



BANK OF THAILAND NEWS

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No. 36/2003

Inflation Report October 2003

Mr. Bandid Nijathaworn, Assistant Governor of the Monetary Policy Group, Bank of Thailand (BOT), announced that the Monetary Policy Committee (MPC) released the October 2003 issue of the Inflation Report on 30 October 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

The Thai economy expanded 5.8 per cent in 2003 Q2, a slowdown from 6.7 per cent in the first quarter, due to the effect of the SARS problem on the services sector. The adverse effect, however, was not as severe as previously expected. In the first half of the year the economy expanded 6.2 per cent due mainly to private expenditure and exports. With regard to 2003 Q3, preliminary data indicated that the economic activity continued to expand, supported by both private and public spending. Although export growth has recently slowed down due to the high base level in the previous year, it still remained an important engine of growth. Furthermore, the accommodative monetary policy contributed to strong investor and consumer confidence.

Overall economic stability remained strong. In 2003 Q3, headline inflation rose year-on-year by 1.9 per cent, whereas core inflation averaged 0.2 per cent which was mainly due to the decline in housing rents. Excluding housing rents, core inflation averaged 0.5 per cent. The flat core inflation did not imply deflation as headline inflation remained positive and economic growth continued to be robust. Regarding the external sector, international reserves remained high despite the early debt repayment to the IMF in July. The current account continued to record a surplus, while foreign debt declined.

Monetary policy stance in the last 3 months

The subdued core inflation facilitated further easing of 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 11 September 2003 meeting, the MPC deemed that the economy continued to grow strongly supported by growth in exports and domestic consumption, as well as acceleration in private investment. Production in the agricultural and manufacturing sectors continued to expand satisfactory. With regard to the services sector, tourism began to recover after the SARS situation subsided. However, external factors continued to pose risks to the Thai economy and should be followed closely. As a result, the MPC decided to maintain the 14-day repurchase rate at 1.25 per cent per annum and agreed on the implementation of additional measures to monitor short-term capital movements in order to prevent speculation.

2. In the latest meeting on 28 October 2003, the MPC viewed that the Thai economy grew strongly with good economic stability. Furthermore, core inflation remained low and in the near term, there was a risk that core inflation may fall below the target range. In addition, external uncertainties continued to be the main risk to future economic growth. As a result, the MPC 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 were expected to improve than previously assessed, especially the US and Japan. Meanwhile the euro area continued to exhibit weak economic performance before picking up slowly in 2004 following the recovery in the US coupled with the ECB's low interest rate policy. The Asian region economies were expected to improve after the SARS problem had subsided.

2) The assumption on crude oil price rose from the previous assessment owing to uncertainties pertaining oil supply from Iraq due to the attacks on Iraqi's oil production area. As a result Iraqi's production and export of oil was unable to fully recover. Furthermore, OPEC decided to reduce the production quota. Dubai crude oil price would remain high in 2003 Q4 before declining in 2004 in line with world production which was expected to increase, especially from economies outside the OPEC group.

3) Fiscal expenditure for the fiscal year 2003 was assumed to be lower than that in the previous *Report*. The lower assumption was due mainly to the lower-than-expected capital expenditure disbursement rate, as well as state enterprise capital expenditure that was assumed to be postponed to fiscal year 2004.

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 6.2 per cent in the first half of 2003 and continued growth in 2003 Q3 witnessed from preliminary data prompted the MPC to assess that in 2003 the Thai economy would grow between 5.75 – 6.25 per cent, an upward adjustment from the previous projection. The probability of economic growth staying within the 5.75 – 6.25 per cent range was around 88 per cent. In 2004, Thailand's GDP growth was expected to accelerate to 5.5 – 6.5 per cent, higher than the previous projection, with a probability of around 80 per cent.

Core inflation outlook

The MPC anticipated that in 2003, core inflation would average around 0 and would slightly increase to 0 – 1 per cent following economic recovery in 2004. Headline inflation would average around 1.5 - 2 per cent and 0.5 - 1.5 per cent in 2003 and 2004 respectively.

Bank of Thailand
30 October 2003

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