Edited Minutes of the Monetary Policy Committee Meeting

Bank of Thailand

28 November 2012

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Members Present

Prasarn Trairatvorakul (Chairman), Pongpen Ruengvirayudh (Vice Chairman), Tongurai Limpiti, Ampon Kittiampon, Narongchai Akrasanee, Siri Ganjarerndee and Aswin Kongsiri.

Financial Markets

Global financial market sentiment improved thanks to progress in policy measures to resolve the eurozone debt crisis and apparent efforts in the US to avert the "fiscal cliff" problem. Stock market indices of major countries edged higher while major currencies appreciated, except the Japanese yen which depreciated as investors anticipated further monetary policy easing after the upcoming election in December. Capital inflows to the region's equity and bond markets started to moderate. The Thai baht moved within a narrow range in tandem with regional currencies.

Money market rates in Thailand as well as short to medium-term government bond yields edged lower following the MPC's decision to reduce the policy rate at the previous meeting. However, long-term bond yields rose due to greater-than-expected supply of government bonds in November. The commercial banks' lending and borrowing rates were lowered in response to the policy rate cut. Most market participants expected the MPC to maintain the policy rate at this meeting.

The International Economy

The overall global economy showed signs of stabilisation and improving prospects. Most US economic indicators released were better than expected and pointed to increasing consumer spending. Signs of recovery in the housing sector and the labour market, together with higher consumer confidence could contribute to greater private investment in the periods ahead. **The eurozone economy** contracted in 2012 Q3, but the economic and financial outlook of the region was projected to be more stable next year as crisis resolution measures should become more concrete and the economies of core countries continued to hold up. Nonetheless, the MPC viewed that the eurozone debt crisis and the fiscal cliff problem in the US remained uncertain and continued to pose major risks to the global economic outlook. **Japan's economy** contracted from the previous quarter following the slowdown in exports, domestic consumption and investment. **China's economy** appeared to regain traction with recent strengthening in key areas including exports, production, domestic consumption and investment, which should bode well for a continued recovery in the fourth quarter and into next year. **Asian economies** improved on the back of better export performance and a pick-up in the Chinese economy, as well as continued buoyant domestic demand. The MPC noted that Thailand's trade with neighbouring countries continued to expand despite the global economic slowdown, reflecting an increased importance of these economies going forward.

Since the last meeting, **most central banks assessed that the global economy had shown signs of stabilisation while inflation remained subdued. Hence, most had decided to keep policy interest rates unchanged** while awaiting greater clarity on domestic and international developments.

The Domestic Economy

The Thai economy in 2012 Q3 expanded at a rate close to the previous meeting's projection as greater-than-expected strength in domestic demand offset the adverse impacts of the global economy. This was partly attributable to faster delivery of cars under the government's first-car tax rebate scheme and more-than-expected post-flood reconstruction investment, along with an upward trend in industrial production for domestic markets. Adverse impacts of the global economy appeared to have been limited to export-related sectors, while exports should begin to pick up during the first half of 2013 on the back of anticipated improvement in the global economy.

The MPC viewed that private consumption and investment would continue to serve as the main drivers of growth. Key supporting factors included favourable household incomes, good employment prospects, strong consumers' confidence, and accommodative financial conditions as evident by high credit growth. Against this backdrop, the MPC noted lessons from past economic crises that a prolonged period of low interest rates could lead to a build-up of financial imbalances in the economy, and thus deemed it necessary to closely monitor high growth of certain types of credits. In addition, if warranted, macroprudential measures could also be used along with the policy interest rate to ensure financial stability.

Overall, the MPC assessed that GDP growth for 2012 and 2013 could be slightly higher than the previous forecast, due mainly to better outlook for private consumption and investment. Looking ahead, subject to continued stabilisation of the global economy, export sector could regain its role as a growth driver in the latter half of 2013, should domestic demand moderate following the expiration of government's stimulus measures. Inflation outlook for 2012 and 2013 remained close to the previous projection.

<u>Monetary Policy Considerations</u>

The MPC assessed that the balance of risks for the Thai economy remained skewed towards growth rather than inflation. While global risks had lessened somewhat, uncertainties surrounding the global economy remained high. As such, an accommodative monetary policy stance was deemed necessary and appropriate to sustain ongoing economic expansion.

Key issues raised during policy deliberation could be summarised as follows:

(1) **The global economy showed signs of stabilisation with a somewhat better outlook than the last meeting while the latest Thai economic indicators showed better-than-expected domestic demand.** Both private consumption and investment remained robust with continuing momentum. While exports and export-related production figures suggested continued external headwinds, domestic demand should help mitigate their impacts. Furthermore, the policy rate reduction in the previous meeting had provided insurance against external risks to a certain extent.

(2) **The current monetary condition remained accommodative and commensurate with the needs of the economy,** as reflected by continued high credit growth and the low level of real interest rates which were supportive of domestic consumption and investment.

(3) **Although prospects for the global economy had improved somewhat since the last meeting, tail risks remained substantial. Thus, it was important to preserve policy space for such contingencies in the future.**

(4) Given high credit growth, especially for certain types of household credits and credits extended by Specialized Financial Institutions (SFIs), maintaining a low policy interest rate for an extensive period could accumulate greater risks to financial stability.

The MPC therefore voted unanimously to maintain the policy rate at 2.75 percent per annum. The MPC would remain vigilant in monitoring global and domestic economic developments and stand ready to take appropriate policy action as warranted.

Monetary Policy Group
12 December 2012