

Edited Minutes of the Monetary Policy Committee Meeting

Bank of Thailand

10 June 2015

Publication Date: 24 June 2015

Members Present

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

The International Economy

The global economy recovered at a pace slower than previously assessed, with greater downside risks stemming from a more-than-expected slowdown in China despite additional expansionary monetary and fiscal measures from the Chinese authorities. The deceleration of growth in China weighed down economic expansion in **other Asian economies** (excluding Japan) as exports to China and intra-regional trade contracted, in line with softening domestic production. **The US economy** decelerated due to larger contraction in net exports and waning investment in the energy sector amid sluggish global oil prices. Nonetheless, sound economic fundamentals should continue to support the ongoing recovery in the periods ahead, prompting market expectation that the FOMC would begin to raise the policy rate this year. Meanwhile, **the euro area's economic recovery** continued with more visible signs of an upturn in private consumption whereas the ECB's Quantitative Easing (QE) measures helped support the economic recovery. However, the economies remain subject to the uncertainty surrounding Greece's debt servicing ability. **The Japanese economy** recovered at a measured pace, and going forward should receive an additional boost from an improvement in private consumption, in part as consumers' confidence was bolstered by results of the annual wage negotiation. Overall, the slower global economic recovery was viewed as one of the factors contributing to a more subdued recovery of Thai exports going forward.

The Financial Markets

The policy rate reduction at the meeting on 29 April 2015 helped ease overall monetary conditions further, as reflected by a corresponding fall in **money market rates and Thai government bond yields**. Nevertheless, medium- to long-term yields moved up since the previous meeting due mainly to sell-offs in the region's bond markets during the first half of May 2015. **The Thai baht** against the US dollar, and **the Nominal Effective Exchange Rate (NEER)** persistently depreciated as market participants' view on the baht turned bearish following the rate decision at the previous meeting, as well as the ensuing announcement of Bank of Thailand's measures on capital flows relaxation on 30 April 2015. Another contributing factor to the weakening of the Thai baht was the sell-offs of emerging markets securities in May which generated net outflows from the Thai bond market. Moreover, volatilities in the bond and foreign exchange markets heightened as a result of concerns over the timing of the FOMC's interest rate lift off, and the Greek debt servicing situation.

Commercial banks' deposit and lending rates were lowered following the policy rate reduction at the meeting on 29 April 2015, but the response in general tended to be slower and smaller than that following the 11 March 2015 meeting.

The Thai Economy

The Thai economy recovered at a pace close to the previous meeting's assessment. Economic momentum in the first four months of 2015 softened due to sluggish private consumption and continued contraction in exports, as a result of a slowdown in the Chinese and Asian economies and a shift in global trade structure. Nevertheless, an increased disbursement of public investment expenditure and a continued improvement in tourism helped shore up the economy. In addition, the consecutive policy rate reductions at the two previous meetings have helped, to some extent, increase liquidity and reduce financial costs of businesses. **In the periods ahead, the economic outlook was projected to improve gradually** as government spending, especially public investment expenditure, was expected to maintain its momentum while tourism activities should continue their positive trend. **However, the economic recovery remains fragile.** Households remain cautious in their spending, due mainly to sluggish income growth and continued strict credit standards. Moreover, exports are subject to downside risks from softer-than-assessed recovery of the global economy particularly the Chinese and Asian economies. Amid a fragile recovery in private consumption and a weak outlook of exports, private investment is potentially delayed further as a result. **On balance, the projection of economic growth was adjusted downward to 3.0 percent in 2015, but revised up slightly to 4.1 percent in 2016.**

Headline inflation continued to stay in a negative territory due mainly to energy costs and raw food prices. However, it was anticipated to pick up in the second half of the year as the base effect of high oil prices should begin to wane, coupled with expected rises in oil and raw food prices as supply of global crude oil and excess supply of domestic agricultural products were expected to fall. Core inflation was still positive but declined somewhat owing to subdued demand-side pressure. **On balance, the projections for the headline inflation and core inflation were slightly revised downward** to -0.5 and 1.0 percent in 2015 and 1.6 and 1.0 in 2016, respectively. **Nevertheless, in the Committee's assessment, the risk of deflation remains low,** as consumption continues to increase, while the prices of most goods and services still increases or stays unchanged, and inflation expectations are close to the inflation target.

The Committee acknowledged the improvement on the compilation of the quarterly Gross Domestic Product (GDP) by National Economic and Social Development Board (NESDB) and discussed its implication on monetary policy. The revisions included a change in compilation method of real GDP from the Fixed Weight Volume Measures with 1988 as a fixed base year to the Chain Volume Measures (CVM). In addition, economic activities included in the new data coverage were broadened and some were reclassified to enhance data comprehensiveness. Following the revisions, the Thai economy structure implied by the new series better reflected the current composition of the economy compared to that suggested by the original series. Nevertheless, the overall assessment of the potential economic growth, the output gap, and the business cycles under the revised data did not change significantly from the previous one. Overall, the Committee deemed the revisions of the GDP data as neutral to the conduct of monetary policy going forward.

Monetary Policy Deliberation

In deliberating monetary policy, **the Committee placed importance on the assessment of trade-offs between effectiveness of further policy rate reduction and a need to preserve the limited policy space for future use.** In this light, the Committee judged that the conduct of monetary policy had thus far eased monetary conditions, while the direction of exchange rate movement had become more conducive to the economic recovery. Nevertheless, commercial banks' responsiveness to an additional reduction in the policy rate was expected to be lesser and slower under the current context. At the same time, as there remain downside risks to growth from both external and domestic sources, the Committee considered the policy space that should be preserved to address those downside risks.

Following the discussion, the **Committee voted unanimously to maintain the policy rate at 1.50 percent.** Members were in agreement that, amid heightened downside risks to growth, the prevailing policy space should be preserved at this juncture, to be employed as warranted by situation and when further policy rate reduction would become more effective. In turn, the recent pickup in fiscal stimulus should help shore up the economy and thus allowed the Committee some time to assess the impact of previous policy actions on the real economy. Furthermore, some members were of the view that, under prolonged low interest rate environment, further policy accommodation could create more financial imbalances, by encouraging search-for-yield behavior while discouraging household saving in the long run.

Going forward, the Committee assessed the outlook of Thai economic recovery to remain fragile, and thus saw a need to maintain continued and sufficiently accommodative monetary conditions by employing appropriate policy tools. The Committee would closely monitor Thailand's economic and financial developments, and stand ready to utilize the available policy space appropriately in order to support the ongoing recovery and maintain long-term financial stability.

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