6. Conclusion

The Thai economy continued to recover in the first quarter of the year, growing faster than projected in the previous *Report*. This is mainly owing to (1) a strong rebound of exports following the global economic recovery, particularly in Asia; (2) the acceleration of private investment in line with an increase in production capacity to support increasing economic activities; and (3) an improvement in employment conditions as well as an increase in farm income, which have been supportive of private consumption.

Going forward, for this year the MPC projects the Thai economy to grow faster than previously anticipated, as a result of robust growth during the first half of the year. In addition, the impact of domestic political situation on the Thai economy in the second quarter is expected to be limited, as reflected by signs of continued expansion in private spending and exports of goods. Nevertheless, momentum in the latter part of the year will diminish somewhat given the sovereign debt problem and concerns over the health of financial institutions in Europe as well as lingering political concerns at home. For 2011, the Thai economy is expected to grow at a pace close to the previous projection. Growing demand and increasing production in line with the economic recovery is expected to gradually bring the output gap to a close. As a result, core and headline inflation are projected to rise in 2011 to levels slightly higher than previously forecasted, although inflationary pressures are likely to be modest in the short term due to an extension of government's subsidies.

With regard to monetary policy, at the meeting on 2 June 2010, the MPC saw the economic recovery becoming more apparent and the need for accommodative monetary policy substantially reduced. Nevertheless, uncertainties in the global economy and domestic political problems continued to pose significant downside risks to the economic outlook. The MPC therefore kept the policy interest rate unchanged at 1.25 per cent per annum. Subsequently, at the meeting on 14 July 2010, the MPC judged that the need for an exceptionally accommodative monetary policy had diminished, as confirmed by increasingly clearer signs of economic recovery together with the limited impacts from domestic political conflicts. With a view to bringing policy interest rate closer to normal levels, the MPC decided to raise the policy interest rate by 0.25 per cent per annum, from 1.25 to 1.50 per cent per annum.

Report: "Economic/Business Information Exchange Programme between the Bank of Thailand and the Business Sector"

As of 30 June 2010

Overall summary

According to the Economic/Business Information Exchange Programme between the Bank of Thailand and 254 firms nationwide during 2010 Q2[1/], overall business conditions continued to improve from the previous quarter despite the political unrest as its impact was limited. Both domestic and foreign demand continued to expand in accordance with the global economic recovery, higher farm income from rising crop prices and improved consumer and business sentiment during the last month of the quarter. Looking ahead, overall business conditions were expected to improve thanks to fiscal impetus and growing demand, pointing to increasing investment activities subsequently. Nonetheless, domestic political instability, uncertainty in the economic conditions and difficulties in price adjustments owing to intense competition represented risks to the business outlook.

- **Private consumption** still expanded despite the political unrest. Sales of household products and durable goods, such as automobiles and electrical appliances, remained at high levels in line with the ongoing economic recovery, rising farm income, various marketing schemes, easing consumer credit standards, together with improved consumer confidence in the last month of the quarter.
- **Tourism** as a whole deteriorated from the previous quarter, especially in Bangkok and the Central Region of the country owing importantly to the domestic political unrest. However, tourism still expanded in the South given an increase in the number of tourists from Singapore and Malaysia. Tourists, particularly those from China, Hong Kong and ASEAN countries, returned at the end of the quarter as political tensions eased.
- **Production and exports** expanded in line with an increase in domestic and foreign orders, particularly for vehicles, electronics and electrical appliances. In light of the political unrest, distribution of goods and raw materials, together with night-shift production where curfew was imposed, was briefly and modestly affected. Overall production remained roughly unchanged from the level in the previous quarter, and orders remained high, especially for vehicles with backlog orders of 2-4 months.
- **Private investment** continued to increase from the previous quarter in preparation for growing demand–in particular, investment in machinery to improve efficiency in the production of automobiles, hard disk drives and electrical appliances. The increase in investment was in line with business purchases of imported capital goods. Data from Thailand's Board of Investment (BOI) also showed the number of investment projects applying for tax privileges–mostly investment in alternative energy power plants, hot-rolled sheet and vehicle parts–rising year-on-year.
- **Employment conditions** improved as reflected by an increase in labour demand in both agricultural and manufacturing sectors. A number of SMEs experienced labour shortage, as they were unable to compete with large firms which offered relatively more competitive wages, leading to a higher turnover rate and longer time to fill vacancies for SMEs. Nevertheless, the entry of new graduates in this quarter helped to alleviate labour market tightness.
- Businesses encountered higher **costs of production**, following a rise in demand for raw materials given increased production in this quarter. In response, businesses focused more on efficient cost management rather than hiking **prices** because of intense competition.
- Demand for **loans** by non-financial businesses slightly increased from the previous quarter. Loans to large businesses were mostly for fixed investment and working capital, whereas loans to SMEs were for working capital and refinancing in response to low interest rates. While credit standards remained almost unchanged from the previous quarter, financial institutions still closely monitored credits granted to businesses in the tourism and real estate sectors.
- **Business constraints and risks.** Domestic political instability remained a crucial risk to businesses even as concerns had somewhat eased. Uncertainty in economic conditions regarding the sovereign debt problem and its potential impacts on financial institutions in Europe, difficulties in price adjustment given intense competition, together with price administration by the government were perceived as risks to businesses going forward.

1/ Including responses from the business sentiment survey (about 520 business firms per month).