

6. Conclusion

The Thai economy continued to expand in 2010 Q3 over the same period last year. Although the pace of expansion appeared to have slowed from its rapid pace seen earlier in the first half of the year, it was in fact returning to a normal trend growth. The ongoing expansion was mainly driven by private consumption and investment, thanks to strong employment, rising farm income, and accommodative monetary conditions. Meanwhile, the export sector remained buoyant despite a slight slowdown in trading partners' economies.

Going forward, the Thai economy is poised to continue to expand. Output growth for 2011 is projected to be close to the projection in the previous *Inflation Report*, with private consumption and investment both driving domestic demand. Meanwhile, net exports will play a smaller role due to acceleration in imports following expanding economic activities. Moreover, inflationary pressures will gradually edge up in 2011, fuelled by both supply- and demand-side factors, especially in a period of continued expansion. In this environment businesses are likely to pass on rising costs to goods prices, having been cooperative with the government in delaying price adjustments in the past.

With regard to recent monetary policy decisions, the MPC judged on 1 December 2010 that the global economy had continued to recover as expected and the broad direction of monetary policy in the major

economies had eventually emerged. At the same time, the fundamentals underpinning the Thai economy remained satisfactory and continued to improve. Meanwhile, inflationary pressures were projected to edge up in the period ahead. Therefore, the MPC decided to raise the policy interest rate by 25 basis points from 1.75 to 2.00 per cent. Then, in its last meeting on 12 January 2011, the MPC viewed risks to the global economy subsiding. Meanwhile, the Thai economy appeared to have gained some traction, with consumption and investment poised to grow further. With economic activity expected to increase, pass-through of rising production costs, in particular oil and commodity prices, to consumer prices would be more apparent. Consequently, the MPC decided to raise the policy interest rate by another 25 basis points from 2.00 to 2.25 per cent.

*Report: “Economic/Business Information Exchange Programme
between the Bank of Thailand and the Business Sector”*

As of 30 December 2010

Overall summary

According to the Economic/Business Information Exchange Programme between the Bank of Thailand and 184 firms nationwide in 2010 Q4^{1/}, overall business conditions continued to expand as the adverse effect from the flood was temporary and limited. Private consumption remained at a favourable level due to marketing promotion and credit expansion. Private investment continued to expand in preparation for increasing demand from both domestic and foreign markets. Going forward, overall business activities in 2011 were expected to grow continuously, supported by increased domestic demand and the government’s stimulus measures. However, difficulties in price adjustments owing to intense competition, appreciation of the Thai baht, higher production costs, uncertainty in the global economy, and domestic political instability posed concerns to the business outlook.

- **Private Consumption.** Private consumption moderated from the previous quarter as consumer confidence deteriorated from the impact of the flood. Nonetheless, the adverse effect was expected to be temporary and demand for durable goods was expected to increase to compensate for damages from the flood. Consumption remained on an increasing trend with favourable economic growth, rising major crop prices, credit expansion, and marketing schemes.
- **Real estate market.** House prices and housing loans moderated due to an increase in the supply of newly launched projects, active marketing promotions, and the termination of the stimulus measures. However, since the share of home loans with the loan-to-value ratio higher than 90 per cent had been gradually increasing throughout the year, the Bank of Thailand thus imposed prudential measures on housing loans as a signal to the market to take a more cautious view. The measures were to take effect in January 2011 for condominiums and January 2012 for townhouses and single-detached houses, leading some home buyers to finalise their purchases sooner.
- **Production and exports** moderated towards a normal trend as the flood affected production temporarily and only in specific areas. Exports of sugar, rubber, tapioca declined due to natural disasters whereas exports of manufactured goods, especially vehicles, increased in response to foreign demand. Nevertheless, businesses’ revenue in baht declined following the appreciation. In response, firms adjusted their operations by seeking new markets, improving productivity, shortening advance order books, increasing prices of products, and using hedging instruments.
- **Private investment** continued to grow from the previous quarter in accordance with the expansion of domestic and external demand as well as the decrease in import prices following the baht appreciation. In addition, new and replacement investments were undertaken by several businesses, particularly vehicle and food processing industries in order to produce advanced technology products or substitute for workers under tight labour market conditions. Regarding the wholesale and retail sectors, new branches and warehouses were planned for Bangkok and elsewhere throughout 2011.
- **Employment** increased from the previous quarter. The agricultural sector employed more workers after the drought, with some workers moving out of the service and manufacturing sectors. This labour reallocation, coupled with an ongoing job-worker qualification mismatch, caused many manufacturing firms to experience labour shortage and high turnover. As a result, businesses adjusted themselves by extending over-time work hours, increasing wages, and hiring more migrant workers.
- **Production costs** edged higher following an increase in oil prices and other commodity prices. In this regard, prices of agricultural products such as rubber, sugar, and palm oil increased because of the supply shortage owing to drought, flood, and pest outbreak. Furthermore, labour costs also rose as a result of an increase in demand for labour and an upward adjustment in the minimum wage.
- **Credit** granted to businesses continued to expand well into the beginning of 2011 in line with economic growth. As business sentiment improved, fixed investment loans tended to rise faster than working capital loans. Household loans, especially hire purchase loans for vehicles, expanded favourably in line with an increase in consumption. Housing credits, however, moderated somewhat.
- **Business constraints and risks.** Price adjustment was proved difficult due to intense competition and prior settlements. Meanwhile, revenue declined owing to the baht appreciation as well as increased costs of production following the increase in oil prices, raw material prices, and wages. In addition, uncertainty in the US and European economies as well as domestic political instability posed concerns to the business outlook.

^{1/} Including responses from the Business Sentiment Survey (about 520 business firms per month).