

Edited Minutes of the Monetary Policy Committee Meeting

Bank of Thailand

29 April 2015

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Members Present

Prasarn Trairatvorakul (Chairman), Pongpen Ruengvirayudh (Vice Chairman), Paiboon Kittisrikangwan, Jamlong Atikul, Porametee Vimolsiri, Veerathai Santiprabhob, and Sethaput Suthiwart-Narueput.

The International Economy

The global economy recovered at a pace close to the previous assessment, with the **US economic recovery** remaining intact despite being temporarily affected by the unusually cold weather. **The euro area economies** exhibited more visible signs of recovery, as private consumption and exports were fuelled by lower funding costs and the weaker euro as a result of the ECB's Quantitative Easing (QE) measures. Nevertheless, uncertainty surrounding Greece's bailout program remained a risk to the recovery in the euro area economies. **The Japanese economy** continued to recover slowly, but going forward should receive additional boost from private consumption which was expected to pick up after the annual wage negotiation. **The Chinese economic growth** continued to decelerate due to waning private investment, thereby prompting the authorities to implement additional expansionary monetary and fiscal policies in order to propel the economy toward the growth target of 7.0 percent in 2015. **Other Asian economies** also slowed down, as their exports continued to be weighed down by weak commodity prices and subdued demand in major trading partners' economies, particularly China, a major importer of commodities.

The Financial Markets

Overall monetary conditions had eased further following the policy rate reduction at the last meeting, as reflected by a corresponding fall in the money market rates and the weakening of the Thai baht against the US dollar. However, the Thai baht subsequently pared losses against the US dollar as the FOMC signaled a possibility that the timing of the federal funds rate increase could be postponed. **The Nominal Effective Exchange Rate (NEER)**, nevertheless, stabilized after having appreciated in the previous period. Meanwhile, **Thai government bond yields declined** in line with the lower policy rate, along with soft domestic data releases, and a more dovish FOMC statement. Moreover, **commercial banks also lowered their lending and deposit rates** following the policy decision. Most banks reduced lending rates by smaller amount than the reduction in fixed-deposit rates, while rates on current and savings accounts, which constituted the majority of deposits, were mostly unchanged.

In addition, the Committee agreed with plans to relax foreign exchange regulations under the Capital Account Liberalization Master Plan, which represented continuing efforts to achieve more balanced capital flows. The measures on capital flows relaxation, scheduled to be announced on 30 April 2015, were acknowledged by the Committee.

The Thai Economy

The Thai economy is projected to recover at a slower pace than assessed in the previous meeting. The pickup in public investment and positive trend in tourism should help shore up the economy, but could not fully offset the weaker-than-expected exports of goods and private consumption in the first quarter of 2015. Exports of goods contracted mainly from quantity reduction while private consumption indicators continued to decline for two consecutive quarters as a result of declining farm incomes, weaker employment outlook, and continued erosion in consumer confidence. **Looking ahead, exports of goods are subject to greater downside risks** from (1) the slowdown in trading partners' economies, especially China and ASEAN; (2) shifting global and regional trade structure as Thailand's major trading partners rely less on imports, curtailing the benefit of their economic recovery on Thai export volume; and (3) pressure from recent Thai baht appreciation, especially on low value-added and highly price-competitive products. Furthermore, **the contraction in exports could weigh down private investment and consumption.** Although the acceleration in public investment and monetary policy easing should help support private investment, the impact was likely to be limited given the excess production capacity and subdued growth in domestic demand.

Inflationary pressure continues to decline broadly in line with softening domestic demand, while costs of production, particularly oil price, remain low. Such development increased the risks of prolonged negative headline inflation. Though not considered to be a deflation at present, more broad-based deceleration of prices, together with a fall in inflation expectations amid weak demand, contributed to a slightly higher risk of deflation in the periods ahead than formerly assessed. **With regards to financial stability, the overall situation did not change significantly from the previous assessment.** The non-performing loan ratio increased somewhat, still at a level deemed manageable by commercial banks given their ongoing conservative provisioning.

The Committee discussed the possibility of the economy regaining momentum in the second quarter of 2015. Some members judged that economic growth was subject to significant downside risks, on the back of the following grounds: (1) the pickup in fiscal stimulus could be temporary, and the disbursement rate, while rising in the first quarter, remained lower than past averages; (2) the benefit of lower oil prices might not be sufficient to offset the impact of falling incomes, as manifested in the recent slowdown in manufacturing employment, and a drop in agricultural employment; and (3) exports of goods might not receive full benefits from the global recovery given the shifting relationship between the global economy and the Thai exports, coupled with the strength of the Thai baht. In addition, **the Committee further discussed the credit quality situation and its implications on the economy.** The Committee were of the view that the somewhat lower credit quality caused commercial banks to be more cautious in extending credit to a certain group of borrowers.

Monetary Policy Deliberation

Committee members were in agreement that the Thai economic growth in 2015 was likely to be weaker than previously assessed, and hence warranting the need to employ available monetary policy tools in order to maintain continued accommodative monetary conditions. This should help shore up public confidence, and support economic recovery in the periods ahead. **At the same time, the Committee also discussed the room to reduce the policy rate further (policy space),** as going

forward, there remained uncertainties in both the internal and external environment. Given the dilemma, the Committee extensively discussed the most effective utilization of the policy space.

Following the deliberation, **five members viewed a reduction of the policy rate by 25 basis points to 1.50 percent as appropriate**, with the following rationale:

- 1) **Considering downside risks facing the Thai economy, monetary policy should be eased further in order to preempt the expected economic slowdown.** Delaying an additional policy rate reduction, on the other hand, could hamper economic recovery.
- 2) **A more accommodative monetary policy** should help reduce funding costs of households and businesses, and also contribute to exchange rate adjustments toward a level more conducive to economic recovery. This should thus help lift the private sector confidence.
- 3) **A reduction of the policy rate would help anchor inflation expectations of the public at an appropriate level**, given that headline inflation is likely to remain below the lower bound of the target band for a longer period of time.

Two members deemed maintaining the policy interest rate at 1.75 percent as appropriate, with the following rationale:

- 1) **The policy space is limited, and hence should be preserved for more appropriate timing. Meanwhile, previous monetary policy actions have contributed to continuous easing of monetary conditions**, while the recent pickup in fiscal stimulus should help shore up the economy to a certain degree. Taking into account the fact that transmission of monetary policy takes time, the Committee should wait to assess the effects of the recent policy rate reduction on the real economy before taking any further action.
- 2) **In an environment of prolonged low interest rates, further policy rate reduction could create more financial imbalances**, by encouraging search-for-yield behaviour while discouraging household saving in the long run.

The Committee therefore voted 5 to 2 to reduce the policy rate by 25 basis points from 1.75 to 1.50 percent. The Committee will continue to monitor Thailand's economic and financial developments, and stand ready to utilize an appropriate mix of available policy tools in order to ensure that monetary conditions are sufficiently accommodative for a continued recovery.

Monetary Policy Group
13 May 2015