



## **BANK OF THAILAND NEWS**

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### **Inflation Report July 2003**

Mr. Bandid Nijathaworn, Assistant Governor of the Monetary Policy Group, Bank of Thailand (BOT), announced that the Monetary Policy Committee (MPC) released the July 2003 issue of the Inflation Report on 30 July 2003. The Report was issued to enhance public understanding of the BOT's policy stance, with the key details summarized as follows.

#### **Recent developments in inflation and economic conditions**

Preliminary data indicated that the Thai economy continued to expand in 2003 Q2, despite external uncertainties, in particular, the Severe Acute Respiratory Syndrome (SARS) problem, which dampened private consumption and investment in April and May. However, the SARS problem that ended swiftly and the accommodative monetary policy were positive factors that contributed to strong investor and consumer confidence. Furthermore, the economic growth of 6.7 per cent in 2003 Q1 will provide further momentum to future economic expansion.

External stability remained strong. Core inflation was low, averaging 0.2 per cent in the second quarter and first half of 2003. The exchange rate remained stable. The current account recorded a surplus throughout the quarter, despite the deterioration in the services sector due to the SARS problem. Meanwhile, international reserves remained high despite the early debt repayment to the IMF.

#### **Monetary policy stance in the last 3 months**

The subdued core inflation facilitated further easing of the monetary policy to enhance economic recovery. In order to determine the appropriate monetary policy stance going forward, the MPC discussed various important issues as follows:

1. In the 2 June 2003 meeting, the MPC deemed that the economy continued to grow satisfactory with strong economic stability, despite the impact of the SARS problem on the

services sector. However, main risks to the Thai economy in the near term emanated from external uncertainties, in particular, the fragility of economic recovery in main industrialized countries, the negative impact from SARS, and the possibility of further declines in the US dollar. Furthermore, there was the risk that core inflation may fall below the target range. As a result, the MPC stressed the need to closely monitor these developments and decided to maintain the 14-day repurchase rate at 1.75 per cent per annum.

2. In the special supplementary meeting on 27 June 2003, the MPC viewed that although economic growth was strong, risks from world economic and financial uncertainties remained. Thus, in order to deal with the uncertainties and reduce short-term capital flow volatilities, as well as lessen the risks of core inflation falling below the target range in the future, the MPC decided to reduce the 14-day repurchase rate by 50 basis points, from 1.75 per cent per annum to 1.25 per cent per annum.

3. In the latest meeting on 21 July 2003, the MPC viewed that the Thai economy grew strongly with solid economic stability. The Thai baht moved in line with regional currencies, while international reserves remained high, despite the early IMF loan repayment which ended in July. Furthermore, further easing of the monetary policy helped reduce the risk of core inflation falling below the target range. However, in the short-term, external uncertainties continued to be the main risk to future economic growth, as a result, the MPC stressed the need to closely monitor these developments and decided to maintain the 14-day repurchase rate at 1.25 per cent per annum.

### **Economic growth and inflation projections**

Compared to the assumptions used in the projection 3 months earlier, the MPC deemed that:

1) Trading partners' economies grew at a slower rate than previously assessed, especially Asian region economies, which was expected to be affected by SARS. Euro area also continued to exhibit weak economic performance.

2) On 25 June 2003, the FOMC cut the Fed funds rate by 25 basis points to 1 per cent per annum. However, uncertainties regarding US economic recovery remained. Thus, the MPC expected the FOMC to continue the accommodative monetary policy, maintaining the Fed funds rate at 1 per cent per annum until mid-2004 before raising the rate slightly when the economy showed clearer signs of recovery.

3) The MPC assessed that uncertainties will continue to pressure world oil prices, while oil supplies from Iraq will take some time to return to normal levels. As a result, the MPC used the assumption that the Dubai crude oil price would average at 25 and 24 US dollars per barrel in 2003 Q3 and Q4, respectively, higher than assumed in the previous Report. From 2004 Q1 onwards, the MPC used the assumption that Dubai crude oil price would remain at 23 US dollars per barrel, the same as in the previous *Report*.

4) The 14-day repurchase rate remained at 1.25 per cent per annum throughout the forecast period.

The year-on-year economic expansion of 6.7 per cent in 2003 Q1 and continued growth in 2003 Q2 witnessed from preliminary data would be a firm basis for sustaining growth going forward. Furthermore, due to the smaller-than-anticipated SARS impact on the economy and the accommodative monetary policy, the MPC assessed that in 2003 the Thai economy would grow between 4.5 – 5.5 per cent, an upward adjustment from the previous projection. The probability of economic growth staying within the 4.5 - 5.5 per cent range was around 88 per cent. In 2004, Thailand's GDP growth was expected to accelerate to 5 - 6 per cent with a probability of around 67 per cent.

### **Core inflation outlook**

The MPC anticipated that in 2003, core and headline inflation would average around 0 - 0.5 per cent and 1-2 per cent respectively, unchanged from the previous forecast. In 2004, core and headline inflation were expected to average around 0 – 1 per cent and 1 - 2 per cent respectively.

Core inflation was expected to remain low and within the target range of 0-3.5 per cent, facilitating the maintenance of an accommodative monetary policy stance to support economic growth.

**Bank of Thailand**

**30 July 2003**

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