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Country Development Strategy Statement

FY 1986

Thailand

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Agency for International Development
Washington, D.C. 20523

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FY 1986 CDSS: THAILAND

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Preface

Thailand is at a crossroads. It is, for the first time in its history, obliged to fundamentally reconsider directions for national development as it enters a new semi-industrialized era. AID/Thailand is also inescapably at a crossroads. For the first time in our 34-year history of cooperation in Thailand we find ourselves a comparatively minor donor and requiring a new mandate now that the Kingdom has developed into a nascent "middle-income" country.

Part I of this CDSS ("Analysis") characterizes Thai development as remarkably successful in attaining social and economic progress. Paradoxically, this very progress has also set the stage for a range of emerging problems (overdevelopment of Bangkok, structural poverty, unemployment, lack of arable land, natural resource degradation, etc.) which, if not dealt with in their early stages, could prove seriously detrimental to the nation's development and stability. As a generalization, we conclude that the maintenance of broad-based rural growth and development will be essential throughout the 1980's. Such a rural development process will require careful analysis and phased structural and policy change, as well as substantial financial resources.

Our analysis also focuses on the past and present posture of USAID in Thailand. USAID is now small in terms of comparative size of ODA (IBRD, Japan and ADB furnish almost 90% of total ODA to Thailand). We are also confronted by a situation in which foreign official or commercial funds are available to virtually every sector of the economy.

Part II ("Program Alternatives and Strategy") draws on Part I and lays out what we believe are the major determinants of a "middle income country strategy" for AID in Thailand during the period FY 1986-90. Simply stated the CDSS strategy contains these key elements:

- A basic strategic objective of establishing a redefined, more mature, collaborative relationship between the U.S. and Thailand in the area of development cooperation which is consistent with Thailand's emerging status as a middle income country.
- A loan program for the CDSS period which consolidates loan resources on the single theme of rural industries and employment. This approach coincides with Thai development concerns, is in an area where loan assistance is an acceptable funding mode, and is consistent with our analysis of Thailand's priority needs.
- A flexible, jointly managed grant program which is designed to provide responsive and timely funding for emerging development problems such as those outlined in Part I of the CDSS.

PART I - ANALYSIS

A. Thailand's Growth and Development

1. Comparative analysis of Thailand's performance

In order to develop a better perspective on the relative status of Thailand's development, the Mission compared Thai performance on 72 development criteria with that of a) the dozen AID recipient countries with equal or higher GNP/capita in 1981 (all roughly categorized as "Middle-Income Countries¹"), and b) the forty-three AID worldwide recipients with populations greater than one million. An abbreviated list of key results is noted in Table 1.

These statistics demonstrate that Thailand ranks generally at the high end of the scale for most criteria, both for MIC's and AID recipients in general. Comparatively, some of the country's salient characteristics include: it is one of the largest and fastest-growing economies among AID recipients; public consumption is relatively small as a proportion of GDP; investment rates are relatively high; net direct private foreign investment and inflows of medium and long-term public or publicly guaranteed loans are among the highest of any AID recipient; debt service ratios are relatively low and reserves relatively high; it is one of the most populated AID recipient countries, but also currently has one of the lowest projected population growth rates; employment and overall population is heavily located in rural, agricultural areas; measures of health such as life expectancy and death rates

¹There is no internationally recognized definition of the term "Middle-Income Country". However, AID has often utilized the IBRD per capita GNP eligibility criterion for IDA (\$730 in 1980, \$795 in 1981) as one quantifiable indicator. Official IBRD statistics show Thailand's GNP per capita at \$670 in 1980 and \$770 in 1981, or nearly the IDA threshold.

TABLE 1: THAILAND'S DEVELOPMENT PERFORMANCE COMPARED TO OTHER USAID RECIPIENT COUNTRIES
Source: IBRD World Development Report 1983

Indicator	Time Period	Value for Thailand	Rank Thailand vs. USAID Recipients with 1981 GNP/Cap. \$770	Rank Thailand vs. All USAID Recipients
-GNP per capita (\$)	1981	\$770	13th of 13	13th of 43
-Avg.an.growth of GNP p.c.	1960-81	4.6%	1st of 13	3rd of 43
-Size of GDP (\$)	1981	\$36.8 billion	2nd of 13	4th of 43
-Avg.an.growth rate of GDP	1970-81	7.2%	2nd of 13	5th of 43
-Avg.an.growth rate of agric.	1970-81	4.5%	2nd of 13	4th of 39
-Avg.an.growth rate of indust.	1970-81	9.9%	3rd of 13	7th of 38
-Avg.an.growth rate of services	1970-81	7.5%	2nd of 13	5th of 38
-Avg. an. rate of inflation	1970-81	10.0%	[R] 3rd of 13	17.5th of 43
-Public consumption as % of GDP	1981	12.0%	7.5th of 12	23.5th of 37
-Avg.an.growth rate of pub.consump.	1970-81	9.3%	4th of 13	9th of 34
-Private Consumpt. as % of GDP	1981	65.0%	9th of 13	33rd of 41
-Av.an.growth rate of prv.consump.	1970-81	6.2%	2.5th of 13	6.5th of 40
-Gross dom. invt. as % of GDP	1981	28.9%	3.5th of 13	10.5th of 43
-Avg.an.growth of gross dom. invt.	1970-81	7.5%	7th of 13	17th of 40
-Exports of goods & non-factor services as of % of GDP	1981	25.0%	6th of 13	16th of 41
-Value of manuf. exports (current \$)	1980	\$1.9 billion	2nd of 13	3rd of 32
-Avg.an.growth rate of exports by volume	1970-81	11.8%	2nd of 13	3rd of 39
-Avg.an.growth rate of imports by volume	1970-81	4.9%	6th of 13	13th of 37
-Energy imports as % of merch.exports	1980	44.0%	4th of 12	12th of 33
-New direct private investment	1981	\$291 million	2nd of 11	2nd of 14
-Net inflow pub. medium & long term loans	1981	\$1,235 million	1st of 13	3rd of 43
-Ext.pub.debt. outst. & disbursed as % of GNP	1981	14.4%	[R] 2nd of 13	6th of 43
-Debt service as % of GNP	1981	1.7%	[R] 2nd of 13	13th of 43
-Debt service as % of exports of goods & services	1981	6.7%	[R] 2nd of 11	12th of 33
-Gross int'l. reserves in months of imports	1981	2.7 months	3rd of 11	13th of 34
-Defense expendtr. as % of central govt. expend.	1980	20.6%	1st of 10	5th of 31
-Population (millions)	mid-1981	48.0 million	2nd of 13	5th of 43
-Avg.an.growth rate of pop.	1970-81	2.5%	[R] 4.5th of 13	10.5th of 43
-Avg.an.projected pop.growth rate	1980-2000	1.9%	[R] 1st of 13	2.5th of 43
-Crude birth rate per 1000 pop.	1981	30 per thous.	[R] 3rd of 13	4th of 43
-Crude death rate per 1000 pop.	1981	8 per thous.	[R] 5.5th of 13	7th of 43
-Life expectancy at birth in years	1981	63 years	4.5th of 13	6th of 43
-Infant mortality (age 0-1) per 1000	1981	53 per thous.	[R] 3.5th of 13	4.5th of 43
-Child death rate (age 1-4) per 1000	1981	4 per thous.	[R] 4.5th of 13	5.5th of 43
-Avg. index of food production per capita	1979-81 (1969-71 = 100)	129	1st of 13	2nd of 43
-Daily per capita calorie supply as % of req'd.	1980	104.0%	7th of 13	11th of 43
-Pop. per physician	1980	7,180	[R] 9th of 13	12th of 43
-Pop. per "nursing person"	1980	1,170	[R] 11th of 12	25th of 42
-Adult literacy	1980	86%	4th of 10	4th of 39
-% of age group enrolled in primary school	1980	96%	10th of 13	16th of 43
-% of age group enrolled in secondary school	1980	29%	10th of 13	14th of 43
-Enrolled in higher edu. as % of pop. aged 20-24	1979	7%	6th of 12	6th of 40
-Commercial energy consump.	1980	370 kg. coal equiv.	9th of 13	11th of 42
-% of pop. of working age (15-64)	1981	56%	2.5th of 13	5.5th of 43
-% of labor force in agric.	1980	76%	2nd of 13	14th of 43
-% of labor force in industry	1980	9%	12th of 13	32nd of 43
-% of labor force in services	1980	15%	12th of 13	26th of 43
-Avg.an.growth of labor force	1970-81	2.8%	3th of 13	15.5th of 43
-Project av. an. growth of labor force	1980-2000	2.3%	13th of 13	37th of 43
-Urban pop. as % of total pop.	1981	15.0%	13th of 13	32.5th of 43
-Avg. an. growth rate of urban pop.	1970-81	3.4%	12th of 13	40.5th of 43

[R] - reversed ranking

for infants and children are good even though access to medical staff and safe water is poorer than would be expected; food production per capita is highest among all groups, but nutrition is less good than would be expected.

These factors all suggest that Thailand is, for all practical purposes, entering a new era of "middle-income" status. The broad characterization of Thailand as a middle-income country also fits well with criteria established by AID in a recent draft policy paper on MIC's.¹

The implications of this for the U.S. foreign assistance program to Thailand are considerable. They suggest the need for a different type of AID strategy, both in terms of our relationship to RTG institutions and in the content of the activities we undertake.

2. Analysis of the national development process

Thailand has enjoyed an era of unprecedented growth and development over the last two decades. Over that period the Thai economy grew at an average real rate of over 7% per annum, resulting in a GDP of some \$40 billion at current prices. Simultaneously, inflation and unemployment have both generally been held to levels below 5%.

A capable national family planning program enabled the annual population growth rate to drop from more than 3% in the 1960's to less than 1.9% today. Individual personal welfare has improved by most estimates: the incidence of "poverty" nationwide is estimated to have been halved in the last twenty years.

Thailand has managed this degree of development essentially in the absence of indigenous oil production (off-shore natural gas resources first

¹AID/PPC. "AID Policy Paper: Middle-Income Countries", July, 1983.

came on stream in 1981) and on the back of widespread and highly diversified small-farm agricultural production. Rural-based agriculture (crops, livestock, fisheries, forestry) has been the primary catalyst to national economic growth. It is currently the source of some 60% of all export earnings and the primary occupation of 70% - 75% of all Thais. It is directly responsible for 21% of GDP, indirectly responsible for at least 50% of all domestic manufacturing, and conceivably is related to another 50% of combined trade and services. It should be noted (as would be expected in a situation of rapid development) that agriculture's contribution to overall GDP is diminishing relatively.¹ Indeed, the year 1982 was symbolically important in that it marked the first time in the history of the Kingdom that manufacturing officially overtook agriculture in its importance to the economy.²

a. Emerging problems and structural imbalances

Recent growth and development have evolved rapidly enough to engender a number of problems which, if not dealt with in their early stages, could prove seriously detrimental to the nation's longer-term potential. Most of these problems are rural and many are themselves interrelated. Most are already the subject of RTG concern and some, of preliminary action. All are potential real obstacles to the future economic growth and political stability of the country. Included among the most critical are:

¹"Agriculture" includes only primary production. Processing of agricultural production, including such elementary processing as rice milling, for example, is included in the "manufacturing" category.

²Manufacturing (20.7%), agriculture (20.6%), wholesale/retail trade (19.5%), services (10.1%), mining (1.8%), using current prices.

(1) Overconcentration of resources in Bangkok: One of the most striking aspects of Thai development is the excessive concentration of modern sector resources in Bangkok. With a current population estimated at 5.5 million, Bangkok is at least 50 times larger than the next largest urban grouping. This demographic primacy (one of the highest in the world) also translates into selected forms of commercial, economic, administrative, and service primacy. According to the latest (1982) official statistics, the city of Bangkok was responsible for almost one third (32.8%) of GDP. In 1979, some 43% of all manufacturing establishments were located in Bangkok (and another 27% in the neighboring Central Region). Bangkok residents have access to piped water (80%), electricity (100%) and telephones (20%) in proportions significantly higher than most other areas.

Bangkok's gradual progression into a position of primacy was mainly the result of spatial and historical imperatives. While forward-looking planners are trying to reverse this trend, it would appear that the city has taken such a preponderant role in national development that its growth is becoming institutionalized: Bangkok now is the source of power and wealth for virtually every major aspect of the economy. Businesses are reluctant, in spite of government incentives, to set up outside the Bangkok metropolitan area because their markets are essentially located there. Government officials are reluctant to work upcountry because all major decisions are centralized in Bangkok and their families are closer to good schools, medical care, and cultural stimulation. Finally, new pressures are also forming which will require even larger public investment to counter such major growing problems as flood control, traffic congestion, air pollution and slum housing.

Over the last several years the RTG has attempted to favor development outside of Bangkok. Considerable progress has been registered in developing rural support infrastructure networks in roads, rail, aviation, ports, electricity, irrigation and communications. Also, future non-Bangkok industrial growth will be actively promoted through the multi-billion dollar Eastern Seaboard Development Program. Finally, the Prime Minister has recently called for a major renewed effort at encouraging industrial development in upcountry rural areas. However, major growth outside the Bangkok area has not materialized and is possible only through a substantially greater reallocation of the nation's human, financial and other productive resources. Failure to decentralize these resources will have a major restraining effect on the long-term growth and development of virtually all upcountry (meaning essentially rural) areas.

(2) Structural or resource-based poverty:

About 90% of Thailand's poverty groups are located in rural areas, often in lowest fertility farmland, with least favorable rainfall, and lacking adequate access to markets and other employment opportunities. As much as 50% of current poverty is located in the Northeast, and another quarter in the North. Rapid national economic growth, success in restraining population growth, the extension of cash crops for export into isolated areas, and major development of basic support infrastructure have all contributed to a steady downward trend in the incidence of poverty over the last two decades.¹ As a

¹Globally, the incidence of poverty is estimated to have fallen from some 50% of the total population in 1962/63 to perhaps 25% in 1975/76, the last date of reasonably accurate statistics.

generalization, these widespread recent improvements in rural conditions have meant that the phenomenon of poverty may increasingly be considered one which is related to localized resource endowments - meaning that remaining poverty groups tend to be "harder core."

Perhaps the most significant inequality nationwide is that between urban and rural areas. This is significant since an estimated 80% of Thailand's population (or some 40 million people) live in rural areas, a percentage which demographers expect to decline only slowly over the next decade. Monetary income levels of rural groups, on the average, are perhaps 50% of median urban incomes, although regional differences may be important.¹ Life expectancy and school attendance are 10% lower, and sanitary installations and piped water 10 times less frequent in rural than in urban areas. This rural/urban dichotomy nationwide indicates the weak linkages between isolated urban economies and the surrounding rural production areas. Among urban groups income differentials are smaller, with Bangkok residents being some 30% better off monetarily than their upcountry urban colleagues. Recent data indicate a steady narrowing of that gap (Deemar, 1983).

It appears that the RTG may have gone as far as it can in reducing poverty with its existing strategy of "trickle-down" growth as supplemented by programs of redistribution and welfare. More creative structural solutions may be necessary, including:

- policy modification at the national level, placing greater focus on the institutional determinants of poverty, such as improved tax collection, selected farmgate price policies, or greater decentralization of economic, political and administrative institutions;

¹It is important to note that, when comparing urban and rural environments, monetary income alone does not reflect lower living costs nor numerous unquantifiable benefits to the rural household.

- more creative and efficient use of existing RTG delivery systems to consolidate past gains (modifying programs on the basis of past experience, maintaining infrastructure systems) as well as to extend services deeper into the hard core poverty areas in a manner which is feasible and mutually acceptable to both the national and the local leaders. Government agencies will increasingly make the difficult step from working for the rural poor to working with those groups, i.e., moving from an output to a process orientation as the primary means of effecting change at that level;
- greater use of non-governmental organizations to complement and/or substitute for government services and to increase the participation of local groups in the development process.

(3) Growing unemployment: Improved public health and income possibilities during the 1960's were primarily responsible for demographic increases of up to 3% per year in the latter part of that decade. Government family planning actions commenced almost simultaneously and were singularly successful in bringing population growth down to under 2% by the 1980's. As a result, it is estimated that the national growth rate for the category "active adults" (15-59 years of age) will remain close to 3% per year over the period 1980-90. This record high supply of labor coincides with a period of exceptionally weak demand, given the recent world economic slowdown and RTG efforts to limit growth of public sector employment. The absorption of this excess labor supply will be a central orientation of the Sixth National Plan (1987-1991).

Professional observers are not unanimous in their estimate of the rate of unemployment nationwide. While current "open" unemployment statistically represents only some 2% of the work force, underemployment may attain 15-20%, and seasonal unemployment some 20-25%. Whatever their exact percentages, all are uncomfortably high from the Thai point of view, and because of previously noted demographic and economic trends will continue to grow through this decade.

Agriculture is the primary occupation of some three-quarters of the active work force, both male and female. Current trends in Thai agriculture, especially increasing intensification and mechanization, degradation of the soil and water base, and fluctuating farmgate prices would seem to augur for a future deterioration of on-farm employment. Off-farm and selected non-farm employment is, and will continue to be, the primary compensatory outlet for labor. A recent Mission-sponsored study (IFCT, 1983) indicates that some 50% of current average total rural household income is derived from these sources. A considerable portion of future welfare and production growth at the household level will therefore depend on the availability of productive employment from these sources.

Serious unemployment and underemployment have also been registered among certain categories of the educated, who have been particularly affected by recent restrictions on growth of public sector employment. Statistics show particular employment problems for graduates in sociology, law, education and vocational studies.

The decade of the 80's will witness new and significant problems in the job sector, which will require: sustained growth in agriculture, accentuated development of non-farm and off-farm employment opportunities (especially through stimulation of new urban and industrial sources of demand), and a restructuring of sectoral priorities within higher education systems so as to enhance, rather than detract from, national development performance.

(4) Lack of arable land: Thai agriculture has been highly competitive on world markets because of low input costs per unit of yield, due in large part to a land-extensive cropping system. One study (IBRD, 1983) attributes 90% of growth in agriculture over the last 20 years to the expansion of crop areas alone.

Although variable according to locality, farmers are now reaching the limits of readily accessible, good arable land. For the first time, they are being obliged to progressively abandon traditional fallow rotations, reduce further farm expansion, and utilize increasingly marginal (poorer soil, higher slope) lands. These practices have logically led to stagnating or lower yield levels, especially in resource poor areas and in the absence of additional inputs.

To maintain a productive agricultural base farming systems must now be intensified, requiring greater use of fertilizers and better integration of competing land uses (livestock, tree crops, small ruminants, etc.). Likewise, new farm management techniques will be required if the farmer is to sustain production over the long-term and ensure proper protection of the local soil and vegetative base. Intensification will not be an easy task and will remain a vital challenge to the creativity of Thai public and private sector institutions over the course of the 1980's and beyond.

Failure to satisfactorily address this emerging problem through creative agricultural intensification, more integrated farming systems management and provision of non-farm income opportunities can be expected to have widespread repercussions, including:

- redistribution of resources away from less advantaged groups to those with higher resource endowments, as intensification is easier for the latter and growing land pressures will offer opportunities for speculators to purchase the land of the poor;
- growing land pressure will place greater stress on marginal lands and forest cover, and lead to declining productivity, particularly for poorer groups who are less able to take corrective action;

- intensification should entail increasing use of commercial energy and other inputs, implying a potential increase in imported oil as well as resulting in a relative decline in Thailand's traditional comparative advantage in agriculture;
- intensification (especially due to mechanization and reduced forest clearing), unless creatively biased toward labor inputs, could lead to growing under and unemployment among rural farm groups.

(5) Degradation of natural resources:

Thailand's land-extensive agricultural traditions and practices in fisheries, forestry and industry have "mined" the natural resource base to a point where each of these sectors exhibits longer-term, but nevertheless significant trends toward resource depletion. Forest cover has declined from 60% of total national area in 1960 to under 30% today. Problematic soil erosion (soil loss exceeding 30 tons/hectare/year) is currently officially estimated as endemic to some 30% of the Kingdom. Streams are carrying a heavy silt load into lowland irrigated areas, wetlands and storage reservoirs. Traditionally abundant fish, shell and other aquatic life have been substantially reduced in the shallow Gulf of Thailand. Soil salinization has become a major problem as soils are inadvertently mismanaged through irrigation and other modern techniques. Air/water pollution in urban areas is widespread.

Thailand's natural resource problems have not yet been successfully addressed for numerous reasons, including: 1) the complexity and newness of the problem, which necessitates innovative, often localized solutions; 2) the necessity for RTG interdepartmental cooperation and field-level decentralized coordination; 3) the fact that solutions often run contrary to short-term economic gain considerations which are pursued by individuals at the expense of the community.

Failure to begin correcting these trends over the coming decade will hinder future national development in that:

- exploitation, as opposed to management, of the nation's natural resources is at best a short-sighted approach to development, and it cannot be sustained in the longer term;
- ecological problems are but the starting points for complex interrelationships within a larger socio-economic and natural resource system, implying considerably larger damage than would be assumed from the problem alone (the problem of soil erosion, for example, is one which ultimately impacts on siltation of productive lowland paddy land, hydropower reservoirs and irrigation systems, flooding, wetland flora and fauna, as well as forest cover degradation, as upland farmers are obliged to move further into remaining forest lands);
- continued degradation of the natural resource base implies increased hardships (decreasing agricultural productivity, less fuelwood for cooking, fewer traditional off-farm opportunities) for the most impoverished groups, ultimately contributing to increased poverty and to a climate of political instability, especially in more isolated rural areas.

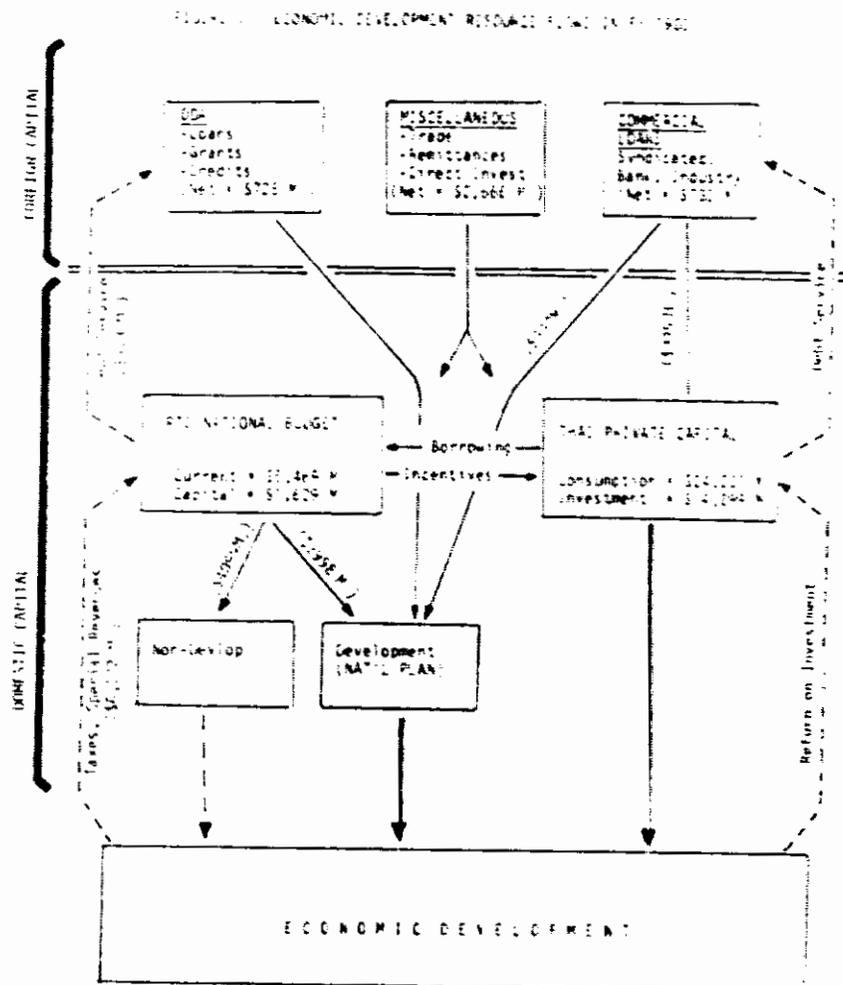
(6) Energy dependence: Thailand is, and will continue to be, vulnerable to major shifts in the world energy context. However, the current energy outlook is temporarily good with a favorable supply/price situation for imported petroleum, and with slowly growing indigenous gas production. But domestic consumption is growing as well, due to patterns of economic and individual income growth, structural changes in industrialization, and more intensive agricultural production, among others. All indications are that these consumption trends will continue.

It can be expected that energy will remain a major potential problem over the course of the next decade. It will represent both a major drain on foreign exchange reserves (\$2.6 billion in 1982) and a primary cause of chronic balance of trade deficits (31% of the total value of imports in 1982). The RTG cannot afford to relax its forward planning in energy conservation, including proper pricing policies, alternative energy development and selected educational, advisory and regulatory measures. Finally, greater attention should be given to rural fuelwood energy, which has

become increasingly rare in recent years due to the dwindling size of forest cover. Significant improvements in this area are closely linked to major changes in forestry and land use policies.

(7) Macro-economic stress: Overarching all domestic initiatives are a number of basic macro-economic concerns which are critical to the proper flow of capital resources to the development system. They are summarized below under the broad headings of limitations on government expenditures, external debt and economic vulnerability.

- Limitations on government expenditures: Figure 1 provides a simplified illustration of the total system of capital resource mobilization (foreign and domestic) which was necessary to sustain national economic development in FY 1982.



Public sector resources are essentially those provided in the Thai national budget, with the notable exception of foreign grants and loans, both ODA and commercial. Table 2 provides summary data on recent RTG budget expenditures, revenues and deficits.

Table 2: RTG Budget patterns

<u>Fiscal Year</u>	<u>Expenditures (\$ Million)</u>	<u>Revenues (\$ Million)</u>	<u>Deficit (\$ Million)</u>
1984 (est)	8,466	7,055	1,411
1983 (est)	7,804	6,658	1,146
1982 (est)	7,098	6,172	926
1981	5,841	5,022	819
1980	5,055	4,213	842

Latest current budget expenditures (FY 83) by functional classification include education (21.0%), defense (20.0%), economic services (19.1%), and debt service (15.3%). Four ministries (Defense, Education, Finance and Interior) receive almost two-thirds of the total. The Ministry of Agriculture and Cooperatives, which includes many of the departments of prime interest to current USAID operations, was fifth in size in FY 1983 with an allocation of \$655 million, or 8.5% of the budget total. In line with its policy of budgetary restraint, the RTG has held budget increases to levels just over inflation in recent years, although recurrent expenditures (especially debt service payments and salaries) have increased more rapidly than investment.

Total revenues in FY 83 were drawn primarily from taxes (89%). Both revenues and taxes, taken as a percent of GDP (13% and 12% respectively) have basically stagnated at this level for the last decade. Major tax classifications in 1983 included business taxes (21.9% of total taxes), import duties (21.7%), corporate income tax (13.7%) and personal income tax (10.4%). Growth in RTG expenditures has not been matched by similar growth in revenues

and fairly large budgetary deficits have become chronic (see Table 2). Budget deficits are covered essentially by domestic borrowing (92% of total deficit coverage in FY 83).

Overall expenditures by the RTG in excess of domestic resource availability have had an impact on inflation, the rate of private business investment, and, in the medium-term, may have an impact on growth. The Mission's review of Thailand's resource mobilization record for the period 1978-82 has corroborated a similar study undertaken by the IBRD on 1970-1978 data, demonstrating that the public sector, given its low propensity to save, relies heavily on foreign resources as well as scarce domestic private savings to fund its investment program. This means, most pertinently, that the RTG is competing with the private sector (especially the informal private sector) for available capital, and, secondarily that it may run a long term risk of exceeding its foreign debt service capacity. While investment is necessary to the growth and transformation of the economy, in many areas RTG investment levels are too high, misallocated, or both.

It would seem generally appropriate that the Royal Thai Government continue to restrain further expansion of public expenditures. The fact that foreign ODA and commercial borrowing do not figure in RTG budget planning further masks the seriousness of the expenditure problem.¹ Finally, it should be remembered that recurrent expenditures are growing disproportionately, implying a reduced RTG capacity to undertake productive investment.

¹Since Thailand only began large foreign borrowing in the late 1970's, current budget deficits do not yet fully reflect the burden on government resources caused by this form of development financing.

Major new RTG investments, such as the Eastern Seaboard Program, must be made with particular care. The key point is that RTG expenditures are already stretched to their "reasonable" limits--meaning that either the government needs to carefully reformulate its developmental role (vis-a-vis the private sector for example), or, do things better within existing budget constraints -- or both.

- Economic Vulnerability - One of the most salient characteristics of the Thai economy and one of the primary determinants of future growth is its linkages to international labor, capital, and commodity markets. The value of international trade in 1982 was \$15.5 billion, representing a surprisingly high 42% of total GDP, and a majority of manufactured goods circulating within the domestic economy are either import products or have a high import content. Through evolving patterns of interdependence, the growth prospects of Thailand remain very much tied to world economic performance, especially that of the industrialized market countries. While the direction of trade is fairly diversified, the two countries of Japan and the United States still represent almost one-third of total trade.¹ Structural, economic or other modifications to the trade posture of a small number of trade partners could have a major negative impact on Thai growth.²

¹Key trade partners in 1982: Japan (\$2,958 M.), USA (\$2,021 M.), Saudi Arabia (\$1,443 M.), Singapore (\$1,049 M.), total trade (\$15,494 M.)

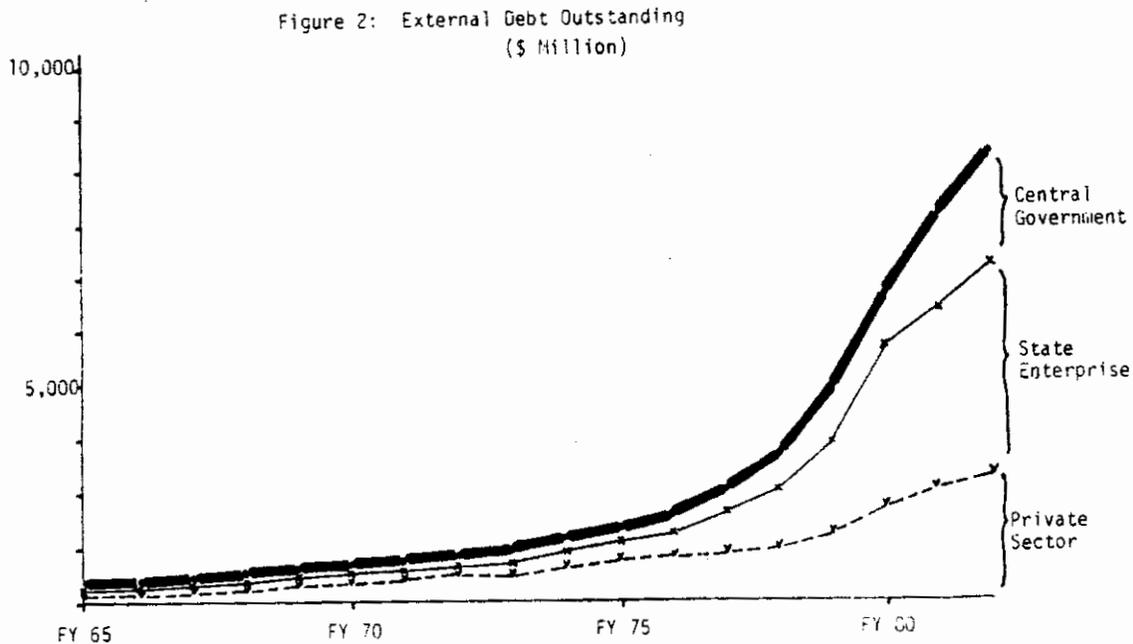
²This could, of course, be positive as well. If, for example, Japan liberalized its current agricultural import policy, it could become a major client for Thai rice, meat or other agricultural products.

Thailand has committed itself to an export-led economic policy for the future, and will, as a consequence, further reinforce the linkages between domestic and international growth. Such a policy is intended to permit a faster and more diversified growth than if reliance were on domestic consumption alone and, obviously, will be a major element of RTG attempts to redress its large and growing balance of trade deficit (\$1.6 billion in 1982). The upstream and downstream impacts of an export-led policy are multiple, however, and merit the careful attention of numerous RTG policy and operational agencies.

Possible negative consequences of such a policy could realistically include: (a) large, new public investments to promote exports, (such as the Eastern Seaboard Program) adversely affect the budget deficit and external debt positions, as well as indirectly affect net national income distribution and employment by drawing off large amounts of limited public resources from other, broader-based RTG programs; (b) a small number of influential groups who control the export sector will disproportionately benefit from increasing concentrations of land and other productive resources; (c) new pressures on land reinforce the natural resource/poverty cycle described previously.

- External Debt - Related to the above, another form of economic vulnerability is the growing problem of external debt. The size of overall foreign capital resource inflows is substantial, and, as is noted

in Figure 2, recent increases in foreign borrowing are major. This increased dependence on foreign capital has essentially been due to RTG attempts to maintain high levels of domestic growth through the difficult post-oil crisis period, especially through expansion of basic support infrastructure. Private sector borrowing followed the public sector lead.



Latest (1983) figures indicate an overall debt service to export ratio of 17%, of which 9% was in the public sector and 8% in the private sector. This is a domestic issue as the legal ceiling for public debt has been established since 1977 at 9% by Cabinet resolution. Recent analysis by the Bank of Thailand suggests that the 9% barrier will be broken this year and should stabilize a few points higher (some sources question this latter conclusion, however). Thailand's previous conservatism in foreign borrowing has permitted temporary increases in foreign borrowing without necessarily jeopardizing the larger economic

picture. Nevertheless, the evolving debt situation dictates prudence in future public borrowing. This is particularly true for commercial borrowing which is substantially more expensive than ODA. In this respect, it would behoove the RTG to develop policies which demonstrate preference for "softer" loans (measured by the "grant content" yardstick).¹

b) Future growth and development

Thailand has progressed steadily since World War II up to the present era of modest agricultural intensification and nascent industrialization. During this timeframe the Kingdom has increasingly come to recognize the key and growing role of the private sector in overall development.

Success in recent national development has however also paradoxically set the stage for the problems to be found in the more dynamic and complex Thailand of the 1980's. The era of "easy" growth now belongs to history. The Thai, from both the public and private sectors, are beginning to grapple with unprecedented competition for land, continuing population pressures, unemployment, and degradation of the natural resource base, as well as fewer export options in a competitive and substantially slower world economy. This new, more difficult decade will most demonstrably impact on the poorer (generally rural) segments of Thai society, who, using commonly accepted definitions, still represent a politically relevant mass of some 12 - 15 million people.

¹ Current "grant element" terms of USAID loans to Thailand are estimated at 71%, Japan at 64%, ADB at 34%, and IBRD at 33%.

The decade of the 1980's will be primarily a period of structural stress and the previously noted emerging problems could be precursors to potential structural failures. Some cross-cutting themes have already been mentioned: increased agricultural productivity requires intensification, itself linked to more efficient extension, creative research and proper price policies; reversal of natural resource degradation trends necessitates revised land policies (both national and individual), new environmental monitoring systems, managed intensification of land use, appropriate energy policies, and industrial regulations; improved government management requires a decentralization of delivery structures, greater sensitivity to locally-adapted techniques, increased interdepartmental cooperation, and creative integration of programs into the rural planning process; fostering of private sector development necessitates improved public/private sector cooperation, decentralization of the revenue and power base, critical examination of the role of state enterprises, and appropriate tax and incentive policies consistent with the national welfare; reduced un- and underemployment requires expanded rural investment, improved incentives and collaboration between the public and private sectors, and the application of new technologies. Finally, and importantly, these and other new critical themes must be met essentially within the limitations of existing RTG human and financial resource levels.

From the Mission perspective (and critical to its future strategy), the maintenance of broad-based rural growth and development will be essential throughout the 1980's. As with Taiwan in the 1950's, Thailand must increasingly support the balanced decentralization of private sector production and government services deeper into rural areas. Because of the

historic sensitivity of rural Thai to market considerations, the Mission concludes that a more productive orientation of resources (especially in lesser developed areas) will be toward enhancement of opportunities for agricultural and non-farm production rather than attempting to force production increases in the absence of an appropriate market. Better prices and greater demand for production will increase employment opportunities, improve revenue (both on and off-farm) and turn the farmer rather than the central government into the principal agent for rural development programs.

B. AID in Thailand

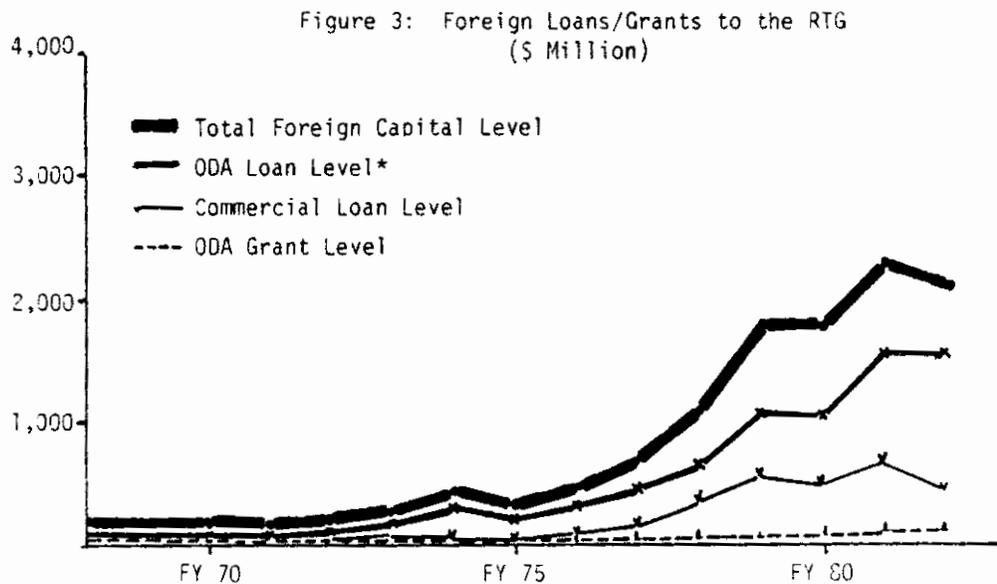
1. AID as part of total foreign donor flows

Foreign official development assistance (ODA) is and will remain an important component of the total economic development process in Thailand. Public sector institutions (central government and state enterprise) are the direct beneficiaries, but clearly the private sector is impacted upon as well. ODA is important because it is a major source of external capital (some 18% of total net foreign capital inflows in FY 82) and because it represents a key source of direct development funding.¹ Because of recent disproportionate increases in the national debt burden and problems with domestic resource mobilization, it can be assumed that ODA will remain a preferential form of national development financing for the foreseeable future.

¹In FY 82, Thai budget resources allocated to "development" were \$3.0 billion, whereas ODA resources amounted to \$1.3 billion, and foreign commercial borrowing some \$400 million. Respective shares of development funding from these three sources are therefore estimated at 64%, 28% and 9%, respectively.

a) Evolution of ODA

Figure 3 illustrates general trends in RTG foreign borrowing since 1968. Total ODA was kept extremely modest through the mid-1970's, (\$100-150 million range) and was globally constituted of 40% grant and 60% concessional loan assistance. AID contributed the majority (some 75%) of ODA grants and IBRD the majority (some 60%) of ODA loans over that period. Following on the heels of the 1973-74 oil crisis and particularly with the Fourth (FY 77-81) and Fifth (FY 82-86) National Plan periods, borrowing from both ODA and commercial sources mushroomed. Total government ODA borrowing reached \$1.1 billion¹ by FY 82 and commercial borrowing over \$400 million.



*ODA loan levels noted here also include defense loans and exim-type credits.

¹Ministry of Finance records for Thai FY 82. Does not include \$127 million of defense loans, nor \$324 million of Exim credits.

ODA grants to the RTG in that same year were \$160 million, indicating that total ODA obligations for FY 82 equaled some \$1.3 billion. Of this total, the IBRD accounted for 38%, Japan (grant and loan) 33%, and ADB for 18%, followed far behind by AID (grant and loan) at under 3%, as well as numerous other small bilateral and multilateral donors. As in the 1960's and early 70's, the IBRD's traditional position as largest ODA lender has continued through 1982 (43%)¹, but Japan has since overtaken AID as largest grantee (51%)².

b) Use of ODA

The Mission reviewed ODA use patterns from official RTG sources for the period 1961-81, and then undertook a similar independent survey of the more recent 1981-83 timeframe from individual donor records.³ While the former contained considerable historical information, the latter was particularly useful in demonstrating latest current trends and has been summarized in Table 3, attached.

Not surprisingly, ODA grant funding has been utilized by the RTG primarily for training and technical assistance. Key sectors for grant investment have traditionally included social development,⁴ agriculture, education, and public health, in that order, although most recent trends demonstrate heaviest emphasis in agriculture and education. ODA loan financing has been generally utilized for commodities, construction and services in the infrastructure sub-sectors of energy, transportation/communications, agriculture (emphasis on irrigation), and public utilities. With much of Thailand's basic infrastructure in place, however, there has been

¹Versus Japan (30%), ADB (20%) and AID (2%).

²Versus AID (10%), EEC (10%) and UN (8%).

³For detailed information on 1961-81 ODA patterns, see Mission Basic Data Memo entitled "Foreign Capital Flows", dated October 11, 1983.

⁴Includes public administration and security.

a noticeable redirection of ODA loans into agriculture, heavy industry and a wide range of other concerns.

On an individual donor basis, Japan and the ADB have historically focussed on energy and heavy infrastructure (roads, public utilities, industry), whereas IBRD lending has been somewhat broader, especially in agriculture and education. All three of these key donors have recently begun branching out into the study of, and investment in, numerous other sectors.

Geographically, distribution of funding by broad region over the last decade has remained remarkably close to percentages noted in Table 3. Despite general donor intentions to the contrary, aggregate lending would still appear to go primarily to the broadly defined Center Region¹ (48%), with the remaining half split up among the North, Northeast and South (16%, 15% and 21% respectively).² This apparent contradiction is largely attributed to the heavy skewing of Japanese aid to the Center Region (67%), itself due to the fairly rare but disproportionately large contributions of ODA to selected major infrastructure there (e.g., Japanese loans of \$130 million and \$100 million to develop the Bangkok airport and Bangkok elevated expressway, respectively). Within regions, Table 3 shows that energy and agriculture are the two primary ODA investment options in the North and the South, and that transportation/communications and agriculture predominate in the Northeast and Center.

¹Includes Bangkok, Center, East and West.

²Distribution should improve somewhat if remaining donors were included in Table 3.

Finally, Table 3 shows that average total ODA over the Thai FY 81-83 period varies somewhat from figures presented earlier for FY 82. Average annual ODA for the FY 81-83 timeframe was IBRD (\$505M), Japan (\$355M), ADB (\$172M), and AID (\$31M).¹

c. ODA projections

While admittedly difficult, it is both useful and possible to attempt some limited forecasting of future flows of ODA to Thailand. Based on discussions with individual donors, ODA levels are planned to continue to grow over the CDSS timeframe. Despite donor intentions, however, obligation levels could actually decline, especially given the recent firmer stand taken by the RTG in accepting foreign loan obligations, both commercial and concessional. RTG policy has become increasingly restrictive in terms of using ODA loans for technical assistance, training or research, and the RTG is more aggressively asserting its preferences to individual donors on the acceptability of specific loan proposals.

World Bank: As now articulated, future IBRD assistance to Thailand will continue to be linked to the basic objectives of the Fifth National Plan, most particularly, 1) the long-term issues of poverty alleviation, promotion of employment and reduction of income disparities, and 2) the medium-term issue of restructuring the development of the industrial sector (e.g. Eastern Seaboard), promotion of domestic energy conservation/development, increased public resource mobilization and improved institutional capacity in the public

¹It should be noted, for the record, that donor internal statistics will differ from these levels because of alternative fiscal years and accounting practices.

sector.¹ An important aspect of this strategy is a shift from project-specific to sectoral lending, especially in agriculture, industry and education. Current Bank planning is for global lending to expand beyond the \$505 million/year average level noted earlier for FY 81-83, if bankable projects are identified. In this regard it is instructive to note, however, that IBRD lending for FY 84 will probably not exceed \$ 300 million.

In part due to persistent Bank emphasis, "structural adjustment" became a main theme in the Fifth Plan, and structural adjustment loans (SAL) became a key aspect of the IBRD's portfolio here. SAL I (\$150 million) and SAL II (\$175 million) have been used as a supplementary tool by the RTG to bring about more efficient reforms in mutually agreed upon selected areas, including State enterprises.

Japan: In recent years Thailand has been the world's largest recipient, on a per capita basis, of Japanese ODA. Japanese assistance is distinct from the aid provided through the other big two donors in that it is bilateral. The Japanese Government has clearly indicated that Thailand is considered vital to Japan's regional interests - politically and strategically because it is an island of free world economic development in Southeast Asia, and commercially, because Japan is Thailand's primary trade partner.

It is anticipated that bilateral Japanese aid to Thailand will grow

¹See "1982 World Bank Country Economic and Sector Work Program".

beyond its average estimated FY 81-83 level of \$355 million (official estimates are for increases of 10% per year). Since 1981, Japanese loan assistance has been oriented toward rural/agriculture development, energy, human resources, and large industry.

Asian Development Bank: ADB - RTG relationships will undertake distinctive changes over the next few years. Whereas overall levels of loan assistance (average \$172 million for FY 81-83) will probably grow only slowly, the nature of lending will shift. Greater attempts will be made to diversify lending out of the traditional energy and transport sectors into others such as agriculture (including irrigation, livestock, fisheries, cotton, sericulture and agricultural credit) and large industry. More "sector" lending will probably be attempted instead of normal "project" lending.

Other donors: While representing perhaps less than 10% of total ODA flows, it is worth noting that several larger members of this group already foresee moderate increases in their ODA. Australia and New Zealand see Thailand as a neighbor and friend, both strategically and economically. The EEC will increase assistance through its cassava-reduction commodity agreements. The United Nations will maintain an important presence, especially since its regional ESCAP office is based in Bangkok. We expect that similar or somewhat larger levels of assistance by this group, and in highly heterogeneous, selected sub-sectors will continue.

2. AID and overall USG posture in Thailand

U.S.-Thai official relations were opened in 1833 with the signing of a treaty of Amity and Commerce. In the ensuing 151 years the two countries have established a series of important relationships spanning a wide variety of mutual interests.

In the sphere of cooperation in development, the first Economic and Technical Cooperation Agreement between the United States and Thailand was concluded in 1950. Our development assistance has consistently been closely linked to larger foreign policy objectives in the region since that time. During the 1950s technical assistance under Point Four gradually evolved into a large infrastructure program centered on transport and industry. In the 1960s and into the early 1970s, events in Vietnam and concerns with internal communist subversion led to a significant increase in U.S. assistance with counterinsurgency becoming the unifying theme of the AID program. As the Indochina conflict drew to a close, a decision was made to phase out economic assistance. Renewed concerns with Thailand's strategic importance and economic stability, however, led to a reversal of this decision. During 1978-82 the AID Mission undertook a development program based on rural poverty considerations stemming from the Congressional Mandate. A total of 24 new projects were initiated during this latest period with a focus on basic services delivery in rural areas, especially in the Northeast.

Although the U.S. development assistance program has undergone changes over time, one element of constancy and major importance has characterized past and present programs. The United States has helped finance the foreign education and training of some 11,000 Thais in various development skills. Recipients of U.S.-sponsored education and training are now to be found across the board in Thai government and non-government institutions, with many in positions of leadership. U.S. participant training has been a major vehicle for development of Thailand's human resources and further strengthens, through old ties and new, the bond between the two countries.

Other forms of U.S.-Thai cooperation have been equally prominent in the overall relationship. The maintenance of Thailand's continued economic growth, territorial integrity, and domestic stability is central to the continued stability and prosperity of Southeast Asia and constitutes a major U.S. foreign policy goal for the region. In implementing our commitment to Thai security, we have developed a close military and security assistance relationship of some \$100 million per year with Thailand, directed primarily towards modernizing the Thai Armed Forces and making them capable of meeting regional threats. This has enhanced Thai cooperation on other important U.S. policy objectives in Thailand, including narcotics control and assistance to Indochinese refugees.

3. Analysis of current AID portfolio

In light of the CDSS analysis of key determinants to growth and development, the Mission reviewed its current development portfolio for its relationship to a future middle income CDSS strategy. The conclusions were mixed.

First, it is believed that several of our current sectoral orientations, can and should furnish useful inputs toward the design and implementation of a new Mission program. These include:

- science and technology transfer: Our expected FY 84 Agricultural Technology Transfer and FY 85 S&T projects will draw on U.S. and Thai sources to break bottlenecks and expedite growth in agricultural, rural, and industrial development.
- private sector: Existing Private Sector Development and Seeds II projects will foster public/private sector cooperation and, when combined with the recent results of the now complete Rural Off-Farm Employment Project, will identify opportunities for private investment outside Bangkok.
- community management: Decentralized Development Management, Northeast Rainfed Agricultural Development and the new Rural Development Monitoring/Evaluation Projects will contribute to an enhanced understanding and future development of decentralized management and planning.

- agricultural productivity: NERAD and the Khon Kaen University Project will promote both improved and sustainable agricultural productivity through their focus on local farming systems research and development.
- population: Population Planning I and II will contribute to overall fertility reduction, itself directly related to a wide range of basic development problems.

Second, it is believed that the past Mission strategy has focussed too extensively on the direct encouragement of local production and management, especially in poorer areas, in the absence of sufficient demand (price or quantity) for the production stimulated. Mission experience in such projects as Lam Nam Oon, Land Settlements, Sericulture and Northeast Small Scale Irrigation have repeatedly shown that strong farmer participation and efficient/relevant RTG support services can only develop in a context where a strong (basically private sector) demand for agricultural and non-farm production already exists.

Third, Mission strategic emphasis on a geographic focus in the Northeast and our "hands-on" operating style in dealing directly with the rural poor have caused numerous projects to become bogged down in implementation detail. Our collective experience demonstrates that such an approach compromises Mission effectiveness in that: a) AID human and financial resources tend to be used in circumscribed, "scattered" pilot area initiatives with few real linkages to key national policies or operations, and in arenas where critical foreign analysis is difficult and not wholeheartedly solicited; b) it necessitates a demand for major Mission management time, and this when reductions, rather than increases, in staff levels are envisaged; c) it places undue limitations on AID flexibility to deal effectively with new problems and has diffused resources in a manner which makes the AID program increasingly peripheral to key middle-income constraints.

These aspects of current AID operations will all be dealt with in this paper. They point to, most pertinently, various degrees of withdrawal from a hands-on strategy to one which focusses more on longer-term institutional and policy constraints, the canceling of an exclusive geographic focus in the Northeast, and a new, more collaborative program and operations working style.

PART II: PROGRAM ALTERNATIVES AND STRATEGY

A. Determinants of a Generalized Middle Income Strategy

The Mission first thought through the fundamental elements of a generalized middle income strategy and then its application to Thailand prior to arriving at the FY 1986-90 program proposal presented in this CDSS. The determinants of a generalized strategy identified include:

- As government interventions in production begin to reach upper limits in productive investment and complexity, MIC status implies a change in the roles of government and the private sector with an increasingly greater reliance on the private sector as the determinant of sustained growth and development. This will require government to reformulate its posture vis-a-vis the private sector, notably to that of creating a policy and infrastructure environment which fosters successful private initiatives.
- Entry into the middle income ranks signals notable progress in moving from a subsistence to a modern, competitive production mode. Scientific and technological advancement is no longer a future objective but an immediate need. Since the economics of most developing states are essentially built around agricultural and selected forms of rural production, a redirection to agribusiness and rural industrialization (and the technology this implies) are necessary intermediate steps in the achievement of self-sustained growth.
- In general, movement into MIC status suggests the need for a greater decentralization of public as well as private development structures. Self-sustaining, equitable growth necessitates eventual broad-based national participation in the economic system and national polity.
- The enhanced institutional, human and financial capabilities of a MIC are an indication of the country's policy-making capacities and its

ability to exert sovereignty over the development process underway in the country. AID's role then becomes increasingly one of buttressing the host government's own priorities and programs. The existence of a strong host country skills and institutional base also calls for a significant shift in emphasis from AID-managed to host government administered programs/projects.

- Achievement of MIC status implies attainment of self-sustaining growth at some future point. Present and future AID programs in MIC countries need to be oriented toward building a strong, cooperative relationship in preparing for the day when AID concessional assistance plays no role.
- AID policy requires a hardening of concessional terms as countries move up the middle income ladder. This means increasing dependence on loan funding in AID assistance programs and a decline in the proportion of grant aid. Implied in a transition from grant to loan financing is a greater voice by the borrowing country in the use of development funds.
- The achievement of MIC levels of human resource development means that large technical assistance packages will become increasingly outmoded over time. As AID moves toward more direct support of host government designed programs and extensive use of loan financing, both factors will tend to produce a reduced and more focused use of expatriate consultants.

Using this framework for reference, Thailand's transition from low to middle income status will require attendant changes in AID's strategy toward the Kingdom.

B. Determinants of a Strategy Specific to Thailand

The formulation of a middle income strategy for Thailand has taken into consideration several determinants:

- Though overall development indicators demonstrate Thailand's very substantial development accomplishments, both in terms of gross national product and quality of life indicators of the average Thai, the macro-indicators mask a number of issues of a structural and institutional nature. Several of these, particularly those related to rural development, have the potential to seriously inhibit future economic progress and possibly to disrupt Thailand's existing social stability. Some of these issues concern organizational changes in the public and private sectors which will be necessary to build a more

diversified, internationally competitive economy. Others concern the maintenance of sufficient progress and a voice for all levels of Thai society so that social cohesion can be maintained in a period of rapid economic change.

- AID currently accounts for less than 3% of total foreign development assistance to Thailand and other donors are now moving into virtually every sector in which AID has traditionally played a major role. The economic contribution of a \$30-plus million annual AID program in Thailand (less than one-tenth of one percent of GDP) is a negligible factor in sustaining Thailand's economic growth. Judged solely on the basis of resource flows, the U.S. has now become a "minor" (although not inconsequential) actor in Thai development and must reorganize its program objectives and content appropriately. Thus, the USAID program must be inexorably linked with the next five year plan, which basically coincides with the CDSS time frame, to ensure relevance.
- The U.S. and Thailand have over the years established a relationship highly valued by both. It is essentially a consequence of the major U.S. role in economic and military assistance played between the 1950's and the early 1970's. A large number of now-senior Thai officials and intellectuals were trained in the U.S. and understand and share our approaches to development. The U.S. development assistance program remains an important and valued source of collaboration between the U.S. and Thailand, the continuation of which would serve the interests of both.
- Redirecting the AID strategy is complicated by the need to shift from a mixed loan/grant to a substantially loan-financed program in line with AID/W strategy for Asia. This transition will be difficult due to existing Thai policies governing the use of foreign loans (infrastructure focus) and the type of policy and institutional goals AID generally wishes to pursue.

C. Basic Strategy Options

The Mission examined a number of broad options in its formulation of a revised strategy for Thailand:

1. To gradually phase down U.S. development assistance activities over the next several years in anticipation of an eventual termination of the AID program. This would be consistent with the level of development which Thailand is achieving and with the reality that, as a portion of total resource flows, our financial contribution to Thailand's development is

minimal. It would, however, result in weakening an important and mutually beneficial linkage between the two countries, possibly weakening the overall U.S. relationship with Thailand in the areas of mutual security, commerce, and trade, narcotics and refugees. It would also ignore Thailand's need for addressing a number of serious emerging problems of an institutional, policy, and structural nature, and the possible major impacts they may have on national stability and growth.

2. To continue themes of the current program and existing modes of operation. This would mean continuing the existing regional emphasis with a hands-on rural poverty focus. Traditional AID programming concepts would be retained and the existing donor-client relationship maintained. This option would essentially ignore the changing nature of the problems facing Thailand, the implications of Thailand's increasing ability to manage its own poverty program, and advances in the sophistication and competence of our Thai counterparts. It also would perpetuate the kinds of implementation problems we have with our current portfolio, as well as preclude strong linkages to policy considerations in areas deemed important by the Mission and Thai counterparts.

3. To work toward a fundamentally redefined relationship in the area of development cooperation, involving a collaborative and balanced exchange of information and technical knowledge, and concentrating on emerging problem areas. This option is consistent with AID's limited resource availabilities, involves a mature partnership and offers the greatest prospect of maintaining and even strengthening technical, intellectual, political and economic relationships between the two countries. This option holds the greatest promise for a successful future program in Thailand.

D. The Strategy

The Mission defines the long term strategic objective as the establishment of a more collaborative relationship between the U.S. and Thailand in the area of development cooperation which goes beyond the traditional donor-client relationship, and which is consistent with Thailand's emerging status as a middle income country. The substance of this relationship will focus on issues of a policy and institutional nature which bear on the productive, equitable, and sustainable development of Thailand's rural resources. The middle income strategy proposed here shifts the focus of AID's program from a regional poverty perspective to one more capable of accommodating evolutionary changes in Thailand's growth patterns and needs. It also provides an opportunity to plan--and prepare for--a future relationship with a wealthier Thailand in which concessional assistance no longer has a role but strong economic cooperation continues.

The Mission believes that the future relationship may evolve into a bi-national commission or council staffed by nationals of the two countries. For the moment it is anticipated that steps taken during the CDSS period will be directed essentially toward more modest forms of collaborative management as well as experimentation with relatively more flexible programming mechanisms.

1. The transition

The path for a new middle income strategy and program structure in Thailand has already been cleared. During FY 1986, only one project not directly related to this strategy will require funding. The total amount needed is \$3 million, beyond which there is no project mortgage. Thus, an entirely new program can be financed during FY 1986-90 which is consistent with the priorities to be established by the Sixth National Plan.

2. Program proposal

The Mission program will be built around four basic elements: (a) a sector loan program, (b) a fund for emerging problems in development (grant), (c) a fund to support NGO development (grant), and (d) increased use of specialized centrally funded AID/W programs, including those in population.

a) Loan program. In order to focus our resources in an area of high RTG priority and to take advantage of AID's unique opportunities to have a positive impact on Thai policies and institutions, we propose one sector loan in rural industries and employment for the entire period of the CDSS.

Our own analysis has shown both lagging rural production and growing un- and underemployment as among the most serious political and economic problems which Thailand will be facing during the next decade. This in itself suggests the appropriateness of a concentrated program in this area. Perhaps more importantly, these two topics are both RTG priority concerns and will be central themes of the Sixth National Plan (which has a timeframe approximately the same as this CDSS). This is key to the Mission objective of developing a new, more mature relationship with Thailand as a MIC, and which requires a greater realigning of our priorities with their own. It is also an area where no major focused foreign donor assistance (with the exception of the Eastern Seaboard Development Program) has been provided to date, and is the only sector identified by NESDB as a priority for AID loan funding. Conceptually, it is anticipated that this program will require particular analysis of, and support in, the following key areas: policy constraints, the role of the public and private sectors, investment opportunities, credit, science and technology, and, underlying all of these issues, employment.

In directing AID resources toward a rural industries and employment program, fundamental objectives will be to increase rural employment, to increase the value added of existing rural production, and to foster the improved welfare of all groups (rural and urban) outside the Bangkok metropolitan area. Particular attention will be given to activities located in less developed areas, which have broad impact, and which remove or relieve the policy and institutional constraints to achieving these objectives.

b) Jointly managed fund for emerging problems of development.

Part I has outlined a number of problems of particular importance to the future of Thai growth and development. In order to provide responsive and timely funding for these and other development problems the Emerging Problems of Development (EPD II) Project will be formulated. It will be future-oriented, jointly programmed, and administered at a policy instead of technical level. This activity will be funded at a level of some \$4-5 million in grant funds annually. The grant will have a wide variety of uses, from the funding of short-term consultants to the financing of collaborative research ventures between Thai and American universities on topics of particular priority concern, including agricultural research, soil erosion and natural resource monitoring, fuelwood, tropical medicine and contraception. Other possible pursuits include grants to leadership groups to facilitate policy dialogue, policy studies, development seminars, as well as a broad range of technical assistance and training needs centered on program as opposed to project requirements. Examples of the topics that might be addressed include: alternative approaches to national budgetary reform; decentralization, implications of the closing land frontier, women in development, and creation of policy settings which would enable greater

engagement of the Thai private sector in development, (e.g. current public service functions, such as health delivery and family planning). We view EPD II as a complement to substantial centrally-funded activities, which the Mission intends to further encourage as a means for technology transfer and the development of long-term linkages between the U.S. and Thailand.

c) Grant fund to support NGO development. Although there are thousands of non-profit associations in Thailand, a recent USAID survey identified only 80 Thai non-profit institutions which have a developmental focus. Beginning in FY 1985 and throughout the CDSS period, AID will utilize a Mission managed grant fund totaling approximately \$1 million annually to encourage and support NGO sponsored development activities. Initially, U.S. NGO's are expected to absorb the bulk of funding available. In the out years, AID financing will increasingly shift to indigenous NGO's. Substantial attention will be given to approaching NGO assistance within the context of broader Mission program strategies, with intent to strengthen NGO capacities and roles within Thailand's larger development effort.

The bulk of resources directed to the NGO's would be for proposals which: a) contribute to development of the NGO's capacity to deal with priority emerging problems on a significant scale; b) develop a strengthened role for private initiative within the broader framework of Thai development policy--quite possibly involving some explicit collaboration between the NGO and one or more public agencies; and c) offer realistic prospects of leading to self-sustaining, self-financing development action.

d) Centrally-funded programs: The current Science and Technology Bureau centrally-funded programs in agriculture and population (e.g., Peanut Cooperative Research Support, Biological Nitrogen Fixation

Center, and programs of the Population Council, Family Health International, and Family Planning International Assistance) are particularly germane to Thailand. They bring to bear the best of U.S. scientific and technical knowledge in areas of importance. In addition, the linkages established between U.S. and Thai institutions through such programs are the kinds that can endure in the future without direct A.I.D. assistance. Particular attention will be given to population, an area that will require constant surveillance to ensure continued decline in the growth rate, and may well call for more highly targeted specialized assistance.

PART III - RESOURCE REQUIREMENTS

Based on the AAPL funding levels furnished by AID/W, we foresee a budget breakdown for the future as follows:

A. Functional Account G/L Levels

<u>Functional Account</u>	<u>Approved Assistance Planning Level</u>					
	(\$000)					
	<u>1985</u>	<u>1986</u>	<u>1987</u>	<u>1988</u>	<u>1989</u>	<u>1990*</u>
AGR/RURAL DEV/NUTRITION	15.6	19	31	32	35	38
POPULATION/HEALTH	2.4	-	-	-	-	-
EDUC/HUMAN RESOURCES	-	-	-	-	-	-
SPECIAL DEVELOPMENT	<u>13.0</u>	<u>14</u>	<u>4</u>	<u>5</u>	<u>5</u>	<u>5</u>
DA TOTALS	31.0	33	35	37	40	43
ESF TOTALS	5.0					

*Estimate

B. Program Budget

	(\$000)					
	<u>85</u>	<u>86</u>	<u>87</u>	<u>88</u>	<u>89</u>	<u>90</u>
Pipeline Projects	2	3	-	-	-	-
Emerging Problems of Development II	3	4	4	5	5	5
Rural Industries and Employment Loan	15	15	30	31	34	37
S&T Loan	10	10	-	-	-	-
NGO Grants	1	1	1	1	1	1
	<u>31</u>	<u>33</u>	<u>35</u>	<u>37</u>	<u>40</u>	<u>43</u>

Depending upon the pace of project design it is possible to fund most, if not all, of the proposed new program initiatives beginning in FY 1985.

C. Staffing Requirements

We have worked out a preliminary mix of skills, Mission organization and structure essential to implement the strategy proposed in this document. In line with the Asia Bureau's regional strategy, the Mission anticipates a gradual reduction in USDH requirements from 22 positions at present to approximately 16 by FY 1989. An outline of the proposed Mission restructuring is described in Part IV.

PART IV - STRATEGY IMPLEMENTATION

In order to implement the strategic changes proposed in this CDSS and to achieve our objective of a new, more mature relationship which reflects Thailand's status as a MIC, the Mission will need to take a number of actions. The first of these is to undertake a series of carefully targeted studies. In close collaboration with Thai researchers and policymakers, we will: (a) pursue studies to identify specific areas of the RTG's rural industries and employment program which will be supported by AID, and (b) lay out realistic evaluation benchmarks for the CDSS period. To move into the proposed strategy, the Mission also plans to make a number of adjustments in how we do our business. This will be done in part by organizational and

staffing changes, in part by procedural changes, and in part by drawing more fully on centrally funded technical resources. These actions are described more fully below.

A. Analytical Requirements

Supplementary study and analysis will be required in order to further define the strategic and operational implications of the CDSS program proposals. Careful forward planning will be particularly necessary for successful development of the CDSS loan proposal, built around the theme of "rural industries and employment." Prior to the May, 1984 Annual Budget Submission, the study series will focus on the three most promising development aspects of that theme: public and private sector cooperation, investment opportunities and credit, and science and technology. In studying the Mission's program in these areas, our underlying objective will be the creation of new opportunities for rural farm and non-farm production in a manner which promotes greater employment, increases the value added of existing rural production, creates new production possibilities, and fosters improved welfare of all groups outside the Bangkok metropolitan area. Particular attention will be paid to less developed areas, broad impact, and policy and institutional constraints.

1. Loan Program

Public and private sector cooperation: This study will undertake a policy analysis of the government's role in promoting the balanced expansion of the private sector in rural areas. Support programs for decentralizing decision-making processes which affect the private sector will be examined, including strengthening representative rural private sector organizations (chambers of commerce, financial institutions, industry, and the Joint Committee for Public/Private Sector Cooperation).

Investment opportunities and credit: Further constraints to the expansion of small rural industry are the lack of commercial credit for small enterprises because of assumed high risks and the virtual absence of mechanisms to enable the formulation and appraisal of investment opportunities. If risks can be minimized and reasonable projects formulated, resources will flow to rural areas.

Among the areas to be investigated during the studies series are: support for credit for small industries, including specialized support for institutional credit to women; expansion of the Department of Industrial Promotion's investment opportunities program; increasing the capability of commercial banks to develop and appraise projects; establishment of a program to minimize the risks on loans to small industries; dissemination of information on local investment opportunities and encouraging their start up/expansion; and establishment of rural business brokering and consulting organizations.

Science and Technology: Thai leaders recognize the growing need and potential for incorporating science and technology into future stages of national development, bringing about new and expanded industries, or industries which have more uniqueness or comparative advantage due to their scientific or technological bases. For the long term the continued viability of Thailand's industry and the optimization of local comparative advantage requires the local capability to adapt and disseminate modern scientific and technological innovations. This capability now is significantly underdeveloped although the need is clearly recognized.

Among the S&T activities to be reviewed are: mobilization of a network of former U.S. trained M.S. and Ph.D. professionals and decision-makers in the application of S&T; evaluation of the structure of the research and development institutes and organizations; evaluation of science and technology development, publication and dissemination or transfer programs; creation of special centers of excellence for science based industry development and upgrading existing institutions through training, workshops, demonstrations, special equipment procurement; reconnaissance of resources and organization of a strategic plan for use of S&T to stimulate investment in rural areas.

Employment: Employment will be studied as a topic which underlies other sectoral concerns. Up-to-date disaggregated statistics on employment will be gathered from existing sources, future trends will be analyzed and key relationships established.

This study series will be undertaken by Thai analysts and institutions, and be supplemented by U.S. technical experts, as needed. While the analysis will be done during the next few months in order to define our proposed FY 1986 program in the upcoming ABS, some studies will continue through the end of the fiscal year and beyond as required. As the theme of rural industries and employment is of priority relevance to both the RTG and the international donor community in Thailand, every effort will be made to coordinate study activities and disseminate studies information. Particular care will be taken to coordinate these studies with the on-going analytical work of the World Bank locally.

2. Evaluation Plan/Benchmarks

Three projects in the existing project portfolio provide an experience base useful for the planned rural industries and employment program:

- Decentralized Development Management
- Northeast Rainfed Agricultural Development
- Private Investment in Development

As the new program is developed and implemented, we will undertake continuing reviews of these projects to help refine objectives and means of achieving them, in part to ensure their consistency with our broader

CDSS objectives. Similarly, we plan to soon undertake an evaluation of six centrally funded agricultural projects to help guide the Mission's plans for a phaseover to central funding in selected areas.

It is too early in the planning process to determine specific benchmarks for the FY 1986-90 program. We have, however, thought through in nominal fashion a number of potential benchmarks to explore in detail. As the program evolves, specific benchmarks will be incorporated into the relevant ABS Workplans. Potential benchmarks are identified below:

Public and Private Sector Cooperation

- Active cooperation in policy studies and analyses to identify regulatory practices which constrain private investment.
- Changes in government regulations, taxation, and business promotion policies.
- Establishment or strengthening of private sector organizations in rural areas and secondary cities.

Investment Opportunities and Credit

- Establishment of new private or public credit institutions and upgrading of existing institutions.
- Studies and analyses of small and medium enterprise investment opportunities and credit requirements.
- Expansion of credit for rural enterprises and special groups, including women.
- Increases in non-farm enterprises that absorb the under- and unemployed.

Science and Technology

- Linkages between science and technology and investment/employment.

- Increased rural productivity based on technological change.
- Increased institutional capacity to transfer technological and scientific knowledge.
- Direct cooperation of the private and public sectors in developing and/or adapting technologies to stimulate rural growth and employment.

Over the coming months the Mission will use the CDSS studies series to develop subgoals, to establish key benchmarks, and to organize an evaluation system to track progress.

B. Organizational/Staffing Requirements

The table shown below outlines the present/future project workload, and respective project completion dates:

AID Development Assistance Program

	<u>FY 84</u>	<u>FY 85</u>	<u>FY 86</u>	<u>FY 87</u>	<u>FY 88</u>	<u>FY 89</u>	<u>FY 90</u>
<u>Agriculture, Rural Devel & Nutr.</u>							
Rural Industrialization							
PVO Co-Financing II							
Agr Technology Transfer							(T)
Rural Development M/E							(T)
Khon Kaen University							(T)
N.E. Rainfed Agriculture							(T)
Mae Chaem Watershed							(T)
Agricultural Planning							(T)
Seed Development II							(T)
N.E. Small Scale Irrigation							(T)
Micro-Mini Hydroelectric							(T)
Private Sector Development							(T)
Decentralized Development Mgmt.							(T)
PVO Co-Financing I							(T)
Land Settlements							(T)
Lam Nam Oon							(T)
Renewable Non-Con Energy							(T)

FY 84 FY 85 FY 86 FY 87 FY 88 FY 89 FY 90

Population Planning

Population Planning II------(T)
Population Planning I------(T)

Health

Provincial Waterworks -----(T)
Rural Primary Health------(T)
Anti-Malaria------(T)

Education and Human Resource Devel

Hill Area Education------(T)

Selected Development Activities

Science and Technology -----
Emerging Problems of Develop. II -----
Emerging Problems of Develop. I------(T)

T: Terminal year.

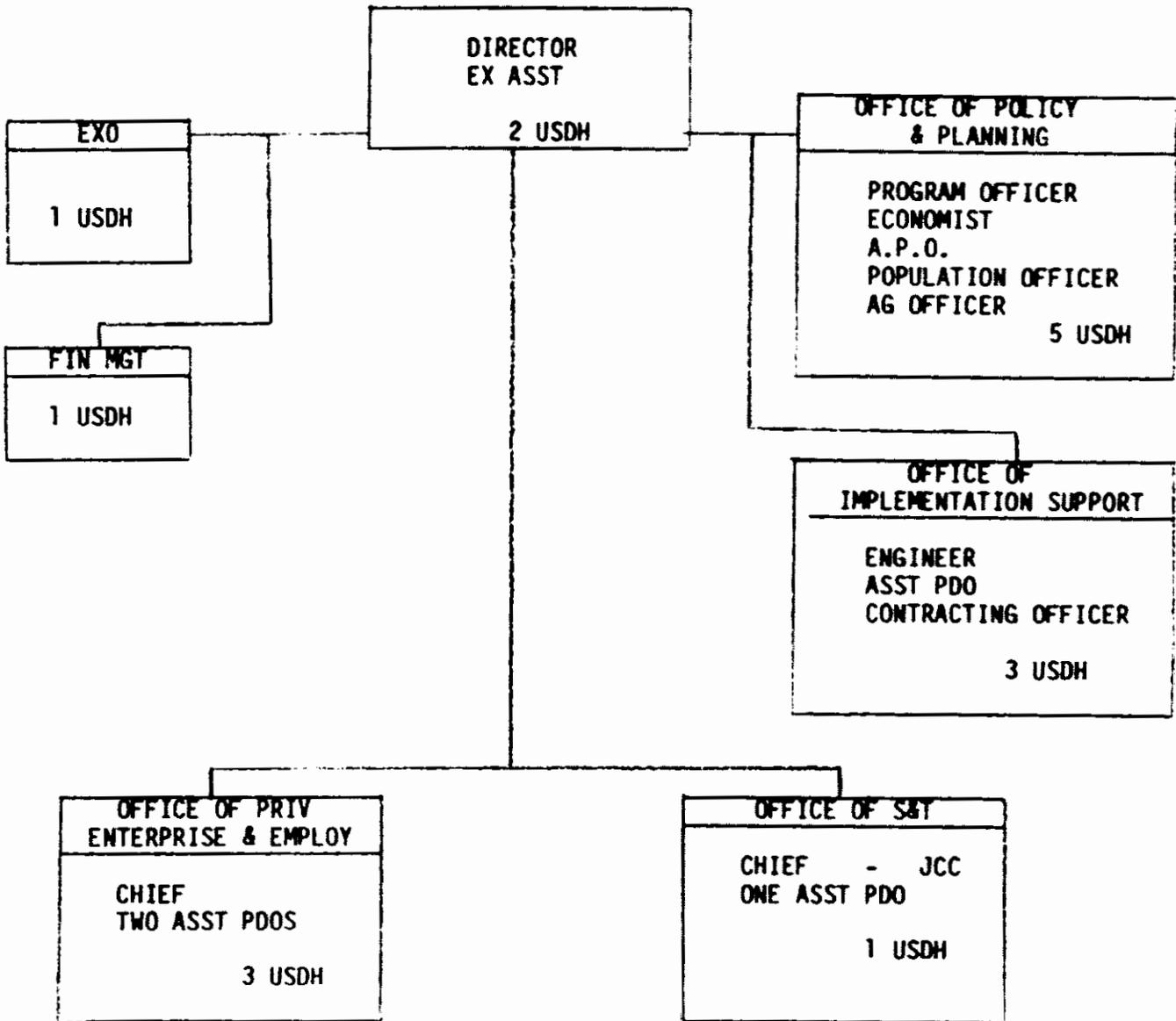
As is evident from this listing, the Mission will continue extensive agricultural, family planning and health programs through FY 1987. Throughout this period we expect to draw upon specialized expertise available through centrally-funded programs. The Mission hopes to enter into a Memorandum of Understanding with the S&T Bureau to ensure that maximum benefits are generated from these resources, particularly in the case of population. Over the long term, as the bilateral program shifts out of some sectors, we would expect to make greater use of centrally funded AID resources and expertise. This will also be a crucial element of the Agency's long-term technology transfer efforts in Thailand, since much of the highest and best technology is available through these central programs. It is also through these programs that Thailand can expand its worldwide information linkages.

In addition, the Mission's attempts to make the AID program more appropriate to Thailand's needs as a MIC clearly imply new directions in its organization and operations: its strategy dictates a new long-term collaborative relationship with Thai institutions, its resources will be focussed, and priority will be placed on addressing the newly-emerging problems of the 1980's and 1990's; its structure will be modified so as to deal with functional, rather than sectoral, problem-solving, implying enhanced analytical capacity, its systems streamlined so as to permit increasing Thai management participation, a simplified operating method (sector loans), a computerization of its financial and management systems, and an improved measurement of performance against targets; its style will become more mature, collaborative and responsive and will entail greater substantive policy dialogue.

In line with such a process of fundamental change Mission management must plan for an evolution in staffing requirements. The Mission conceives of this evolution along the following lines:

1. to reduce direct-hire staff, in line with reductions in our existing project portfolio and consolidated operations;
2. to progressively expand the role of the Mission's Thai professional staff and carefully selected U.S. contract employees; and
3. to provide a sharpened program focus that maintains current commitments but does not limit future planning to traditional fields and sectors.

By 1987/1988 we envision a complete organizational changeover to the strategy elucidated in this CDSS, and as exemplified in the diagram on the following page:



This proposed structure offers a number of advantages not normally possible within the more traditional field mission organization:

- fewer units of management;
- enhanced policy planning and analysis capability to include contract analysts in the field;
- a more efficient division of labor between project support and project officers; and
- closer integration of the policy, technical and implementation components of Mission operations.

Basic functions and organizational responsibilities an planned along the following lines:

<u>Function</u>	<u>Responsible Office</u>
1. Policy Dialogue and Programming, and Management of EPD II.	O/DIR O/PP
2. Preparation of new CDSS and definition of program in line with 7th RTG Five Year Plan.	O/DIR O/PP
3. Preparation of new program/project documents in in line with 2 above.	O/PP O/IS
4. Management of ongoing projects Rural Industries and Employment Agr Technology Transfer Rural Development M/E Khon Kaen University Science and Technology	O/PE O/ST O/PE O/PE O/IS
5. Management of Centrally Funded Projects Private Enterprise Agriculture Population Science & Technology Other	O/PE O/PP O/PP O/ST O/IS
6. Management of NGO Program	O/PP
7. Implementation Support Engineering Project Reviews and Reporting	O/IS O/IS
C. <u>PID/PP Schedule</u>	

The Mission's current project design workload will decrease dramatically by the beginning of CDSS planning period. Only three new project starts are proposed for FY 84, four in FY 85, and no further new initiatives through FY 1990. This is of major significance in terms of reduced staffing needs over the long term. Equally important in the near

term, existing staff resources can be devoted more intensively to project implementation. Listed below is the Mission's schedule for PID and PP completion:

FY 1984 Projects

<u>Title</u>	<u>PID</u>	<u>PP</u>
Provincial Waterworks	(approved)	(approved)
Agr Technology Transfer	(approved)	Feb 84
Rural Devel. Monitoring/Eval.	(approved)	Feb 84

FY 1985 Projects

PVO Co-Financing II	(approved)	Mar 84
Emerging Problems of Devel. II	Feb 84	May 84
Science & Technology	June 84	Nov 84
Rural Industries and Employment	Nov 84	Apr 85