



BANK OF THAILAND NEWS

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Governor Tarisa Watanagase's Announcement

on the Direction of Policy of the BOT

Dr. Tarisa Watanagase, the Governor of the Bank of Thailand (BOT) announced the direction of policy of the BOT in the forthcoming period as follows:

As policymaking is intimately connected with economic and financial conditions today and going forward, I shall begin with the issues of economic and financial conditions.

With regard to the economy, no particular concern stands out. Indeed, the Thai economy has displayed a respectable degree of resiliency despite a host of unfavorable disturbances to production and costs during the past 2 years. High oil prices, natural disasters and political instability notwithstanding, the economy has been expanding at an annual rate of 4-5 per cent. This pace of expansion is proof to Thailand's ability to withstand future adverse challenges. The Bank of Thailand's priority is to ensure a sustainable economic growth path with stability. In 2007, economic growth is expected to pick up on the back of lower domestic retail oil prices, stable interest rate outlook, and the disentanglement of the political gridlock as well as expansionary fiscal policy. On the whole, domestic factors have become more supportive to growth.

However, vigilance and close monitoring are necessary with regards to external developments. The risks include the softening of world economic growth, a surge in world oil prices, a weakened US dollar in view of US current account deficit as well as highly volatile exchange rates on the back of intensified capital flows within the region.

With respect to monetary policy, the public has accepted the efficacy of the inflation targeting framework. Monetary policy will continue to operate under this framework. The aim is to maintain price stability according to the announced target range. In the meantime, the Bank of Thailand is undertaking a study to determine the appropriateness of the current inflation target and monetary policy instruments. Should adjustments become necessary, with the consent of the Monetary Policy Committee, the Bank of Thailand may make changes to further strengthen the effectiveness of monetary policy.

With regard to the exchange rate, the principles of managed floating will continue to be applied. That is, market mechanism determines the rate of exchange. The Bank of Thailand's role is to prevent excessive exchange rate volatility, particularly that which is brought on by speculative short-term flows; in view of the fact that the baht's misalignment with other regional currencies and its disconnection from fundamentals can adversely affect trade and business activities.

Fast and sudden cross-border capital flows and the problem of global imbalance, which affects the value of the USD, will continue to present a challenge. To some extent, the Bank of Thailand may be able to limit excess volatility in the baht exchange rate, but we are not able to resist the depreciating trend of the US dollar. It is, therefore, necessary that the business sector manages the exchange rate risk they face as well. Up to now, capital inflows to Thailand face no impediment, but some obstacles are still present in relation to outflows from Thailand. These obstacles may have limited investment and saving opportunities for Thai residents. In future, measures to restrict capital outflows will be relaxed. In the process, all parties involved must learn to improve the management of risks associated with the exchange rate as well as other financial risks. Aside from limiting excessive exchange rate volatility, the Bank of Thailand will place financial market development as a priority to ensure that the money, capital and foreign exchange markets are deep enough to withstand large volume of flows.

With regard to financial institutions policy, the Bank of Thailand's top priority will continue to be the stability and resiliency of financial institutions. I remain committed to the framework and direction that former Governor M.R. Pridiyathorn Devakula and I have laid down over the years and will take the task to completion.

Policy priorities can be summarized into five key points, as follows:

1. Enhance financial institution's resiliency by strengthening regulatory and supervisory standards to meet international best practices, such as the introduction of Basel II capital requirement, the new provisioning rule under International Accounting Standard No. 39, as well as other measures provided for under the new Financial Institutions Businesses Act, particularly consolidated supervision. Toward this end, the Bank of Thailand and other relevant agencies are scheduled in the first quarter of 2007 to take part in the Financial Sector Assessment Program (FSAP), which is a joint project conducted by the IMF and the World Bank to assess the strengths and weaknesses of the financial system and its supervisory framework.

2. Increase emphasis on good corporate governance at financial institutions, particularly with respect to the structure of the Board of Directors, fit and proper criteria for senior management, honesty and transparency in business practices as well as fair treatment of customers. The Bank of Thailand will also emphasize information disclosure by financial institutions in the manner that is sufficient for depositors, borrowers, and investors to make informed choices, thus facilitating effective market discipline over financial institutions.

3. Encourage financial institutions to improve operational efficiency, especially in the area of risk management, which has become increasingly more complex and requires greater investment in information system, technology, and human resources. This will be a critical factor that determines financial institutions' ability to meet the challenges from a more globalized and competitive market going forward.

4. Continue the second phase of the Financial Sector Master Plan (FSMP) following the first phase, the implementation of which is near completion. The second phase will aim to induce improvement in the efficiency of domestic financial institutions through competition under a phased introduction of new players, both domestic and foreign. The implementation of this phase will be made in gradual pre-announced steps to give financial institutions time to make necessary adjustments.

5. Urge all parties to promote greater financial literacy to the public in order to facilitate informed decisions on financial services and products that are appropriate to their needs and circumstances. This will enhance their understanding of risks and ensure resiliency in the face of challenges that may arise from more intensified competition and proliferation of new products.

For the Bank of Thailand to conduct monetary policy effectively and ensure financial stability in accordance with the outlined goals under a changing financial landscape, changes to the current laws are necessary to facilitate our principal missions. To enhance the effectiveness of monetary policy conduct, a principal mission, changes to the Bank of Thailand Act and the Currency Act are under way. The essence of this undertaking is to give the Bank of Thailand independence while securing an appropriate system of checks and balances. The Bank of Thailand's conduct will be made transparent with full accountability. In addition, we plan to expedite the enactment of two financial institutions acts namely, the Financial Institutions Businesses Act, which will enable us to handle a complete set of new financial businesses as well as empower the Bank of Thailand not only to supervise and regulate financial institutions and protect consumers more effectively, but also to deal promptly with financial institution problems; and the Deposit Insurance Agency Act, which will create the Deposit Insurance Agency to replace in a gradual fashion the existing blanket guarantee scheme with limited guarantee on deposits.

In view of heightened economic uncertainty in the coming years and the requirement that our staff must be able to identify and deal with challenges in a forward-looking manner, the Bank of Thailand will inculcate into our staff the willingness to learn as well as to adapt. In this light, the Court of Directors of the Bank of Thailand together with top management have determined that the following shall be the vision of the Bank of Thailand for the next five years: "A forward-looking organization with competent staff dedicated to ensuring the resilience of Thai economy against shock and instability." We will do our utmost to realize this vision.

Bank of Thailand

15 November 2006