



July 7, 2021

Excellency,

No. BOT.MPD.(02) 646/2564 Statement pertaining to the average headline inflation in the past 12 months residing below the lower bound of the monetary policy target

On December 9, 2020, the Minister of Finance and the Monetary Policy Committee (MPC) mutually reached the agreement to set the monetary policy target for price stability such that the headline inflation is to reside within the range of 1.0 – 3.0 percent for both the medium-term horizon and for the year 2021. The agreement also designated the MPC to write an open letter to the Minister of Finance should the average headline inflation over the previous 12 months or a forecast of the average headline inflation over the next 12 months breach the target range.

On July 5, 2021, the Ministry of Commerce issued a statement indicating that the June 2021 headline inflation stood at 1.25 percent. This resulted in the below-the-target average inflation of 0.18 percent over the past 12 months (July 2020-June 2021). Abiding by the above Memorandum, this open letter issued by the MPC shall outline (1) the dynamics of the headline inflation over the past 12 months which resulted in the average inflation being below the target; (2) the projected inflation trend and the potential time frame for the headline inflation to revert to the target; and (3) monetary policy actions taken to guide the headline inflation back to the target at an appropriate time. Details are as follows.

The average headline inflation over the past 12 months resided below the monetary policy target

The average headline inflation over the past 12 months fell below the target mainly because of the impact the prolonged COVID-19 outbreak had on both supply-side and demand-side factors since the mid 2020. Over this time period, the supply-side inflationary pressure declined, following the subdued energy prices resulting from weak demand induced by the restrictive measures implemented to suppress the spread of the virus and the uncertainty surrounding the development of the pandemic situation. Moreover, the government relief measures, namely electricity and liquefied petroleum gas (LPG) price reductions in the first half of 2021, also contributed to this disinflationary pressure. Consequently, the average energy inflation over the past 12 months stood at just 0.20 percent while the fresh food inflation expanded only slightly at 0.85 percent from the previous year. On the demand side, the demand-pull inflationary pressure was marginal, in line with the unfavorable economic conditions following the surge in the COVID-19 cases during the first half of 2021, which led to the deterioration of employment, household income, and consumer purchasing power. As a result, businesses found it difficult to raise prices of goods and services under such circumstances, leading to the low average core inflation of 0.26 percent over the past 12 months.

### Inflation dynamics going forward and the potential time frame for the headline inflation to revert to the target

The MPC anticipated that the average headline inflation over the next 12 months should fall within the monetary policy target range. Even though the headline inflation did surge in the second quarter of 2021, the effect was deemed temporary due to the low base of energy prices and several price relief measures employed by the government in the previous year. Looking ahead, the headline inflation should decline and hover around the lower bound of the target range by the end of 2021, while the medium-term inflation expectation remained well-anchored. Such outlook corresponded to the subdued demand-side inflationary pressure induced by a slow economic recovery with a high level of uncertainty; thus affecting household income and making the labor market more vulnerable. On the supply-side, the inflationary pressure was expected to gradually increase with the global oil price trend. **As for the issues regarding the reflationary pressure in advanced economies, the global commodity price surge, and global supply constraints, these factors should have limited pass-through effect on the Thai headline inflation.** Such events were expected to be temporary, as the rising inflation was caused by the short-term pent-up demand which should decline shortly afterwards. The global commodity price surge and global supply chain shortages were caused by the production disruption during the pandemic and should recover as soon as the normal production resumed in early 2022 after the pandemic was well-controlled. Furthermore, most of the Thai consumer products depended primarily on domestic supplies. Hence, the pass-through from such external factors to both producer price index (PPI) and consumer price index (CPI) remained somewhat minimal.

### Monetary policy actions taken to guide the headline inflation back to the target

Amid a high level of uncertainty and risks surrounding the economic recovery, the MPC's current priority remained to support the economic recovery. While the MPC aimed at promoting sustainable economic growth, the committee also sought to ensure that the medium-term price stability and financial stability objectives were met. The demand-pull inflationary pressure stemming from such economic recovery would be the key factor to navigate and accommodate the headline inflation to reside within the target range. The MPC's recent actions are discussed below.

The MPC had kept the policy rate at 0.5 percent since the second half of 2020 in order to continuously provide accommodative financial conditions. Furthermore, the MPC also encouraged the Bank of Thailand (BOT) to implement additional financial measures that were more proactive and more targeted so as to further mitigate the impact of the COVID-19 outbreak on both business and household sectors, to minimize the economic scarring that could hinder the economic recovery and financial stability and to help support the headline inflation to remain within target. During the first half of 2021, the BOT, in collaboration with the Ministry of Finance, implemented additional financial measures to assist those who were affected by the COVID-19 pandemic, especially SMEs and individual borrowers, in order to alleviate the negative impact on

employment, household income, and the overall purchasing power. **Looking ahead, the MPC viewed that the continuation of policies and close coordination among authorities were key to promote sound and sustainable economic recovery and to ensure financial stability.** While sufficient and targeted fiscal measures would play a leading role in cushioning any further negative impact and upkeep the public purchasing power, monetary policy should remain accommodative for some time in order to ensure the continuous economic recovery. Moreover, the economic structural reform, with the effort put forth by all parties through joint monetary, financial and fiscal measures, would help increase the potential growth and enhance the long-term stability of the Thai economy in the post COVID environment; hence leading to a more sustainable recovery and a more resilient economy that could better withstand shocks in the future. Going forward, the MPC would continue to monitor the development of key events closely and stand ready to take further monetary policy actions if necessary to support the economic growth as well as to attain both price stability and financial stability objectives.

According to the latest Memorandum of Understanding between the MPC and the Minister of Finance, the MPC will write an open letter to the Minister of Finance again six months from now, should at that time the average headline inflation over the past 12 months or the forecast of the average headline inflation in the next 12 months breaches the monetary policy target range. In addition, to enhance the transparency and clarity of BOT's communication to the general public, the MPC wished to publish this letter on the BOT's website.

Yours sincerely,

(Mr. Sethaput Suthiwartnarueput)

Governor

Chairman of the Monetary Policy Committee

The Honorable Mr. Arkhom Termpittayapaisith

Minister of Finance

Bangkok