

Urgent Action Vital to Cope with Human Face of Crisis

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A resounding thump seems to have taken the place of any holiday cheer this year. Rich countries are collectively expected to face the deepest recession since the Second World War. Emerging markets, whose financial systems so far have remained relatively unscathed, are unlikely to be so lucky with their real economies.

Conditions are deteriorating very quickly as a result of the sharp slowdown in demand from rich countries. In the case of Thailand, the impact will be especially hard, given that the extended political crisis at home over the past few years has dampened domestic demand, making exports the main driver of growth.

But with worsening prospects for exports throughout the region – Thailand's export growth contracted by -18.6% in November – this last hope for growth seems likely to fade quickly.

Monetary policy is a relatively blunt instrument in this situation. The Bank of Thailand's historic 1% reduction in the policy interest rate to 2.75% at the MPC's December meeting helped to lower firms' cost burdens somewhat. But as firms face worsening demand prospects – everyday brings news of declines in export orders going forward – firms are likely to cut down on labour costs.

The relatively low October unemployment data from the National Statistics Office, which registered at 1.2%, coupled with the persistence in economic weakness, indicated that the labour markets have so far remained flexible, with unemployed workers reentering the labour force with relative ease. However, the headline unemployment data masked a more worrying trend by employers – who tend to cut costs by first reducing overtime and bonus payments – before actually laying off workers, beginning with migrant and low-skilled employees, followed by higher-skilled employees.

This trend hides the fact that employees' incomes may have in reality fallen substantially – particularly for low income workers – where overtime pay can account for up to half of their monthly income. In addition, the shift of labour from the manufacturing sector to the agricultural or services sector may actually entail a significant decline in income, which is not reflected in the unemployment numbers. These changes are likely to be reflected in weaker purchasing power and lower consumption, further depressing domestic demand.

Going forward, with expectations of both a continued drop in export orders and weak domestic demand, a coordinated response by monetary and fiscal authorities is required to support the economy. In the absence of inflationary pressures, monetary policy can alleviate the financial burden of firms. At the same time, any fiscal stimulus should be targeted directly at those affected sectors. The government's planned 180 billion baht public spending package, which is intended to be used to create new job prospects, can play an important part in supporting employment. At the same time, measures to help the cost of living of low income groups should also continue to support the economy. In order for these measures to be effective, the government needs to ensure that this spending is disbursed as quickly and efficiently as possible.