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Monetary Policy Report September 2014

Mr. Mathee Supapongse, Assistant Governor of the Bank of Thailand (BOT) and Secretary of the Monetary Policy Committee (MPC), released the September 2014 issue of the *Monetary Policy Report*. The *Report*, published quarterly, is aimed at enhancing public understanding of the MPC's policy stance and its assessment of Thailand's economic outlook, with main details summarized as follows.

1. Economic Outlook

The global economy continued to recover, but at a slightly slower pace than previously estimated, with greater growth differentials across regions. The Euro area economies became more fragile from exposure to geopolitical risk while the Japanese economy was affected by consumption tax hikes more than previously anticipated. On the other hand, the US economy recovered more firmly on the back of improving employment and financial position of the private sector, helping Asian economies' exports to partially offset their domestic demand slowdown.

The Thai economy in 2014 is likely to expand at the same rate as formerly projected as stronger-than-expected domestic demand helps compensate for weaker-than-expected export performance. The slow merchandise export and tourism recoveries are projected to continue into 2015 and contribute to lower growth outlook for the year. Greater political clarity and restoration of government ability to perform its regular roles has revived government expenditure and private sentiments, leading to stronger-than-expected consumption of nondurable goods and gradual recovery of construction investment. On the external front, a combination of weak external demand and domestic supply-side constraints has contributed to poor merchandise export performance. The supply-side constraints stem from Thai manufacturers suffering from limited production capability to take full advantage of increasing global demand for new generation of high-technology products. Moreover, a sizeable share of Thai exports is in agriculture which has been impacted by low prices. These factors are likely to take time to overcome and will affect exports throughout the forecast period. As for exports of services, tourism has recovered more slowly than expected due to continued caution over domestic and international political situations. Thus, merchandize exports and tourism are likely to contribute much less in 2015 than previously expected, lowering overall economic growth.

Inflationary pressure declined on the back of decreases in global and domestic oil prices. The MPC lowered Dubai oil price and domestic fuel price assumptions slightly, while continuing to maintain assumptions of steady diesel and liquefied petroleum gas (LPG) prices throughout the forecast period. While demand pressure is likely to increase in tandem with economic recovery, it is likely to remain modest due to anchored inflation expectations.

2. Projection for Growth and Inflation

Forecast Summary			
Percent per year	2013*	2014	2015
GDP Growth	2.9	1.5 (1.5)	4.8 (5.5)
Headline Inflation	2.2	2.2 (2.6)	2.1 (2.5)
Core Inflation	1.0	1.6 (1.7)	1.3 (1.4)

Note: * actual data
Source: NESDB, MOC, and forecasts from BOT

In light of the economic assessment above, **the MPC maintained its growth projection for 2014, but lowered growth for 2015 from the previous forecast**. The projection assumes risks in 2014 to be skewed to the downside, as exports could be affected by supply-side constraints more than expected, and government investment projects might not be expedited as much as expected. In 2015, however, risks are more balanced as public spending could gain more traction following clearer government policy on infrastructure projects, which could result in stronger-than-expected private investment growth. The fan chart for growth is thus downward-skewed for 2014 and is balanced for 2015. **Headline and core inflation forecasts were revised down for both 2014 and 2015**. Risks to the forecasts are balanced between upside risk from possible hike of LPG price and higher cost pass-through during the economic recovery, and downside risk from lower demand pressure if the economy recovers slower than expected. Therefore, the fan charts for both headline and core inflation are evenly distributed over the forecast period.

3. Monetary Policy Deliberation

The MPC deemed the current degree of monetary policy accommodation is still needed to support economic recovery, amidst slow global recovery while not posing risks to financial and price stability. In the August 6, 2014 meeting, the MPC expected reduced political uncertainty to enable a private spending-led recovery in the face of some delay in government spending and export recovery. At the same time, inflationary pressure was expected to remain contained. The MPC therefore voted unanimously to maintain the policy rate at 2.00 percent per annum, to complement the government's reform efforts to lift the economy's potential growth. In the most recent meeting on September 17, 2014, the MPC assessed that improving private confidence and rebound of public and private spending have shored up domestic demand, which should help sustain economic momentum. On the other hand, export growth continues to be affected by supply-side limitations and low agricultural prices. The MPC therefore viewed the prevailing monetary policy stance to be appropriate given that the economy is in an early stage of recovery, and that the stance does not pose risk to long-term financial stability. The MPC thus voted unanimously to maintain the policy rate at 2.00 percent per annum.

Bank of Thailand
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