taxes, and only 3 percent of local government revenues were locally collected and retained. The central government has also appointed most local officials, determined local government salaries, and approved local budgets. The new Constitution emphasizes decentralization, with the Decentralization Act (1999), the Decentralization Master Plan (2000), and the Decentralization Action Plan (2002) providing the impetus. Some functions have begun to be devolved to local governments, and the share of local government revenue is slated to increase from 20 percent in FY01 to 35 percent in FY06. However, many issues remain to be resolved. Fiscal transfers are not based on transparent formulas and hence are unpredictable. The devolution of revenues, functions, and personnel has not been integrated, and very few personnel have been transferred to the local level. Furthermore, local government capacity is extremely limited and many local governments are of insufficient scale, which could affect service delivery. Without a clear framework for addressing these issues, the move to decentralization poses substantial fiscal and other risks.

- ***Transparency and anti-corruption.*** Corruption remains problematic. According to a corruption perception survey in 2000, about 80 percent of Thai firms surveyed pay for services from government agencies that handle transactions.[4] The Constitution and the Official Information Act (1997) aim to improve transparency and accountability by empowering the public to monitor public policies and public actions and by establishing independent oversight bodies. These new bodies will require sufficient financial and technical resources and independence to carry out their mandated functions effectively. Sustained commitment at the highest levels is needed to achieve substantial progress.

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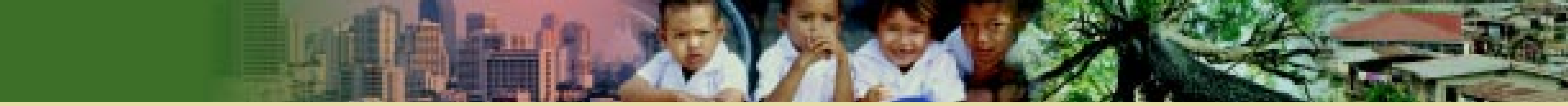
[4] Survey results presented in Poapongsakorn, Nipon et al., *Anti-Corruption Strategy in Thailand in the Year 2000,* November 2000. This publication was prepared for the Thailand Development Research Institute 2000 Year-End Conference.

- ***Public participation.*** Traditionally, public participation has been limited. Through various articles, the Constitution has improved the environment for public participation and granted greater roles and responsibilities for citizens in public policy design and implementation. As a result, greater civic participation has slowly been accepted as common in many government agencies, and civil society has become much stronger and active in that process. Despite this positive development, the public's a bility to participate is limited by a lack of understanding of the respective duties, rights, and responsibilities of government agencies and the public and by poor access to information. In addition, some agencies do not yet recognize why participation is beneficial and how it can be carried out meaningfully. Capacity building for civic groups and other stakeholders—including some government agencies—and formal mechanisms for public participation in policy formulation, program implementation, and monitoring are needed.

- ***Gender equality.*** Inequality of participation and representation of women is evident in a variety of areas beyond economic participation. In the latest parliamentary election, women accounted for only 9 percent of the representatives elected in 2001 and for only 21 of the 200 elected Senators. The representation of women in the civil service is also low, at about 18 percent in the upper ranks and only 4 percent at the highest level. Gender equality is one of the main tenets of the Constitution, and the Government has endorsed a new Women's Development Plan (2002-2006) as a framework for action. Additional measures needed include developing a gender-disaggregated database to facilitate policymaking, increasing awareness and understanding of gender issues among officials and the public, and enforcing equal rights and opportunities.

Thailand's Development Challenges in a Regional Context

Thailand actively supports and contributes to regional initiatives aimed at economic cooperation, including the Asia-Pacific Economic Cooperation (APEC) Forum, the Association of South-East Asian Nations (ASEAN), and "ASEAN Plus Three" (ASEAN plus China, Japan, and Korea). The Initiative for ASEAN Integration, for example, seeks to adopt common policies on trade and investment and meet the requirements for AFTA. Thailand also participates in the Greater Mekong Subregion (GMS) Program and the Mekong River Commission (MRC), initiatives which are now being strongly supported by the concerned governments and are contributing significantly to the development of the GMS. Thailand is in a good position to contribute to and benefit from such regional public goods. Given the myriad, ongoing reform efforts in the region, there is also substantial scope for trilateral cooperation to share lessons and experiences.



Box 3. Millennium Development Goals: Summary of Thailand's Progress

Goal 1: Eradicate extreme poverty and hunger

Target 1: Halve the proportion of people whose income is less than one dollar a day between 1990 and 2015

Target 2: Halve the proportion of people who suffer from hunger between 1990 and 2015

	1990	**2000**
Headcount poverty ratio (%)	27.2	14.2
Percentage share of income/consumption held by poorest 20%	4.2	3.9

The number of poor is declining, but Thailand's poverty rate of 14.2% in 2000 is 3 percentage points above the pre-crisis level. It is very likely that all regions will halve poverty by 2015, but some localities may not be able to achieve this goal. Inequality is also problematic as the percentage share of income accruing to the poorest quintile decreased from 4.2% in 1990 to 3.9% in 2000.

Goal 2: Achieve universal primary education

Target 3: Ensure that by 2015, children everywhere—boys and girls alike—will be able to complete a full course of primary schooling

	1990	**2000**
Gross primary enrollment ratio	100.5	103.6
Youth literacy rate (% ages 15-24)	98.1	98.9

Universal gross primary enrollment has been achieved, while net universal primary rate is also likely to be achieved. Enrollment in both secondary and tertiary education is anticipated to pick up as the reform program, which aims to achieve universal secondary enrollment, progresses. Universal primary enrollment at the regional level should be achieved by 2015. However, hill tribes may not be able to attain this goal.

Goal 3: Promote gender equality and empower women

Target 4: Eliminate gender disparity in primary and secondary education preferably by 2005, and to all levels of education no later than 2015

	1990	**2000**
Ratio of girls to boys in primary and secondary education	94.1	96.1
Ratio of young literate females to males	99.0	99.0
Share of women employed in the nonagricultural sector (%)	45.4	47.3
Proportion of seats held by women in national parliament	2.8 (1988)	9.2 (2001)

Good overall progress is being made at all levels. The literacy rate of elderly women remains low and informal education opportunities could bridge this gap. Although women's participation in politics has been quite limited, the number of women in the Parliament is increasing.

Note: Only MDG indicators with data for both 1990 and 2000 are included here for illustrative purpose.

Source: Based on the National Workshop on the Relevance and Application of MDGs in Thailand, August 2002, convened by the National Economic and Social Development Board, UNDP and the World Bank.

Box 3. Millennium Development Goals: Summary of Thailand's Progress *(Continued)*

Goal 4: Reduce child mortality

Target 5: Reduce by two-thirds the under five-mortality rate between 1990 and 2015

	1990	2000
Under 5 mortality rate (per 1,000)	41.0	33.2
Infant mortality rate (per 1,000 live births)	37.0	27.9
Immunization, measles	80.0	96.0

Good progress has been made at the national level, but attention needs to be given to hill tribes and adolescent mothers for whom access to social services is a major issue. To achieve the MDG target, the rate will have to be lowered to 27 per 1,000.

Goal 5: Improve maternal health

Target 6: Reduce by three-quarters the maternal mortality ratio between 1990 and 2015

	1990	2000
Maternal mortality ratio (per 100,000 live births)	24.8	13.2

Maternal mortality continues to decline, but hill tribes and adolescent mothers are likely to be vulnerable as access to social services is limited and greater awareness raising is needed.

Goal 6: Combat HIV/AIDS, malaria and other diseases

Target 7: Have halted and begun to reverse the spread of HIV/AIDS by 2015

Target 8: Have halted and begun to reverse the incidence of malaria and other major disease by 2015

	1990	2000
Prevalence of HIV among pregnant women (% ages 15-24)	0.21	0.78

The number of HIV-infected women is on the rise, resulting in an increase in mother-to-child transmission. The existing prevention programs are only stabilizing the transmission but not slowing it down. The vulnerable groups include fishermen, youth and adolescents, hill tribes, injecting drug users and construction workers. Deaths due to tuberculosis have fallen by nearly 30 percent between 1985 and 1997, while information on malaria remains sketchy.

Goal 7: Ensure environmental sustainability

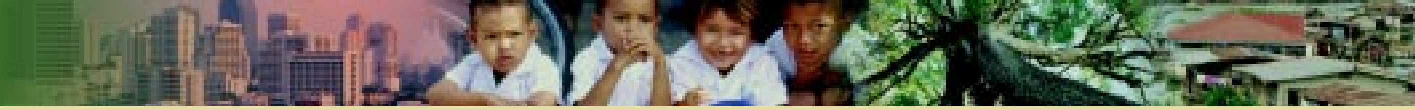
Target 9: Integrate the principles of sustainable development into country policies and programs and reverse the losses of environmental resources

	1990	2000
Forest area (% of total land area)	28.0	28.9
Nationally protected areas (% of total land area)	12.4	15.8
Access to improved water source (% of population)	71.0	92.7
Access to improved sanitation (% of population)	73.8	97.7

The access to water source indicator is likely to be achieved, but rising water pollution levels continue to threaten the viability of freshwater sources and could setback the achievements. Air quality in Bangkok, water quality in major rivers, and deforestation are major environmental problems.

Note: *Only MDG indicators with data for both 1990 and 2000 are included here for illustrative purpose.*

Source: *Based on the National Workshop on the Relevance and Application of MDGs in Thailand, August 2002, convened by the National Economic and Social Development Board, UNDP and the World Bank.*



Thailand and the Millennium Development Goals

The Government has traditionally used the five-yearly national economic and social development plans to establish broad targets for achieving its priorities. However, these targets have mostly been reflected in input and output indicators, with little attention paid to results measurement. Prompted by a more outcomes-focused design of the Ninth Plan, the Government is now shifting to a more outcomes- and impact-based system for allocating resources and assessing progress, and in this context, is carefully reviewing how best to utilize the MDGs.

On an aggregate basis, Thailand is likely to meet most of the MDGs and indeed has already met several *(Box 3).* However, for some indicators—including maternal and child mortality, communicable diseases, and environment—the MDGs may not be achieved, especially for specific regions and subpopulations. To better track developments at the disaggregated level, the Government is now developing an enhanced "MDG+" approach which will disaggregate the MDGs by regional and subpopulation groups and which will be integrated into its national planning, monitoring, and evaluation framework.

F. MEDIUM-TERM ECONOMIC PROSPECTS AND EXTERNAL DEVELOPMENTS

Thailand is expected to grow at around 4 percent a year and attain its poverty reduction targets *(Table 1).* Thailand's medium-term prospects for growth and poverty reduction depend on the speed and depth of structural reform and fiscal consolidation. Annual growth rates of around 4 percent are the likely "base case" over the next three years, given the country's national development agenda and the expected global economic recovery. Under the base case scenario, export growth is projected to increase, and private investment to rise gradually, but still remain significantly lower than during 1975-90. However, if an acceleration in reforms boosts private investment and total factor productivity, growth could reach 5.0-5.5 percent a year.

Table 1. Medium-Term Base Case

	2001 (actual)	2002 (est.)	2003 (proj.)	2004 (proj.)	2005 (proj.)
Poverty (% living on less than US$1.60 per day)	13.0	12.7	12.4	11.9	11.4
GDP growth (%)	1.8	3.8	4.0	4.0	4.0
Current account (% of GDP)	5.4	4.0	2.8	1.7	0.0
Public sector balance (% of GDP)	-3.5	-5.4	-4.0	-2.8	-1.8
Inflation (%)	1.7	1.0	2.2	2.5	2.5

The Ninth Plan target of poverty reduction for end-2005 is expected to be achieved, provided the degree of income inequality in the country remains stable over this period. The target could be exceeded if growth is higher. However, this projection is contingent on policies that not only support sustained growth but also ensure a more vigorous participation of the poorer Northeast in that growth so overall income inequality does not rise.

The projected global recovery will enable export growth rates of around 6 percent a year. Although most analysts have recently revised their 2003 growth forecasts downward for high-income economies, all forecasts show significant recovery in global growth, trade volumes, and commodity prices. With domestic policies becoming more favorable for improved competitiveness, it will be possible for Thailand's export growth rates to increase and be sustained over the next three years.

China's WTO accession provides export opportunities to Thailand, even as it poses new challenges in third-country markets. There is considerable scope for increasing exports to a more open China, as evidenced by the very large increases in exports—from the Philippines, Malaysia, Singapore, Korea, Thailand, Indonesia, and Vietnam—to China in the first half of 2002. These exports include not only land-intensive products like sugar, oil seeds, and wood products but also high-tech products as inputs into Chinese high-tech exports. In third-country markets, there is strong Chinese competition—particularly in garments and textiles—although the impact has been limited so far.

The recently initiated fiscal consolidation will reduce fiscal risks but also reduce public investment. The Government plans to reduce the public sector deficit to about 2 percent of GDP by 2005 and to zero by 2008, in line with the aim of capping public debt at 65 percent of GDP and debt servicing at 16 percent of government expenditures. As this will involve fiscal consolidation as well as a focus on revenue measures, the challenge is to ensure that roads, education, and health—all suffering significant cuts in public investment after the crisis—receive a larger share of the investments to maintain and improve them.

Most of the deficit can be financed domestically, but some external financing is likely. In 2001, the public sector deficit and current account surplus were funded by an excess of private savings over private investment of around 9 percent of GDP. As private consumption and investment grow, this excess of private savings will decline over the next three years, and external financing of some of the public sector deficit might then be needed.

Thailand's medium-term economic prospects face risks in three areas:

- *Fiscal consolidation may not progress as planned, and public debt dynamics could become unfavorable.* The Government is making every effort to consolidate the fiscal situation and to manage debt judiciously. However, if revenue measures generate less collection than expected and expenditure reduction turns out to be more difficult because of higher state enterprise deficits or higher local government spending due to decentralization, the public sector deficit could be higher than currently projected. In addition, unfunded contingent liabilities could turn out to be higher than estimated, and growth could slow due to slow implementation of the development agenda or a precipitous deterioration in the external environment. All these factors could worsen the public debt dynamics. Mitigation of these risks will require a pace of decentralization consistent with improvements in local administrative capacity, close monitoring of fiscal developments, and a willingness to react quickly to the possibility of significant deterioration in fiscal and public debt variables.

- *The external economic environment could worsen sharply on several fronts.* Business and consumer confidence in high-income economies could worsen more than currently projected, reducing export demand. Further incidents of terrorism in the region could sharply lower tourism receipts. The rising tensions in the Middle East could also push oil prices to new heights over a sustained period, generating a major terms of trade shock. Any of these three external factors alone would not significantly affect the base case growth scenario, but if they occur together, growth in Thailand could be significantly lower than now projected.

- *Structural reforms to improve the business environment and restructure the financial and corporate sectors could slow.* Given the Government's growing commitment to medium-term reforms and to sustained growth and poverty reduction, this risk is seen as low. However, the risk of a more gradual pace of some key reforms cannot be eliminated.