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Monetary Policy Report, March 2021

The Bank of Thailand (BOT) released the March 2021 issue of the *Monetary Policy Report*. The *Report*, published quarterly, is aimed at enhancing public understanding of the Monetary Policy Committee (MPC)'s policy stance and its assessment of Thailand's economic outlook. Details are summarized as follows.

Monetary Policy Conduct in the First Quarter of 2021

At the meetings on February 3 and March 24, 2021, the Committee voted unanimously to maintain the policy rate at 0.50 percent. The Committee assessed that the Thai economy continued to expand despite the impact from the new wave of COVID-19 infections due to less strict containment measures relative to last year, the timely implementation of fiscal stimulus measures, and exports recovery in line with trading partner economies' growth. Nevertheless, the economic recovery remained uneven across economic sectors and would be subject to risks and uncertainties. Main risk factors include the efficacy and distribution of COVID-19 vaccines, the recovery in foreign tourist figures, and the continuity of government measures. The financial system remained sound, but vulnerabilities increased in the business and household sectors, especially SMEs and low-income households. Headline inflation would return to the target range around mid-2021 and remain close to the lower bound of the target range throughout the forecast period. The Committee viewed that the Thai economy still needed continued support from the low policy rate; in addition, given the risks and uncertainties ahead, the Committee viewed that the limited policy space should be preserved for the most appropriate timing to maximize policy effectiveness.

The Committee viewed that the continuity of government measures and policy coordination among government agencies would be critical to the economic recovery going forward. The government should prepare measures to provide continued support to the economic recovery and to respond to relevant risks in each period, together with devising additional measures for worst-case scenarios as needed. The Committee also saw the need to expedite the implementation of the new financial rehabilitation measures for businesses affected by COVID-19 pandemic proposed by the Bank of Thailand, the Ministry of Finance, and other related parties. These measures include the soft loan facility to support viable businesses and the asset warehousing program.

Assessment of the Economic and Financial Outlook as the Basis for Policy Formulation

1. Global Economy

The global economic outlook has improved on account of the large economic stimulus package in the U.S. and a strong recovery in Asia's exports. Looking ahead, the global economy would continue to recover on the back of the distribution of COVID-19 vaccines that would likely increase in many countries, as well as the support from ongoing fiscal stimulus measures and accommodative monetary policy. **The Committee assessed that Thailand's trading partner economies would grow 5.5 percent in 2021 and 3.8 percent in 2022. Meanwhile, the balance of risks was still tilted to the downside overall.** Near-term risks receded as the U.S. trade policy became more supportive of global trade and as COVID-19 vaccination coverage increased. However, there remained risks stemming from the new wave of COVID-19 infections that could be severe and prolonged, as well as the more fragile global financial stability.

Governments worldwide continued to implement monetary and fiscal measures, particularly in the U.S. with the recent 1.9 trillion U.S. dollars fiscal stimulus package. Central banks also continued to maintain their accommodative monetary policy by keeping policy rates low as well as through quantitative easing.

2. Financial Conditions and Financial Stability

Overall financial conditions in Thailand remained accommodative. Short-term interest rates in financial markets remained at low levels consistent with the policy rate. Meanwhile, long-term government bond yields increased in tandem with their U.S. counterparts, which rose on account of higher inflation expectations in the U.S., better economic outlook in light of the U.S. stimulus package, as well as the U.S. Treasury bond supply that was expected to rise given the stimulus package. Nevertheless, this had limited impact on overall financial conditions and financing costs in Thailand in the recent period. Financial markets were able to adjust accordingly through market mechanism and function as normal. Benchmark lending rates of commercial banks remained at low levels, while new loan rates (NLR) have declined across all loan sizes. On exchange rates, the baht against the U.S. dollar and the effective exchange rate depreciated from the previous quarter due to appreciation of the U.S. dollar following the announcement of the large U.S. stimulus package. Despite the pressure on the baht having eased as a result of the significant reduction in Thailand's current account surplus in 2021, the Committee would closely monitor developments in the foreign exchange market and capital flows and their implications for the economic recovery going forward, together with assessing the necessity of additional appropriate measures, while continue to expedite the the new FX ecosystem in Thailand.

The Thai financial system remained vulnerable amid the slow economic recovery due to fragile balance sheets and debt servicing capabilities of households and businesses. Looking ahead, the new wave of COVID-19 outbreak would exacerbate the uneven recovery across sectors, with tourism-related services being most affected. As such, it would be necessary to closely monitor balance sheets and debt servicing capability of households and businesses going forward.

3. Economic and Inflation Outlook

The Thai economy was projected to expand 3.0 percent in 2021, which is lower than the previous assessment. The downward revision to the growth forecast was attributable to the new wave of COVID-19 infections at the beginning of the year and lower foreign tourist figures. Meanwhile, the less restrictive containment measures relative to last year, the additional government measures, and the recovery in merchandise exports in tandem with trading partner economies' growth were key factors supporting Thailand's economic growth. **The Thai economy would grow 4.7 percent in 2022,** slightly lower than the previous assessment on account of lower government expenditure under the fiscal year 2022 annual budget. Nevertheless, the anticipated rebound in foreign tourist figures on the back of widespread vaccination in Thailand and abroad would support the return of Thailand's GDP to the pre-pandemic level in the second half of 2022.

The value of Thai merchandise exports was projected to grow by 10 percent in 2021 and 6.3 percent in 2022 – an upward revision from the previous assessment. Export growth prospects would be driven by higher export prices following the increase in crude oil prices, as well as higher export quantity owing to trading partners' improved economic outlooks. In particular, the large U.S. stimulus package would drive the U.S. economy and would also have positive effects on other trading partners.

Exports of services would continue to fall and recover at a slow pace. The number of foreign tourists was projected to decline to 3.0 million in 2021 and 21.5 million in 2022 due to the delay in Thailand's re-opening plan to foreign tourists, international travel restrictions faced by Chinese tourists, delays in COVID-19 vaccination in some countries, and the mutation of COVID-19 which affected tourism sentiment.

Current account surplus was projected to decline significantly in 2021 due to high import growth. The current account balance was projected to register a surplus of 1.2 billion U.S. dollars in 2021, owing to low foreign tourist figures as well as higher import prices following the rise in crude oil prices. However, the decline in current account surplus in 2021 would be partly attributed to temporary factors such as an increase in gold imports when gold prices drop and higher transportation costs from shortage of freight containers. **Current account balance would record a larger surplus of approximately 25 billion U.S. dollars in 2022 following the recovery in foreign tourist figures.**

Private consumption would expand more-than-expected in the near term but would likely be subdued later. Private consumption in the fourth quarter of 2020 turned out stronger-than-expected due to (1) car purchases during the end-of-year sales promotion campaigns and (2) positive effects of additional government measures in response to the new wave of COVID-19 outbreak. Nevertheless, the recovery in labor income was not yet broad-based. Given the fragile balance sheets of households and weak labor market, private consumption in the period ahead would likely be subdued.

Private investment would recover at a gradual pace. Investment in machinery and equipment grew on the back of international trade and better-than-expected private consumption. Meanwhile, public-private partnership (PPP) investment projects, particularly in the Eastern Economic Corridor (EEC), were progressing with greater clarity.

Going forward, Thailand's economic outlook would remain highly uncertain and could face downside risks due to the following factors. First, Thailand's border re-opening to foreign tourists could delay given the limited progress of COVID-19 vaccination. Second, fiscal stimulus could be lower given delay in approval process for remaining projects under the Emergency Decree which would remain in effect until the third quarter of 2021. Third, balance sheets of businesses could deteriorate, possibly triggering permanent shutdowns and layoffs. This could leave scarring effects and hinder recovery of businesses and labor even after the pandemic subsided. Fourth, the non-performing loan ratio in the business and household sectors could surge after the phase-out of credit relief measures.

The Committee assessed the different recovery scenarios for the Thai economy which would depend largely on the foreign tourist figures. The assessment based on three scenarios – the base case, the worse case, and the worst case – indicated that foreign tourist figures in 2021 could be between 0.1 million to 3 million, which would result in GDP growth ranging from -1.7 to 3 percent. For 2022, the number of foreign tourists was estimated between 0.1 million to 21.5 million which would correspond to GDP growth ranging from -0.3 to 4.7 percent.

Headline inflation was projected to be 1.2 percent in 2021 and 1.0 percent in 2022. The rise in headline inflation in 2021 would be mainly on account of supply-side factors, namely the increase in Dubai crude oil prices to an average of 60 U.S. dollars per barrel. Headline inflation would also spike temporarily in the second quarter of 2021 due to the low-base effect as Dubai crude oil prices were low at about 30 U.S. dollars per barrel in the same period last year. Core inflation projections were largely unchanged at 0.3 percent in 2021 and 0.4 percent in 2022. The Committee assessed that headline inflation would return to the target range around mid-2021 and would remain close to the lower bound of the target throughout the forecast period.

Bank of Thailand
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