Edited Minutes of the Monetary Policy Committee Meeting

Bank of Thailand

4 November 2015

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Members Present

Veerathai Santiprabhob (Chairman), Mathee Supapongse (Vice Chairman), Paiboon Kittisrikangwan, Jamlong Atikul, Porametee Vimolsiri, Apichai Boontherawara, and Sethaput Suthiwart-Narueput.

The International Economy

The global economy recovered at a slower pace than previously assessed, as the impact of China's economic slowdown further materialized. The Chinese economy continued to decelerate on the back of softened manufacturing production and private investment. Nevertheless, the slowdown was expected to be gradual, as the economy continued to receive support from the service sector and the ongoing fiscal and monetary stimulus measures. However, weakening private investment led to a large decline in Chinese imports of goods, thereby adding downward pressure on global commodity prices. This had repercussions on **other Asian economies**, particularly those with strong trade linkage with China, heavy reliance on income from commodity exports, and a rapid build-up of corporate debt under the low global interest rate environment. Going forward, such factors are likely to weigh on the recovery of these economies. However, the overall financial stability of most Asian economies, including Thailand, remained sound. Meanwhile, **the Japanese and the euro-area economies** were further affected by the slowdown in China and emerging market economies. Coupled with lingering concerns over subdued inflation, the impacts might prompt additional monetary easing by the European Central Bank and the Bank of Japan in order to buttress the recovery of their respective economies. **The US economy** continued to expand with ongoing improvement in its economic fundamentals, adding to market expectations that the FOMC would raise the policy rate by the end of this year.

The Financial Markets

Over the intermeeting period, financial market conditions were largely influenced by shifting market expectations about the timing of the FOMC's rate hike. As it became apparent that the rate lift-off would not occur in the October meeting, volatility in the global financial markets subsided. As a result, there were signs of capital flows returning to Asian emerging economies, especially to the bond markets, causing a decline in Thai government bond yields from the last meeting, particularly in the maturities of 10-15 years. **The baht also strengthened rapidly against the US dollar during the first half of October.** The Nominal Effective Exchange Rate (NEER), however, appreciated to a lesser extent than did the bilateral exchange rate, as the baht's movement was in line with the regional currencies. Meanwhile, the government's announcement of additional stimulus measures helped shore up sentiment in domestic financial markets, prompting an increase in domestic stock prices.

The Committee were of the view that the global financial markets remained subject to risks from China's slowdown and the uncertain timing of the Fed's policy normalization. Looking forward, volatility might increase; therefore, the Committee would continue to closely monitor developments in the global financial markets as well as the associated risks to financial stability.

The Thai Economy

The Thai economy in the third quarter of 2015 gradually recovered at a pace close to the assessment at the previous meeting. The momentum of the tourism sector, as well as tourism-related service sector, softened due to a temporary fall in the number of tourists. Concurrently, exports continued to contract due to cyclical slowdown in Thailand's major trading partners, coupled with structural limitations which weighed on the country's competitiveness. Nevertheless, domestic demand slightly improved on the back of increased consumer spending on non-durable goods and business investment in certain sectors, especially telecommunications, alternative energy, and construction, which were supported by government policies. However, other sectors which rely on consumer loans, such as real estate and automotive, remained weighed down by high household debt and subdued consumer confidence. Nonetheless, it was expected that the fiscal stimulus measures, particularly through credit and tax measures for SMEs and real estate sector, and the acceleration of government spending in the fourth quarter will help support the economy, and partially compensate for the slowdown of external demand.

Inflationary pressure was stable from the previous meeting. Headline inflation continued to stay in negative territory due to a substantial fall in oil price from last year. Nevertheless, headline inflation is projected to rise gradually going forward, and to turn positive in the first quarter of next year. Meanwhile, deflationary risks remain contained as demand continues to expand and core inflation is still positive, with the prices of most non-energy items stable or trending upwards. In addition, public's medium-term inflation expectations stay close to the inflation target.

Looking ahead, a slowdown in the Chinese and other Asian economies, as well as a potentially severe drought, represent key downside risks to the economic recovery. In light of such risks, economic expansion and inflation momentum in 2016 may fall below the baseline projections, an issue warranting close monitoring going forward. Despite a gradual recovery of the global economy, led by G3, the recovery of exports will continue to be weighed down by shifting global trade structure and a decline in competitiveness of certain manufacturing sectors, such as apparels and garments. In this regard, the Committee saw the need for structural adjustment in both exports of goods and services, in order to enhance their competitiveness.

Monetary Policy Deliberation

In deliberating monetary policy, **the Committee voted unanimously to maintain the policy rate at 1.50 percent per annum** as all members agreed that the overall monetary conditions remained accommodative, while the exchange rate movements stayed conducive to the economic recovery, despite prevailing downside risks from global economic uncertainty, structural limitations, and volatility in the global financial markets.

Most members were of the view that further reduction in the policy rate during this period was likely to have a limited impact on the economic recovery, while potentially contributing to risks to financial stability. Meanwhile, fiscal stimulus measures should help support the economic recovery to a certain extent. Most members were also in agreement that the policy rate should be kept on hold to preserve the policy space for future use, while some members continued to see the need to monitor risks to economic and financial stability, which might arise from search for yield behavior under the prolonged low interest rate environment. Nonetheless, some members were concerned that exchange rate movements were, at times, volatile or became unconducive to the economic recovery. This issue warranted close monitoring going forward.

Looking ahead, **the Committee were in agreement that monetary policy stance should continue to be sufficiently and continually accommodative.** The Committee will closely monitor the issue of China's economic slowdown, global financial markets, and the impact of fiscal stimulus measures on the economic recovery. The Committee stands ready to utilize an appropriate mix of available policy tools in order to support the economic recovery, while ensuring financial stability.

Monetary Policy Group
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