



BANK OF THAILAND NEWS

Communications and Relations Office, Management Assistance Department
Tel. 0-2283-5016-7 FAX 0-2281-5648 www.bot.or.th

No.116/2000

Inflation Report October 2000 Press Release

The Monetary Policy Board (MPB) releases the second issue of the **Inflation Report (October 2000)**. This Inflation Report is an important mechanism in fostering public understanding of the monetary policy decision-making process. A summary of key issues is as follows:

Recent developments in inflation and economic conditions

In the third quarter of 2000, core inflation remained at a low level of 0.8 percent, while headline inflation was higher due to cost-push factors such as the surging trend of world crude oil prices and weakening exchange rate. Economic recovery in the third quarter slowed down slightly compared to the second quarter.

Inflation and GDP growth forecasts

Compared to the previous set of assumptions used in the economic forecasts three months ago, the MPB views that

1. Recent developments in the world oil market along with the crisis in the Middle East have led to the increase in oil prices. It is assumed therefore that world crude oil price will be at an average rate of 29 US dollars per barrel in the fourth quarter of 2000, and will decline slightly to an average rate of 28 US dollars per barrel in 2001 (compared to the previous assumption of 25 US dollars per barrel).

2. The depreciation of the Euro against the US dollar has reduced EU export prices in US dollars term and has helped slow down the increase in world commodity prices, especially the manufacturing unit value index and non-fuel product price index.

3. The IMF projects that in 2000 and 2001, the world economy as a whole is likely to grow at the rate of 4.7 percent and 4.2 percent respectively (compared to its previous forecasts of 4.2 percent and 3.9 percent respectively).

4. It is now less likely for the US economy to encounter a hard landing.

Outlook for GDP growth

The economic recovery has been modest given the slowdown in the growth of private consumption and investment.

In July 2000, the MPB viewed that there is a 72 per cent probability that GDP growth for 2000 will lie between 4.5-5.5 percent. However, the current view is that GDP will fall within the lower range of 4.5-5 percent with a 61 percent probability, raised from an earlier estimate of 35 percent. As for the upper range of GDP growth between 5-5.5 percent, the probability is reduced from 42 percent to 10 percent.

GDP growth in 2001 was previously forecasted to lie between 4-6 percent with a 65 percent probability. At present, the probability that GDP growth remains within 4-5.5 percent stands at 57 percent, compared to the previous estimate of 52 percent. GDP growth is likely to exceed 5.5 percent with a 6 percent probability, a fall from 13 percent estimated in July.

Outlook for Core Inflation

Core inflation in 2000 is likely to remain low as previously forecasted, with a 94 percent probability that it will lie between 0.5-1 percent, compared to an estimate of only 36 percent probability in July. This reflected that the effect of higher oil prices on consumer goods prices is not as large as anticipated.

As for 2001, the probability that core inflation will fall within 1.5-2 percent range is 26 percent, higher than the estimated probability of 14 percent in July. As a result, the MPB adjusted its average forecast for core inflation in 2001 to 1.5-3 percent, a little wider than its previous forecast of 2-3 percent.

The MPB views that core inflation may exceed the target ceiling of 3.5 percent towards the end of 2001, as a result of the planned VAT rate increase from 7 percent to 10 percent. Although the probability that core inflation overshoots the target ceiling is as high as 65 percent in the final quarter of 2001, it will reduce gradually in the following quarters.

Monetary Policy Stance

From the assessment of developments in the economy and outlook for inflation, the MPB decided to maintain the key policy rate at 1.5 percent per annum to continue to support the economic recovery. The MPB views that core inflation is likely to remain within the target range for most of the periods and that domestic demand, especially private investment, will have to pick up faster than at the present rate for a stable economic recovery. Therefore, the MPB decided to keep interest rates low to further stimulate credit expansion and the economy.

The Bank of Thailand will release the third issue of the Inflation Report at the end of January 2001.

Bank of Thailand

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