

Edited Minutes of the Monetary Policy Committee Meeting

Bank of Thailand

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Members Present

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

The International Economy

The global economy recovered at a slower pace than previously assessed, due mainly to a slowdown in the Chinese and Asian economies, and was subject to higher risks stemming from heightened volatility in China's financial markets and uncertainty regarding the timing of Fed's rate hike. The Chinese economy was projected to expand more slowly, particularly in industrial production that was highly linked with global supply chain and international trade. Nevertheless, the slowdown was expected to be gradual, as the economy continued to receive support from the service sector, fiscal stimulus and currency depreciation. **Exports of other Asian economies** were expected to be affected by softening demand from China and the weaker Yuan, although the depreciation of Asian currencies should partially offset these impacts, including from competition in third markets. Meanwhile, domestic demand of Asian economies weakened in line with dampening consumer confidence. By contrast, **G3 economies** showed signs of continued expansion. Although China's slowdown might delay the recovery, the effect was expected to be marginal, especially for **the US economy** which was supported by improvements in the labor market and consumer confidence. Nevertheless, subdued price outlook and increasingly volatile global financial markets reinforced market expectations that the Fed would not raise the policy rate in September.

The Financial Markets

Volatility in the Thai financial markets heightened in line with the global movements. Foreign investors reduced their holdings of Asian stocks and bonds amid growing concerns over China's slowdown. As a result, **the baht weakened against the US dollar**, which was generally in line with regional peers. The sell-off by foreign investors also contributed to a decline in **domestic stock market indices** and a rise in **Thai government bond yields**. Nevertheless, the Committee were of the view that heightened volatility in the global financial markets was likely to have limited impact on the Thai economy, as external stability remained sound and there was sufficient cushion against increased volatility. Indicators of external resiliency include persistent current account surplus, low external debt to GDP ratio, and adequate international reserves. However, the Committee will continue to monitor developments in the financial markets which could adversely affect investor confidence and cross-border capital flows.

The Thai Economy

From the second quarter to July 2015, the Thai economy gradually recovered, with softer-than-expected growth momentum as risks were skewed towards the downside. Growth projections for the year 2015 and 2016 were therefore revised down to 2.7 and 3.7 percent, respectively. Most members were concerned about the ongoing sluggish trend in the export of goods, which was further weighed down by Chinese and Asian economic slowdown. This not only affected export volumes, but also contributed to a decline in the prices of commodity and electronic products, of which China was the world's major consumer. Moreover, the recovery of the export sector would continue to be impeded by a shift in the global trade structure and loss of competitiveness of some products, though the depreciation of the baht should partly help increase liquidity of businesses. In addition, farm income was likely to decline further, particularly as rubber prices kept pace with the lower-than-expected crude oil price. At the same time, sluggish household income prospect was likely to hamper consumer confidence and consumption, with further repercussions on private investment. Nonetheless, the economy should receive some support from continued improvement in tourism, accelerated disbursement of public investment expenditure, and recent fiscal stimulus measures. In the periods ahead, the Committee were of the view that the economy might be affected by the negative factors by more than what was reflected in the baseline projection. Exports, in particular, could be hit more severely by China's slowdown, while private investment seemed to lack positive factors to drive its momentum going forward. These scenarios were incorporated into the downside risks to the projection.

Inflationary pressure declined due mainly to lower-than-expected crude oil prices. Consequently, headline inflation was projected to stay in negative territory for the rest of 2015, before turning positive in the first quarter of 2016, later than previously assessed. **Headline inflation projections for 2015 and 2016 were revised down to -0.9 and 1.2 percent, respectively.** In the Committee's assessment, however, **deflationary risks remained contained** as core inflation was still positive, with the prices of most non-energy items stable or trending upwards. In line with that, **the projection of core inflation in 2015 remained close to the previous assessment at 1.0 percent while that of 2016 was slightly below the previous assessment at 0.8 percent.** Furthermore, inflation expectations stayed close to the target, albeit with the short-term indicator declining slightly. Nevertheless, the Committee saw the need to monitor the development of global crude oil prices, as they might decline further from current baseline assumption due to higher-than-expected excess supply.

Risks to overall financial stability increased somewhat, as the slow economic recovery hampered wealth and debt-servicing ability of households and businesses, especially small businesses, although it was unlikely to have systemic implications. Risks in the real estate sector increased as excess supply rose while short-term speculative demand in the condominium market picked up slightly. Nevertheless, risks to financial stability remained contained as the majority of developers were large in size, with strong financial position and sound risk management practices. In addition, most buyers engaging in speculative activities did not rely on debt financing, but rather reallocated their savings to higher-yielding assets. However, the Committee deemed it necessary to continue monitoring the impacts of slow economic recovery

on private sector's debt-servicing ability and excess supply in the real estate sector, which could potentially contribute to financial system fragility in the period ahead.

Monetary Policy Deliberation

In deliberating monetary policy, the Committee were of the view that the Thai economy remained subject to negative factors, particularly on the external front. The momentum of domestic recovery was therefore weakened, while risks remained skewed to the downside. Meanwhile, global financial markets became more volatile as a result of developments in China's financial markets and uncertainty regarding the timing of Fed's rate hike. In this light, the Committee placed emphasis on considering the different global financial market scenarios and possible consequences on domestic economy.

The Committee agreed that monetary policy at this juncture should give due weight to maintaining financial stability, and therefore voted unanimously to keep the policy rate unchanged at 1.50 percent per annum. Most members were of the view that overall monetary conditions, including the exchange rate, continued to remain conducive to the ongoing economic recovery and therefore supported the decision to keep rate on hold at this meeting. Moreover, further reduction in the policy rate during this period was likely to have a marginal impact on the economic recovery, while contributing to financial stability risks. **Going forward, the Committee were in agreement that the Thai economy would continue to face downside risks and therefore warranted the need for adequate and ongoing support from monetary policy.** In this regard, the Committee would closely monitor Thailand's economic and financial developments and stand ready to utilize an appropriate mix of available policy tools in order to support the economic recovery, while maintaining economic and financial stability.

Monetary Policy Group
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