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Members Present

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The Global Economy

Trading partner economies would exhibit more stabilizing growth in 2020 due to improving global trade volume and declining business inventory from previous high levels, resulting in improving prospects of the manufacturing sector and employment. Trading partner economies would also be supported by a recovery of the electronic cycle in the first half of next year and by improving business confidence after the US and China reached an unofficial agreement on the phase one trade deal. **Advanced economies** would expand at a moderating pace this year but would be stabilizing in 2020 due to improvements in the manufacturing sector and services employment, favorable private consumption, as well as more fiscal stimulus. **China** would moderate in line with the government's target thanks to the prudent stimulus measures, including tax cuts and accommodative monetary policy. These measures would foster quality growth despite headwinds from uncertainties pertaining to trade protectionist measures. **Asian economies** (excluding Japan and China) would gain traction from merchandise exports in line with improvements in global trade volume, the electronic cycle, and trade negotiations between the US and China. In the period ahead, economic growth would be driven by favorable private consumption and employment as well as more government stimulus. **Monetary policies of trading partners** were accommodative, particularly after the Federal Reserve (Fed) and the European Central Bank (ECB) continuously cut policy rates and injected liquidity into the financial system in the second half of 2019. Meanwhile, the Bank of Japan (BOJ) would ease monetary policy further if economic growth weakened significantly. Most of the other regional central banks kept policy rates unchanged since the previous meeting.

The Committee assessed that there was a probability of trading partner's economic growth being lower than the baseline projection due to higher medium- to long-term risks as a result of risks to global financial stability. Lower-for-longer policy rates would encourage greater leverage by businesses, non-banks, and public sectors in many countries. Moreover, investors would search for higher yields across almost all asset classes, which could lead to underpricing of risks. In addition, **some other risks still warranted close monitoring**, including (1) trade tensions that could be more intensified and prolonged than previously assessed, especially trade negotiations between the US and China, as well as the likelihood that the US would increase tariffs on all auto imports in the future, (2) uncertainties regarding the timeline and outcome of Brexit, and (3) geopolitical risks that could become widespread and intensified, particularly recurring protests in several countries which exhibited common patterns. The Committee thus saw a need to monitor developments in the trading partner economies, together with the risks mentioned above, and closely evaluate their impacts on the Thai economy that could occur through various linkages.

The Financial Markets

Sentiments in the global financial markets improved in the short term due to the prospects of an agreement between the US and China over the phase one trade deal, greater clarity on Brexit, as well as stabilizing economic data in advanced economies. Consequently, asset prices in the global financial markets became less volatile. Moreover, the continuation of accommodative monetary policy by advanced economy central banks was an additional positive factor contributing to risk-on sentiment and rising prices of most risky assets. Regarding domestic financial markets, the policy rate cut in the previous meeting contributed to a decline in short-term Thai government bond yields. Meanwhile, long-term government bond yields increased in line with the US counterpart. Nonetheless, an increase was limited owing to higher demand for long-term Thai government bonds from both domestic and foreign investors, after an increase in the weights of Thai bonds in a benchmark index for global government bond investment.

On exchange rates, **the Thai baht remained broadly unchanged from the previous meeting, exhibiting two-way movements and becoming more in line with regional currencies.** The baht initially depreciated after the policy interest rate cut and the announcement of the relaxation of foreign exchange regulations. Moreover, latest weaker-than-expected economic outturns caused movements in the baht to diverge from those of other safe-haven assets such as the yen and gold prices. Nevertheless, the continuation of the Fed's accommodative monetary policy and better global financial market sentiment resulted in US dollar depreciation. In addition, a credit rating agency upgraded Thailand's credit rating outlook to positive. There was thus subsequently some appreciation pressure on the Thai baht.

The Committee viewed that financial markets would remain highly uncertain going forward due to both external and domestic factors. Such factors included, for example, uncertainties regarding trade negotiations between the US and China that could be prolonged, geopolitical risks, the potential slowdown of global and Thai economies, as well as the monetary policy outlook of advanced economies. These factors could affect cross-border capital flows and cause volatility in Thai asset prices and exchange rates. Furthermore, the Committee remained concerned about baht appreciation against trading partner currencies. The Committee thus saw the need to continue to closely monitor developments of exchange rates and capital flows amid heightened external uncertainties. The Committee would also monitor the effectiveness of the relaxation of foreign exchange regulations to encourage capital outflows and consider implementing additional measures if necessary.

Domestic Economic Conditions

The Thai economy would expand at a lower rate than the previous projection and further below its potential. Merchandise exports would contract more than the previous forecast and recover slowly. This would be due to (1) the global trade volume decelerating more than expected from trade tensions and (2) structural changes in the manufacturing sector affecting export competitiveness. **Exports of services** would continue to expand on the back of increasing tourist figures in almost all nationalities. **Private consumption** in the final quarter of this year would expand at a faster pace than the previous forecast, supported mainly by government stimulus measures. However, private consumption growth would be slower-than-expected next year due to such measures phasing out, falling household income and employment, particularly in export-related manufacturing sectors, as well as drought and elevated household debt. **Private investment** would expand at a lower rate than previously forecasted partly from delays in some public-private partnership infrastructure investment projects. Nevertheless, private investment would be supported by the gradual recovery in exports and the progress of other infrastructure investment projects. **Public expenditure** would grow at a lower rate than the previous forecast partly due to delays in some state-owned enterprise investment projects and a reduction in state-owned enterprise investment budgets for fiscal year 2020.

The Committee projected economic growth to be 2.5 percent in 2019 and 2.8 percent in 2020, a downward revision from the previous *Monetary Policy Report* at 2.8 and 3.3 percent respectively. However, **the economy was expected to accelerate in 2021** due to the postponement of some public-private partnership projects and public investment projects to 2021. **Risks to the economic projection remained tilted to the downside** due to the following factors. First, global trade volume and trading partner economies could slow down more than assessed from re-intensifying trade tensions. Second, domestic demand could soften more than expected from delays in the enactment of the Annual Budget Expenditure Act, B.E. 2563 (A.D. 2020) and government policy implementation. Moreover, private consumption could be subdued more than expected in tandem with moderating household income given various factors, including the impact of the slowdown in exports on employment and intensifying natural disasters. Third, global financial stability risks could affect the Thai economy in the medium term. Nevertheless, **there were possibilities that the Thai economy would expand at a higher rate than the baseline projection** owing to (1) higher-than-expected trading partners' economic growth in the case of additional stimulus policies, alleviating trade tensions, as well as a faster recovery in the electronic cycle, and (2) higher-than-expected domestic demand given public infrastructure investment and public-private partnership investment projects, together with potentially additional government stimulus measures.

The Committee engaged in extensive discussions regarding economic growth in the period ahead. The Committee assessed that, despite better prospects of global trade volume, Thai exports would not fully gain benefits due to some structural factors. For example, (1) global trade volume improvements occurred in countries with small contributions to Thai exports and (2) structural changes in the manufacturing sector would affect Thai export competitiveness. The Committee furthermore discussed deterioration in employment across sectors. The Committee would in particular monitor structural changes in the labor market which would affect employment and private consumption in the period ahead. Such changes included automation, changes of the employment pattern from full-time to temporary contracts, as well as challenges in upskilling and reskilling the labor force.

The annual averages of headline inflation in 2019 and 2020 were projected to be lower than the previous forecast and below the lower bound of the inflation target. This would be due to lower-than-expected energy prices in line with a subdued global economy and increased energy supply, as well as the lower-than-expected minimum wage increase in 2020. **Core inflation** was expected to increase in line with better economic prospects next year, resulting in headline inflation rising toward the target in the second half of 2021. **Risks to the headline and core inflation projections remained tilted to the downside** in line with risks to the economic projection.

<u>**Monetary Policy Decision**</u>

The Committee assessed that the Thai economy would expand at a lower rate than the previous forecast and below its potential due to the contraction in merchandise exports which affected employment and domestic demand. Headline inflation would be below the lower bound of the inflation target. Overall financial conditions remained accommodative as a result of the previous two policy rate cuts. Real interest rates and government bond yields remained at low levels. Liquidity in the financial system remained ample. Meanwhile, exchange rate appreciation against trading partner currencies abated. The recent movements of the Thai baht were two-way and more in line with regional currencies. Financial stability had already been addressed to some extent but there remained pockets of risks that warranted monitoring. The Committee viewed that more accommodative monetary policy stance in the recent period would contribute to the continuation of economic growth and should support the rise of headline inflation toward target. **The Committee therefore voted unanimously to maintain the policy rate at 1.25 percent at this meeting and would assess risks in the period ahead in order to deliberate appropriate monetary policy. The Committee discussed key considerations underpinning the policy decision. Their conclusions were as follows.**

1) The Thai economy was expected to expand at a lower rate than previously projected and below its potential due to larger-than-expected contraction in merchandise exports and its slower-than-expected recovery which affected employment and domestic demand. Nonetheless, the global economic outlook would start to stabilize and contribute to gradual improvement of the Thai exports and economic growth next year. Public expenditure and private investment would expand at a lower rate than previously assessed due to delays in some investment projects. Private consumption would grow at a slower rate owing to declining household income and employment in various sectors, especially in the export-related manufacturing sectors. **The Committee viewed that the Thai economy would encounter uncertainties from both external and domestic factors** including (1) uncertain trade tensions and geopolitical risks that could dampen the economic outlook of trading partners, especially China and Asia, (2) uncertainties pertaining to public expenditure and the progress of important public-private partnership infrastructure investment projects and the knock-on effects on private investment, (3) more-than-expected slowdown in private consumption as a result of declining employment and income, and (4) risks from drought next year which could affect agricultural production and income.

The Committee remained concerned about baht appreciation against trading partner currencies despite its slower pace and two-way movements over the recent period. The exports and overall economy remained affected, particularly production and employment in export-related manufacturing sectors. Businesses profitability and liquidity were also impinged. Moreover, debt servicing capability worsened in those industries exacerbated by exports. The Committee thus saw the need to (1) closely monitor developments of exchange rates and capital flows, (2) monitor the effectiveness of the relaxation of foreign exchange regulations to encourage capital outflows, and (3) consider implementing additional measures if necessary.

2) Headline inflation would be below the lower bound of the inflation target in 2019 and 2020 due to lower-than-expected energy prices in tandem with subdued global economic growth and increasing energy supply. Core inflation would increase in line with the improving economic outlook. In the period ahead, the Committee viewed that inflation would face uncertainties from oil price fluctuations and weather conditions. Moreover, structural changes such as impacts from the expansion of e-commerce, heightened price competition, and productivity upgrades which reduced production costs could cause inflation to rise at a slower pace than in the past. Nevertheless, the Committee assessed that more accommodative monetary policy in the recent period would support the rise of the headline inflation toward target within the second half of 2021.

3) Some financial system risks had been partly addressed by the implemented macroprudential measures. For instance, property sector risks abated after the implementation of the revised loan-to-value (LTV) measure. This was reflected by moderation in speculation and adjustments of developers. **However, other financial stability risks had yet to improve and thus warranted continued monitoring.** First, debt servicing capability of households and SMEs could worsen amid economic slowdown, particularly in the case of further negative income shocks, while elevated household debt could build up vulnerabilities in the household sector. Second, search-for-yield behavior in the prolonged low interest rate environment could lead to underpricing of risks, especially by large corporates and saving cooperatives. Third, the property sector remained oversupplied in some areas.

Given the outlook of economic growth below its potential with some remaining risks to financial stability, the Committee viewed that the policy interest rate, along with microprudential and macroprudential measures, should be appropriately combined to address financial stability risks. Moreover, the Committee supported the Bank of Thailand to cooperate with related organizations in order to push forward structural measures to address household and SME debt problems. Such measures included putting into practice guidelines for responsible lending, debt restructuring and the debt clinic, and building financial discipline as well as promoting household savings. The Committee also saw a need to continue monitoring impacts of the implemented measures, especially those on the overall economy, and study additional appropriate measures to curb potentially increased risks in the future.

The Committee engaged in a discussion regarding monetary policy transmission after the policy rate cut. The Committee viewed that benchmark lending rates and time deposit rates along with overall short-term government bond yields declined in line with the policy rate cut. Nevertheless, the Committee would be data-dependent by closely monitoring the economic growth, inflation, and financial stability together with other associated risks in deliberating monetary policy going forward. The Committee would stand ready to use policy tools as appropriate. Furthermore, **the Committee saw the need for policy coordination between related public and private organizations to support an economic recovery and to restructure the economy**, given that the Thai economy would face with structural problems affecting competitiveness and the economic growth outlook going forward that should be firmly addressed by all related parties.

Monetary Policy Group
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