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Members Present

Veerathai Santiprabhob (Chairman), Mathee Supapongse (Vice Chairman), Paiboon Kittisrikangwan, Sethaput Suthiwart-Narueput, Kanit Sangsubhan, Subhak Siwaraksa, and Somchai Jitsuchon

The Global Economy

Trading partner economies would expand at a slower pace. Advanced and Asian economies were affected by economic and political uncertainties, particularly global trade slowdown, together with country-specific factors such as the temporary impact of US government shutdown, extended political issues in Europe, and uncertainties of trade protectionist measures between the US and China. These uncertainties subsequently impinged on economic activities, especially production and merchandise exports. However, favorable labor market conditions would bolster private consumption and drive the economy going forward. **The Chinese economy** would expand at a slower pace despite some supports by government measures and accommodative monetary policy. The overall **monetary policy stance of trading partners** would be more accommodative. The Federal Reserve (Fed) was expected to delay its further rate hike due to growing concerns over the economic outlook and downward pressure of inflation. The European Central Bank (ECB) would hold its policy rate at least through the end of 2019, which was longer than market expectations. The ECB also announced a plan for additional liquidity injection into the financial system through targeted longer-term refinancing operations (TLTROs). The Bank of Japan (BOJ) was expected to maintain its accommodative monetary policy stance. Monetary policy stance of other regional central banks were expected to be more accommodative, with policy rates mostly kept unchanged throughout this year.

The Committee assessed that there was a probability of trading partner economies' growth being lower than the baseline owing to the risks of trade negotiations between the US and China as well as a no-deal Brexit. **The Committee saw a need to closely monitor developments of the aforementioned risks and evaluate their effects on the trading partner economic outlook**, particularly the rise in inventory among advanced economies during the fourth quarter of 2018, which would impact production and private consumption going forward.

The Financial Markets

Overall sentiments in global financial markets improved in the near term despite some increased concerns about the global economic slowdown. This was due to a more accommodative monetary policy stance of the Fed and the ECB, improvement in trade negotiations between the US and China, and a declined risk of a no-deal Brexit early in the quarter. Foreign investors thus continuously increased holdings of risky assets. Net capital inflows into equity markets of emerging market economies (EMs) increased, while net capital outflows from EM bond markets slightly decreased, resulting in higher prices of risky assets in the region. **Meanwhile, Thai asset prices recently experienced additional pressures from political uncertainties.** The Stock Exchange of Thailand (SET) index declined slightly, while regional indices increased. Thai government bond yields rose slightly due to a reduction in foreign bond holdings. On exchange rates the Thai baht depreciated slightly against the US dollar since the previous meeting in line with regional currencies. The nominal effective exchange rate (NEER) index also depreciated.

The Committee viewed that global financial markets would remain highly uncertain due primarily to (1) monetary policy direction of advanced economies, (2) progress on trade negotiations between the US and China, and (3) Brexit and political situation in the euro area that could intensify and affect the global economy as well as cross-border capital flows, which in turn could exert pressures on asset prices and regional exchange rates. Moreover, Thai asset prices might face additional pressures from domestic uncertainties following the announcement of election results and the formation of the new government. The Committee would thus continue to closely monitor developments in the global financial markets and exchange rates, as well as their impacts on the Thai economy.

Domestic Economic Conditions

The Thai economy as a whole was expected to continue expanding around its potential on the back of domestic demand despite external demand slowdown. **Private consumption** was expected to continue expanding across all product categories on the back of increasingly broad-based improvements in both farm and non-farm income with additional supports from government measures. Nevertheless, private consumption was restrained by elevated household debt. **Private investment** was projected to continue expanding thanks to the relocation of production base in some industries to Thailand, public-private partnership (PPP) infrastructure investment projects, and favorable business sentiment. Meanwhile, **merchandise exports** would expand at a slower pace due to (1) the effect of trade protectionist measures between the US and China on global trade volume and trading partner economies and (2) a down cycle of electronic products. However, merchandise exports would later improve during the second half of 2019 due partly to (1) redirected orders from China as well as relocation of production base in some industries to Thailand, and (2) exports of Thai electronic parts benefitting from infrastructure investment pertaining to 5G technology in foreign countries. **Exports of services** would continually expand due to recovery in tourist figures with regained sentiments and the extension of the visa on arrival fee waiver until the end of April 2019. Meanwhile, tourism expenditure would expand at a lower rate than previously assessed due to a slowdown in trading partner economies. **Public expenditure**, both consumption and investment, were expected to grow but at a slower pace than previously assessed due to (1) delayed progress on some state-owned enterprise infrastructure investment projects, (2) changes in the investment structure of some public-private partnership projects to allow for greater investment by the private sector, and (3) higher-than-expected expenditures for replenishment of the treasury account balance in the budget structure for fiscal year 2020, resulting in a smaller composition of capital and current expenditures.

The Committee expected the Thai economy to expand around its potential in 2019 and 2020 despite growing at a rate somewhat slower than expected due to external demand slowdown, while domestic demand would continue to gain traction. The Thai economy was projected to grow at 3.8 percent in 2019, which was lower than previous assessment at 4.0 percent, and at 3.9 percent in 2020. **There were possibilities that the Thai economy would expand at a rate below the baseline projection** due to (1) lower-than-expected trading partner economic growth due to uncertainties such as trade protectionist measures between the US and China that could be intensified and (2) lower-than-expected private investment due to political uncertainties. Nevertheless, there were possibilities that the Thai economy would expand at a higher rate than baseline projection owing to (1) the Chinese economy slowing down only marginally due to economic stimulus measures and (2) higher-than-expected domestic demand from public investment in infrastructure, PPP projects, earlier-than-expected acceleration of private investment after political uncertainties eased up, as well as additional government measures in supporting private expenditure.

The Committee engaged in an extensive discussion regarding the economic outlook and viewed that future economic activity would still expand around its potential. The momentum would come from domestic demand, especially private consumption that was driven by the continuation of favorable labor market conditions across almost all sectors. Private investment started to show some signs of clarity expected to be in the second half of this year. This would also continue to support growth momentum, particularly investment under Eastern Economic Corridor (EEC) and PPP projects in addition to the relocation of production base from other countries to Thailand that had been partly proceeded.

The Committee saw a need to closely monitor (1) domestic demand momentum, both private consumption and investment, (2) policy direction under the new government which could affect the continuation of public and private investment projects, imports of capital goods, the current account adjustment in the period ahead, as well as risks to financial stability and risks to medium-term fiscal position, **and (3) drought condition** which could intensify and affect economic activities going forward.

Headline inflation increased from the previous meeting due to higher energy prices. Additionally, fresh food prices rose as the excess supply of pork and eggs alleviated. Meanwhile, **core inflation** was lower than expected due to the prices of food-in-core category, housing rent, public transportation services, and vehicles. The Committee assessed that **the annual average headline inflation was broadly in line with previous projection** due to (1) continued upward pressure on energy prices due to the OPEC’s cut in oil production to compensate for the decrease in demand in tandem with the global economic slowdown, and (2) fresh food prices that would likely increase due to drought that could intensify. The Committee thus kept the headline inflation projection unchanged at 1.0 percent in 2019 and expected headline inflation for 2020 to rise to 1.1 percent. **Core inflation would increase gradually in line with domestic demand** and was revised to 0.8 percent for 2019, down from the previous assessment of 0.9 percent, while the forecast for 2020 was expected to average at 0.9 percent. There is a **probability of headline and core inflation being lower than the baseline** in line with risks to the economic projection.

Monetary Policy Decision

The Committee assessed that the Thai economy would expand around its potential on the back of continued support from domestic demand, despite a slowdown in external demand.

Headline inflation was expected to be around the lower bound of the inflation target, while core inflation would be lower than previously assessed. Overall financial conditions remained accommodative and conducive to economic growth. Nevertheless, global economic and domestic uncertainties increased. **The Committee therefore unanimously voted to keep the policy rate unchanged at this meeting in order to assess the clarity of impacts from such uncertainties.** The Committee also viewed that, going forward, there remained a need to address financial stability risks through a combination of policy tools, including appropriate changes in the policy rate, as well as the use of macroprudential and microprudential measures.

In their policy deliberation, the Committee discussed key considerations underpinning the policy decision. Their conclusions were as follows.

1) The Thai economy would continue to expand at the level around its potential in line with the previous assessment. This expansion would be driven by strong momentum from domestic demand, both private consumption and investment, which would be supported by government measures, the relocation of production base to Thailand, and the prospect of PPP projects. Tourism also continued to gain traction. Meanwhile, merchandise exports growth would weaken due to the global economic slowdown, the plateauing electronics cycle, and the impact of trade protectionist measures between the US and China.

The Committee viewed that the economy would experience increased uncertainties from domestic and external factors that could affect economic growth in the period ahead. These uncertainties included in particular (1) trade protectionist measures between the US and China that could intensify and subsequently affect trading partner economies and Thailand's merchandise exports, (2) global growth, particularly in China and Europe, that could slow down and could impinge on domestic demand, and (3) limited progress on significant infrastructure investment projects that could have knock-on effects on private investment, especially during the transition period of policy formation by the new government.

2) There were pockets of risks in the financial system that could pose vulnerabilities to financial stability in the future. First, household leverage increased, driven particularly by auto-leasing and personal loans. Meanwhile, credit quality of mortgage and auto-leasing loans continued to deteriorate due in part to more relaxed credit underwriting standards in the previous period. Second, search-for-yield behavior in the prolonged low interest rate environment could lead to underpricing of risks. For example, the assets of saving cooperatives continued to grow. Large saving cooperatives also played a greater role in the cooperatives system by extending more loans to other saving cooperatives. Meanwhile, large corporates increased their fundraising in the prolonged low interest rate environment, representing a larger share of the bond market and commercial bank loans. Third, risks in the real estate sector remained, including oversupply of property in some areas, foreign demand for Thai properties, as well as competition in the mortgage loan market, despite commercial banks exercising greater caution in ensuring that new loans extended to borrowers would correspond to their financial positions. Meanwhile, real estate developers continued to increase their funding through commercial bank loans and bonds.

In the period ahead, the Committee viewed that an appropriate level of the policy rate would still be necessary to preserve financial stability. Macroprudential and microprudential measures could only address risks in connection with loans and financial institutions under the Bank of Thailand's supervision. These measures would also be effective only for new loans. Moreover, most Committee members deemed it necessary to monitor the impacts of the implemented macroprudential measures, and to study additional appropriate macroprudential measures to more effectively prevent systemic risks. Most Committee members also viewed that both rising household leverage and large corporates that might underprice risks warranted monitoring.

3) Headline inflation would be largely unchanged compared with the previous assessment. This would be attributable to higher energy and fresh food prices offsetting the lower-than-expected core inflation. The Committee therefore would monitor factors that could affect crude oil prices in the period ahead, including oil price expectations inferred from the financial markets and the oil production outlook, especially regarding the OPEC. Moreover, the Committee would monitor factors, particularly an intensified drought, that could increase fresh food prices. **The Committee viewed that current accommodative monetary policy had allowed headline inflation trajectory to be consistent with the inflation target.** Nevertheless, structural changes such as the impacts from the expansion of e-commerce, heightened price competition, and productivity upgrades which reduced production costs all could cause inflation to rise at a slower pace than in the past despite the continued expansion of the Thai economy.

In addition, **the Committee discussed monetary policy outlook** and judged that, for the current meeting, the Committee would need to wait and assess the clarity of various factors due to heightened global economic and domestic uncertainties. Therefore, current accommodative policy would remain appropriate. Going forward, a policy rate increase would be gradual and follow a data-dependent approach, with a careful assessment of the outlook for growth, inflation, and financial stability, together with associated risks, in deliberating appropriate monetary policy in the period ahead.

Monetary Policy Group
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