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The Development of the Thailand Currency Crisis: A Chronological Review

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中国における貸付債権の新分類方法導入

中南米諸国の直接投資統計

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Executive Summary

This paper describes and analyzes the events that led to the currency crisis and deepening of the crisis in Thailand.

(1) Before the devaluation. Prior to the de facto devaluation (free floating) of July 2, 1997, there were three causative factors that were important. First, the general deterioration of macroeconomic fundamentals was the major reason that forced the devaluation. The growth rate of gross exports plummeted (from more than 20% to negative) from mid-1995 to 1996, and the real GDP growth rate declined in 1996. The current account deficits have remained high (8% of GDP) since 1995. A combination of high current account deficits and low growth proved to be too risky for investors. Second, the bubble burst in 1995 and 1996. Stock and land prices declined and financial institutions were beset with nonperforming loans. In particular, finance companies needed liquidity support from the central bank from the beginning of 1997. Financial fragility also rang alarms for investors. Third, with the domestic fragile situation, speculators, including hedge funds, saw their opportunity and attacked the currency which had been de facto pegged to the U.S. dollar, and the central bank defended it, spending a large amount of foreign reserves. In one week of May 1997, the central bank lost more than 15 billion dollars. However, it was in the forward (swap) market, so that the position was not disclosed until August. Devaluation was the result of essentially exhausting foreign reserves in a forward position.

(2) Devaluation and IMF package. The baht was freely floated on July 2. It was de facto devaluation, since the currency immediately depreciated by 17 percent. After one month of struggle, the Thai authorities decided to ask for IMF support. Prior to receiving an IMF package, an additional 42 finance companies were suspended. The amount of support exceeded what IMF usually allows a member country to borrow (access limit). A meeting was held in Tokyo on August 11, to put together the support package, amounting to more than 16 billion dollars, led by Japan. The IMF package of August 20 was expected to turn Thailand around.

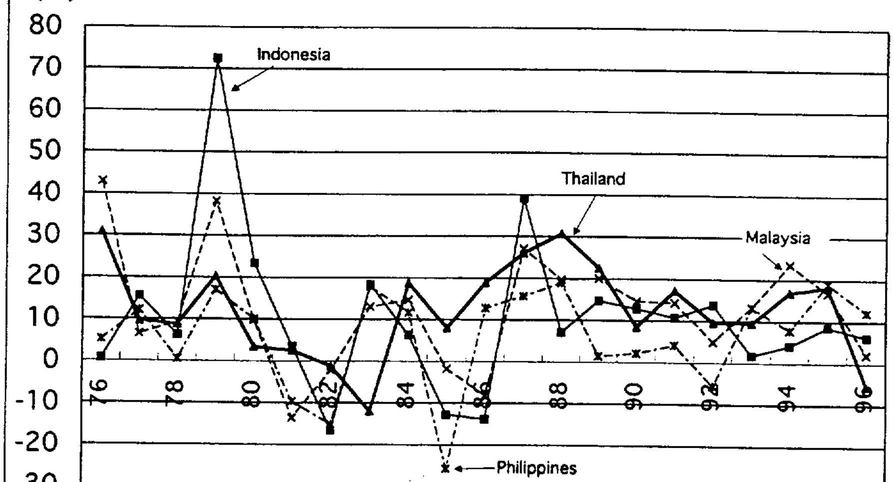
(3) Reasons for a lack of recovery. After implementation of the IMF package of August was begun, the baht continued to depreciate. One of the reasons is that financial reforms did not proceed as quickly as envisaged in the letter of intent. Another reason is suspected that the IMF package did not boost confidence in the government, either because the package was too small or because it was too contractionary on the fiscal side. The political base was weak to carry out decisive reform. It took a change of the government (late October to the beginning of November) to move toward decisive action, and it was only decided on December 8, that 56 out of 58 finance companies would be closed.

These developments provide many lessons to other countries with emerging market economies. First, IMF should advise countries with a fixed exchange rate system when to exit from this arrangement, if fundamentals change adversely. The timing becomes tricky when large capital inflows are masking or aggravating the problems in fundamentals. Second, countries should float their currencies with ample reserves. Exhausting the reserves like Mexico and Thailand makes it more difficult to regain confidence after devaluation (float). Third, in order to predict their timing of crisis, a set of early warning signals may be developed, but their reliability at this moment is not great. Fourth, the strength of the financial system (banks and nonbanks) is crucial in fending off attacks on the currency and in rebuilding confidence after devaluation. Bank supervision has to be strengthened when capital controls on inflows are to be liberalized. Fifth, burden sharing by investors in emerging market financial instruments (bonds and bank deposits in particular) may have be considered when risky investments need later to be bailed out by an IMF program, directly or indirectly. Sixth, regional surveillance is even more important, as contagion becomes a severe problem. The Manila framework, introduced in November, is expected to encourage peer pressure in the Asia-Pacific region. Seventh, IMF funds have to be increased to meet the need for larger funding. The access limit should be carefully reconsidered in case of emerging market economies. In the IMF package for South Korea, the limit was extended by the newly-created SRF facility.

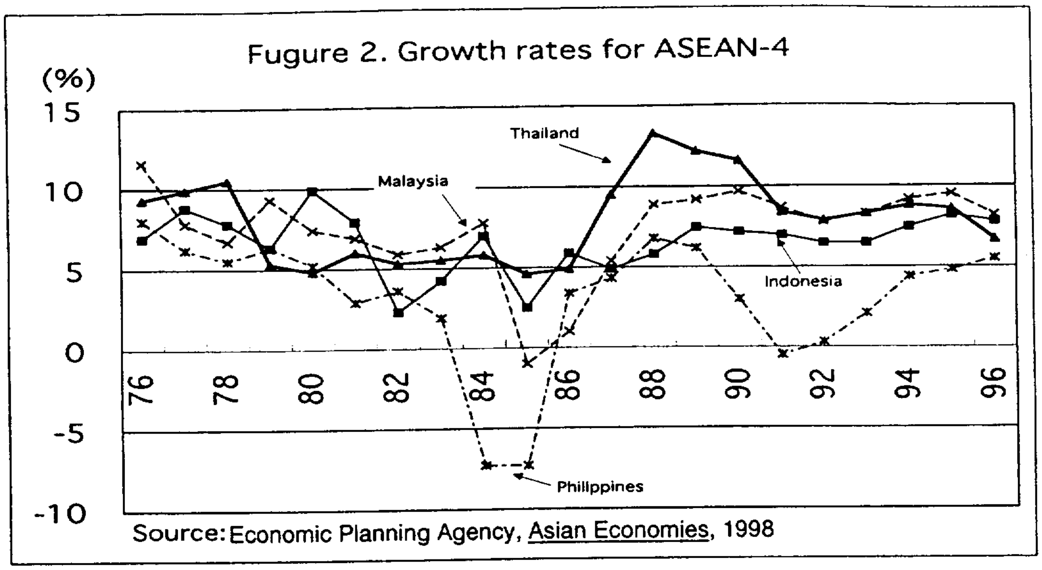
1. Background (1980s to 1996)

(i)Growth slowdown. The high economic growth of Thailand from the late 1980s became the showcase of the Asian economies. The growth rate often exceeded 10 percent in the late 1980s, and was at an average of 8 percent in the 1990s. However, in 1996 Thailand fell into a growth recession and the growth rate declined below 7 percent. The economy continued to stagnate in 1997. (See Figure 1) A decline in (gross) export growth contributed to the decline in economic growth, and the 12-month export growth rate had become zero by the beginning of 1997. (See Figure 2) Suddenly, the engine of growth, namely exports, failed and the sustainability of current account deficits became questionable. Large current account deficits, 8 percent of GDP, had been more than offset by capital inflows. A high growth rate means that a country may be able to grow out of debt (in the ratio to GDP), while a low growth rate means that the debt (in the ratio to GDP) will accumulate very quickly. The difference in the economic growth rate affects confidence among investors. Even the current account deficits/GDP ratio is the same, a country with a high economic growth rate (Thailand in 1995) is less likely to be attacked in the currency market by speculators, while a country with a low economic growth rate (Thailand 1997) is more likely to be attacked.

Figure 1. Export (volume) growth, ASEAN-4



Source:Economic Planning Agency, Asian Economies, 1998



One of the reasons for the export slowdown in the region was the overvaluation of the currencies that pegged their values to the U.S. dollar. Although the Thai baht was under the basket system, it was essentially pegged to the dollar, as an overwhelming weight was placed on the U.S. dollar. The situation was similar in Malaysia and Indonesia. When the U.S. dollar depreciated against the Japanese yen (like the period when Japanese currency was worth 80 yen per dollar in April 1995), Southeast Asian goods sold well in the U.S. and Japan. However, when the dollar appreciated (like the period from April 1995 to the late 1996 when the Japanese currency yen went from 80 yen to 125 yen per dollar), the price competitiveness of Southeast Asian exports was lost.

Since all of these countries had a significant trade relationship with Japan, and, some have products which directly compete with Japanese products in the global (mostly U.S.) markets, the fluctuation in the yen/dollar exchange rate has had a large impact on their trade accounts. When the yen appreciated in the first half of the 1990s (from 120 yen in 1993-94 to the peak at 80 yen/dollar in April 1995), these countries enjoyed a boom in exports. However, the subsequent depreciation of the yen (back to the 120 yen rate range in 1995-96) sent exports of these economies into a tailspin.

(ii) Industrial Structure: Falling from the flying-geese pattern

Export slowdown was not limited to Thailand, although it was most dramatic in Thailand. Most of the de facto dollar-pegged Asian countries, from Thailand, to Malaysia, to South Korea, had experienced a slowdown in exports.

The problem of overvaluation was aggravated by a slump in the worldwide semiconductor industry in 1995-96. The growth in electronics exports declined from 27.2 percent in 1995 to 5.5 percent in 1996, and 8.9 percent in the first half of 1997. For Thailand, the above problems were further complicated by the loss of competitiveness in less sophisticated manufactured goods. Its textile exports declined by 16.8 percent in 1996 compared to 1995. This may reflect competition from China, which increased its competitiveness after a large devaluation of the official exchange rate (unification with the market rate) in January 1994. (See Figure 3)

Table 1. Thailand, Trade Composition

Export (dollar value) growth rates

	Total Exports	Manufacturing	Textile	Machinery	Electronics	Consumer Electronics	Food
1993	13.5	18.6	4.3	28.9	33.4	3.8	-3.6
1994	21.6	22.6	14.4	30.0	35.5	40.7	18.7
1995	23.6	24.8	6.7	36.4	27.2	16.7	17.2
1996	0.4	0.0	-16.8	22.0	5.5	3.6	-0.4
1997, 1-6	3.4	4.6	0.0	-0.5	8.9	7.7	-7.7

Import (dollar value) growth rates

	Total Imports	Consumer goods	Raw Materials and Semifinished Products	Steel	Capital Goods	Machines	Others (incl. Autos)
1993	12.9	10.4	5.5	7.4	17.6	17.5	17.1
1994	17.4	26.5	12.9	9.2	22.5	15.3	7.1
1995	28.8	25.6	29.2	39.2	30.6	33.6	25.2
1996	3.9	6.0	-7.1	-10.7	5.3	7.3	19.1
1997,1-6	-4.3	-5.3	-8.8	-13.9	-0.9	-14.6	-5.9

Source: Japan Export-Import Bank

The Asian economies are often considered to form a flying-geese pattern: the countries are lined up in the order of industrial sophistication. Japan is the leader in high technology industries and is shedding less sophisticated industries, such as consumer electronics, steel, and shipbuilding, to countries next in line, such as South Korea and Taiwan. In turn, South Korea and Taiwan yield textile industries to ASEAN countries. Thailand has been shifting from textiles to the auto-assembly and electronics industries. One of the problems for Thailand was that it could not upgrade its industrial structure in time, as China started to catch up with Thailand. The flying-geese pattern seems to have been disturbed, and Thailand fell from the formation.

It has been pointed out that there is a shortage of skilled workers for more sophisticated industries. The education system has to be enhanced, and more job training has to be provided.

(iii) Trade Relationship

Japan accounts for one-third of Thailand's total imports, most in the categories of parts and semi-finished products. The resulting manufactured or assembled goods are exported mostly to the United States (accounting for 20 percent), Japan (15 percent) and other Asian countries (30-40 percent). (See Table 2) Therefore, the dollar peg has gradually lost its significance for these countries. One of the benefits of having the dollar peg is to boost the confidence of the investors. However, by the mid-1990s, high growth impressed investors so much that capital inflows became too much.

Table 2. Export Destination and Import Origin

Million baht

	1993		1994		1995	
	Exports	Imports	Exports	Imports	Exports	Imports
Total	935,862	1,166,595	1,137,600	1,369,035	1,406,311	1,763,591
Japan	159,479	353,509	194,413	413,323	236,101	538,711
	17.04%	30.3%	17.09%	30.19%	16.79%	30.55%
US	202,227	136,051	239,098	162,064	250,684	211,947
	21.61%	11.66%	21.02%	11.84%	17.83%	12.02%
EU	155,978	172,316	169,385	185,820	204,312	255,014
	16.67%	14.77%	14.89%	13.57%	14.53%	14.46%
China	13,637	27,610	23,338	34,898	40,868	52,187
Taiwan	18,692	59,127	24,690	69,366	33,715	85,220
Korea	11,684	49,315	14,372	49,746	19,937	61,643
Hong Kong	49,583	13,577	59,989	17,362	72,775	18,581

Source: Bank of Thailand, Monthly Bulletin

Million baht

	1996	
	Exports	Imports
Total	1,412,111	1,832,836
Japan	237,523	518,107
	16.82%	28.27%
US	253,800	228,974
	17.97%	12.49%
EU	216,640	244,597
	15.34%	13.35%
China	47,371	49,501
Taiwan	36,024	79,682
Korea	14,372	67,991
Hong Kong	82,121	21,641

Source: Bank of Thailand and Customs Department

Another factor that indicates a strong link of the Asian economies to Japan as well as the United States is the ratio of yen invoicing in Japanese exports to, and imports from, East Asian countries. According to MITI statistics, the yen invoice ratio for Japanese exports to the region increased from 30 percent in 1981 to more than 50 percent in the beginning of the 1990s. The yen invoice ratio of the Japanese imports from the region increased from 2 percent in 1983 to more than 25 percent in 1993. While the Asian economies had large shares of exports and imports quoted in the yen, the currencies were still pegged to the dollar. The fluctuation in the yen-dollar rate has a large impact on their trade accounts.

<u>(iv) Boom and Bust</u>

The real side of the Thai economy was booming from 1991 to 1995. Private fixed investment was rising at 9 to 13 percent in 1993 to 1996, while consumption was rising at 6 to 8 percent a year. (See Table 3)

Table 3, Aggregate Demand Components at 1988 Prices

Billion Baht

% change from previous year.

	1993	1994	1995	1996
Private Consumption	1585	1711	1835	1949
	8.0%	8.0%	7.3%	6.2%
Government Consumption	1380	1380	1614	1712
	8.4%	7.9%	8.3%	6.1%
Private Investment	806	877	987	1035
	10.5%	8.8%	12.5%	4.8%
Public Investment	191	235	271	308
	4.6%	22.5%	15.6%	13.5%
Exports	1048	1197	1375	1410
	12.7%	14.2%	14.8%	2.6%
Imports	1108	1269	1484	1525
	11.6%	14.5%	16.9%	2.8%
GDP	2481	2702	2936	3124
	8.5%	8.9%	8.7%	6.4%

Source: Bank of Thailand

Also, the trade structure reveals that consumption was not the origin. The import increase of 1995 was mostly in raw materials, semi-finished goods, and capital goods. In particular, steel and ICs showed growth rates near 40 percent (recall Table 1). It was more an investment boom than a consumption boom. This distinguishes Thailand from pre-crisis Mexico.

At the time of economic boom, 1993-1995, lending to real estate had risen fast, especially from finance companies. About a quarter of the loans from finance companies was concentrated in the real estate sector, while only 10 percent of commercial banks was directed to the real estate sector. (See Table 4)

Table 4: Loans Classified by Sectors

Credits Granted from Thai Commercial Banks to Various Sectors (unit, million baht)

	1994,Dec	1995, Dec	1996, Dec	1997, May
Total	3,051,311	3,646,821	4,187,037	4,336,576
Manufacturing	670,434	824,011	985,808	1,041,648
	21.97%	22.6%	23.54%	24.02%
Commercial	592,370	733,011	840,050	896,578
Banking & Finance	169,717	210,953	227,087	219,583
Construction	130,139	166,787	209,672	223,519
Real Estate	316,636	353,484	380,692	377,208
	10.38%	9.69%	9.09%	8.7%
Others	1,172,015	1,358,575	1,543,728	1,578,040

Source: Bank of Thailand

Loans extended from Finance Companies, classified by Sectors (unit = million baht)

	1993, Dec	1994, Dec	1995, Dec	1996, Dec	1997, May
Total	683,505	937,514	1,213,971	1,398,795	1,334,849
Manufacturing	98,731	127,457	175,274	218,041	209,242
	14.44%	13.6%	14.44%	15.59%	15.68%
Commercial	69,072	91,739	120,792	155,329	146,765
Banking	68,642	101,074	133,167	149,718	139,148
Construction	19,441	26,504	40,191	56,738	55,653
Real Estate	163,417	237,897	321,454	365,579	364,719
	23.91%	25.38%	26.48%	26.14%	27.32%
Others	283,643	352,843	423,093	453,390	419,322

Source: Bank of Thailand

As the economy slowed down, the real estate bubble burst. Some of the bank credit, which had increased in 1994, went to the real estate sector. Office buildings were over-built. As the financial bubble collapsed, stock prices and real estate prices declined sharply, and nonperforming loans increased. The stock price index, SET, peaked at 1,754 in January 1994, and stayed at around 1,200 in 1994 and 1995. Then it declined sharply in 1996, from 1,200 in January to 800 in December. By the time the currency was devalued, the stock price index had become 500. The bubble burst in the stock market preceded devaluation by at least 18 months.

The land price index is not available, but circumstantial evidence suggests that land prices had been declining sharply for a year or two before the currency crisis hit. The real estate industry was in trouble and banks and nonbanks, which lent to the sector, were accumulating nonperforming loans. Finance companies, which were fast-expanding nonbank financial institutions, were particularly hard hit by the bubble bursting. A sign of weakness appeared first when the Bangkok Bank of Commerce failed (later taken over by the government) in 1996.

In the spring of 1997, the Bank of Thailand had to start a liquidity support for the troubled finance companies, because funds started to flee institutions that were perceived to be weak.

The central bank extended loans to finance companies through the Financial Institutions Development Fund (FIDF), which is vaguely similar to a deposit insurance system. By the time these finance companies were suspended (13 in June and another 42 in August), 430 billion baht had been lent. These financial troubles weakened the confidence of foreign investors in the economy and currency. As discussed in Section 2, Thailand had large inflows to its banking sector. Hence impacts on foreign investors' confidence in the financial system being lost on the capital flows and on the economy in general were much stronger than otherwise would have happened.

In order to alleviate the property loan problem, Thai authorities set up the Property Loan Management Organization (PLMO) in the spring of 1997 to help restructure property loans. However, finance companies became cash strapped before PLMO became operational.

2. From Speculative Attack to Devaluation

Speculators attacked the currency on May 13 and over the following few days. Capital control was introduced on May 15 to defend the baht, and make it more costly for speculators to borrow the baht. After the finance minister was replaced on June 19-20 (FM Amnuy resigned on May 19 and FM Thanong was appointed on May 20), more favorable situation toward devaluation was created. Domestic financial sectors were in trouble too. Sixteen finance companies were suspended on June 27.

(i) Battle in May

In general, weak macro fundamentals, such as large current account deficits and slow growth, are a first sign of currency depreciation pressure. The banking and currency crises go hand in hand. When the banking sectors are weak (i.e., undercapitalized and with large nonperforming loans), the currency becomes vulnerable. Hiking the interest defense in the hope of stopping capital outflows cannot be deployed when financial institutions are weak, and capital flight becomes a serious concern. Precisely at this moment, the probability of success for a speculative attack increases. Thailand was picture perfect for this. Speculative attacks took place in little waves in January, February, and March 1997. However, it was not until May 1997, that speculative attacks became so massive that they changed a course of the economy permanently.

A massive speculative attack on the baht took place in the week of May 12. The baht was sold both in the spot and forward markets. The forward selling took place in the form of swap arrangements, that is, speculators effectively bought the baht in the spot and sold the baht forward, paying the interest rate costs, but expecting that devaluation would take place soon. The central bank countered by intervention, defending the de facto dollar peg. When the central bank becomes a counterparty of swap deals, the central bank is able to acquire dollars on the balance sheet (as a result of the spot transaction, the first leg of the swap arrangement) while having dollar liability as an off-balance sheet item.

If the future liability of dollar selling and buying baht were to be consolidated, the true foreign reserve level at the end of May would have revealed a substantial decline in foreign reserves. At that point, keeping the de facto fixed rate would have become impossible. The Thai authorities must have hoped for some events that would make the central bank regain a comfortable level of foreign reserves before the forward liability would become due, but no such event took place, and worse, some residents started to become less confident in the fixed exchange rate. It would be revealed later that the central bank in fact engaged in forward contracts of more than $17 billion in the offshore market (mostly in Singapore).

(ii) Squeeze play

On May 15, the central bank advised domestic banks to refrain from providing liquidity to offshore banks. The baht market was segmented into onshore and offshore markets. The intended effect was to squeeze "speculators," or short sellers or forward sellers. Those nonresidents who had sold the baht short were caught. They had to pay a very high rate to obtain the baht which was needed to close the contract delivering the baht and receiving the dollar. The two-tier market was formed. Offshore baht started to be traded at a premium. The two-tier market continued to exit until the end of June. Those who took the short-selling (of the baht) position in the one-month forward market in May must have had losses due to the two-tier market.

Although nonresidents could not borrow the baht, they could repatriate proceeds from selling bonds and stocks. Hence, as the spot rate became higher in Singapore, nonresidents tended to send the baht back to Singapore. Eventually the premium started to disappear in late June.

(iii) Announcement of Foreign Reserves and Suspension of 16 finance companies

On June 26, the Bank of Thailand announced that it had lost $4 billion in foreign reserves during the month of May, and the level stood at $33.3 billion, the lowest level in two years. The loss in reserves was attributed to the currency defense. The market knew at this point that the central bank had engaged in forward contracts and the announced reserves did not include the potential reserve loss from forward contracts. The market also realized that private debts had far exceeded the level of foreign reserves. But, there was no panic.

> "The fall in reserves is worrying for two reasons, analysts said. First, the number does not reflect the amount of forward contracts the central bank took out

last month defending the currency. Most of those contracts are expected to come due in mid-August, when many analysts believe Thailand will experience another bout of currency instability.

"Second is that the country has as much as $66 billion in private sector debt coming due in the next year. If that credit is not rolled over and Thailand keeps facing a balance of payments deficit, the country may not have enough dollars to pay those loans back.

"Nevertheless, analysts said that foreign capital may start to flow back into Thailand if the country's new measures to deal with cash-strapped finance companies are implemented successfully and quickly." (Financial Times, June 27, 1997)

What the market did not know was the size of forward contracts that the central bank had engaged in. The exact size of forward contracts, more than $17 billion in offshore and $23.4 billion altogether, remained as the best kept secret until it was forced to be revealed at the time of IMF program in late August.

The fact that the announced foreign reserve level changed little from May to June reflected the fact that the central bank countered spot selling of the baht by intervening in the market, while engaging in swap arrangements of a similar magnitude. Although the central bank would manage to keep the fixed rate until July 2, and the squeeze play worked in June, it could not keep the tightrope operation going any longer.

At this point, another problem was how to deal with the finance companies, which were known to be burdened by the nonperforming loans. Liquidity was supported by the central bank (through BIBF). The central bank suspended operations of 16 finance companies on Friday, June 27, a day after it announced the drop of $4billion in foreign reserves in the month of May. The central bank was to set up panels to take control of each company. The step was regarded as positive, and the stock market went up by 1.6%. How to rehabilitate or liquidate these institutions was not decided upon at this point, although the 16 finance companies were ordered to submit rehabilitation plans in 14 days. It took another six months, instead of 14 days, for them to submit plans to be evaluated as events would evolve. There were other finance companies with weak balance sheets, and obviously how the 16 would be dealt with would affect the businesses of other operating finance companies. At this point, the monetary authorities seem to have leaned toward a merger plan, rather than liquidation of the troubled companies.

The authorities have urged finance companies to resolve the problems on their own and seek a strategic alliance with foreign financial institutions. There has been progress on this front with 26 finance companies having already increased their capital or are in the process of increasing their capital, while another two have concluded agreements with foreign partners. ... There remain, however, 16 companies which have not been able to independently raise their capital and should therefore transfer ownership and control to the core groups of financial institutions (purchase and assumption method). ... Companies proposing to act as a core financial group include the Krungthai Thanakit Public Co. Ltd. It is a government-owned financial institution, with support by the Financial Institutions Development Fund. Another three groups of finance companies with a strong financial position have notified the authorities of their interest.

- statement by the Ministry of Finance and the Bank of Thailand, 27 June 1997

In order to assure depositors, the monetary authority made a blanket guarantee. Depositors in the institutions that were closed are protected by exchange of the deposits for bonds issued by a state bank (Krung Thai Bank), while depositors in other institutions would be protected in the future.

Depositors should be assured of protection for both principal and interest. . . . Whatever measure is taken, honest depositors shall be protected in all cases. The Bank of Thailand wishes to assure the public not to panic and to have full confidence in this package to solve the financial institution problem. (Emphasis in original)

- statement by the Ministry of Finance and the Bank of Thailand, 27 June 1997

The guarantee turned out to be less than full, when the bonds that are exchanged for deposits carry coupons with less than the market interest rate. These details were not revealed at the time. Whether to guarantee deposits in full or not has an important implication in dealing with failing institutions. A full guarantee would cause a moral hazard, in the sense that depositors would seek higher interest rates disregarding the solvency of financial institutions, while

However, less than full guarantee might cause bank runs, and worsen the already-distressed financial institutions. In fact, one of the problems with the Indonesian package imposed by IMF (in October) was that it had a less-than-full guarantee, and caused a quick withdrawal from the remaining banks.

3. From Devaluation to the IMF Package

The baht was freely floated on July 2. It was de facto devaluation, since the currency immediately depreciated by 17 percent. After one month of struggle, the Thai authorities decided to ask for IMF support. The amount of support exceeded what IMF usually allows a member country to borrow (access limit). A meeting was held on in Tokyo August 11, to form a support package, amounting to more than $16 billion, led by Japan. The IMF package of August 20 was expected to turn Thailand around.

(i) Devaluation

On July 2, the Thai government announced it was abandoning the old exchange rate regime, the basket system. The basket system was a de facto dollar peg, since the weight on the U.S.

dollar was overwhelming. The new system was called managed float but was a de facto free float. The exchange rate immediately depreciated by 17 percent from B24.5 to B28.8. The decision to go off the 13-year-old regime did not surprise many informed observers, since it was made after several speculative attacks and countermeasures. However, the timing was somewhat surprising, in that measures to strengthen financial institutions, that were regarded as efforts to avoid devaluation, had just been taken. The market reaction was positive in fact in expectation that the interest rate, which was raised in defense of the baht, would be lowered.

The Bank of Thailand did not appear to intervene after the de facto devaluation. There are two reasons why the Bank of Thailand did not even try fixing the exchange rate at a new rate. First, Mexico did not adopt once-and-for-all devaluation in an attempt to find a new equilibrium rate. Since a new equilibrium was not known, the Bank of Thailand wished to let the market find the new equilibrium rate. Second, although it was not public knowledge, the level of net foreign reserves was extremely low, and it was impossible to defend another attack.

The exchange rate movement was relatively calm just after the baht was floated. In the case of Mexican peso, the devaluation by 15 percent on December 20, 1994 was followed by massive capital outflows and the new level was not defendable. The new peg had to be abandoned in two days and the exchange rate went to a free float. The peso vis-à-vis the U.S. dollar depreciated by 50% in one week. This kind of crash did not happen for the baht. After the devaluation, the baht was sliding down, but after one month, the rate was still within 20 percent devaluation.

The Thai monetary authorities asked for support from Japan and the United States in mid-July. The Thai finance minister met with the Japanese finance minister on July 18, in Tokyo. However, the Thai delegation was told to consult with IMF. Thailand officially asked for the IMF support on July 29.

<u>(ii) Finance companies</u>

The Thai monetary authority hurried reforms to prevent further depreciation. In consultation with IMF, the financial sector fragility was identified as the crucial point in economic reforms. On August 5, the Bank of Thailand and the Ministry of Finance announced that 42 finance companies would be closed, in addition to the 16 that had been suspended. Then, how to deal with the 42 finance companies became the problem, even before the final solution for the 16 was decided upon. The criteria for suspension, one of which is that borrowing from FIDF exceeded the capital of the finance company, were made public.

What made difference between the 16 finance companies, 42 finance companies, and 33 surviving finance companies were their loan decisions. More than 40% of the loans from the 16 finance companies were directed to the real estate sector, as opposed to only 25% or less for the 42 companies and 33 companies.

The magnitude of the problem can be understood from Table 5.

Table 5, Finance companies, Balance sheet items

	16 Finance Companies	42 Finance Companies
Deposits(Promissory notes to public)	B 125,030 million (US$ 4 bn)	B 294,006 million (US$ 9.3 bn)
Domestic Creditor claims	B 187,466 million (US$ 6 bn)	B 184,106 million (US$ 5.8 bn)
Foreign creditor claims	B 16,354 million (US$ 0.5 bn)	B 22,194 million (US$ 0.7 bn)
Assets	B 379,116 million (US$ 12 bn)	B 602,744 million (US$ 19.1 bn)
FDIF liquidity support as of August 5	B 163,000 million (US$ 5 bn)	B 269,000 million (US$ 8.5 bn)
Total Lending	B 324,218 million	B 516,048 million
Real Estate sector lending In % of Total lending	B 110,415 million (43%)	B 129,842 million (25%)
Creditors protection		
Shareholders	0%	0 %
Creditors	0%	100 % KTB bonds
Depositors(PN holders)	100% with KTT bonds	100 % KTB bonds

Source: Bank of Thailand
Notes: All numbers are at the end of June 1997, unless otherwise noted. The surviving 33 finance companies had assets 545,185 million, of which 126,277 million (23%) were lent to real estate sector.
KTT bonds and KTB bonds will carry an interest rate substantially lower than the market rate, so that the protection is only a fraction of the discounted present values of original claims.

At this point, finance companies were being managed by the managers who had managed them before suspension, under close supervision by the Bank of Thailand. At this point (mid-August 1997), it was determined that the fate of 16 finance companies would be decided by September 27, and that of the 42 finance companies would be decided by November 3, after plans for rehabilitation strategies covering due diligence were submitted within 60 days from suspension (by October 3). There was no question that the 16 finance companies had the worst asset quality. However, some doubts were raised whether all 42 deserved to be suspended. The criteria were applied mechanically, in pursuit of transparency, and the asset quality may not have been evaluated carefully. Hence, the chance to rehabilitate should be given, it was argued.

The pattern of FDIF support was also worrisome. First, the FDIF support to the 16 finance companies increased sharply in March and continued to increase until they were suspended in June. Then FDIF support to 42 finance companies increased sharply in June and July. They ended up suspended on August 5. There was no guarantee that other weaker financial institutions (33 surviving finance corporations and 15 commercial banks) would not receive FDIF support after August.

Creditors and Depositors (Promissory note holders) are protected even under the suspension. However, they receive bonds which carry an interest rate substantially lower than the market rate (which turned out to be 2%), so that they share the burden. Creditors and Depositors of the surviving institutions were given a full guarantee, in order to avoid bank runs.

(iii) IMF package

On August 11, the Tokyo meeting for supporting Thailand took place. The IMF realized that the support that IMF could give to Thailand would fall far short of what Thailand needed, just as in the case of Mexico. Mexico obtained five times its IMF quota. The same multiple would mean that Thailand would receive $4 billion. However, it was soon to be revealed that the forward contract that the central bank had committed amounted to $23 billion and the private external debt (bank borrowings) amounted $438 billion. The IMF and Japan asked Asian countries to contribute to the package so that Thailand could obtain enough liquidity in foreign reserves. In total, $15.7 billion was pledged at the time of the meeting, and in a few days, $17.2 billion became the total package:[1]

> IMF $4 billion; World Bank, $1.5 billion; ADB $1.2 billion; Japan $4 billion; China $1 billion; Australia $1 billion; Hong Kong $1 billion; Malaysia $1 billion; Singapore $1 billion; Korea $0.5 billion; Indonesia $0.5 billion; and Brunei $0.5 billion. The United States was conspicuously absent from the rescue package.

By this time, a consensus was emerging that Thailand had liberalized financial markets too hastily without sufficient supervision. Therefore, when the United States sent a mission to Asia in mid-August to force further liberalization in the financial services so that WTO negotiations would proceed, it was greeted with skepticism.

On August 20, the IMF board approved a three-year stand-by arrangement (SBA) in an amount of SDR 2,900 million (505 percent of quota), about US$3.9 billion. The Board considered the request under the emergency procedure, so that the review was only for a week, and the front-

[1] The IMF had calculated that at least $14 billion are needed to fill the balance of payment gap in coming months. The IMF (represented by Mr. Sugisaki) was the chair and Japan was the host. Participating countries and institutions in the meeting were Thailand, Australia, China, Hong Kong, Malaysia, Indonesia, Korea, Singapore, USA, Canada, France, Germany, UK, World Bank, and ADB. China did not commit its amount at the time of the Tokyo meeting, but committed $1 billion on August 14th. Brunei did not come to the meeting,

loaded disbursement of US$1.6 billion was immediate.

Main contents of the program were as follows:
(1) Growth rate target was 2.5% in 1997 and 3.5% in 1998.
(1) Inflation target is 4-5 percent.
(2) Financial sector restructuring has to be carried out, identifying and effectively closing insolvent financial institutions, and with a temporary guarantee to remaining financial institutions.
(3) Target fiscal surpluses of 1 percent. VAT should be increased.
(4) The exchange rate system will remain as a managed float, but intervention must be limited to smoothing fluctuations.
(5) Target of broad money growth is 7 percent in 1997.

Whether fiscal surpluses of 1 percent GDP is needed would become controversial. The IMF maintains that at the time of the program, the economy was not expected to become too weak (3% GDP growth was targeted) and the 1% surplus was needed to pay for the financial sector restructuring. However, the growth forecast would turn out to be too optimistic.

As a part of the conditions for the IMF program, the Bank of Thailand announced that it had forward liability of $23 billion. The market participants knew the fact that the central bank had engaged in the swap arrangements, but they did not have precise information on the size of the swaps that the central bank had engaged in. The amount, $23 billion, included both on-shore and off-shore forward contracts. The on-shore contracts were an outcome of repo arrangements to provide the baht liquidity, while the off-shore contracts were mainly for counter measures against speculation. However, the distinction was too subtle, and the size surprised the market. The IMF package looked too small for this kind forward liabilities.

4. Slow Financial Reform and Political Change (August 20 to December 8)

After the IMF package of August, financial reforms did not proceed as quickly as envisaged in the letter of intent. The political base was too weak to carry out a decisive reform, especially in dealing with the suspended 58 finance companies. In October, Finance Minister Thanong resigned after a tax increase did not pass the parliament. Prime Minister Chavlit resigned in early November. Reform had to be carried by a new government, formed on November 9, by Prime Minister Chuan. It was decided on December 8, that 56 out of 58 finance companies would be closed.

(i) Political Uncertainty

The financial reforms were top priority after the IMF agreement of August 20. Under the IMF program, it was envisaged that the fate of 58 finance companies would be decided in one month. However, the screening committee was twice abandoned partly because of political pressure and lack of authority, before the task was handed over to a newly-created FRA in late

October. The FRA asked finance companies to submit rehabilitation plans by the end of November.

Among others, the focus of the market was on how to "close" permanently or revive 58 finance companies that had been "suspended." The major problem was the legal authority to do so. Although there was a committee to consider the resolution of finance companies, its authority and mandate was unclear. Since a bankruptcy law for financial institutions was not available, it was legally and politically difficult for the committee to decide the fate of the finance companies. In particular, the following problems and questions were insurmountable for the committee. First, the legal authority to decide upon the failure of financial institutions had to be devised. Second, criteria to separate suspended finance companies into ones to be liquidated and ones to be rehabilitated had to be set. Third, the central bank had injected 430 billion bahts ($12 billion at 35 baht to a dollar) into the troubled finance companies. Any resolution plan had to address how to repay these senior credits to the central bank. Fourth, treatment of foreign creditors to finance companies had to be addressed fairly.

A turning point came in mid-October. The government prepared for decisive action on the closed finance companies. The action was prepared in advance of the first review by IMF. The steering committee on the finance companies could not make a decision and the chair, Amaret Sila-on, resigned on October 12, citing political interference in the criteria for dissolving the finance companies.[2] A reform package was announced on October 14, a day earlier than expected. The package included the following measures: (1) to allow foreigners to own majority stakes in all financial institutions for at least 10 years; (2) to provide a government guarantee to both depositors and creditors of banks and finance companies excluding the 58 suspended finance companies; (3) to enact new laws permitting the central bank to take control of a troubled institution and make shareholders pay for losses; (4) to establish the Financial Restructuring Authority (FRA) to decide how to close or rehabilitate 58 finance companies; (5) to give suspended finance companies until the end of October to submit rehabilitation plans. (6) to establish an Asset Management Company (AMC) to manage assets of failed financial institutions, (7) to improve the bankruptcy law so that creditors can collect collateral faster; and (8) to tighten loan classification rules and bring provisioning rules up to international standard by 2000.

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[2] "Amaret Sila-on, along with three other "neutral" members of the six-member committee who also resigned, were afraid that last week's intense lobbying of Chavalit Yongchaiyudh, prime minister, and Chatichai Choonhavan, a senior adviser, by executives of the suspended companies would result in a relaxation of the committee's tough criteria for suspended companies to reopen. ... A key component of that programme is a quick and orderly resolution to the fate of the suspended companies, who borrowed Bt430bn ($12bn) in emergency liquidity from the central bank before the International Monetary Fund put a halt to the practice. Mr Amaret's committee set tough criteria for those companies to reopen, a move applauded by World Bank and IMF officials who think most of the suspended companies should be shut permanently." (Financial Times, October 13, 1998)

On October 21, the Emergency decrees were approved by the cabinet. The decrees, drawn up by experts from the World Bank, would amend the Commercial Banking Act and the Finance Business Act to allow the central bank to intervene in institutions more quickly, and the FRA and AMC were established.

As the financial reforms moved ahead, the pressure mounted for a political change. Finance Minister Thanong, resigned on October 19. The coalition government also pressed the Prime Minister to reshuffle the government by collecting resignation letters from other cabinet members on late in the evening of the 19th. The cabinet was reshuffled on the 24th, and Kosit Panpiemras became the new finance minister was. However, the financial markets were not impressed by the developments, and the baht continued to decline, and reached a psychological barrier of 40 baht/dollar on October 31. The reshuffle without changing the Prime Minister did not boost confidence.[3]

Prime Minister Chavlit Yongchaiyungh announced his resignation on November 3. At that point, there were two contenders for the top post: Chatichai Choonhavan (head of the second largest party in the ruling six-party coalition) and Chuan Leekpai (the opposition leader). Chatichai, age 77, would become Prime Minister if the coalition held, but the market regarded him as a part of the Chavlit government which brought Thailand into a crisis. Chuan, age 59, had been Prime Minister from 1992 to 1994, and had led the second largest party since the end of military rule in 1992. When Chuan succeeded in drawing supporters from the coalition, it became certain that Chuan would become Prime Minister. When the news was revealed on November 7, the SET responded positively.

The markets reacted positively to news that Chavlit would resign and that Chuan was getting support from some members of the coalition. For example, the baht rose 6.1 percent (to B38.60/$) on November 4 and 2.6% (to B37.95/$) on November 7, and the stock market climbed 6.9% (to 478.33) on November 4, and 3% (to 493.04) on November 7. On November 9, Chuan formally became prime minister, and shortly afterward, Tarrin Nimmanhaeminda was named Finance Minister.

(ii) Decision to close finance companies

The new government started to negotiate with IMF on revision of the conditions set in the agreement of August. By this time (late-November), the crisis had spread to Indonesia and South Korea. Indonesia had agreed with IMF, World Bank, and ADB on a $23 billion package with additional funding if necessary from Japan, Singapore, the U.S., and other Asian countries. South Korea was negotiating intensely with the IMF. The conditions in Thailand

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[3] Dissolving the parliament and forcing a new election was not possible at this point, because as a condition to enact the new constitution in October, a new election will not be held until the related laws will be passed within 240 days.

and among its trading partners were much weaker than those in late August. This warranted revision of growth forecasts, and policy conditionality. The growth forecasts for 1997 and 1998 were reduced to 0.6 and 0.1 percent, respectively, from previous target levels of 2.5 and 3.5, respectively. On November 25, a second tranche was requested.

One of the greatest challenges for the new Thai government, and one of the conditions for the IMF second tranche to be released, was to press for a conclusion on the fate of the 58 finance companies. At the time of the IMF agreement of August 25, it was planned to finish the work by October. Later, it was delayed due to a change in the steering committee. Then the deadline for submitting rehabilitation plans was set for October 31 and the FRA decision was to be made by November 30. Additional documentation and clarifications continued to be filed until November 30. Now that the decrees had been issued, the new government was in a position to take decisive action.

The decision was reportedly made on November 30, but sealed until December 8, due to the national holiday (December 5). By November 30, 38 rehabilitation proposals were filed. Since some of them had a merger proposal, the number of plans was less than the number of suspended finance companies. Only two out of 38 proposals were accepted. This meant that only two finance companies would be reopened, and it was decided to close 56. This decision was welcomed by IMF and the market. FRA had set conditions for mergers and capital injection after due diligence. It also required them to pay back FDIF lending to the central bank within a certain period. Only two proposals satisfied these tough conditions. With this decision, the most difficult problem was overcome.

Special managers were sent to the 56 institutions to separate good and bad assets, and then auction off good assets, while collecting bad assets. AMC would make sure that the auction would be successful.

The market conditions, including stock prices and the baht, were dampened by spillovers from Indonesia and South Korea in December and January. The trouble in the banking sector was not over either. The Thai monetary authorities had to take over weaker institutions in the first quarter of 1998. However, the progress in reforms was sufficient to convince IMF to release the third disbursement of $3 billion and the World Bank the disbursement of $3.5 billion in March.

(iii) Finance One

Table 6, Finance One, hypothetical disposal plan

TABLE 1:	------------>	LIQUIDATION PROCEDURE PER FRA RULES				BENEFITS / LOSSES	
Reconstituted Balance Sheet of Finance One (Fin One) Before its suspension and after closure per FRA decision in Baht Million	Starting Point 1996 / 97 data for Fin One (1)	Asset valuation assumptions (% of book value) (2)	Liquidation Proceeds & Revenue (3)=(1)x(2)	Payment of Creditors per FRA rules (proportion of outst. credits) = (4)	Payment of Shareholders per FRA rules after creditors are paid first = (5)	Benefits (+) or Losses (-) by class of asset / liability Baht Bil. (7) = difference	% of Stake = (8) = (7) as % of (1)
ASSETS		**ASSET DISPOSAL**					
Cash and cash equivalent	1,417	x 100% =	1,417			0	0%
Securities	27,840	x 100% =	27,840			0	0%
Government Bonds	0	x 100% =	0				
Corporate Bonds	0	x 100% =	0				
Other assets corrected (Premises & Equip)	3,808	x 75% =	2,856			-952	-25%
Provisions for loan losses	0	x 100% =	0				
Accrued interest receivable	0	x 100% =	0				
Loans and advances to customers	65,628	x 57% =	37,436			-28,192	-43%
o/w Good Assets (*)	42,058	x 75% =	31,544			-10,515	-25%
Impaired Assets (*)	23,570	x 25% =	5,892			-17,677	-75%
Other assets nie	3,718	x 75% =	2,788			-929	-25%
Total Assets	102,411		72,337	<- Proceeds to be used for payment		-30,073	-29%
LIABILITIES			**PAYMENTS**				
Due to the FIDF (*)	50,153		to FIDF	41,035		-9,118	-18%
Foreign Debt (creditors) (**)	10,020		to Foreign cred.	8,198		-1,822	-18%
Borrowings from financial institutions	16,452		To other Creditors	13,461		-2,991	-18%
Total Borrowings	76,625						
Promissory Notes	11,785		To prom. Notes	9,643		-2,142	-18%
Accrued interest and others	0		Acc. Interest	0		0	
Total Liabilities	88,410		Paid Tot. to Creditors ->	72,337			
Issued and paid-up capital	4,140						
Unappropriated retained earnings	3,190						
Total shareholders' equity = (6)	14,001			Paid Tot. to Shareholders ->	0	-14,001	-100%
Total Liabilities and shareholders' equity	102,411						

Source: Published Balance Sheets of Finance companies for end-1996 except for (*), where source is Rehabilitation Plan submitted December 10, 1997
For calculation of liquidation re-payment process FRA rules were used; asset valuation assumptions are our own
(**) assumes that 50% of foreign debt of the 16 suspended finance companies is owed by Fin One.

Finance One, the largest finance company, with assets of B102 billion in December 1996, was the focus of attention, since many foreign creditors were hoping to reopen it. The balance sheet shows that B65 billion were loaned out. With an assumption of recovery ratios of 75 % for good assets (B42 billion), and 25% of impaired assets (B23billion), about 28 billion was lost. Combined with possible loss of B2billion from other assets, a loss of about B30 billion has to be recovered. The amount exceeds shareholders equity (B14 billion) by B16 billion. This has to be charged to creditors: FDIF (B50billion), foreign debt (B10billion), borrowings from financial institutions (B16billion), and depositors or promissory note holders (B12billion). If creditors were proportionally charged for the loss, it meant that the creditors would take an 18 % loss on their holdings. (See Table 6 for details.) If the loan recovery ratio is much lower, the loss for creditors would be more.

Before November 30, Credit Suiss First Boston (CSFB), a creditor of Finance One, had proposed to rescue Finance One, with a debt-for-equity swap.[4] CSFB held $63m eurobond of Finance One. It tried to inject capital to save the eurobond, as detailed in its plan. On December 3, Westdeutsche Landesbank, in cooperation with J.P. Morgan, was making a last minute attempt to take over Finance One with capital injection.

Their proposals are believed to have included a condition to convert FDIF lending to Finance One into equities, or to shelve the FDIF lending for the time being, in return for converting proposing institutions lending to equity holdings and, in the case of Westdeutsche Landesbank, fresh capital injection. It would have been hard to believe why senior creditors would recover bad assets as well as good assets, when the chance to bid for good assets are provided for in the future FRA disposal plan, unless enough losses were somehow shifted to FDIF. Both proposals were rejected.

Even after the decision of December 8, some creditors tried to make an exception for Finance One. International Finance Corporation, a member of the World Bank group, tried to purchase Finance One as a whole.

5. Road to a Recovery

With the IMF second disbursement, other supporting institutions disbursed their contribution. The ADB Board approved the Thai financial market reform and released $0.3 billion on December 19. On December 23. The World Bank Board approved the Thai financial sector reform, and the release of $0.35 billion. The Export-Import Bank disbursed its second installment of 99.3 billion yen on January 6.

The baht weakened to 47.95 to the U.S. dollar on December 15, mainly due to the spillover from South Korea and Indonesia. On that day, the Bank of Thailand announced that foreign reserves had fallen to $26.3 billion at the end of November, primarily due to unwinding of six-month forward contracts that had been taken back in May. Outstanding forward contracts were disclosed to be $18.3 billion, and cost of settlement was increasing quickly, as the baht fell. Although the level of $26.3 billion exceeds the target of $23 billion set by IMF, the baht was weakened because of the Thai corporation hedging for their payments of $6 billion in

[4] On December 4, CSFB revealed the details of its proposal, countering the WL proposal. According to the Financial Times, CSFB would inject Bt 6.24bn ($146m) into Finance One to purchase between 70.5 percent and 80 percent of the company. The Thai government and other senior creditors would be issued new notes at 66.67 percent of face value of their original debt. The new debt would mature in eight years. In addition, the creditors would receive 29.5 percent of the equity of the reopened company. Eurobond holders would receive a new note equal to 30 percent of their original debt, carrying a 10-year maturity. "CSFB, which is a significant creditor of Finance One through its holding of 48 percent of the Thai company's $63m eurobond, made a bid for Finance One in mid-November that irked senior creditors who have direct loans to Finance One. On Wednesday [December 3] the senior creditors enlisted WestLB, the German bank, to submit a rival offer." (Financial Times, December 5, 1997)

foreign debts, and speculators taking positions on the news that the central bank had lent another B59.9 billion ($1.24 billion) to troubled financial institutions in the preceding two weeks.

6. Hindsight

With the benefit of hindsight, alternative paths in history can be explored. Of course, all of the following scenarios are extremely hypothetical, and counter-factual. However, they pose questions from which some lessons can be learned.

First of all, the Bank of Thailand should have devalued the currency much earlier than July 2. The currency was under attack periodically since the summer of 1996. Speculative attacks in January, February and March were relatively large, although much smaller than the eventual attack in May. A decision could have been made back then before losing a massive amount in foreign reserves in forward contracts. The lesson from Mexico, that is, if devaluing, do it when foreign reserves are still ample, was not learned. The IMF insists that it had advised Thailand repeatedly to change the exchange rate regime to a more flexible one. The outcome might have been different if the baht was floated before May. This scenario poses a general question on the exit strategy for a country with a fixed exchange rate and the early warning signals of a currency crisis.

Second, if the finance companies problem had been dealt with decisively, namely closure and liquidation of the worst, insolvent finance companies, early in the stage (say, before devaluation), then confidence would have been maintained, and the currency crisis might have been avoided, and certainly the "cleaning-up" cost for the government would have been much less. Real estate loans and declining land prices should have been a warning signal. Even after the devaluation, and even after the IMF program, the decision could have been made quicker. It was envisaged at the time of the IMF program, the decision on 42 finance companies would be made by early November. It was delayed by one month, during which Indonesia and South Korea became victims of contagious currency crises. This experience shows how important it is to have sound bank supervision and a legal framework to close and liquidate financial institutions orderly.

Third, the size of the IMF package could have been larger. It was unfortunate that a 500% of quota was the de facto limitation for Thailand. Only when South Korea became a problem, was another facility created to provide ample liquidity from IMF. (South Korea obtained 2000% of quota, of which 1500 % was under the newly created facility.) The market was not convinced that Thailand was out of woods when the IMF package was announced. If in addition, the United States had contributed to the IMF package, it might have stabilized the baht level at the time of the Tokyo meeting. This aspect, in conjunction with slow financial restructuring, contributed to a further decline of the baht after August, and possibly caused the contagion for the rest of the region.

It can be concluded that precious time was lost from late August to December in settling on a framework to resolve the problem of weak and debt-ridden financial institutions and strengthen the rest. It may have been necessary for the democratic process to take time. It took a new government to implement necessary reforms.

However, the Thai government could have taken more decisive action right after the IMF program, and the World Bank could have taken more prompt action in advising Thailand. The delay was costly: the baht and the stock prices continued to slide and the government had to change to restore confidence.

7. Lessons for other countries

Many lessons can be drawn from the Thailand case.

(1) **Exit Policy.** IMF has to come up with a better plan for a country with a peg system on how to exit from a (dollar) peg regime without losing the confidence of investors. The peg system often invites overvaluation, leading to current account deficits. It is easy to say that the currency has to be "flexible." However, a flexible exchange rate under heavy capital inflows would appreciate the currency, and aggravate the misalignment. Both Mexico and Thailand, in the midst of 8 percent current account deficits, were accumulating foreign reserves in the presence of current account deficits, up to only months before their crises. Going flexible a year earlier would have meant appreciation, making the subsequent crash of the currency harder. A counter-argument would be that by making the exchange rate flexible, currency risk would have alerted investors, thus reducing inflows.

(2) **Early warning signals.** Developing early warning signals that predict a crisis in the near future, is crucial for the IMF to warn a country. However, once it is developed reliably, investors will change their behavior in order to be one step ahead of the signals. The so-called Lucas critique applies here.[5]

(3) **Bank supervision.** The IMF, the World Bank, and the BIS are working on the standard of bank supervision. It has become a standard interpretation that the mistake committed by some of the emerging market economies was to liberalize capital accounts without an adequate change in bank supervision. When short-term capital came in, bank management operated as if deposits came from domestic investors who would have little choice in their portfolio management. Bank management, and also foreign institutional investors, counted on implicit guarantee on deposits by the government. Under these conditions, banks tend to over-lend to risky projects, (usually the real estate sector) as liquidity becomes abundant due to capital inflows, and lenders did not check the bank's risky investment. When supervision is tightened,

[5] The Lucas critique became famous in the context of rational expectation macroeconomic models: The market participants adjust their behavior when policy is changed, so that changing the policy rule based on regressions under a previous policy rule is not advisable.

capital markets can be liberalized, the reformer would argue. However, it is difficult to train human capital in supervision as well as in bank management. Even the United States, United Kingdom, Japan, and the Scandinavian countries, among others, suffered from lax bank supervision. How quickly financial and capital markets can be liberalized basically depends on how quickly human capital standards in finance can be met.

(4) **Burden sharing.** IMF should devise some ways to prevent moral hazard of lenders, while preventing a systemic risk. It is clear that overborrowing is also overlending. When IMF programs continue to bail out lenders, investors become more convinced that country and default risk is minimal. After the Mexico crisis, there was an argument that even a sovereign debt (i.e. Tesobonos in the case of the Mexican crisis) should not be considered risk free (Group of Ten (1996)). Hence, there was no guarantee that Thailand's private bank would have been protected. Of course, in reality, it was difficult not to guarantee the stakes of the creditors with the fear of liquidity crisis arising. At the time of the June 27 announcement, if a blanket guarantee had not been provided, a panic withdrawal might have occurred (just as the case in Indonesia several months later). It is the role of IMF to determine how burden sharing can be arranged without causing a systemic risk.

(5) **Regional surveillance.** Regional surveillance will become important in light of the contagion. Also peer pressure may work better than the IMF warning or conditionality. As the contagion is a real threat, neighbors may have more at stake and credibility in putting pressures on a country in a (near-)crisis. Regional surveillance became a part of the Manila framework (November 1997).

(6) **Larger funds.** IMF must be equipped with larger funds to support larger packages. A reversal of capital flows could be massive compared to imports or current account deficits. In order to stabilize credibly a country in a crisis, the amount of the IMF assistance has to be large. One institutional difficulty was an implicit limit in the Stand By Agreement. Mexico received 500% of quota from IMF, and the Thai program was 500% of quota. These numbers were far too little for them. That was why, the United States lent to Mexico and Japan lent to Thailand.

8. Concluding Remarks

This chronological report provides many details on the developments of the Thai baht crisis. Lessons can be learned from several turns of the event. It is important to distinguish what were known to the monetary authorities at the time and what should have been in done in hindsight. However, hindsight in Thailand would serve to provide as lessons to other countries.

These details provide many lessons to other emerging market countries. IMF should advise countries with a fixed exchange rate system when to exit from this arrangement, if fundamentals change adversely. The timing becomes tricky when large capital inflows are masking or aggravating the problems in fundamentals. Second, countries should float their currencies with ample reserves. Exhausting the reserves like Mexico and Thailand would make it more difficult to regain confidence after devaluation (float). Third, in order to measure the timing of a crisis, a set of early warning signals may be developed, but their reliability at this moment is not great. Fourth, the strength of the financial system (banks and nonbanks) is crucial in fending off attacks on the currency and in rebuilding the confidence after devaluation. Bank supervision has to be strengthened when capital controls on inflows are to be liberalized. Fifth, burden sharing by investors in emerging market financial instruments (bond and bank deposits in particular) may have be considered when risky investments are to be bailed out by a IMF program, directly or indirectly. Sixth, regional surveillance is even more important, as contagion has become a severe problem. The Manila framework, introduced in November, is expected to help create peer pressure in the Asia-Pacific region. Seventh, IMF funds have to be increased to meet the needs for larger funds. The access limit should be carefully reconsidered in case of emerging market countries. In the IMF package for South Korea, the limit was extended by the newly-created SRF facility.

ロシア担保法制の現状
——新抵当法の制定を機に——

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はじめに

旧社会主義体制の下では、担保制度は、ごく限定的な質権以外には存在しなかった。そもそも私的所有権の範囲がきわめて限られていたために、担保制度の存在意義がそれほどなかったのである。しかし、社会主義体制の崩壊と市場経済の導入により、担保制度を整備する必要性が認められるようになった。1990年に制定されたソビエト連邦民法の基礎は、本格的に担保制度について規定した初めての立法であった。続いて1992年にはロシア連邦担保法が制定された。もっとも、これらの立法は必ずしも整った法律とはいえず、多くの空白がみられた。

これに対して、1994年に制定されたロシア連邦民法典第一部は、債権法の部に担保に関する包括的な規定をおいた。すなわち、民法典は、債務履行の担保と題する一章をおき、その中で、保証、銀行保証などの制度とともに、担保について規定したのである。ロシア連邦民法典では、担保権は、「帝政ロシア以来の伝統により」、物権ではなく債権とされる。帝政時代に民法は、ロシア帝国法令大全第10巻に規定されていたが、そこでは担保権は、物権ではなく、契約法の部に、保証、手附などとともに規定されていた。[1]　ロシア連邦民法典は、この例にならったものである。担保権が債権とされるのは、それが対人的権利である、債務者からの優先弁済権として構成されるためと思われる。

一方、1992年の担保法は、民法典に反しない限りで適用されることになった。債権担保などについては民法典の規定が十分ではないため、なお1992年法の適用の余地はある。さらに、1998年7月に特別法として抵当法が制定され、施行された。

ロシア連邦以外の旧ソビエト連邦諸国をみると、カザフスタン民法典は、ロシア民法典をもとにしており、担保法にも共通な部分が多い。アゼルバイジャン、トルクメニスタン、ウクライナ、キルギスタンなどでは、単行の担保法がある。これらはロシアの1992年担保法に類似している。

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* 小田博ロンドン大学教授（弁護士、加藤・西田・長谷川法律事務所）はロシアCIS及び東欧法の第一人者であり、本行はロシア東欧関係のアドバイスを随時依頼している。