BANK OF THAILAND

Thailand's Economic conditions in 2014

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Year 2014 at a Glance and Outlook for 2015

The Thai economy in 2014 expanded only by 0.7 percent, owing to internal and external constraints that inhibited growth. In the first half of the year, the economy experienced zero growth as political situation hindered certain government operations and undermined the confidence of households, businesses and foreign tourists. An elevated level of household debt contributed to restrained consumer spending as well as to cautious lending by financial institutions. Recovery of merchandise exports was slow due to a gradual improvement in global demand. In addition, Thai manufacturers still suffered from limited production capability in high-technology products. Under these circumstances, businesses delayed production and new investment.

In the latter half of 2014, the Thai economy recovered gradually after the easing of political uncertainty. Domestic spending and the tourism sector improved, while the government resumed its normal operation. Additionally, investment in telecommunications and retail businesses gathered pace to meet the expected growing future demand. However, overall economic recovery was sluggish as merchandise exports remained weak in tandem with major trading partners' economic conditions, particularly China, Japan and Europe, while household spending was hurt by low farm income and high debt burden. The confidence of foreign tourists was not fully restored because many countries still maintained their travel warning advisory levels. Most businesses continued to defer investment, awaiting economic recovery and the government's infrastructure investment.

Overall economic stability was nonetheless well preserved. Headline inflation declined on account of a sharp fall in domestic oil prices, while core inflation increased due to the pass-through of higher liquefied petroleum gas (LPG) prices to food prices. At the same time, financial position of businesses and financial institutions remained strong. Private household and corporate credits slowed down, in line with the overall economic conditions and cautious lending of financial institutions, after a high rate of growth in the preceding years.

External stability was also well maintained. The current account registered a surplus owing mainly to a decline in imports following the economic slowdown and the fall in oil prices towards the end of the year. The capital account was in a deficit as Thai investors increased investment abroad, both in the form of direct investment and portfolio investment. Meanwhile, the movements of **Thai baht** were driven by the political situation, signs of the U.S. economic recovery, and differences in monetary policy of major economies. However, overall the Thai baht experienced low volatility comparing to the previous year and depreciated slightly at the end of 2014. At the same time, the Effective Exchange Rates appreciated, owing to the depreciation of the yen, euro and ruble in tandem with weak economic recovery in Japan and the euro area as well as the economic slowdown in Russia.

Monetary conditions were consistently accommodative. In March 2014, the Monetary Policy Committee (MPC) reduced the policy rate from 2.25 to 2.00 percent per annum, with a view to mitigate the risks stemming from political uncertainty and provide support for the early stage of economic recovery. In the second half of the year, the MPC judged that continuation of accommodative monetary policy was necessary to support Thailand's economic recovery without undermining financial stability.

Looking ahead, the Thai economy in 2015 is projected to perform better than in 2014. Private spending, benefited by the decline in oil prices, and the revived tourism sector are expected to be the main engines of growth. Government spending would also add to the growth momentum, contributing to improved business sentiments and investment climate. Merchandise exports are likely to edge up gradually in line with trading partners' economic conditions. **Inflation is likely to remain low** due mainly to falling global oil prices and subdued inflationary pressure from domestic demand.

Risks that render close monitoring include the following: (1) export recovery could be constrained by economic conditions in China, Japan and Europe—as well as the limited production capability of Thai manufacturers in high-technology products; (2) volatile capital flows could arise from more diverging monetary policies of major economies; (3) the continuity of government policy and government ability to meet fiscal spending targets may affect growth prospects; and (4) household's purchasing power still suffers from weak farm income, held down by low agricultural prices, as well as elevated debt burden.

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Thailand's Economic Conditions in 2014

	2012	2013			2014		
	Year	H1	H2	Year	H1	H2	Year
(Annual percentage change, unless specified otherwise)							
Gross Domestic Product [1/]	**6.5**	4.2	1.6	**2.9**	0.0	1.4	**0.7**
Demand (expenditure)							
Private consumption expenditure	**6.7**	3.4	-2.7	**0.3**	-1.3	2.0	**0.3**
General government consumption expenditure	**7.5**	5.4	4.5	**4.9**	3.1	2.5	**2.8**
Gross fixed capital formation	**13.2**	5.2	-8.8	**-2.0**	-8.1	3.0	**-2.8**
- Private	**14.4**	2.4	-8.1	**-2.8**	-7.2	4.0	**-1.9**
- Public	**8.9**	17.0	-11.2	**1.3**	-11.3	-0.6	**-6.1**
Exports of goods and services	**3.1**	5.6	2.9	**4.2**	-0.5	0.5	**0.0**
Imports of goods and services	**6.2**	6.3	-1.4	**2.3**	-8.8	-0.7	**-4.8**
Supply (production)							
Agriculture	**3.8**	1.5	1.2	**1.4**	2.7	-0.4	**1.1**
Manufacturing	**6.9**	1.9	-1.7	**0.1**	-2.2	0.0	**-1.1**
Construction	**7.8**	7.6	-5.0	**1.0**	-7.5	0.0	**-3.8**
Services and others	**6.6**	6.2	4.6	**5.4**	1.5	2.8	**2.2**
Domestic stability							
Headline Consumer Price Index	**3.02**	2.70	1.67	**2.18**	2.23	1.56	**1.89**
Core Consumer Price Index (excluding raw food and energy)	**2.09**	1.23	0.78	**1.00**	1.45	1.72	**1.59**
Unemployment rate (percent)	**0.7**	0.7	0.7	**0.7**	0.9	0.7	**0.8**
Public debt (end of period, billion baht)	**4,961**	5,224	5,450	**5,450**	5,655	5,624	**5,624**
Share of GDP (end of period, percent)	**43.7**	44.5	45.7	**45.7**	47.1	45.8	**45.8**
External stability (billion U.S. dollars)							
Trade balance	**6.0**	-2.5	9.2	**6.7**	12.2	12.4	**24.6**
Current account balance	**-1.5**	-6.2	3.7	**-2.5**	4.9	9.3	**14.2**
Capital account balance	**0.2**	0.1	0.1	**0.3**	0.0	0.1	**0.1**
Financial account balance	**13.7**	8.1	-7.8	**0.3**	-6.5	-8.9	**-15.4**
Balance of payments	**5.3**	0.2	-5.2	**-5.0**	-1.1	-0.1	**-1.2**
Gross international reserves (end of period)	**181.6**	170.8	167.3	**167.3**	168.2	157.1	**157.1**
External debt (end of period)	**130.7**	140.9	141.9	**141.9**	144.8	140.8	**140.8**
International reserves to short-term debt (percent)	**3.1**	2.7	2.7	**2.7**	2.7	2.7	**2.7**
External debt to GDP (percent)	**38.0**	39.3	38.7	**38.7**	39.2	37.5	**37.5**
External debt to export value (percent)	**51.5**	53.1	51.9	**51.9**	52.6	50.3	**50.3**
Short-term debt to external debt (percent)	**44.5**	45.6	43.6	**43.6**	43.1	40.6	**40.6**
Monetary statistics (end of period) (billion baht)							
Monetary base	**1,497.8**	1,386.1	1,581.3	**1,581.3**	1,508.1	1,666.8	**1,666.8**
Annual percentage change	**9.7**	4.2	5.6	**5.6**	8.8	5.4	**5.4**
Narrow money	**1,598.3**	1,519.7	1,661.3	**1,661.3**	1,585.2	1,681.3	**1,681.3**
Annual percentage change	**13.0**	4.6	3.9	**3.9**	4.3	1.2	**1.2**
Broad money	**14,966.8**	15,446.0	16,062.2	**16,062.2**	16,119.8	16,808.0	**16,808.0**
Annual percentage change	**10.4**	10.2	7.3	**7.3**	4.4	4.6	**4.6**
Financial institutions' deposits including bills of exchange [2/]	**14,656.5**	15,214.1	15,764.2	**15,764.2**	15,788.5	16,402.0	**16,402.0**
Annual percentage change	**11.1**	10.4	7.6	**7.6**	3.8	4.0	**4.0**
Financial institutions' private credits [2/]	**13,359.0**	13,989.9	14,688.9	**14,688.9**	14,892.7	15,351.0	**15,351.0**
Annual percentage change	**15.3**	12.9	10.0	**10.0**	6.5	4.5	**4.5**
Interest rates (end of period) (percent per annum)							
- Repurchase rate, one-day	**2.75**	2.50	2.25	**2.25**	2.00	2.00	**2.00**
- Overnight interbank rates (mode)	**2.65**	2.40	2.15	**2.15**	1.90	1.90	**1.90**
- Time deposit rate, one year [3/]	**2.46**	2.40	2.23	**2.23**	1.73	1.73	**1.73**
- Prime rate (MLR) [3/]	**7.00**	7.00	6.84	**6.84**	6.75	6.75	**6.75**
Exchange rate (end of period) (baht per U.S. dollar)	**30.61**	31.02	32.86	**32.86**	32.45	32.90	**32.90**

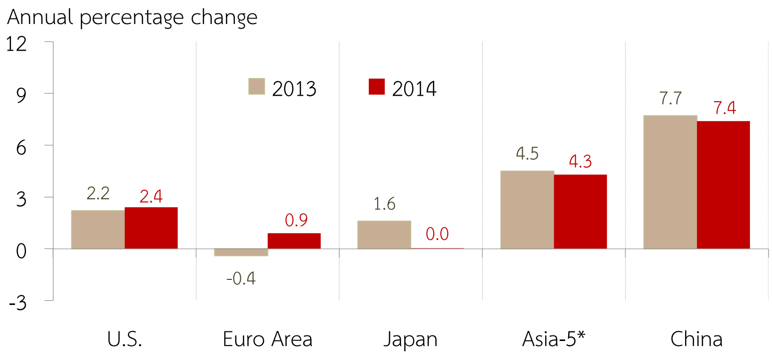
Note: [1/] At constant prices
[2/] Financial institutions consist of all deposit-taking institutions except the Bank of Thailand
[3/] Average rate of four largest commercial banks
E = estimated data

Sources: Office of the National Economic and Social Development Board, Ministry of Commerce, National Statistical Office, Public Debt Management Office and Bank of Thailand

1. Global Economies

In 2014 the world economy improved from the previous year, but the pace of recovery was fragile and uneven across different regions. The U.S. economy posed a strong growth, underpinned by steady improvements in economic fundamentals. However, economic recovery in the euro area and the Japanese economy remained slow. The Asian economies expanded at a slower rate, with China's economic growth beginning to moderate following economic reform.

Global Economic Growth in 2013 and 2014



Note: * GDP-PPP weighted average of five countries: Indonesia, the Philippines, South Korea, Taiwan, and Singapore

Source: Bureau of Economic Analysis (U.S. Department of Commerce), Cabinet Office of Japan, CEIC, Eurostat, and calculations by Bank of Thailand

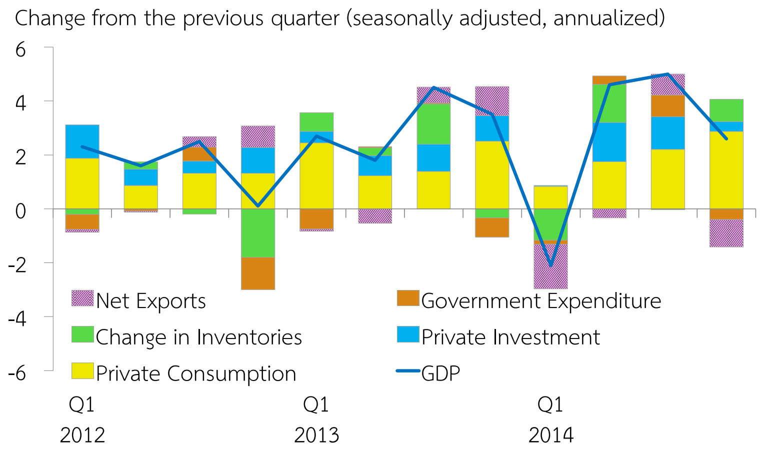
Major industrialized economies (G3)

The U.S. economy expanded well as a result of continued improvement in economic fundamentals.

In 2014 the U.S. economy expanded by 2.4 percent, up from 2.2 percent in the previous year. In the first quarter of 2014, the economy contracted amidst the unusually cold weather that disrupted economic activities. However, positive GDP growth resumed in the second quarter, driven by the expansion of household spending, private investment, exports and inventory accumulation.

In the latter half of the year, the U.S. economy continued to grow thanks to steadily improving economic fundamentals, especially better conditions in the labor market. The housing market recovered gradually, leading to the decision of the Federal Open Market Committee (FOMC) in its October meeting to end the purchase of longer-term treasury securities and mortgage-backed securities[1]. The U.S. economic growth in the periods ahead is likely to be sustained by 1) the invigorated labor market, 2) more buoyant business and consumer sentiments, 3) low oil prices, 4) better households' balance sheet in line with rising asset prices, and 5) the continued easing of monetary policy.

Contribution to U.S. GDP Growth



Source: U.S. Department of Commerce

[1] At the meeting on October 28 - 29, 2014, the FOMC decided that it would maintain the federal funds rate at 0 - 0.25 percent per annum and end its asset purchase program of longer-term treasury securities and mortgage-backed securities.

The euro area[2] expanded at a slow pace due partly to geopolitical tension.

Euro area economies grew by 0.9 percent in 2014, rebounding from a 0.4 percent contraction in the preceding year. Nevertheless, the pace of the recovery was gradual. Economic activities accelerated in the first quarter, thanks to the unusually warm weather in Europe that encouraged private investment, particularly in the construction sector. In the second quarter, however, growth was held down by the tension between Russia and Ukraine, which dented business confidence and caused delays in private investment.

Euro area economies remained weak in the second half of the year, owing mainly to the escalating conflict between Russia and Ukraine following the European Union's imposition of sanctions on Russia, as well as the lagging progress of structural reforms in France and Italy. In addition, the risk of prolonged low inflation[3] prompted the European Central Bank (ECB) to persistently ease its monetary policy starting in June 2014[4]. In the periods ahead, the ECB's accommodative monetary policy, falling oil prices, and gradual waning of fiscal drag are expected to support the euro area's modest economic growth. However, a sustained economic recovery requires the completion of long-term structural reforms.

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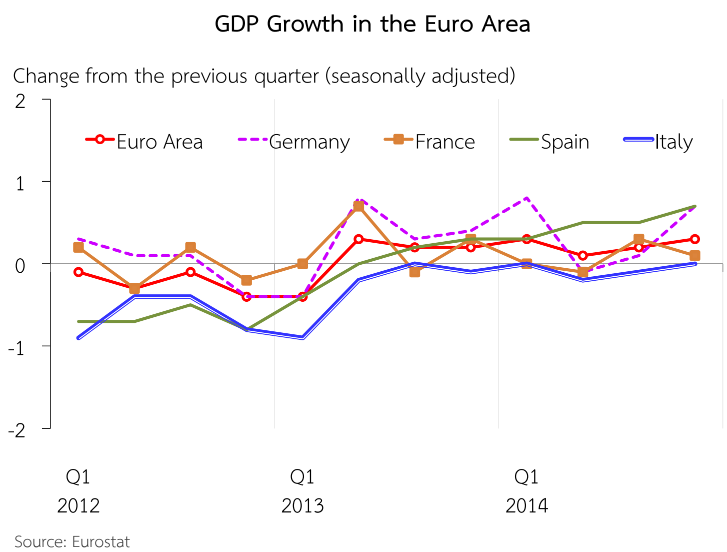
[2] The euro area comprises 18 countries using the euro currency. The economies of Germany, France, Italy and Spain have 29, 22, 16 and 11 percent share of the total euro area's economy in 2013 respectively. The economies of Greece, Ireland and Portugal combined made up 5 percent share of the euro area.

[3] In October 2014, the International Monetary Fund (IMF) made an assessment that recession risks in the euro area had risen to 38 percent, up from 20 percent in April 2014.

[4] The ECB (1) cut the interest rates in two meetings (June and September, 2014) by a total of 0.2 percent, with the refinancing rate, the ECB marginal lending rate, and the ECB deposit rate reduced to 0.05, 0.3 and -0.2 percent respectively, (2) announced the Targeted Longer-term Refinancing Operations (TLTROs) scheme, designed to provide liquidity to commercial banks in order to encourage long-term, low-interest lending to private sectors, and (3) announced its asset-backed securities purchase program and covered bonds purchase program.



Japan's growth stalled as a result of consumption tax hike in the second quarter of 2014.

The Japanese economy flattened in 2014. The first quarter saw robust growth from accelerated economic activities in anticipation of the upcoming consumption tax increase[5]. The tax hike, however, caused households and businesses to cut down on spending, sending the economy into contraction in the second quarter and a technical recession in the third quarter of the year.

Given subdued economic conditions, the Bank of Japan's Monetary Policy Committee announced additional quantitative easing[6] to support economic growth and bring inflation back to the target of 2 percent. The government also postponed the second-round tax increase[7] from October 1, 2015 to April 1, 2017. The monetary policy easing, the yen depreciation, and the tax hike delay should boost the Japanese economy in the short-run. Nevertheless, for a sustainable growth in the long term, structural reforms and definitive growth strategies are required.

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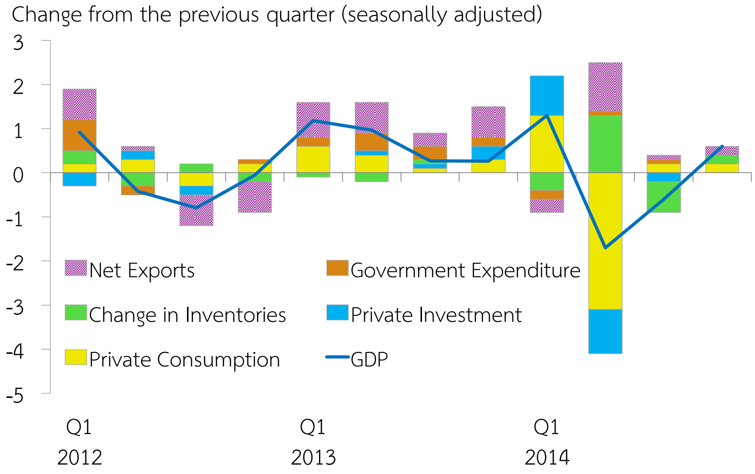
[5] Japan's consumption tax was raised from 5 percent to 8 percent on April 1, 2014.

[6] At the meeting on October 31, 2014, the Bank of Japan (BOJ) announced an expansion of the Quantitative and Qualitative Monetary Easing (Q-Squared). The BOJ announced to increase Japan's monetary base by 80 trillion yen each year (up from 60-70 trillion yen per year) via purchases of various assets, particularly the Japanese government bond.

[7] The second-round adjustment will raise the consumption tax rate from 8 percent to 10 percent.

Contribution to Japan's GDP Growth



Source: Cabinet Office of Japan

Chinese and other Asian economies expanded at a slower pace than last year mainly because of weakened domestic demand although exports of many countries recovered following expansion of major industrialized economies (G3).

The Chinese economy grew by 7.4 percent in 2014, down from 7.7 percent last year, as a result of subdued domestic demand. Contributing in part to the softened demand were reform measures aimed at reducing risks in the financial and the fiscal sectors. Investment slowed down particularly in industries with excess capacity and in the real estate sector in provinces with excess supply. Over the first half of 2014, overall consumption weakened, in large part due to fiscal consolidation. Meanwhile, exports posted a slower increase compared with the high base of the previous year, which saw inflated export figures due to over-invoicing by companies that channeled cash into the Chinese financial markets for speculation.

In the second half of the year, the economy continued to soften, owing importantly to the decline in investment. Consumption, however, started to stabilize thanks to rising wages and declining oil prices that supported purchasing power. Exports also improved, driven by the recovery of the U.S. economy - a major trading partner, and by the up-cycle of the electronics sector, where new products were released toward the end of the year.

The Chinese government unveiled various targeted measures to mitigate the impact of financial reforms on the agricultural sector and SMEs, which accounted for large shares of total employment, and to remedy supply and demand mismatch in the real estate sector. The Chinese government implemented targeted measures, including a reduction in Reserve Requirement Ratio (RRR) for commercial banks that primarily serviced large share of small and local businesses. Moreover, in an effort to provide adequate liquidity to promote private investment and consumption, the government cut the policy interest rate in November 2014, keeping borrowing costs at a level deemed appropriate. The government is expected to seek to strike a balance between supporting economic growth and pursuing structural reforms. Consequently, growth will likely remain moderate in the periods ahead.

Asian economies excluding China[8] expanded in 2014, albeit at a slightly slower pace than last year, mainly as a result of a slowdown in investment. During the first quarter, most economies showed signs of improvement as exports edged higher thanks to two main factors: 1) the recovery in major industrialized economies, particularly the euro area and Japan, and 2) the rebound of electronics exports in line with the global electronics cycle. However, growth began to subside in the second quarter due to sluggish exports, especially to Japan.

In the second half of 2014, Asian economies continued to slow down, owing importantly to the decline in exports growth to Japan, the euro area and China, and a more cautious lending climate that weakened private investment, particularly in the real estate sector. Nevertheless, private consumption expanded, thanks to high levels of employment. Going forward, the Asian economies are poised to expand in line with private consumption growth, which will likely to be supported by sound labor market conditions and low global oil prices. Exports are also expected to improve, due mainly to economic recovery in the U.S., a major export destination.

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[8] Asian economies considered include Taiwan, Hong Kong, South Korea, Malaysia, Indonesia, Singapore, and the Philippines.

2. Supply Side

2.1 Manufacturing Sector

In 2014, overall manufacturing production contracted from the previous year, particularly production for domestic sales following a marked slowdown in economic activities in the first half of the year. However, overall manufacturing production improved after the easing of political uncertainty in the middle of the year, and recorded a small positive growth in the fourth quarter.

Manufacturing production fell from the previous year in line with the decline in domestic market-oriented production. Domestic demand recovered slowly because of political uncertainty in the early months of 2014 and the elevated level of household debt which continued to weigh on private consumption. Depressed agricultural prices, especially in the latter half of the year, further dented purchasing power and prompted households to remain cautious with their spending.

Nevertheless, export-oriented manufacturing benefited from gradually improving external demand on the back of the steady recovery of the world economy. Several manufacturing industries, such as integrated circuits (IC), auto parts, rubbers and plastics products, were invigorated by the rebound in global growth. However, the hard disk drive (HDD) industry suffered from structural constraints, as it failed to respond effectively to changing preferences of global consumers. Meanwhile, the frozen shrimp industry failed to satisfy external demand as production was hit by a shortage of raw shrimps, caused by the spread of the shrimp disease. Despite these setbacks, the overall growth of external demand underpinned the gradual recovery of Thai manufacturing production in the second half of the year as reflected by increases in non-residential electricity consumption and employment in the manufacturing sector over the same period last year.

Key industries that enjoyed solid growth in 2014 included:

◆ **Integrated circuits (IC).** Manufacturing of IC continued to expand on the back of growing demand from other related industries. The automobile industry, in particular, used an increasingly high proportion of IC in vehicles such as electrical control of temperature, lights, seats and rear-view mirrors. Higher demand for IC also stemmed from growth in communication devices.

◆ **Rubbers and plastics products.** Manufacturing of plastics products grew, partly as a result of increased demand for plastics in everyday life. Moreover, there was stronger demand from other industries that used plastics as material base, both in Thailand and abroad.

◆ **Apparels.** The apparel industry posed a robust growth especially in the second half of the year, partly because of a temporary surge in demand ahead of the end of Thailand's Generalized Scheme of Preferences (GSP tax privilege) in 2015. There were also more orders for Thai apparels from the Japanese market.

◆ **Chemicals.** Manufacturing of chemicals rose in line with the growth in plastic granules production, as granules were used as materials in several related industries.

Key industries that contracted in 2014 were:

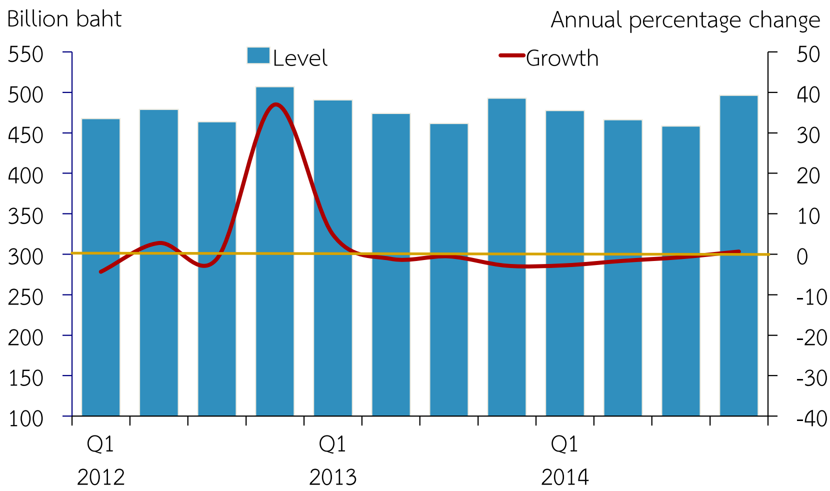
◆ **Automobiles.** Automobile production fell as a result of several factors: (1) manufacturers reduced production after completing the delivery of cars purchased under the first-car tax rebate scheme, (2) low farm prices and an elevated level of household debt deterred consumers from buying cars, (3) financial institutions were cautious with auto loans, amidst growing concerns over deterioration of loan quality, (4) the delay in some government's megaprojects held back commercial car purchase by private firms, and (5) the slowdown of automobile production for exports during the second half of the year due to softened demand from Thai major export destinations, outweighed the promising signs of this industry in the first half of the year.

◆ **Petroleum.** Petroleum production contracted mainly because an unusually high number of refineries were temporarily closed for maintenance. Softer domestic demand for oil in the context of unspectacular economic conditions was chiefly responsible for the abnormally high maintenance closure. Moreover, Thai producers cut petroleum production towards the end of the year, as the continuing slump in crude oil price created uncertainty in crude oil price forecasts and caused stock loss for producers.

◆ **Food and beverages.** Production of food and beverages declined, primarily as a result of a fall in frozen shrimp output. The frozen shrimp industry suffered from a shortage of raw shrimps, against the backdrop of the continuing spread of Early Mortality Syndrome (EMS) disease. Meanwhile, beer production decreased as sales were hit by lower domestic demand.

◆ **Hard disk drive (HDD).** HDD manufacturing production contracted in line with subdued global demand, as consumers turned away from HDD to higher-technology products and other substitutes, such as solid-state drive (SSD). At the same time, demand for new models of personal computers which primarily use HDD grew more slowly than previously anticipated. Large manufacturers therefore opted to delay new production in order to run down their inventory, which had been accumulated in the earlier periods. According to these factors, overall HDD production fell from last year. The structural constraints are expected to continuously restrict HDD production in the periods ahead.

Manufacturing Production at 1988 Prices



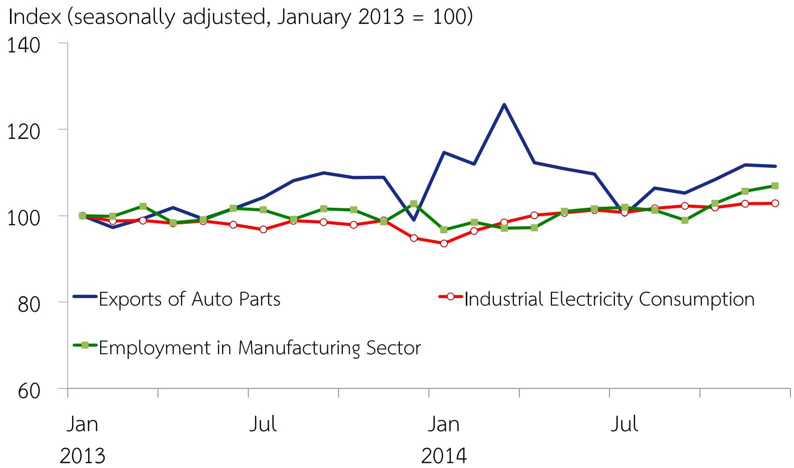
Source: Office of the National Economic and Social Development Board

Manufacturing Production Index (MPI)

Industry (Annual percentage change)	Weight 2000	Relative Weight 2012	2013	2014	2014			
					Q1	Q2	Q3	Q4
Food and beverages	15.5	14.1	-6.7	-2.7	-3.4	-5.0	-1.9	-0.4
Petroleum	10.4	8.6	-2.0	-6.3	-6.7	2.4	-11.0	-8.6
Textiles	7.3	2.1	3.3	-1.4	-0.5	-3.5	-1.1	-0.6
Apparels	7.1	4.2	-4.4	3.2	8.0	-2.4	-0.3	8.3
Hard disk drive (HDD)	7.2	24.3	-7.5	-1.7	-7.8	2.3	2.5	-3.8
IC & Semiconductor	6.8	4.4	-0.3	11.2	5.8	11.2	19.8	7.8
Automobiles	5.4	15.8	1.4	-22.5	-26.2	-29.3	-22.6	-9.4
Cement and construction	4.8	4.7	2.1	-4.1	-1.6	-5.4	-4.5	-4.9
Chemicals	4.4	4.2	-0.9	2.7	2.2	1.3	1.3	6.0
Rubbers and plastics	4.0	3.0	2.4	2.5	4.0	4.3	2.1	-0.4
Electrical appliances	3.7	4.9	-2.1	-1.3	-0.6	-7.4	-1.9	6.7

Source: Office of Industrial Economics

Other Manufacturing Production Indicators



Source: The Federation of Thai Industries, National Statistical Office, Metropolitan Electricity Authority and Provincial Electricity Authority, index calculations by Bank of Thailand

2.2 Agricultural Sector

In 2014, farm income[1] fell in line with declining agricultural prices, while agricultural output increased slightly.

Farm income declined for the third consecutive year, owing to depressed prices of rubber, rice and sugarcane — Thailand's top three economic crops that accounted for an overwhelming 59 percent of total agricultural output. Rubber, rice and sugarcane prices dropped by 26, 18 and 5 percent respectively. Low agricultural prices were attributable to three key factors: 1) rubber prices fell markedly on the back of lower global demand, particularly Chinese demand because China had a large stock of rubber. In addition, the slump in oil prices encouraged the switch from natural rubber to synthetic rubber in some cases, 2) rice prices declined following the end of the rice pledging scheme and the offloading of government rice stockpiles, and 3) sugarcane prices fell due to global excess supply caused by expansion of output in major world producers, especially Brazil.

Annual percentage change	2013	2014				
		Year	Q1	Q2	Q3	Q4
Farm income	-3.0	-5.3	2.3	-2.0	-5.5	-13.0
Agricultural output[P]	-2.2	1.0	3.1	5.4	1.8	-3.5
Agricultural prices	-0.8	-6.2	-0.8	-7.0	-7.2	-9.8

Note: Farm income does not include government transfers, which consist of income from the rice pledging scheme, subsidies for farmers, and compensation for production costs for farmers affected by natural disasters.
P = Preliminary data for the latest year
Source: Office of Agricultural Economics, calculations by Bank of Thailand

Agricultural output increased by 1 percent in 2014. Fruit and vegetable production rose, thanks to favorable weather conditions at the beginning of the year. Livestock output, especially poultry meat, increased in line with higher external demand and resumption of production by a large agricultural firm in the middle of the year. Rubber production stayed at a similar level from last year. Although rubber plantation areas expanded in the early part of 2014, output fell in the latter half of the year because farmers delayed their rubber tapping amidst depressed

[1] Farm income does not include effects of government measures.

prices. Meanwhile, rice output remained stable, as total cultivation area was close to last year's level.

Thai Agricultural Prices

(Unit: Baht per ton)

	2013	2014				
	Year	Year	Q1	Q2	Q3	Q4
Agricultural Price Index (2005 = 100)	**152.2**	**142.7**	**149.3**	**141.9**	**141.3**	**138.4**
Δ%	-0.8	-6.2	-0.8	-7.0	-7.2	-9.8
1. Crop Price Index (2005 = 100)	**158.1**	**142.3**	**149.5**	**141.0**	**140.2**	**138.3**
Δ%	-6.1	-10.0	-7.1	-11.8	-10.6	-10.7
Hom Mali Paddy	15,582	13,782	14,220	13,853	13,991	13,065
Δ%	3.2	-11.6	-10.4	-12.2	-10.7	-12.9
Paddy Class 1 (5%)	9,385	7,713	7,741	7,118	8,088	7,907
Δ%	-7.1	-17.8	-25.7	-27.5	-11.4	-3.3
Rubber	74,755	55,415	62,573	60,893	53,033	45,160
Δ%	-16.9	-25.9	-22.8	-19.4	-25.6	-36.6
Maize	7,897	7,241	6,677	7,360	7,440	7,487
Δ%	-12.7	-8.3	-23.8	-14.3	-2.2	12.8
Cassava	2,130	2,103	2,200	2,113	1,903	2,197
Δ%	5.7	-1.3	5.8	-4.9	-11.2	5.9
Oil palm	3,617	4,354	5,137	3,543	4,107	4,630
Δ%	-24.2	20.4	53.0	10.3	17.1	5.5
2. Livestock Price Index (2005 = 100)	**127.9**	**139.9**	**228.8**	**188.7**	**143.2**	**135.9**
Δ%	12.5	9.3	14.8	11.9	7.7	3.4
3. Fishery Price Index (2005 = 100)	**161.6**	**182.7**	**136.7**	**123.8**	**174.0**	**167.2**
Δ%	55.4	13.0	70.4	16.1	4.6	-18.0

Note: Δ% indicates percentage change from the same period last year

Source: Office of Agricultural Economics

2.3 Tourism Sector

The tourism sector contracted in 2014 due to prolonged domestic political uncertainty, along with deteriorating economic conditions and falling income of major tourist groups. As a result, the number of tourist arrivals declined for the first time in four years.

The number of tourist arrivals totaled 24.8 million in 2014, falling for the first time in four years by 6.7 percent from the previous year. The decline was due to three main factors. First, protracted political demonstrations starting in late-2013 led to the issuance of Emergency Decree for State of Emergency, the imposition of martial law, and the change in government on May 22, 2014. Against this backdrop, various countries issued travel warning advisory and raised the security risk levels according to the unfolding political developments. Second, fragile economic conditions in Russia, Japan and Europe, together with the depreciation of their respective currencies, led to a fall in tourist arrivals from these countries, which accounted for about 30 percent of total tourist arrivals. Third, there was stricter enforcement of a regulation that prohibited private buses registered in Malaysia from traveling outside Songkhla province. This resulted in a decline in the number of Malaysian tourists who, by nationality, formed the second largest foreign tourist group to Thailand.

However, the number of Chinese tourists, the number-one visitors to Thailand, picked up quickly after the domestic political situation was resolved. Despite moderating economic conditions in China, the number of Chinese tourists hit a historical record in the last quarter of the year, in part due to the Thai government measures to restore confidence and the three-month visa fee exemption for Chinese and Taiwanese tourists (August 9 – November 8, 2014). The strong rebound of Chinese tourists helped offset the fall in number of tourists from other countries, particularly Russian tourists—the third largest tourist group who were suffered by economic problems. The growth of Chinese tourists not only fueled the recovery of the Thai tourism sector in the latter half of 2014, it also contributed to a promising prospect for growth of the tourism sector in 2015.

Tourism Indicators

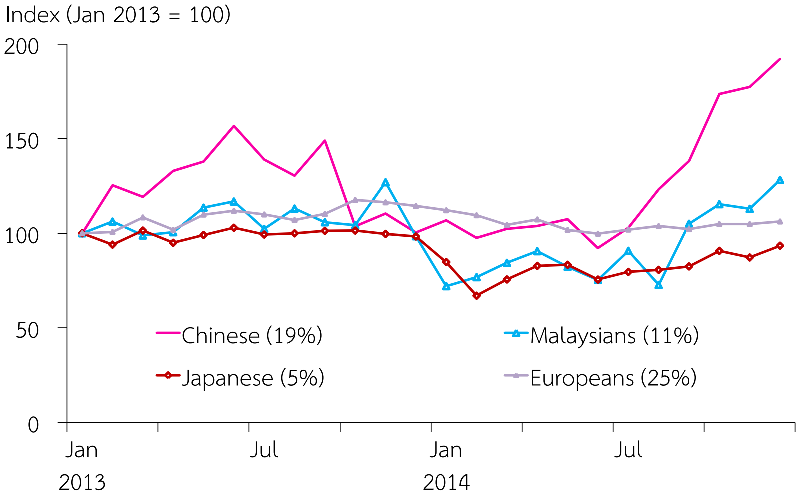
	2013	2557P				
	Year	Year	Q1	Q2	Q3	Q4
1. Number of foreign tourists (million persons)	26.5	24.8	6.4	5.1	5.8	7.5
Δ%	18.8	-6.7	-9.0	-15.9	-10.1	7.0
2. Tourism income (billion baht)	1,293.3	1,249.8	333.5	240.4	281.0	394.8
3. Occupancy rate (percent)	64.9	55.6	60.3	47.3	51.7	64.2

Note: P = Preliminary data

Δ% represents percentage change from the same period last year

Source: Department of Tourism and Bank of Thailand

Number of Foreign Tourists Index



Note: Number in parentheses is the share of tourists of that nationality in the total number of foreign tourists

Source: Department of Tourism, index calculations by Bank of Thailand

Number of Countries that Issued Travel Warnings on Thailand

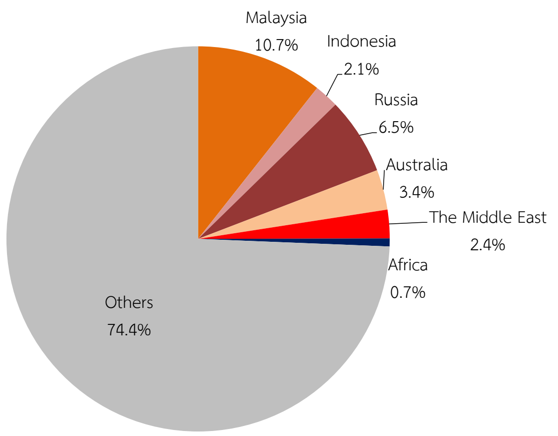
	Total	Levels 1-3	Levels 4-5
April 2014	50	46	4
May 2014	62	47	15
June 2014	66	48	18
July – August 2014	60	54	6
September 2014	58	54	4
October – November 2014	Unchanged		
December 2014	56	52 (Argentina and Croatia lifted their warnings)	4

Note: *Levels 1-3: Normal situation warnings,

Levels 4-5: Reconsideration of travel need warnings

Source: Ministry of Foreign Affairs, 11 December 2014

Share of Foreign Tourists from Major Oil-exporting Countries (2014)



Source: Department of Tourism

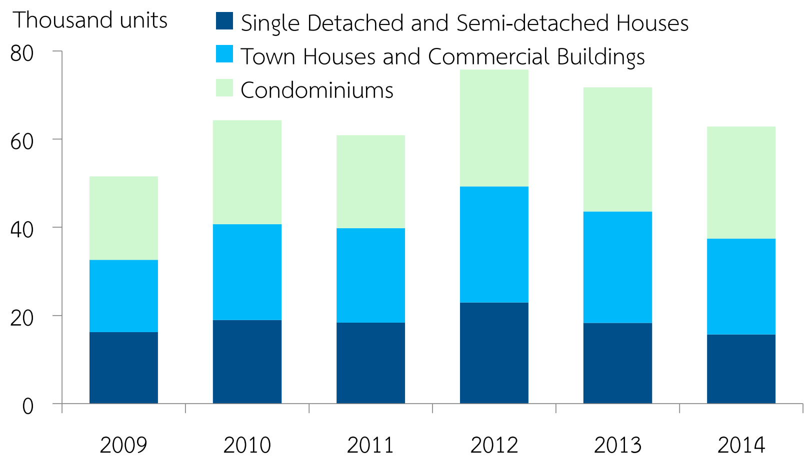
2.4 Real Estate Sector

The real estate market contracted in the first half of 2014. Political uncertainty and economic slowdown resulted in subdued market conditions in both demand and supply sides, reflected in a decline of property transactions. However, there were signs of recovery in the second half of the year.

The real estate market cooled down from the previous year, as seen in a decline in property transactions in the first half of the year. Softer demand and weaker supply underlined the concerns of consumers and property firms over the broader economic and political prospects. Flagging market conditions were reflected by a decrease in mortgage lending for properties in Bangkok and its vicinities, as well as a fall in the unit reservation rate from 34.7 percent in Q4 2013 to 20.4 percent in Q2 2014. Financial institutions also became cautious with their mortgage lending. This prompted property developers to offer new residential projects of smaller sizes and postpone some sales openings, especially condominiums, in anticipation of clearer market conditions.

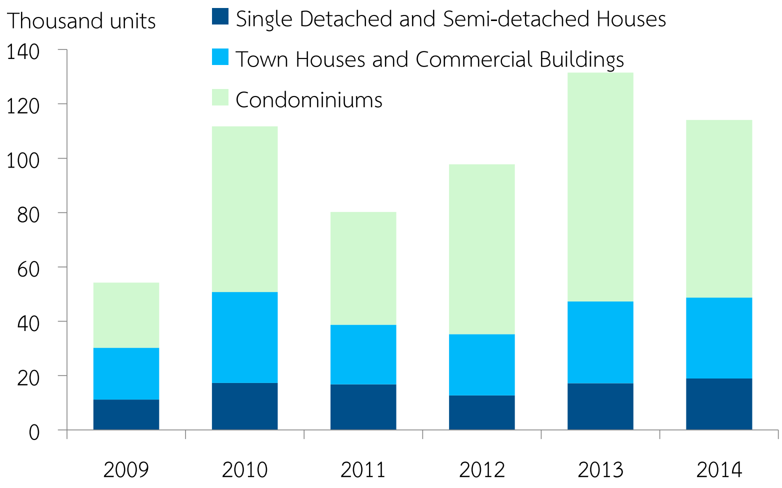
Improved economic and political conditions provided a platform for the real estate market to rebound fairly in the latter half of the year. The unit reservation rate increased to 27.8 percent in Q4 2014, due mainly to higher demand for condominiums. Property developers also accelerated new sales openings in late-2014, reflecting restored business confidence in the real estate sector.

New Mortgage Loans in Bangkok and Its Vicinities, Classified by Housing Types



Source: Bank of Thailand

New Residential Projects in Bangkok and Its Vicinities, Classifed by Housing Type



Source: AREA

Farm Income Prospect in 2015

Farm income in 2015 is expected to continue to contract for the fourth consecutive year due mainly to negative agricultural price growth. Consequently, subdued farm income is likely to contribute to the declining purchasing power of farm households, which makes up over one-third of the country's households, thereby hindering the recovery of private consumption.

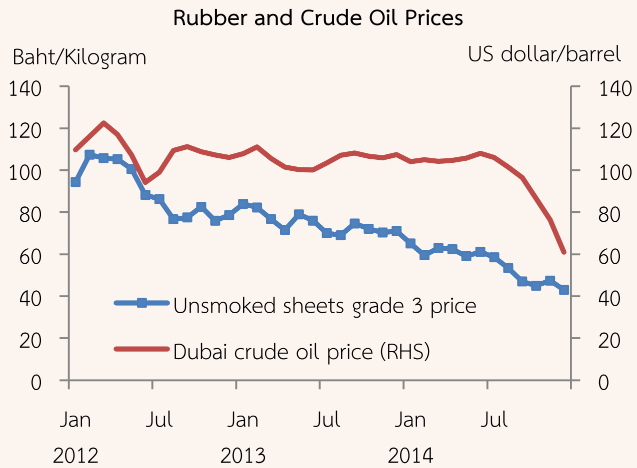
Farm Income, Agriculture Outputs and Agricultural Prices

Annual Percentage Change	2012	2013	2014	2015[F]
Farm income*	-6.0	-3.0	-5.3	-1.2
Agricultural output	4.9	-2.2	1.0	0.4
Agricultural prices	-10.3	-0.8	-6.2	-1.6

[F] Forecasted data

* Does not include income from government subsidies, which consists of income under the rice pledging scheme and subsidies for farmers.

Agricultural prices are expected to contract in 2015 due to the following: **1) Rubber prices**, the annual average price of which is expected to fall slightly from the previous year. Although the rubber price may rebound slightly from its low level during the end of 2014[1], global demand has not fully recovered, especially amidst China's economic slowdown[2]. Additionally, the increasing demand for synthetic rubber as an alternative to natural rubber—a response to the significant decrease in oil price—will continue to exert downward pressure on the price of rubber throughout the year. Moreover, the expected offloading of rubber stockpiles in Thailand is another contributing factor that may cause the global price of rubber to remain low, as Thailand is the world's largest exporter of rubber (35 percent share in the global market). **2) Shrimp and swine prices**, supply of which is expected to increase following the waning of disease. This is

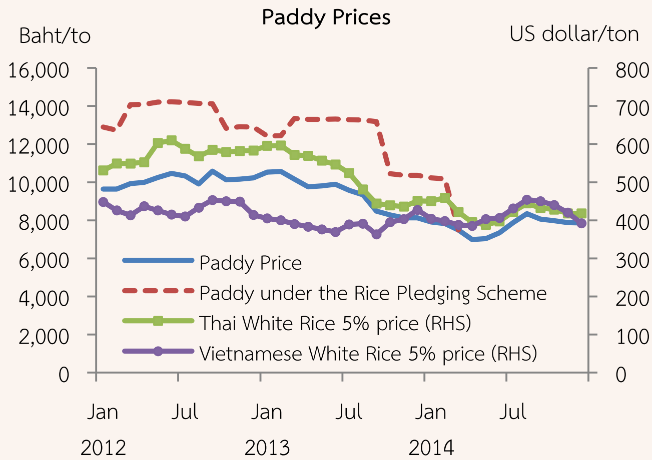


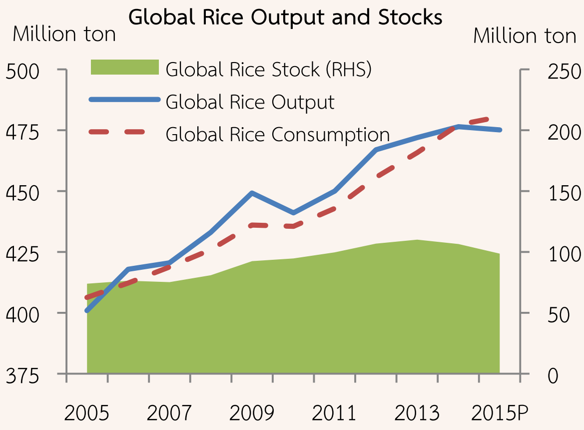
[1] The price of unsmoked rubber sheets grade 3 is 43 baht/kg. as of the end of December 2014.

[2] Rubber consumption in China constitutes 36 percent of the global consumption.

specially the case for shrimp, which is expected to return to its normal level of production at 300,000 – 400,000 ton[3] – a sharp increase from the 240,000 ton figure in 2014.

The annual average **paddy price** is expected to remain low, hovering around its 2014 level at approximately 7,700 baht per ton. Although the demand for rice in 2015 is expected to increase in all regions[4] and exceed the global production capacity, there are domestic and external factors that could affect the rice price. These factors include: (1) The Thai government's offloading of rice stockpiles, which would further increase the supply of rice in the global market. The buyers would force down the price of Thai rice in the global market as the market estimates that the Thai rice stock makes up as much as 20 percent of the global stock. (2) Vietnam's decision to reduce its rice price in an effort to maintain its market share.





P = Preliminary figure

In conclusion, farm income is expected to continue to contract because of subdued agricultural prices, especially those of rubber, as the slow global growth would still affect the demand for the Thai agricultural products. Meanwhile, the recent government's measures might not significantly increase farm income as much as past measures. This is because most of the current measures aim at mitigating short-term effects of low agricultural prices, avoid direct market intervention[5], and place increasing emphasis on the restructuring of the agricultural production[6] which would strengthen the sector rather in the long run.

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[3] According to the estimation by Thai Frozen Food Association as of 17 November 2014.

[4] EIU and USDA projected that global rice consumption in 2015 would increase by 0.8 and 0.7 percent respectively, compared with a 0.6 rise in 2014 (projections as of December 2014).

[5] As reflected by measures such as the Barn Storage Program and the Buffer Fund for rubber which took effect in 2014, and have taken only 12 percent of hom mali paddy rice and 5 percent of rubber out of the market.

[6] For example, balanced agricultural zoning and restructuring of the agricultural production for improved efficiency, especially for rice and rubber.

Key Government's Policies in the Agricultural Sector[7]

Project	Agricultural Product	Budget (billion baht)	Government Banks' Credit Limit (billion baht)
Income support of 1,000 baht per rai	Rice and rubber	48.5	-
Barn Storage Program	Rice	3.9	34.8
Buffer Fund	Rubber	6.0	-
Low-interest working capital credit	Rice and rubber	1.6	40.0
Long-term low-interest credit	rubber	0.6	20.0

Source: Compiled from the Cabinet's Resolutions

[7] Most of the government's measures in the agricultural sector commenced in the fourth quarter of 2014 and continue on in 2015, with the exception of the 40 billion baht income support program for farmers, most of which has been distributed in 2014.

3. International Trade and Balance of Payments

Exports

Export value fell for the second consecutive year, in contrast with sound export growth in other countries in ASEAN, reflecting structural problems in Thailand's manufacturing sector. Additionally, a sharp fall in global commodity prices caused export prices to decline.

In 2014, export value continually dropped from the preceding year as a result of falling prices. Although the quantity of exports slightly increased, export prices deteriorated for the second consecutive year on the back of the persistent and significant drop in global commodity prices. Rubber prices stagnated because of excess supply while rubber demand slowed down. At the same time, Thai rice export prices hit a 7-year low[1] due to the termination of the rice pledging scheme, together with the offloading of government stockpiles and higher global supply.

[1] Nevertheless, export value of rice expanded well from its export quantity hitting the highest historical record of 11 million ton as a decline in prices of Thai rice became more comparative.

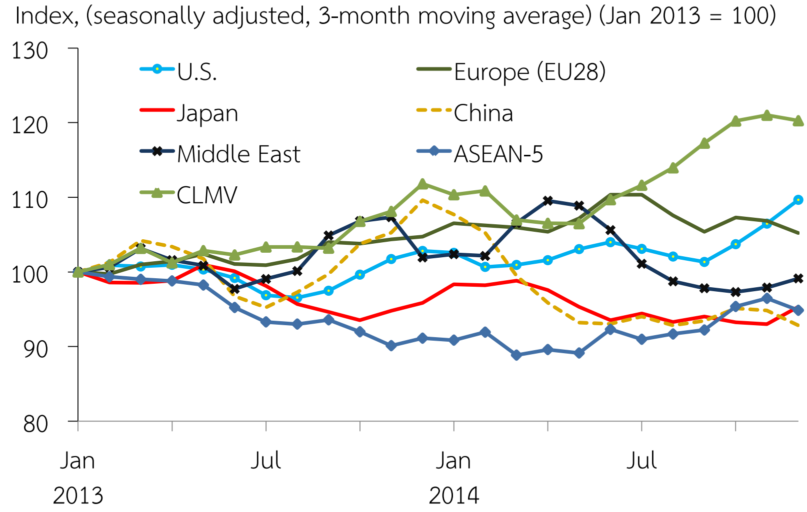
The acute fall in agricultural prices was the main factor behind the contraction of export prices in 2014.

Apart from price contraction, Thailand's exports continued to suffer from limited production capability in response to the increasing global demand toward hi-technology items, which weighed on export recovery. In 2014, the growth of Thai electronics exports lagged behind that of other Asian countries. The sluggish growth reflected weaker global demand for hard disk drives (HDD), Thailand's major electronics exports. The poor export performance is also an indication of the country's lack of productive capacity to manufacture solid state drives (SSD), the main alternative to HDD. By contrast, other Asian economies, such as South Korea, Taiwan, Malaysia and the Philippines, had made continual investment to upgrade their respective electronics industry. Given their advanced production technology, these Asian economies outperformed Thailand in the exports of high-value-added products, such as SSD and integrated circuits (IC). Moreover, automobile exports contracted due in part to softened demand from Australia, a major importing country. At the same time, production structure among ASEAN shifted as Indonesia continued to expand its production capacity in automobiles, which explained the significant drop in exports of automobiles to Indonesia. Nevertheless, exports of automobile parts to Indonesia continued to grow, since imported parts for the production remained necessary.

Despite the contraction of export value in certain categories, some products consistently performed well. Exports of petrochemical products posed a solid growth both in terms of quantity and price, following waning global supply amidst a slowdown in Chinese investment in expanding production capacity. Exports of machineries and equipment, particularly printers, also picked up in tandem with rising foreign orders because Thai manufacturers had invested and improved their production technology, which enhanced printer compatibility with smartphones and tablets.

On the market front, Thai exports to Asian fell in 2014, due mainly to softened Chinese and Japanese economies as a result of economic reforms. Furthermore, lower export revenue in major commodity-exporting countries in line with their economic slowdown, especially Australia and the Middle East, also dented their demand for Thai exports. However, exports to the U.S. improved in tandem with steady economic recovery. Exports to the euro area also edged higher, due in part to 1) improved growth momentum in the first half of the year; and 2) a temporary boost ahead of the expiration of Thailand's Generalized Scheme of Preferences (GSP) tax privilege of all goods in 2015. Moreover, exports to neighboring markets, namely Cambodia, Lao PDR, Myanmar and Vietnam (CLMV), showed a rapid growth, consistent with favorable economic conditions in these countries. Consequently, the share of Thai exports to CLMV countries rose to 9.1 percent, close to the shares of exports to China, the U.S., Europe and Japan.[2]

Thailand's Major Export Destinations



Source: CEIC and calculations by Bank of Thailand

[2] In 2014, Thai exports to the top-5 destinations: ASEAN-5 (Singapore, Malaysia, Indonesia, the Philippines and Brunei Darussalam), China, the U.S., Europe and Japan stood at 17.0, 11.0, 10.5, 10.3 and 9.6 percent of total exports respectively.

Export Value Classified by Product (in US dollars)

Annual percentage change	2013	2014P	2014P			
			Q1	Q2	Q3P	Q4P
Manufacturing products	1.8	0.1	-3.1	-0.4	0.9	3.1
Agro-manufacturing products	-2.6	-2.5	-7.8	-5.4	1.8	1.8
Electronics	-0.8	1.8	-0.4	-1.7	2.4	6.6
Automobiles	7.6	0.1	3.0	-1.6	-3.9	3.3
Petrochemical and petroleum products	1.8	-2.4	-5.0	5.9	-0.7	-8.9
Electrical appliances	2.3	4.5	7.2	2.0	0.1	8.8
Metal products	-5.5	-11.2	-34.2	-5.5	-0.9	5.9
Apparels and textile materials	3.6	-0.3	-1.3	0.9	-0.4	-0.2
Agricultural products	0.0	-1.3	-2.0	2.7	4.4	-8.5
Rice	-4.6	23.0	4.6	21.5	25.2	39.3
Rubber	-5.9	-26.9	-15.5	-24.0	-24.8	-42.1
Total Exports	-0.2	-0.3	-1.1	0.3	-1.7	1.5
Total Exports (excluding gold)	1.3	0.0	-2.9	0.1	1.0	1.7

Note: P = Preliminary data

Source: Ministry of Commerce and Bank of Thailand

Imports

Merchandise imports contracted across all categories, owing to weak domestic demand, slow recovery of exports, and steep fall in crude oil prices.

Import value in 2014 experienced a substantial decrease across all product categories as a result of three key developments: 1) private consumption and investment in the first half of 2014 were dampened by political situation and slow export recovery, which in turn dented demand for imports of raw materials, intermediate goods, capital goods, and automobile and auto parts; 2) a number of oil refineries were temporarily closed for maintenance, reducing the imports of crude oil to 25.2 million barrels per month in 2014, lower than the previous year's figure of 27.8 million barrels per month; and 3) plummeting global crude oil prices had a significant impact on Thailand's imports as crude oil imports constituted 14.6 percent of total import value.

Import Value Classified by Product (in US dollars)

Annual percentage change	2013	2014P	2014P			
			Q1	Q2	Q3P	Q4P
Raw materials and intermediate goods	0.4	-4.8	-4.7	-10.0	1.1	-5.0
Fuel and lubricants	9.8	-8.7	1.8	-12.8	1.0	-22.9
Raw materials and non-fuel intermediate goods	-4.4	-2.5	-8.2	-8.2	1.2	6.3
Capital goods	-4.5	-5.5	-11.1	-9.2	1.9	-3.5
Consumer goods	3.7	-1.7	-7.3	-4.5	1.1	4.0
Non-durables goods	5.6	-2.7	-9.9	-4.5	2.0	2.2
Durables goods	0.2	0.1	-2.2	-4.4	-0.3	7.4
Other imports	6.7	-39.8	-60.3	-39.5	-23.0	-22.3
Automobiles and parts	-6.2	-27.5	-31.7	-32.8	-27.9	-15.1
Total Imports	-0.5	-8.5	-14.7	-11.8	-0.8	-5.7
Total Imports (excluding gold)	-1.8	-5.0	-6.3	-9.4	0.4	-4.2

Note: P = Preliminary data
Source: Ministry of Commerce and Bank of Thailand

Current Account

The current account registered a sizable surplus of 14,231 million US dollars in 2014. The trade balance swung to a considerable surplus after two years of deficit. The positive turnaround in the trade balance offset the widening deficit of net services, income and transfers caused by a decline in tourist receipts, which were affected by the protracted political impasse in the first half of the year.

Financial Account and the Balance of Payments

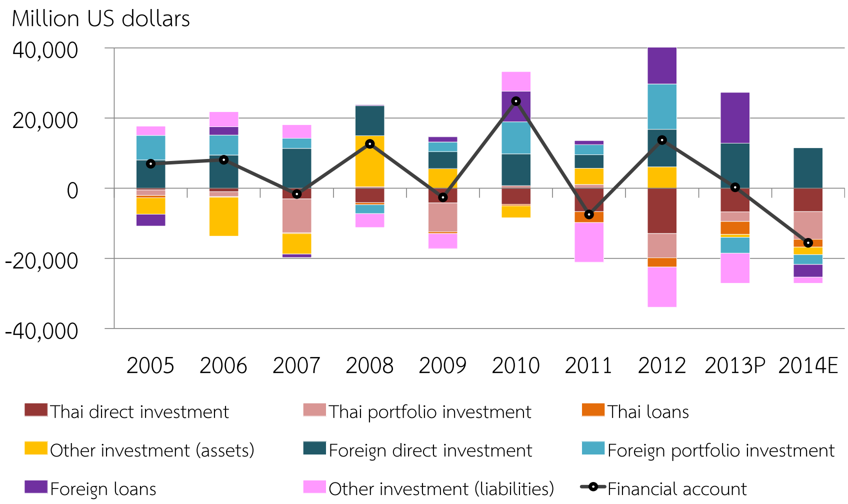
The balance of payments recorded a deficit in 2014. The substantial current account surplus was outweighed by a larger deficit in the financial account owing to outflows of direct and portfolio investment overseas by Thai investors as well as foreign portfolio investment. This was attributable to political uncertainty and volatility in global financial markets following the divergence of the monetary policy in major economies.

In 2014, the financial account posted a net deficit of 15,541 million US dollars. Thai investors continued to expand their overseas investment, motivated by greater opportunities and higher rates of return as well as more diversification. These investments took three forms: 1) direct investment, especially in the petroleum industry, financial intermediaries and insurance businesses, and manufacturing of rubber and plastic products. 2) portfolio investment both debt and equity securities, and 3) deposits in foreign banks, mostly through Foreign Investment Fund (FIF) in Hong Kong, Indonesia and Macau. Additionally, financial institutions made repayments of short-term loans to manage their foreign exchange positions, in line with a fall in Thai exporters' demand for currency hedging.

Meanwhile, foreign investors continued to sell off Thai securities from the previous year. Foreign investment in the equity market recorded net outflows, given their volatile investment during the year following political situation in Thailand and divergent monetary policies in major economies. Nonetheless, net inflows of foreign direct investment (FDI), especially from Japan, the U.S. and Hong Kong increased from the preceding year. The net FDI inflows reflected robust investor confidence in the country's long-term economic fundamentals, in spite of political uncertainty in the first half of the year.

Overall, the financial account recorded a deficit of 15,541 million US dollars, higher than the current account surplus of 14,231 million US dollars. As a result, the balance of payments registered a deficit of 1,210 million US dollars in 2014, lower than the deficit of 5,049 million US dollars in the previous year.

Financial Flows Classified by Type



Note: P = Preliminary data, E = Estimated data
Source: Bank of Thailand

Balance of Payments

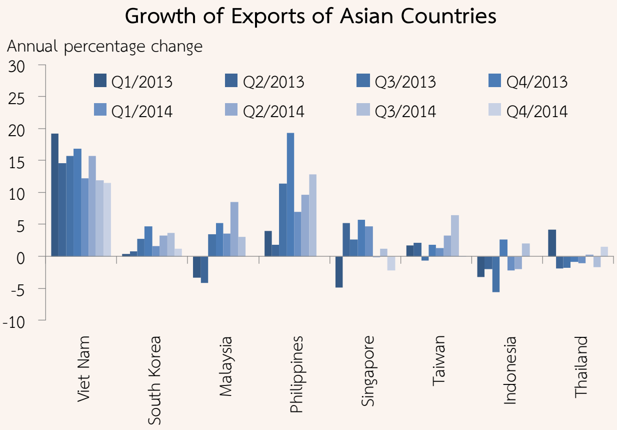
(Unit: million US dollars)	2013P	2014E	Q1 2014E	Q2 2014E	Q3 2014E	Q4 2014E
Exports, f.o.b.	225,409	224,792	55,378	55,718	56,934	56,763
Δ% YoY	-0.2	-0.3	-1.1	0.3	-1.7	1.5
Imports, f.o.b.	218,748	200,210	49,099	49,830	52,154	49,127
Δ% YoY	-0.5	-8.5	-14.7	-11.8	-0.8	-5.7
Trade balance	6,661	24,582	6,279	5,887	4,780	7,636
Trade balance minus gold	18,380	28,376	6,176	6,617	6,722	8,861
Net services, income and transfers	-9,113	-10,351	-786	-6,439	-5,306	2,180
Current account	-2,452	14,231	5,493	-552	-526	9,815
Current account minus gold	9,267	18,025	5,390	178	1,416	11,041
Capital account	281	105	23	25	57	0
Financial account (net)	264	-15,363	-7,524	1,020	-1,852	-7,006
Asset	-14,003	-19,099	-5,950	-4,480	-2,485	-6,184
Thai direct investment	-6,729	-6,786	-426	-2,255	-1,758	-2,348
Thai portfolio investment	-2,764	-7,964	-1,976	-3,324	-1,870	-794
Thai loans	-3,704	-2,276	-909	11	502	-1,880
Other investment (assets)	-806	-2,074	-2,639	1,088	640	-1,162
Liabilities	14,267	3,736	-1,575	5,500	633	-822
Foreign direct investment	12,807	11,837	3,176	2,814	3,558	2,289
Foreign portfolio investment	-4,490	-2,751	-1,678	518	274	-1,865
Foreign loans	14,487	-3,610	-2,983	2,263	-2,669	-221
Other investment (liabilities)	-8,538	-1,740	-90	-96	-529	-1,025
Net errors and omissions	-3,143	-182	1,546	-1,099	2,359	-2,988
Balance of payments	-5,049	-1,210	-462	-606	37	-179

Note: P = Preliminary data, E = Estimated data

Source: Bank of Thailand

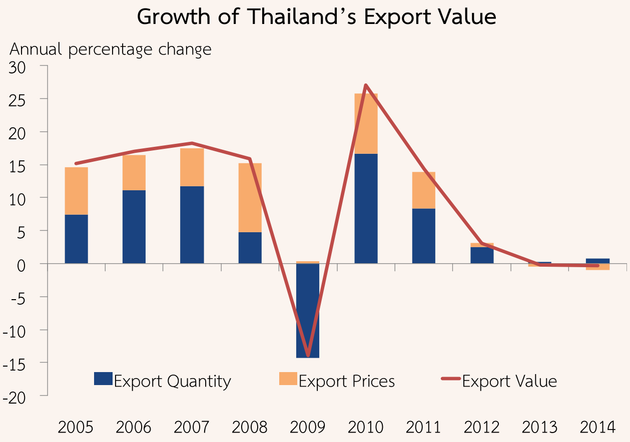
Thailand's Exports Face Challenges in 2015

In 2014, Thailand's exports contracted for the second consecutive year, unable to perform their traditional role as the primary engine of growth. By contrast, many Asian countries enjoyed strong export growth on the back of modest global economic recovery. This suggests that structural problems in the Thai exports sector were a major constraint on the country's international competitiveness. Given the underlying structural problems and the prevailing external risks, growth of Thai exports faces a challenging outlook in 2015.



Source: CEIC

There are two main structural constraints in the Thai exports sector. **First, a lack of investment in new production technology for years resulted in limited production capability to take full advantage of the increasing global demand for higher technology products.** The problem is especially evident in the manufacturing of HDD, which used to be the main driver of Thai exports. Meanwhile, Thai firms have expanded investment in the integrated circuits (IC) industry and secured a presence in the global supply chain of smartphones and tablets. However, in terms of value added, the products made by Thai manufacturers still lag behind those of other Asian countries. The growth of Thai IC exports, as a result, remains low relative to that of other countries. The second major structural constraint is the high proportion of agricultural products in Thailand's total exports. As a result, Thai exports are severely hit by the slump in global commodity prices, especially rubber prices.



Source: Ministry of Commerce

Apart from these domestic structural problems, external risks continue to pose threats to Thai export recovery in 2015.

(1) The geopolitical risks stemming from the prospect of Russia's deteriorating relations with Europe and the U.S. could undermine Thai export recovery. Although exports to Russia account for only 0.5 percent of total exports and European sanctions on

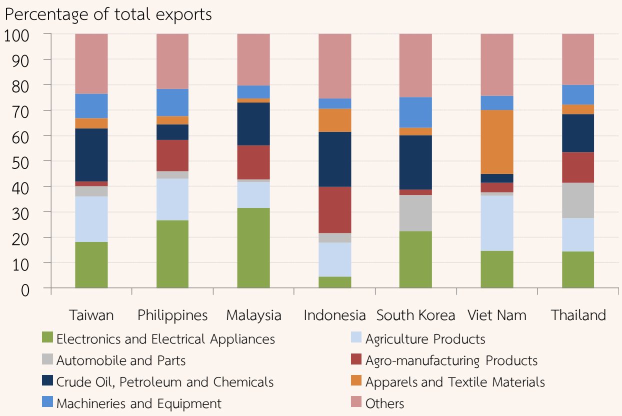
Russia may create higher demand in Russia for Thai products as alternatives to European-made products, this indirect positive effect could be offset by the adverse consequences of geopolitical tensions on the Russian economy. In particular, the depreciation of the ruble could dampen Russian's purchasing power and demand for imported goods. Moreover, if the geopolitical tensions drag on and escalate, they could cause a slowdown in several European economies that are Russia's major creditors. Such a scenario could have sizable indirect negative impact on Thai exports, given that exports to Europe made up 10.3 percent of Thailand's total exports in 2014.

(2) Structural economic reforms in major export destinations could lead to slower-than-expected recovery of trading partner economies. Exports to China and Japan are of particular importance as they account for 11 and 9.6 percent of total exports respectively. Structural reforms in the Chinese economy could reduce the demand for Thai goods that are used for domestic consumption, such as petroleum products, chemicals, rubber and rubber products. However, there should be lesser impact on Chinese demand for Thai electronics products which are used as inputs in the manufacturing of Chinese exports to third countries. At present, the two categories of Thai exports to China (those used for domestic consumption in the Chinese market and for manufacturing of exports to third countries) each account for half of total exports to China. Meanwhile, economic slowdown in Japan is likely to dampen demand for Thai goods. Japanese importers could also negotiate for lower prices of Thai exports in order to compensate for yen depreciation.

(3) World crude oil prices are expected to remain low throughout 2015, resulting in subdued demand for Thai exports in major net oil exporters, especially the Middle East and Malaysia. The low crude oil prices are also likely to exert downward pressure on Thai exports prices of oil-related goods, namely rubber, cassava, petroleum and chemical products which account for 18.4 percent of total exports.

In 2015, Thailand's export value is expected to grow at a slower pace than that of regional economies. Thailand's exports are more diversified across different products than those of other countries. This diversified export composition helped cushion the adverse impact of the global economic crisis on Thai exports. However, if world economic recovery is not broad-based, Thai exports will not reap the full benefits of global growth. As at present, the rebound in

Composition of Exports in Asia



Source: Trademap and calculations by Bank of Thailand global demand is limited to high-tech electronic products, which account for a relatively small share of Thai exports, compared with other countries. Moreover, since Thailand has a higher share of automobile exports in its total exports compared with other countries and oil-exporting countries are also major destinations for Thai automobile exports, slower economic growth in these markets is therefore expected to adversely affect Thai exports relatively more than it does to exports of other countries.

Against the backdrop of these external risks and the underlying structural constraints in the domestic manufacturing sector, Thailand's export value is estimated to grow at a low rate in 2015. As such, the public and private sectors need to step up their collective effort to tackle the structural problems. The government has geared up its effort, with the introduction of changes in the Board of Investment (BOI) criteria for privileges, designed to promote investment in research-and-development-oriented industries. The private sector needs to invest more in new production technology in response to changes in global demand and consumer preference. Moreover, to be more competitive in the global market, Thai exporters should focus more on improving product quality rather than targeting low price products.

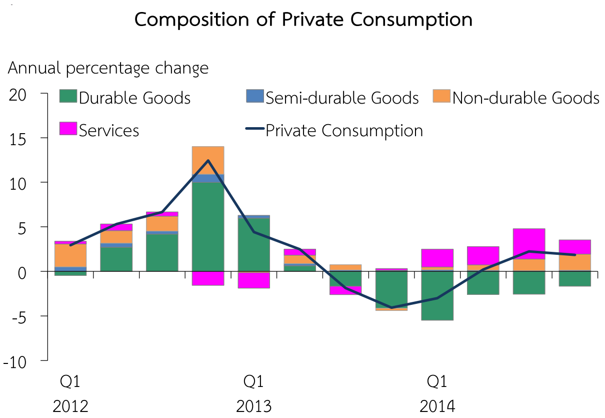
4. Domestic Demand

4.1 Private consumption

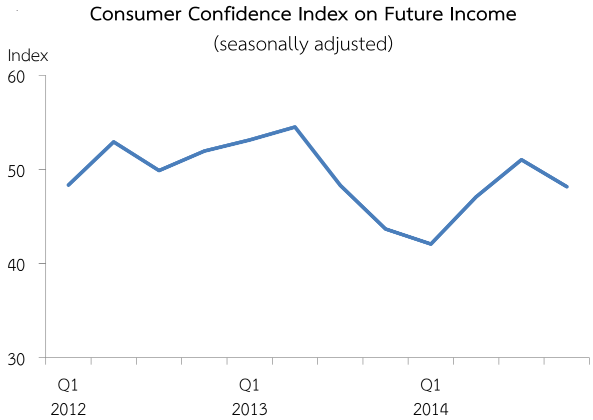
Private consumption improved from the year earlier, but the rate of growth was below historical average as a result of political uncertainty in the first half of the year, a high level of household debt, and depressed farm income.

In the first half of 2014, private consumption continued to contract from last year as political uncertainty and an elevated level of debt prompted households to be cautious with their spending.

In the second half of the year, private consumption gradually picked up, following two developments. First, consumption of nondurable goods and services increased, thanks to higher consumer confidence after political uncertainty subsided. Second, non-farm income helped support consumers' purchasing power. However, private consumption growth still lingered below its normal levels. Spending on durable goods, especially automobiles, continued to stall because many consumers had already purchased cars under the first-car tax rebate scheme. At the same time, financial institutions were cautious on household credit extension amidst growing concerns over declining loan quality. Farm income was also dampened by falling prices of rubber and rice.



Source: Office of the National Economic and Social Development Board



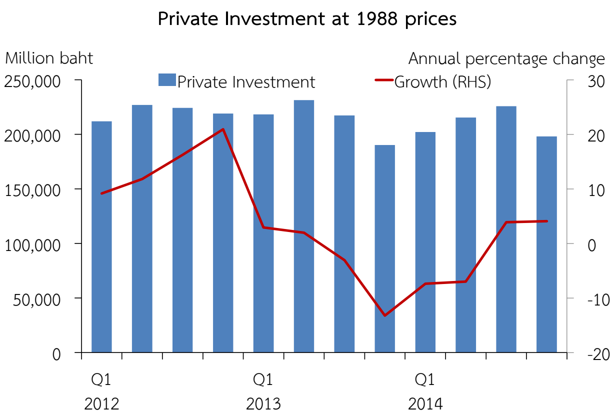
Source: Bureau of Trade and Economic Indices, Ministry of Commerce, and calculations by Bank of Thailand

4.2 Private Investment

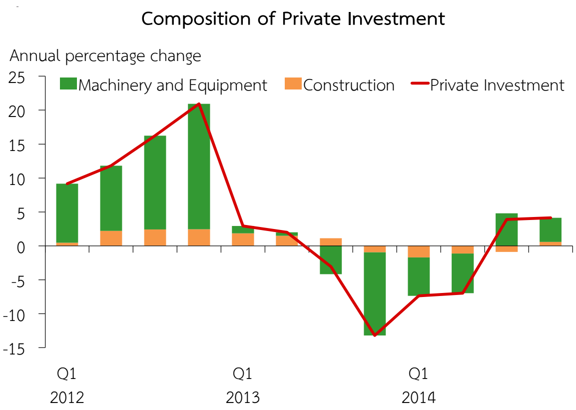
Private investment contracted from the previous year, owing importantly to political uncertainty in the first half of the year, below-par growth in private consumption, and weak recovery of merchandise exports.

Private investment both in machinery and equipment and in construction contracted in the first half of the year. Investment was dented by a combination of 1) political gridlocks that disrupted operations of some government agencies; 2) cautious spending by consumers, and 3) slow recovery of merchandise exports. Businesses therefore postponed their investment, awaiting the clarity of political and economic prospects.

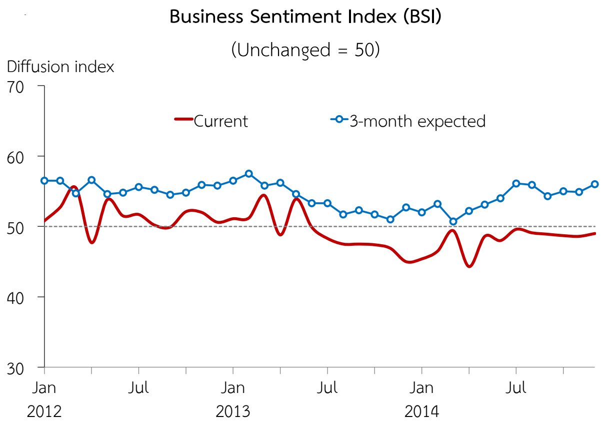
In the latter half of the year, private investment edged higher on the back of greater political stability and improvements in private consumption. Following a prolonged contraction in four successive quarters, private investment began to turn around in the third quarter of 2014, accompanied by an improvement in the Business Sentiment Index (BSI) compared with the first half of the year. Investment in machinery and equipment expanded, due to 1) investment in telecommunication businesses, 2) a resumption of government services, a swift allocation of permit for factory operation (Ror. Ngor. 4), and approvals of investment promotion by the Board of Investment (BOI). Investment in construction also showed signs of recovery in the second half of the year as businesses launched new property projects, especially the development of condominiums along mass transit railways. Large retail businesses also set up new branches in other provinces outside Bangkok. Nonetheless, investment in several industries remained sluggish because 1) there was still excess production capacity; and 2) many private firms opted to defer their investment, awaiting a clearer sign of recovery in domestic market and clarity on government policy and investment plans.



Source: Office of the National Economic and Social Development Board



Source: Office of the National Economic and Social Development Board



Source: Bank of Thailand

4.3 Fiscal Sector

Budget disbursement was held down by political stalemate in the first half of the year. But even in a more stable political environment in the latter half of the year, the disbursement rate did not improve much, hindering the government's effort to stimulate the economy. Nevertheless, fiscal policy stance still provided support to economic growth, as evident by the increase in the government's cash deficit to a larger-than-targeted level, following a substantial shortfall in revenue.

In fiscal year 2014, the government announced a 250 billion baht budget deficit to stimulate the economy, with an emphasis given to infrastructure investment projects that were intended to enhance the country's competitiveness. However, in the first three quarters of the fiscal year, budget disbursement was disrupted by political stalemate. And even though the political environment became more stable afterwards, disbursement was still restrained, particularly that of capital expenditure. The new government measures to enhance transparency and curtail corruption forced government agencies and state enterprises to re-examine their investment projects and procurement procedures. As a result, the overall disbursement rate in 2014 was only 89 percent, well below the target of 95 percent and the five-year average of 92.6 percent.

On the revenue side, collection fell short of projection by 8.8 percent. Income tax revenue declined because of a reduction in income tax rates and the economic slowdown. Collection of consumption taxes was also below the target. The value added tax (VAT) revenue fell on the back of weak performance of private consumption. Automobile excise tax collection dropped in tandem with declining car sales, while petroleum excise tax revenue also declined following the extension of the diesel tax cut. In line with the substantially lower-than-expected revenue, the government's cash deficit was 327 billion baht or 2.7 percent of GDP, a marked increase from 1.8 percent of GDP in the previous fiscal year. Consequently, treasury cash balance fell to 496 billion baht at the end of fiscal year 2014.

In fiscal year 2015, the government planned to run a budget deficit of 250 billion baht, with a view to stimulate the economy and hasten infrastructure investment. Capital expenditure made up 17.5 percent of the total budget, the same percentage as last year, with impending and urgent projects accorded a higher priority. Moreover, as the formerly proposed bill that would have empowered the Finance Ministry to borrow funds to invest in transport infrastructure was ruled unconstitutional by the Constitutional Court, the government decided to find other sources of extra-budgetary funding. These include revenue contributions from state enterprises, government loans as specified in the Public Debt Management Act, joint venture public-private partnerships, and infrastructure fund.

In the first quarter of fiscal year 2015, the government implemented several measures to accelerate budget disbursements, especially capital expenditure, in order to boost the economy. However, fiscal spending was constrained by two main factors: 1) inefficiency in budget disbursements by government agencies; and 2) revision of investment plans of state enterprises that faced financial problems and imminent reforms. At the same time, revenue collection in the first quarter of fiscal year 2015 was higher than projection, thanks to a surge in state enterprises' remittance and a rise in value added tax collection as targeted in line with a gradual recovery in private consumption.

Fiscal Position[1/]

(Unit: billion baht)

Fiscal year

	2011	2012	2013[P]	2014[P]
Cash receipts from operating activities[2/]	1,892.0	1,977.7	2,163.5	2,071.7
(Annual percentage change)	(10.7%)	(4.5%)	(9.4%)	(-4.2%)
Cash payments for operating activities[3/]	1,801.9	1,981.7	2,106.7	2,147.4
(Annual percentage change)	(15.1%)	(10.0%)	(6.3%)	(1.9%)
Net cashflow from operating activities	90.2	-4.1	56.8	-75.7
Net cashflow: investment in non-financial assets	201.4	229.6	268.4	249.2
Budget cash balance	-111.3	-233.7	-211.6	-324.9
Non-budget cash balance	-48.7	-53.3	2.7	-2.4
: of which Stimulus Package 2	-61.1	-24.4	-7.5	-3.3
Overall cash balance	-159.9	-287.0	-208.9	-327.3
Net incurrence of liabilities	241.9	335.4	244.3	218.0
Use of treasury cash balance	-82.0	-48.4	-35.4	109.3
Treasury cash balance (end of period)	521.3	569.7	605.0	495.7

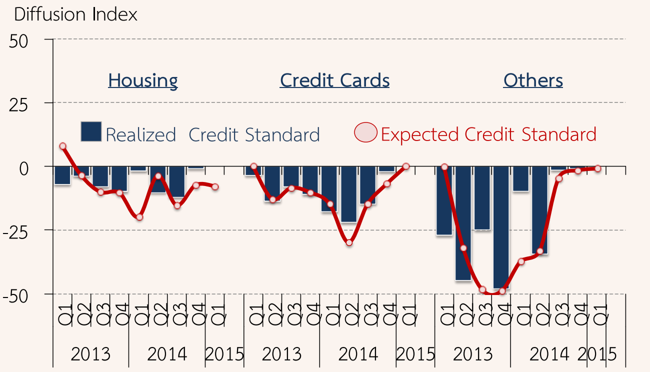
Notes: [1/] Data dissemination follows the standards prescribed by the IMF's GFSM 2001.
[2/] Revenue data in this table is on a cash basis, received from the Fiscal Policy Office.
[3/] Excluding principle payment
P = Preliminary data

Sources: Fiscal Policy Office, Ministry of Finance
Statistic and Information Systems Department, Bank of Thailand

Implications of Household Debt on Private Consumption

Even though household spending began to pick up pace when political situation eased in mid-2014, private consumption growth was still held back by the high level of household debt. The critical question, then, is when the household debt problem will subside so that private consumption can resume its normal growth.

Credit Standards for Household Loans

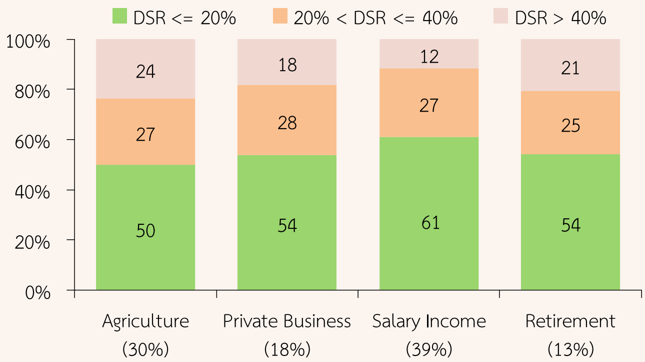


Note: Credit standards are from the Bank of Thailand's survey of 22 banks and 15 non-banks, which account for 90.3 percent of total lending. Diffusion Index (DI) < 0 suggests tighten credit standard compared to the previous quarter, DI = 0 suggests unchanged credit standard, while DI > 0 signals more relaxed credit standard compared to the previous quarter.

Source: Bank of Thailand

Household Debt Service Ratio by Employment

DSR by employment types in 2013 (share of households)



Note: DSR (Debt Service Ratio) is the ratio between debt repayment (principal plus interest) and average monthly income. Numbers in parentheses show the shares of households with debt in each employment category.

Source: Household socio-economic survey, National Statistical Office, calculations by the Bank of Thailand

Excluding outlays on durable goods, household spending had bottomed out after the first quarter of 2014. Consumption of nondurable goods and services grew on the back of improved sentiments and non-farm income. However, the recovery was not sufficient to compensate for the drop in spending on durable goods, as households were dragged by elevated debt burden[1] and depressed agricultural prices.[2] Therefore, overall private consumption still fell short of its normal growth rate. These two factors discouraged household spending and borrowing, especially among low-income groups, including farmers who tended to have higher levels of debt-to-income ratio than others. In addition, concerns over declining loan qualitiy led to cautious lending behavior among financial institutions, as evident in their increasingly tightening credit standards. Yet, on the bright side, such financial discipline among households and financial institutions would contribute to stable economic growth in the future.

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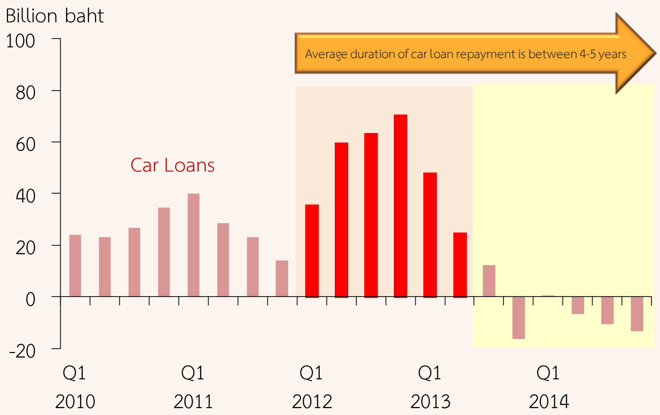
[1] The household debt-to-GDP ratio in the third quarter of 2014 recorded at 84.7 percent, a slight increase from the last quarter of 2013.

[2] Albeit government's agricultural support policies, purchasing power remained low because farmers spent the bulk of additional income on debt repayment and production inputs, leaving only 20-30 percent for consumption.

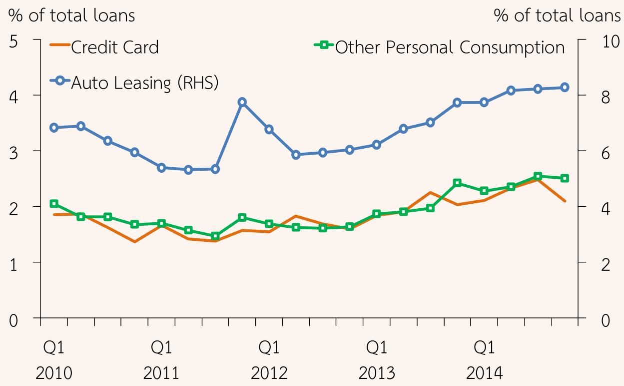
The next question is: when will household debt problem subside so that household expenditure can resume its growth trajectory? Considering factors that influence household spending, **household debt is expected to remain a drag on spending throughout 2015,** as households would still need to repay their loans and financial institutions would remain cautious with their lending. **Nevertheless, the situation should be alleviated at the beginning of 2016** due to three reasons. (1) Car loans associated with the first-car policy, will be paid off starting 2016. This will reduce the debt burden of households, especially the middle-income group, allowing them to allocate more of their income for consumption. Also, improvement in loan quality, particularly with moderating car loans growth after accelerating earlier, may prompt financial institutions to be more lenient in their lending, thereby households could access to credit easier. (2) Household income is expected to rise in line with increasing manufacturing and service activities. (3) Agricultural prices are likely to increase in 2016, thanks to global economic recovery. These three factors will spur a stronger growth of private consumption in 2016, compared with the past three years.

Changes in Outstanding Car Loans



Source: Bank of Thailand

Special-mention Loans*



Note: * loan overdue above 1 month but not more than 3 months
Source: Bank of Thailand

Nevertheless there are risks to household balance sheet that need to be monitored in the periods ahead. First, agricultural prices, that may remain subdued for some time, could induce farmers to accumulate more debt through both formal and informal lenders. Second, the scheduled increase in excise tax on automobiles in 2016 may stimulate car purchases by households in 2015. Despite these downside risks, if households accumulate debt only as necessary, keep their debt within affordable levels, and are disciplined in their debt servicing, then private consumption will resume as one of the key drivers of stable economic growth going forward.

Special Economic Zones: Implications for Thai Economy

Border trade is becoming increasingly important for the Thai economy, as the value of border trade continued to have high rates of growth. A number of areas along the Thai border possess immense potential to be key linkages within the growing networks of production, trade, and services in the ASEAN Economic Community, which will be realized in 2015. Recognizing such potential, the government has designated 5 Special Economic Zones (SEZs) in 2014.[1] This article will discuss the implications of the SEZs for the Thai economy.

What are Special Economic Zones?

The SEZs is considered as "tools" to achieve strategic development goals by promoting targeted economic activities at specific locations, such as promotion of trade, export-oriented manufacturing or high value-added industries. These goals are achieved through 1) relaxation of laws and regulations that hinder trade and investment, 2) special management that facilitates trade and investment in the area, 3) fiscal resource allocation, such as investment in infrastructure to improve the area, and 4) grants of permits for private investment in the area that would ensure worthiness and economic returns.

What are the implications of Special Economic Zones on the Thai Economy?

With high potential for trade expansion, the development of the five SEZs by the government can serve as a major growth driver going forward.[2] Especially promising are those bordering Myanmar, Cambodia and Lao PDR, where manufacturing production in these countries is likely to increase markedly as their wages are relatively cheap and the GSP, which expired in early 2015 for Thailand, still applies. Furthermore, these countries have developed their own industrial estates across the borders, particularly to promote labor-intensive industries. Thailand with public utilities readiness can utilize these production bases to establish the country as a regional hub for trade, transportation, and efficient production chain in the region. In particular, investments along the Southern Economic

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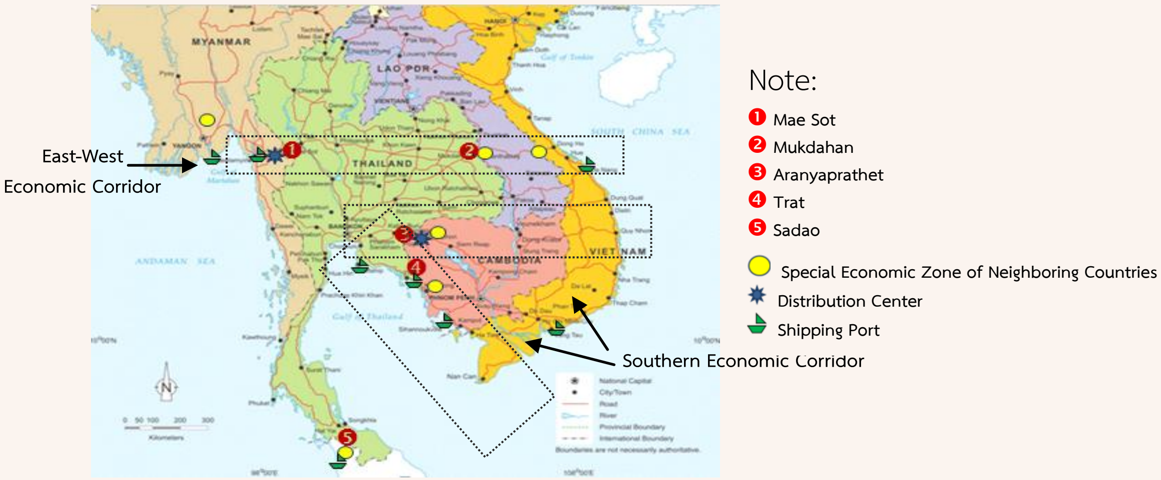
[1] The Policy Committee on Special Economic Zones at the first and second meeting in 2014 has approved target sites in the 5 border provinces which are 1) Mae Sot, Pob Phra, and Mae Ramad districts in Tak province, 2) Muang, Whan Yai, and Don Tan districts in Mukdahan province, 3) Sadao district in Song Khla province, 4) Aranya Pradesh and Wattana Nakorn districts in Sakeaw province, and 5) Klong Yai district in Trad province. The goals of the Special Economic Zones are (1) economic development via enhancement of competitiveness, greater employment, and improved living standards, (2) national security through the abolition of illegal immigrants and agricultural smuggling, and (3) reduction of population density near border controls.

[2] International experiences show that border Special Economic Zones should be developed as Free Trade Zones or Export Processing Zones (FIAS 2008).

Corridor linking Thailand, Lao PDR, Cambodia and Vietnam, as well as the East-West Economic Corridor linking Myanmar, Thailand, Lao PDR and Vietnam, will support intra-regional transport, facilitate regional production chain, and enhance the efficiency of Thailand's domestic industries. Although wages in Malaysia are more expensive than in Thailand, SEZs bordering Malaysia with high potential for trade expansion can serve as a manufacturing base for exports of processed goods,[3] such as rubber products.

Potentials of Special Economic Zones in Thailand and Neighboring Countries



Source: Map from www.oknation.net
Information on the map from site visits by the Bank of Thailand, interviews of the Customs Department and business owners, ADB reports, and NESDB reports.

Studies on international case of successful Special Economic Zones point to the following key challenges that require the government's attention.

1. The development of logistics infrastructure which spurs three major categories (1) Hub and IT logistics: construction of warehouses, goods handling systems, distribution centers and convenient transport system, and enhancement of efficient customs services by IT systems, (2) Logistic Resources: improving human resources and attracting foreign investment in logistics business; and (3) Logistic Relations: collaborations with neighboring countries to reduce barriers in trade and transport.

2. The streamlining of regulations in order to facilitate trade and investment. For example, improvements in documentation process and other regulations would facilitate customs procedures. Reduction in, or exemption of, profit remittance tax would eliminate the double-counting of income tax. Also, the government could consider granting land ownership permission for foreign business owners.

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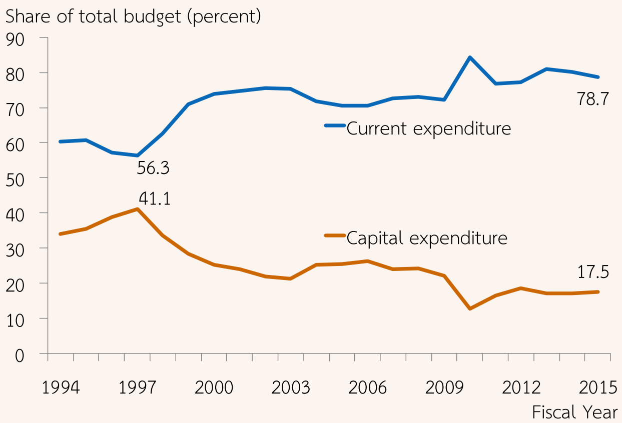
[3] FIAS (2008) shows that successful Export Processing Zones are located on the border with higher-wage neighbors, thus lower labor cost could attract FDI into the country. For example, Poland attracts FDI from Germany, and Mexico attracts FDI from the U.S.

3. Policy consistency and appropriate communication with locals that will forge constructive understanding and support for the development of the area. The constitution upholds that projects should be carefully evaluated on environmental impact and developers have to hold public hearings for any projects that may affect environment in the area. Thus, project continuity, along with policy communication that encourages participation and support among the locals, is crucial for successful operations of Special Economic Zones.

Fiscal Reforms: A Path towards Higher Economic Growth for Thailand

For the past decade, Thailand's potential growth has gradually diminished, in part because both government and private investments have remained low for a long period of time[1]. Fiscal reforms, both on the revenue and expenditure sides, are a means to help unlock this constraint on growth. Such reforms will restore fiscal balance and boost efficiency in government spending, by allocating a greater portion of the government budget towards capital expenditures, especially in growth-enhancing infrastructure development.

Share of Current and Capital Expenditures



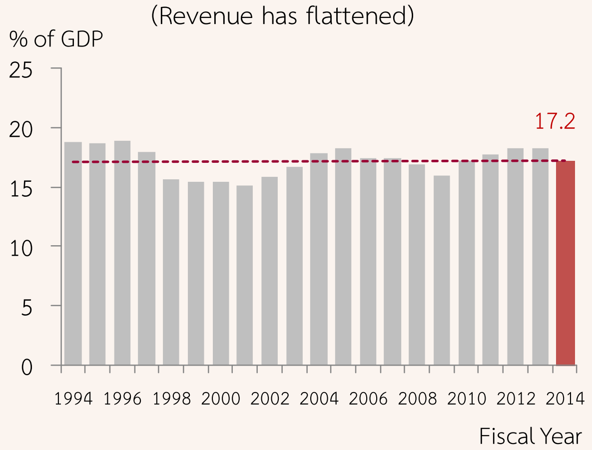
Source: The Ministry of Finance, assembled by Bank of Thailand

Two fiscal imbalances have contributed to subdued government investment over an extended period. **These include:**

(1) Government revenue has been growing slower than spending.[2] Various tax policies recently put into place have resulted in lower government revenue, despite the fact that efficiency improvements in tax collection have helped offset part of the loss.

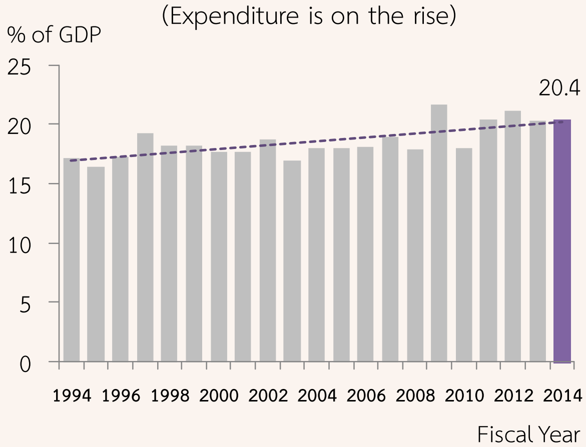
Net Government Revenue to GDP

(Revenue has flattened)



Government expenditure to GDP

(Expenditure is on the rise)



Source: Fiscal Policy Office and NESDB, calculations by Bank of Thailand

[1] The 3-year average investment-to-GDP ratio is 22 percent, while the minimum ratio required for a sustainable 4.5 percent GDP growth is 25.9 percent (Nakornthab, 2014).

[2] The government revenue-to-GDP ratio hovers around 18.3 percent, while the average among emerging Asian countries is 21.8 percent.

(2) A significant share of the budget is allocated to current expenditures, which are on an increasing trend. The rise in current expenditures is due to the mounting spending on healthcare and welfare, salaries, as well as short-term transfers and subsidies put in place by various governments**. Inevitably, investment spending has fallen, from more than 25 percent of total budget**[3] **during 2004-2006, down to merely 17.5 percent in** fiscal year **2015.**

For government investment spending to lift up Thailand's growth potential, higher efficiency in revenue collection, government expenditure, and other public administrations is needed. The current government recognizes this necessity and have initiated reforms in all three aspects, namely revenue, expenditure, and fiscal processes.

(1) Revenue reforms are designed to increase government revenue, encourage decentralisation of power to local administration, and reduce inequalities in income and land ownership. Reform measures include an introduction of property-based taxation, such as **land and property tax and inheritance tax**; as well as a crackdown on tax evasion via the introduction of **income tax on partnership and non-juristic associations**[4]. Moreover, the government plans to gradually raise **VAT** in successive steps at appropriate times, and introduce **measures to reduce existing loopholes in tax collection.**

(2) Expenditure reforms are aimed at reducing unnecesary spending and boosting the share of investment spending in the government budget.

Energy price reforms include an adjustment in the rate of contributions from oil and gas sales to the government's oil fund, and a increase in the excise tax rate on diesel. The two measures will ensure that energy prices reflect the true costs of energy, thus promoting more efficient energy consumption and eliminating distorted behaviors. The government will also benefit from the reduction in subsidies and the rise in excise tax revenue.

Expenditure structure reforms is done by raising the government's investment budget to 20 percent in fiscal year 2016, from 17.5 percent in fiscal year 2015.

State enterprise reforms are vital to upgrading the country's growth potential because state enterprises are responsible for key assets and public utilities. Furthermore, they account for a large share of the government's capital expenditure. Recognizing the importance of state enterprises, the government established the State Enterprises Policy Committee tasked to spearhead reform policies and monitoring standards, in order to help state enterprises fulfill their missions more efficiently. The Committee will also resolve financial troubles in enterprises facing losses or liquidity problems before they become a

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[3] A part of the Fiscal Sustainability Framework.

[4] In the past, a person could register a non-juristic body of persons to divide his or her income, so as to reduce his or her tax base and tax payment.

fiscal burden. Additionally, it has introduced Integrity Pact and Construction Sector Transparency Initiative (CoST) program, with an objective to improve information disclosure and transparency in government procurement.

These reforms will cut down the cost of corruption and improve the quality of service in state enterprises. In addition, they will boost the efficiently of investment, especially investment in infrastructure, which will in turn reduce logistic costs, increase production capability, and distribute wealth to the provinces. Ultimately, they will help Thailand achieve and sustain higher levels of growth in the long run.

(3) Fiscal Process Reforms are designed to foster fiscal discipline and sustainability.

Proposed draft of the new Public Finance Act is expected to establish fiscal rules, including a cap on the public-debt-to-GDP ratio and annual budget allocation. For example, capital expenditure must not be smaller than the budget deficit. Quasi-fiscal activities will also be subject to a set of regulatory and monitoring requirements, such as declaration of sources of funding and conduct of thorough cost-benefit analyses prior to operations. In addition, state enterprises will be asked to seperate the operating account and the Public Service Account (PSA), to reduce the risk of off-budget spending. As of February 2015, the Ministry of Finance is preparing to submit the draft Act to the Cabinet.

Modification of approval process for certain large-scale investment programs. For example, investment in infrastructure, which was considered off-budget in the past, will now be part of the regular budget.

Although the three-pronged reforms may cause a drag on the economy in the short run due to potentially delayed disbursements, they will pay off in the long run. They will help eliminate fiscal imbalances, enhance transparency, and increase the size and efficiency of fiscal spending especially in investment. Additionally, they will reduce fiscal risks that may create costs to the economy and undermine economic and financial stability. The reforms will also boost business confidence and create incentives for private investment, thereby contributing to higher growth potential of the Thai economy in the future.

5. Monetary Conditions

5.1 Monetary Conditions and Exchange Rates

Monetary conditions remained accommodative.

Monetary policy continued to be accommodative throughout 2014, as with the previous year. In order to further support the economy amidst political uncertainty that plagued domestic demand and tourism, the Monetary Policy Committee (MPC) lowered the policy rate at its March 12, 2014 meeting. Such accommodative stance was deemed necessary to facilitate the economic recovery, given that the global economy remained volatile and fiscal stimulus took time. The policy rate at the end of 2014 stood at 2.00 percent per annum, down from 2.25 percent per annum at the end of 2013.

Short-term money market rates and short-term government bond yields declined from the previous year, in line with the movement of policy rate. At the end of 2014, the overnight interbank rate and the 1-month government bond yield stood at

1.90 and 2.04 percent per annum respectively, both approximately 0.25 percent down from the end of 2013. Meanwhile, yields on medium and long-term government bonds hit record lows, according to falling yields in U.S. Treasuries, lower-than-expected supply of Thai government bonds, and higher demand from both domestic and foreign investors. The low inflation environment, created by the oil price decline, and the gradual economic recovery also contributed to the fall in yields. At the end of 2014, the 10-year government bond yield traded at 2.83 percent per annum, representing a 1.1 percent decline from the same period last year. The volatile movement in the bond and exchange rates markets in 2014 was driven by three key external factors. These included 1) uncertainties on the timing of the Federal Reserve's policy rate hike, 2) monetary policy divergence among major economies, and 3) global geopolitical risks.

On commercial bank rates, during the first half of 2014, both deposit and loan rates fell from the end of 2013 following the policy rate cut, before leveling off in the second half of the year. Meanwhile, loans and deposits moderated compared to last year.

At the end of 2014, the average Minimum Lending Rates (MLR) of the four largest commercial banks stood at 6.75 percent per annum, down from 6.84 percent of last year's end. Private credits extended by depository institutions[1] remained subdued. Household loans were held down by the tightening of credit standard by financial institutions that reflected weakened households balance sheet amidst fragile economic conditions. As for business loans, sluggish recovery of private investment was responsible for the slowdown. Moreover, financial institutions were reluctant to issue loans to small and medium-sized businesses, while large firms increasingly turned to raise fund through corporate bonds and equity instruments, partly because they offered lower funding costs. In sum, private credits at the end of 2014 grew by

[1] Depository institutions include domestically-registered commercial banks, branches of foreign banks, international banking facilities (ceased operations in 2006), financial companies, specialized financial institutions, savings cooperatives, and money market mutual funds, excluding the Bank of Thailand.

4.5 percent over the year, down from 10-percent growth rate of the previous year.

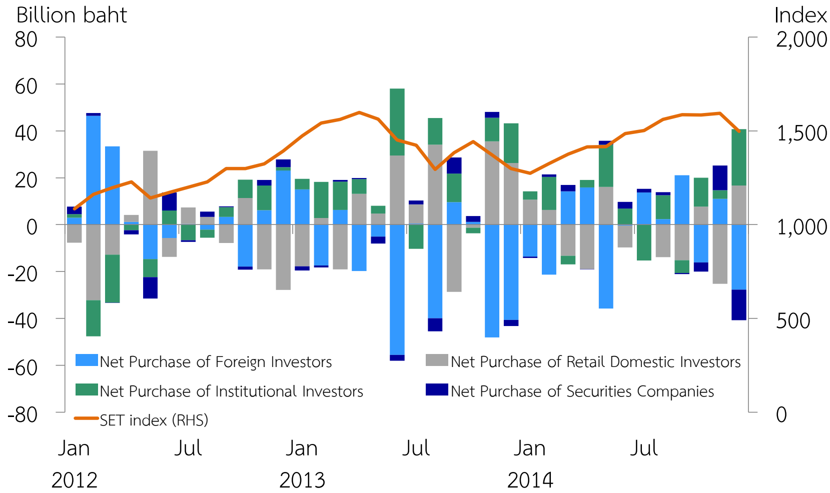
The picture was similar on the deposit side. The 12-month time deposit interest rates of the four largest commercial banks averaged at 1.73 percent per annum at the end of 2014, down from 2.23 percent one year earlier. The interest rates offered on special savings products by commercial banks and Specialized Financial Institutions (SFIs) edged down, most notably in the first half of the year. Such decline was induced by the policy rate cut, as well as lower demand for deposits owing to subdued private credits. However, interest rates of special deposit products rose slightly in the fourth quarter, as economic prospects and credit growth outlook improved. Total deposits including Bills of Exchange grew by 4.2 percent in 2014, lower than 7.6-percent growth in 2013. The slower pace of deposits growth was largely a result of the fall in household deposits, as depositors sought higher yields in alternative assets such as bond and equity funds. Nevertheless, new deposits started to increase towards year-end.

The Thai Stock market picked up after political situations eased, while the fall in global oil price remains a risk factor.

At the end of 2014, Thailand's Stock Exchange Index closed at 1,498, higher than 1,299 at year-end 2013. Uncertainty in economic outlook and political situation contributed to foreign selling from the end of 2013 to the first half of 2014, although domestic buying helped shore up the fall. As the political situations stabilized by the end of the second quarter, reduced uncertainties and resumption of government activities boosted confidence among foreign and domestic investors, thus spurring demand for Thai stocks. At the same time, the Index was hit by a number of external shocks as well. These included foreign political conflicts, uncertainties regarding the timing of Federal Reserve's rate hike, and the rapid fall in global oil prices, which was particularly pronounced in the price of energy stocks with high market capitalization.

Stock Exchange of Thailand (SET Index)

(As of December 30, 2014)



Source: Stock Exchange of Thailand (SET)

The Thai baht moved in two directions in line with global economic outlook and monetary policy decisions of major economies.

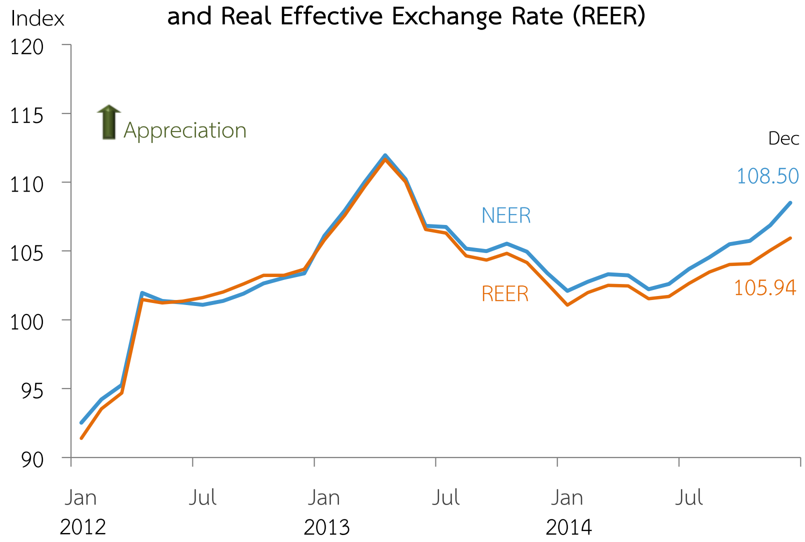
The Thai baht moved in two directions, moving up and down over 2014 to close at 32.90 baht per US dollar at year-end, comparable to previous year's close at 32.86 baht per US dollar.

The currency appreciated against the US dollar over the first half of 2014, as the U.S. recovery remained uncertain. The baht depreciated briefly in May, 2014, however, when favorable U.S. data prompted investors to speculate that the Federal Reserve might raise its policy rate sooner than expected. Concerns over Thailand's political situation at the time of government transition also added to the depreciation. The baht later resumed its appreciation path when political clarity on the establishment of government and policies restored investors' confidence in the Thai economic outlook.

Along with major and regional currencies, the baht depreciated against the US dollar throughout the second half of the year, as a result of divergent growth outlooks of major economies. That is, while the U.S. economy exhibited strong signs of recovery, the euro area and Japanese economies remained fragile, prompting additional Quantitative Easing (QE) measures from the respective central banks. Against such backdrop, the US dollar appreciated against most other currencies. The slowdown in Asian economies, including Thailand, also contributed to the weakness of the baht and regional currencies. Yet, the baht depreciated by a lesser degree than some regional currencies, because Thailand as a net oil importer benefited from the fall in global oil prices.

The Nominal Effective Exchange Rate (NEER) in December 2014 stood at 108.50, increasing by 4.9 percent from the same period last year. Weaker values of yen, euro, and ruble against the baht contributed substantially to the rise in the NEER. The Real Effective Exchange Rate (REER) reached 105.94 in December 2014, up by 3.2 percent from December last year in line with the rise in the NEER.

Nominal Effective Exchange Rate (NEER) and Real Effective Exchange Rate (REER)



Source: Bank of Thailand

6. Assessment of Thailand's Economic and Financial Stability

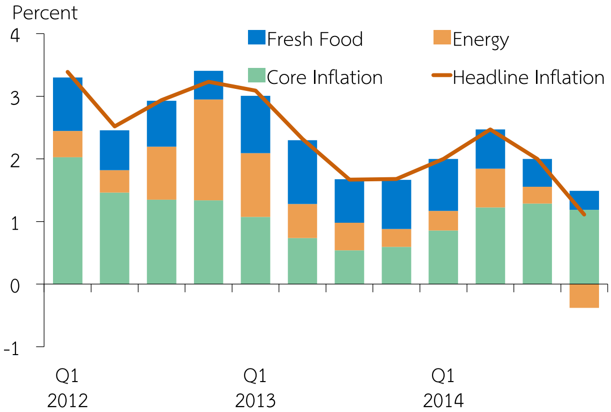
6.1 Internal Stability

Overall internal stability remained well preserved, with moderating headline inflation and low unemployment rate. Nevertheless, political situation and lackluster economic recovery put a drag on income and loan repayment ability, especially household debt, thereby worsening consumer loans quality. Financial institutions, however, proved to be resilient due to sufficient levels of provision and capital.

Headline inflation declined from the previous year to 1.89 percent. During the first half of the year, headline inflation rose on the back of increases in core inflation and fresh food prices. In the second half of the year, it decelerated due to retail oil prices edging down, albeit to a lesser extent compared to the fall in global oil prices[1] as the energy price reforms were underway.

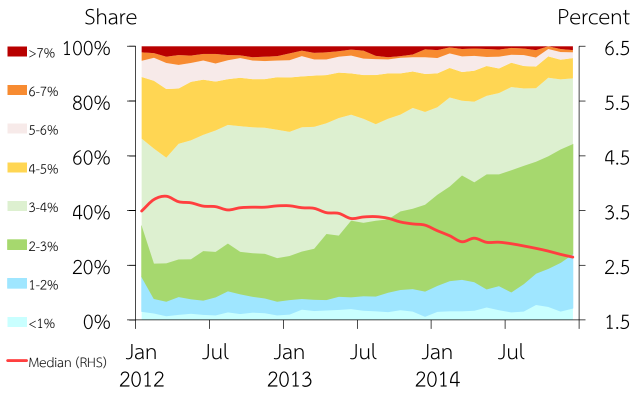
Core inflation edged up from the previous year to 1.59 percent, owing to the pass-through of rising LPG costs to prices of prepared food in the first half of the year, before waning in the final quarter. Nevertheless, overall goods and services prices were held down by the decrease in other production costs and the sluggish recovery of domestic demand. Thus, inflation pressure was mild in 2014. Despite the gradual reduction in LPG and NGV price subsidies,[2] inflation pressure is projected to remain low in 2015 due to declining global oil prices.

Contributions to Headline Inflation



Source: Bureau of Trade and Economic Indices, Calculations by Bank of Thailand

Inflation Forecast for the next 12 months



Source: Business Sentiment Survey by Bank of Thailand

The overall labor market conditions in 2014 were comparable to last year. In the first half of the year, political uncertainty contributed to slightly higher unemployment rate and employment contraction in both agricultural and non-agricultural sectors, especially in construction, trade, and hotel and restaurant industries. The depressed labor market conditions at the time

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[1] The fall in global oil prices was a result of structural change in global oil market due to rising oil supply, particularly from the U.S., as technological advances have unlocked shale oil production potential. This coupled with declining oil demand due to slow global economic recovery.

[2] In October 2014, the government adjusted the LPG price for transport industry to match that applied for household use. Later, the prices for both sectors were raised so as to reflect the true cost of energy. Currently, LPG price is at 24.16 baht/kilogram, the same with that applied for the manufacturing sector. Regarding NGV, price adjustments by the government are also underway in 2015 to raise its price to around 14-15 baht/kilogram, after an earlier raise from 10.50 to 12.50 baht/kilogram in 2014.

were also reflected in the decline in consumer confidence and number of tourists. Employment in the agricultural sector began to fall in the second quarter, suffering from depressed agricultural prices that discouraged production. In the second half of the year, economic activities improved gradually, leading to lower unemployment rate and an improvement in overall employment, particularly in non-agricultural sectors.

Key Labor Market Indicators

Annual percentage change	2013	2014*	2014*			
			Q1	Q 2	Q3	Q 4
Employment	-0.1	-0.4	-0.4	-1.2	0.3	-0.1
Agricultural	-0.1	-2.4	1.0	-2.9	-2.2	-4.9
Non-agricultural	-0.1	0.7	-1.0	-0.3	1.7	2.5
Manufacturing	0.8	1.6	-0.8	1.9	1.0	4.4
Others	-0.3	0.4	-1.1	-1.0	1.9	1.9
Unemployment (thousand persons)	283.5	322.7	341.1	385.7	326.6	237.3
Unemployment rate (%)	0.7	0.8	0.9	1.0	0.9	0.6
Underemployment (thousand persons)	336.2	256.3	277.9	258.1	245.1	244.1
Underemployment rate (%)	0.9	0.7	0.7	0.7	0.6	0.6

Note: *2010 Population Database
Source: National Statistical Office

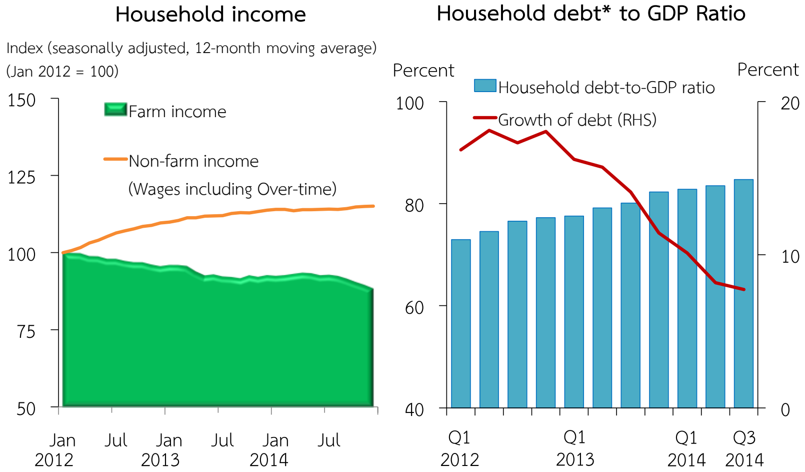
Despite stable employment conditions, slow economic recovery and high level of household debt rendered households' financial stability more fragile. This was particularly for low-income group who relied heavily on farm income and was hit by slumping agricultural prices. As a result, the loan repayment ability among households deteriorated, as shown in the share of loans overdue above 1 month among commercial banks edging up slightly from 5.7 percent at the end of 2013 to 5.9 percent at the end of 2014.

Nonetheless, because households had become more cautious with spending, and financial institutions had become more careful with lending, the risk of further household debt accumulation declined, as evident in the stalling household credit growth. That is, total amount of household loans held by financial institutions[3] expanded by 7.7 percent at the end of third quarter

[3] Refers to both depository and non-depository financial institutions, such as commercial banks, specialized financial institutions, credit unions, pawnshops, finance companies, credit card, leasing and personal loan companies, and insurance companies.

of 2014, down from 11.4 percent at the end of 2013. Despite such decelerating trend, household credit growth still exceeded GDP growth, resulting in a mild increase in household debt-to-GDP ratio. At the end of third quarter of 2014, the ratio stood at 84.7 percent, up from 82.3 percent of previous year's end.

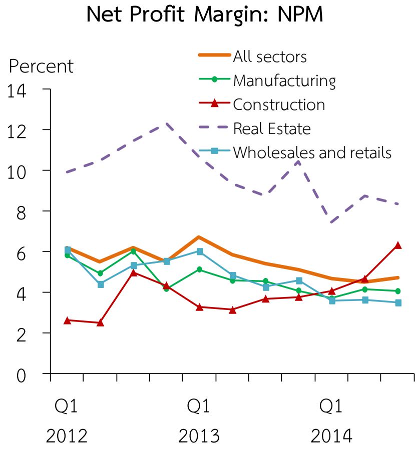
Household Stability Indicators

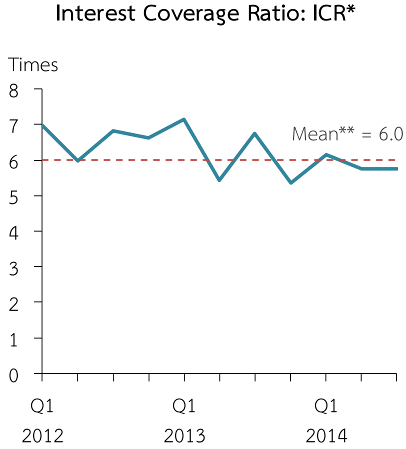


Source: Office of Agricultural Economics, National Statistical Office, calculations by Bank of Thailand

Note: *Household loans issued by various financial institutions
Source: Bank of Thailand

Non-financial institutions remained healthy overall, as shown by the debt-to-equity and current ratios, which hovered close to past average. Yet, profitability dropped given weak economic growth. As a result, net profit margin (NPM) among firms listed on the Stock Exchange of Thailand, especially in wholesale and retail sale businesses, dropped at 4.6 percent during the first three quarters of 2014. This figure was well below the 6 percent level for the same period last year and the ten-year average. The interest coverage ratio declined from 6.4 of previous year to 5.9, suggesting some deterioration in debt repayment abilty of firms. Compared to large corporates, SMEs experienced more severe impact from political situation and sluggish economic recovery. Additionally, SMEs faced more stringent credit standards from financial institutions, impairing their liquidity.

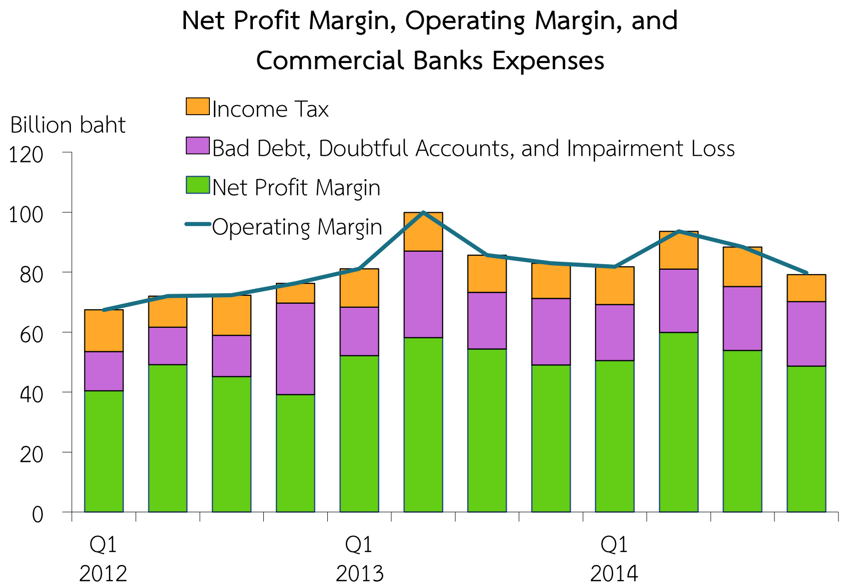




Note: * Median **Mean from Q3 2004 – Q3 2014

Source: Stock Exchange of Thailand, calculations by Bank of Thailand

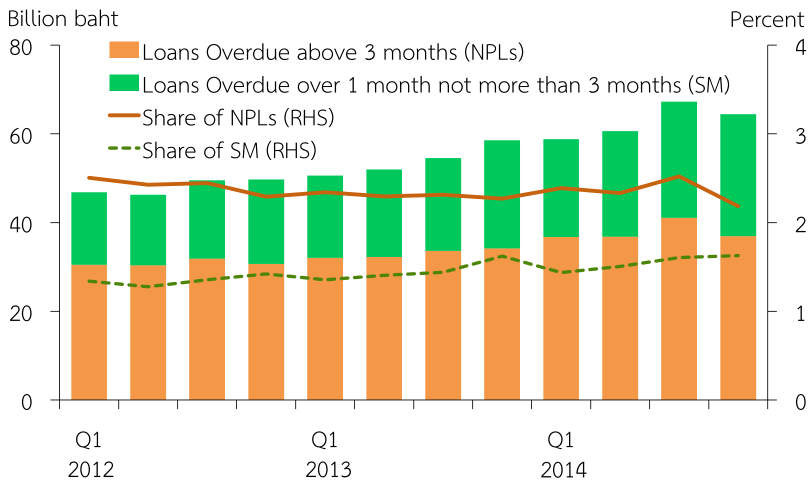
The financial institutions in 2014 remained resilient, with high provision and capital adequacy to withstand economic shocks. At the end of 2014, the ratio of actual reserves to reserve requirement and the capital adequacy ratio (BIS ratio) recorded at 169.4 and 16.8, respectively. Commercial banks' operating profits and net profit margin stalled due to slowdown in credit growth, against the backdrop of weak economic conditions and banks' more cautious lending to customers that had weakening balance sheets, particularly SMEs and households. Although the non-performing loans (NPLs) to total loans ratio remained steady at 2.15 percent, the special-mention loans to total loans ratio rose from 2.4 to 2.6 percent. There were also signs that SMEs and consumer loans quality fell moderately from the previous year.



Source: Bank of Thailand

The real estate sector was sound, thanks to recovery in domestic demand in the second half of the year following the easing of political situation. Home buyers' loans repayment ability remained sound, with a small share of loans overdue above 1 month. Nevertheless, sluggish demand recovery had resulted in slight increase of excess housing supply at the end of the year, even though a number of new housing sales openings were postponed.

Mortgage Loans Quality of Commercial Banks (Post Finance)

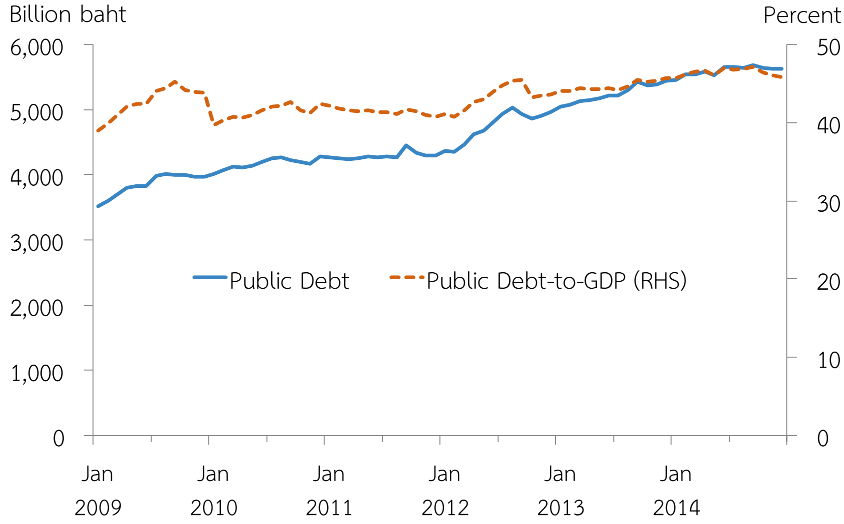


Source: Bank of Thailand

Overall fiscal stability remained solid, despite increased risks stemming from quasi-fiscal activities in the previous period. The debt-to-GDP ratio rose marginally from 45.7 at the end of 2013 to 45.8 at the end of 2014. The increase in debt resulted from the additional borrowing of 250 billion baht for financing the budget deficit to stimulate economy, and from debt guarantees for specialized financial institutions that funded quasi-fiscal activities, notably the rice pledging scheme in 2014.

Going forward, a major risk for fiscal stability stems from government's limited capability to expand its revenue, following the reduction in corporate and personal income taxes designed to stimulate the economy. Meanwhile, fiscal spending is on the rise due to growing current expenditure and large-scale infrastructure investment projects planned. Fiscal reforms on both tax and expenditure sides, which are beginning to take shape, along with a commitment to fiscal discipline, are crucial to ensure fiscal sustainability in the long run.

Fiscal Stability Indicators



Source: Public Debt Management Office

6.2 External Stability

External stability was well maintained, with nearly all indicators on liquidity and loan repayment ability improving from the previous year, and remaining above international standards. Thailand posted the large trade surplus, partly as a result of the significant drop in global crude oil price. Outstanding external debt also declined from the previous year following the fall in short-term debt due to two factors. (1) Commercial banks had paid back the short-term debt used to manage their foreign exchange positions in the previous period. Besides, demand among Thai exporters for currency hedging decreased in 2014, thus banks were required to borrow less foreign currencies to manage their positions. (2) Foreign investors sold their holdings of short-term Bank of Thailand bonds. Nonetheless, long-term debt grew due to the net foreign purchase of long-term government bonds and corporate bonds issued by Thai businesses.

External Stability Indicators

	International benchmarks	2013	2014[E]	2014[E]			
				Q1	Q2	Q3	Q4
Indicators of debt servicing ability (percent)							
- Current account balance[1/] to GDP	n.a.	-0.6	3.8	5.9	-0.6	-0.6	10.2
- External debt to GDP[2/]	48-80 [4/]	38.7	37.5	38.1	39.2	38.7	37.5
- External debt to value of exports of goods and services [1/ 2/]	132-220 [4/]	51.9	50.3	50.9	52.6	52.2	50.3
- Debt service ratio[3/]	< 20	4.0	4.4	3.9	4.6	4.6	4.4
Indicators of liquidity							
- Gross reserves to short-term external debt	> 1 times	2.7	2.7	2.8	2.7	2.7	2.7
- Gross reserves to import value (months)	> 3-4 months	9.2	9.4	9.6	9.9	9.5	9.4
- Short-term external debt to total external debt (percent)	n.a.	43.6	40.6	42.7	43.1	41.4	40.6

Notes: [1/] Since October 2006, "Reinvested Earning" has been recorded as part of direct investment in the financial account and its contra entry recorded as "Investment Income" in the current account.

[2/] Outstanding debt divided by averaged quarterly GDP or export values for the last three years starting from the quarter considered.

[3/] Principals and interest payments (both short and long terms) of external debt divided by value of exports of goods and services.

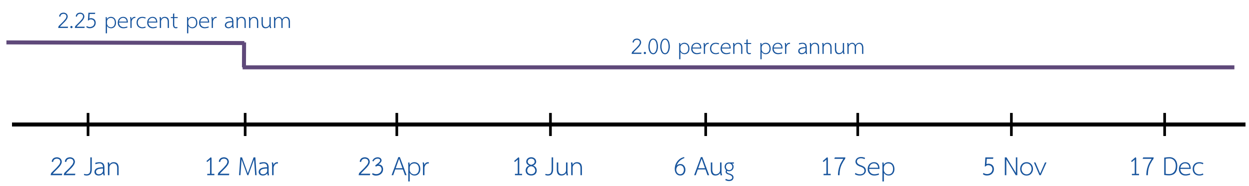
[4/] Benchmark for middle-income countries, i.e. with GDP per capita of 756 – 9,265 US dollars per year.

Source: Bank of Thailand

7. Important Policies and Measures

Interest Rate Policy

Policy Interest Rate



Monetary Policy Committee (MPC) Meetings in 2014

Source: BOT News No. 2/2014, 7/2014, 13/2014, 22/2014, 34/2014, 40/2014, 49/2014 and 55/2014

○ At the first MPC meeting of the year on January 22, 2014, the Committee decided to maintain the policy interest rate at 2.25 percent per annum. This level of policy rate was deemed sufficiently accommodative to support economic recovery while maintaining the country's financial stability, a key basis for economic recovery going forward. The Committee was also of the view that the fundamentals of the Thai economy were strong and able to cushion the economy against short-term risks posed by the political situation.

○ At its second meeting on March 12, 2014, the MPC decided to reduce the policy rate by 0.25 percent per annum, in response to the increased risk posed by the prolonged and highly uncertain political situation. The political risk hindered the recovery of private consumption and investment, and had adverse impacts on the tourism industry. Moreover, given low inflationary pressure and reduced risks to financial stability in line with greater stability in the global financial markets, monetary policy could be eased up to curtail risks and provide an impetus for the economy. Subsequently at its third meeting on April 23, 2014, the Committee decided to maintain the policy rate at 2 percent per annum as the monetary condition was deemed sufficiently accommodative to support the economy.

○ Following the improved political situation at the end of May 2014, the Committee judged that the economy was on its path towards recovery, and that there was a clearer policy direction from the government, contributing to the rebound of private confidence and domestic demand. Under such circumstances, the monetary policy should remain accommodative to support the initial stage of economic recovery. The Committee therefore decided at its subsequent meetings on June 18, August 6 and September 17, 2014 to maintain the policy rate at 2.00 percent per annum, a level deemed appropriate for the maintenance of long-term financial stability.

○ In the last quarter of 2014, Thailand's economic growth appeared to be slower than the MPC's past assessment. Economic recovery was also exposed to increased risks in the global economy and delays in public investment. However, the Committee viewed that monetary policy was adequately accomodative and appropriate for the economic conditions, which were expected to gradually improve in 2015, without undermining long-term financial stability. The Committee therefore decided at its meetings on November 5, and December 17, 2014 to maintain the policy rate at 2 percent per annum.

Financial Market Measures

Foreign Exchange Control

Measure	Key Content	Effective Date
Relaxation of regulations on exchange rate-hedging derivatives transactions.	1. Permits Thai residents to cancel exchange rate-hedging derivatives transactions for direct investment, lending and borrowing nominated in foreign currencies. Financial institutions are required to ensure that customers agree not to conduct duplicative derivatives transactions or exchange rate hedging. 2. Permits government agencies to conduct exchange rate-hedging derivatives transactions without submitting proof documents to the Bank of Thailand, and to cancel such transactions in every case.	November 3, 2014

Source: BOT Circular No. FMD(21) W.39/2014 dated October 21, 2014