Edited Minutes of the Monetary Policy Committee Meeting

Bank of Thailand

3 February 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 expanded at a slower pace compared with the assessment in the previous meeting due mainly to weaker Asian economies, in particular **China**. A slowdown in China's industrial production resulted in a decline in merchandise export growth of **other Asian economies** (excluding Japan) through strong manufacturing and trade linkages. In addition, some Asian economies faced negative domestic headwinds that led to weaker domestic demand. In contrast, the **G3 economies** continued to recover, supported by domestic consumption, improving labor market conditions, and accommodative monetary conditions. The Bank of Japan recently reduced the interest rate paid on commercial bank excess reserves to -0.1 percent given the low inflation in **Japan** together with concerns about repercussions from weakening Chinese and other emerging market economies. Meanwhile, the European Central Bank signaled that it might undertake additional monetary easing in order to lend support to the **euro area** recovery, and the Federal Reserve was expected to slow down the pace of monetary policy normalization on the back of a weaker economic and inflation outlook in the **US**.

The Committee judged the balance of risks to the global economy tilted more to the downside given the risks surrounding China's economy and financial markets, monetary policy divergence among advanced economies, subdued global commodity prices, and geopolitical risks. With regard to China, financial market and business sentiment would depend critically on policy certainty and clear communication by the authorities. Meanwhile, risks to financial stability in China that might arise from corporate defaults warranted close monitoring. The Committee would also pay close attention to the geopolitical risks that intensified since the previous meeting and could potentially affect the global economic recovery through trade, tourism, and investment channels.

The Financial Markets

Global financial markets experienced heightened volatility since the beginning of 2016 on the back of fluctuations in China's financial markets, declining oil prices, and monetary policy divergence among advanced economies. These factors caused volatile movements in capital flows and exchange rates, especially after the announcement of a negative interest rate policy by the Bank of Japan, together with an increasing prospect that the European Central Bank would undertake additional monetary easing. As a result, investors raised their holdings of emerging market assets, including Thailand, which contributed to increases in **Thai equity indices** and significant declines in **government bond yields**. Lower bond yields were also partly due to expectations of subdued inflation in Thailand following a further decline in oil prices. Meanwhile, the **baht** appreciated against the US dollar similar to other currencies in the region. However, the extent to which the baht appreciated outpaced most regional currencies, causing **the Nominal Effective Exchange Rate (NEER)** to appreciate, which according to some Committee members might not be as conducive to Thailand's economic recovery as it had been in the past.

Domestic Economic Conditions

The Thai economy in the final quarter of 2015 grew at a pace largely in line with the assessment at the previous meeting. The recovery was supported by high disbursement of government funds, increasing number of tourists especially from China, and improving private consumption, the last of which was due partly to a temporary boost from the government's year-end tax deduction measures and accelerated purchases of automobiles prior to the increase in vehicle excise tax rates to take effect in 2016. However, overall private investment remained subdued, while the total merchandise export values markedly contracted. Exports would likely continue to be held down by both a weak cyclical recovery in major trading partners' demand and domestic structural constraints weighing on the country's export competitiveness. Going forward, Thai exports, therefore, might receive rather limited benefits from a recovery in the global economy.

The Committee judged that the Thai economy would likely grow in 2016 at a rate close to the projection at the previous meeting. The growth momentum would be largely driven by domestic demand — in particular, sustained public spending, private investment in some industries such as telecommunication, and household spending supported by falling oil prices despite lower farm incomes following declining commodity prices. Nevertheless, **downside risks to growth were judged to increase, largely attributable to external factors** including the prospect of economic recovery in major trading partners, changes in the global trade structure, subdued commodity prices, and monetary policy divergence in advanced economies. The Committee assessed that these increasing risks to global growth could weigh on Thai exports, and that warranted close monitoring.

Inflationary pressures continued to subside since the previous meeting following a faster- and larger-than-expected decline in global oil prices, causing risks to inflation to skew further to the downside. Nevertheless, headline inflation rate, currently below zero, was projected to rise gradually and turn positive during the first half of 2016, although the inflation outlook would largely depend on the trajectory of oil prices. In any case, **deflation risks remained limited** as attested by a pickup in demand and positive core inflation, which reflected stable or rising prices of most non-energy goods, consistent with the public's medium-term inflation expectations that stayed close to the inflation target.

The Policy Decision

The Committee voted unanimously to maintain the policy rate at 1.50 percent at this meeting. Under the Committee's assessment, the prevailing monetary policy stance remained accommodative and conducive to economic recovery, while the economic and inflation outlook did not change significantly from the previous meeting. The Committee was mindful of the risks to financial stability stemming particularly from the search for yield behavior in the prolonged low interest rate environment. The Committee also saw the need to preserve policy space should significant risks and uncertainty, especially from the external front, negatively affect economic recovery going forward. In addition, some members viewed that further monetary policy easing could only marginally improve the economic and inflation outlook given that the current policy stance was already accommodative.

Looking ahead, the Committee concurred that **monetary policy should continue to remain sufficiently accommodative** in order to facilitate economic recovery. The Committee would closely monitor global economic and financial market developments, together with domestic monetary conditions and exchange rate movements, and 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
17 February 2016