Edited Minutes of the Monetary Policy Committee Meeting
Bank of Thailand
23 March 2016
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Members Present

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

The Global Economy

The global economy recovered at a slower pace compared with the assessment at the previous meeting due to weaker Asian economies whose adverse spillover impacts on the G3 economies became more apparent. As a result, market participants anticipated the US Federal Reserve to raise the policy rate more slowly despite the continuing improvement in the fundamentals of the **US economy**. Meanwhile, further monetary policy accommodation by the European Central Bank and the Bank of Japan was expected to provide some additional support to the recovery of the **euro area and Japanese economies**. However, growth in **other Asian economies** continued to slow because of both cyclical and structural factors, with some economies experiencing specific factors that further weighed on domestic demand. Taken together, the pace of global growth in 2016 was expected to remain largely unchanged from last year, in contrast with the assessment at the previous meeting where global growth was expected to pick up. In addition, the Committee judged that the relationship between global output and global trade had changed significantly such that the growth of trade volume was much lower than previous trend growth. This proved to be a major drag on exports of Asian economies including Thailand. **With regard to the balance of risks to global growth, the Committee judged it tilted more to the downside owing mainly to fragility of the European financial sector**. The risks surrounding China's financial sector and its economic slowdown remained and might also affect the recovery of Asian economies going forward.

The Financial Markets

Overall confidence in the financial markets improved given the likelihood of a slower pace of policy rate increases by the US Federal Reserve and recent gains in crude oil prices. Consequently, investors increased holdings of emerging market financial assets, including those of Thailand, prompting a rise in the **Thai equity market indices** and an appreciation of **the baht against the US dollar**. As the baht appreciation was in line with movements in other regional currencies, the **Nominal Effective Exchange Rate (NEER)** remained broadly unchanged from the previous meeting. With regard to the bond market, the **Thai government bond yields** continued to fall primarily because of a strong demand from local investors. There was no indication as yet of significant capital flows from Japan to Thailand after the Bank of Japan implemented the negative interest rate policy.

The Committee anticipated that monetary policy divergence among advanced economies would continue to be a source of volatilities in financial markets and cross-border capital flows. Nevertheless, Thai financial assets proved attractive to foreign investors thanks to strong external fundamentals, together with the baht having displayed low volatility relative to regional currencies. These factors could potentially result in steady foreign capital inflows to the Thai financial markets.

Domestic Economic Conditions

The Thai economy continued to recover gradually supported by fiscal spending, tourism, especially in major cities which saw a broad-based increase in foreign visitors, and a pickup in private investment in some business sectors, in particular those benefiting from government policies such as alternative energy and telecommunications. However, the overall economic momentum slowed down, following dissipation of the temporary boost from the government's tax rebate measure around the end of last year and from the accelerated car purchases prior to the increase in vehicle excise tax this year. In addition, the value of merchandise exports still contracted significantly and looked to rebound slowly, leading to lower employment in some industries. Nevertheless, some workers were able to move into service industries which continued to expand strongly, helping to mitigate some of the negative impacts on non-farm household incomes. As a result, private consumption continued to grow, in particular, consumption of nondurable goods.

According to the Committee's assessment, the degree to which the structural problems weighed on the export sector was greater than previously anticipated. Structural constraints limiting export opportunities included shifts in the global trade structure, changes in consumer preferences, and a decline in Thailand's export competitiveness in certain industries, especially those that had failed to make meaningful investments during the past several years to upgrade their manufacturing technology. Consequently, the recovery of exports was expected to be gradual and would likely weigh on household income and spending as well as business investment. **The Committee therefore revised the 2016 growth projection to 3.1 percent, down from 3.5 percent** estimated in December 2015. Looking ahead, the Committee deemed **risks to the recovery of the Thai economy skewed to the downside** due to the fragile outlook of the global economy and the impact of the drought that could be more severe than expected.

Headline inflation remained negative largely due to global oil prices, which had declined by more than expected toward the end of last year. Meanwhile, core inflation, excluding the impact of excise tax hikes on tobacco products and automobiles, edged lower, reflecting weakening price pressure from the demand side. **The Committee thus revised down the headline inflation forecast for 2016 from 0.8 percent to 0.6 percent, and lowered this year's core inflation forecast slightly from 0.9 percent to 0.8 percent**. Volatile global crude oil prices continued to pose uncertainty to the headline inflation projection. Meanwhile, medium-term inflation expectations remained close to the inflation target, albeit edging down slightly. Going forward, the Committee would monitor the recovery of domestic demand and developments in inflation expectations closely.

Overall risks to financial stability rose somewhat on the back of investors' search-for-yield behavior and weakened debt service ability of farm households and SMEs due to a delayed economic recovery. Some members of the Committee noted that the financing costs of large corporations were at low levels, which could reflect some underpricing of risks. The Committee would monitor and assess these developments closely.

The Policy Decision

The Committee voted unanimously to maintain the policy rate at 1.50 percent at this meeting. Although the economy was expected to grow more slowly compared to the previous assessment and the recovery was likely to be uneven across sectors, the prevailing monetary conditions were deemed accommodative and conducive to fostering overall economic recovery. The Committee was mindful of financial stability risks that could arise in the prolonged low interest rate environment, especially the search-for-yield behavior, weakened debt service ability, and elevated household debt. Consequently, the Committee decided to keep the policy interest rate unchanged at this meeting. The Committee also saw the need to preserve the policy space should significant risks and uncertainty, such as from a further delay in the global recovery or intensifying geopolitical conflicts, negatively affect economic recovery going forward. Some members also judged that monetary policy easing would have provided limited support to the economy and inflation, as the current slowdown of the Thai economy was in part attributable to global and domestic structural problems. Nonetheless, all members concurred that the strengthening of the baht with respect to other currencies during some recent periods might not be as conducive to the economic recovery as it could be.

Looking ahead, the Committee concurred that monetary policy should continue to remain sufficiently accommodative. The Committee would stand ready to utilize an appropriate mix of available policy tools in order to support the economic recovery and ensure financial stability.

Monetary Policy Group
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