Edited Minutes of the Monetary Policy Committee Meeting (No.4/2021)
23 June 2021, Bank of Thailand
Publication Date: 7 July 2021

Members Present

Sethaput Suthiwartnarueput (Chairman), Mathee Supapongse (Vice Chairman), Paiboon Kittisrikangwan, Kanit Sangsubhan, Rapee Sucharitakul, Somchai Jitsuchon, and Subhak Siwaraksa

The Global Economy and Financial Markets

The global economy continued to recover thanks particularly to the progress of COVID-19 vaccination in major advanced economies and better-than-expected exports in Asian economies. There were also continued support from monetary and fiscal policies. Looking ahead, the global economy would continue to gain strength in tandem with the vaccination progress and large-scale US economic stimulus. Nevertheless, the recovery would remain uncertain owing to virus mutations and vaccine efficacy.

The global financial market sentiment had been more risk-on. However, volatilities increased after the Federal Open Market Committee (FOMC) meeting in June 2021 where investors priced in faster-than-expected US monetary policy tightening. Before the FOMC meeting, prices of risky assets, namely equities and commodities, rose in line with major advanced economies thanks to the vaccination progress. Thai equity prices also rose due to the progress of domestic vaccine procurement and distribution. Nevertheless, global equity and gold prices decreased somewhat after the FOMC meeting. Investors assessed that the Federal Reserve may need to tighten monetary policy earlier than expected to keep rising inflation in line with the long-term target. Despite the fall in long-term US Treasury yields, the Thai counterparts stabilized due to the potentially rising supply of domestic government bonds following the Emergency Decree Authorizing the Ministry of Finance to Raise Additional Loans to Solve Economic and Social Problems as Affected by the Coronavirus Disease Pandemic, B.E. 2564 (2021). In addition, investors remained cautious about emerging market assets, including Thailand, owing to outbreaks in several countries and the US monetary policy outlook. On exchange rates, the baht depreciated against the US dollar more than regional currencies. The nominal effective exchange rate (NEER) depreciated from the previous meeting.

Looking ahead, volatility in the global financial markets would remain high owing to the US monetary policy outlook. Investor decisions would be primarily based on the US economic recovery, communications by the Federal Reserve, uneven economic recovery across countries, and emerging markets' vaccination progress**. Meanwhile, the new wave of domestic outbreak would be the main contributor of volatilities in the Thai financial markets in the period ahead**. However, the impacts of the US monetary policy outlook on domestic long-term government bond and equity prices would be limited. This was due to low foreign participation in the long-term Thai government bond market compared with other regional countries, as well as the continuous underweighting of foreign investment in Thai equities over recent periods.

<u>**Domestic Economy**</u>

The Thai economy would expand by 1.8 and 3.9 percent in 2021 and 2022 respectively, down from the March projection. This was due to the more prolonged and severe third-wave outbreak that significantly affected foreign tourist figures and domestic demand. Businesses and the labor markets would be more fragile and recover slowly. Nevertheless, the following factors would provide additional economic support. First, public expenditure would be higher thanks to the new Emergency Decree authorizing 500 billion baht borrowing which would serve as the main support of household purchasing power and private consumption affected by the third-wave outbreak. Second, positive vaccine developments from the previous quarter, both increasing procurement and distribution, would contribute to a pickup in economic activities. Third, merchandise exports were expected to post solid gain in line with the global economic recovery, partly shoring up manufacturing production and employment. Despite that, there would be some supply constraints such as factory outbreaks and global shortages in containers and electronic parts, though these would alleviate by the first half of 2022. **Headline inflation would temporarily increase in the second quarter of 2021** due to the low level of crude oil prices in the same quarter last year. Core inflation would be subdued owing to weak domestic demand. Medium-term inflation expectations remained anchored within the target range.

Looking ahead, the Thai economy faced significant downside risks and uncertainties from various factors that needed to be closely monitored. First, prolonged outbreak and virus mutations from existing and new variants would reduce vaccine efficacy. This could lead to a public health crisis, affect domestic spending, and delay the reopening plan to admit foreign tourists. Second, government spending on economic relief and restoration could be lower than expected if projects under the Emergency Decree faced approval delays or low disbursement rates. Third, the new outbreak could exacerbate financial positions of businesses, especially the services sector, leading to widespread business closures and lay-offs. Dismissed workers could be unemployed for extended periods and eventually give up finding jobs. Further deterioration in business and household balance sheets would thus impinge on economic activities and cause a rise in debt defaults. Fourth, the supply disruption and increase in shipping costs would have greater impacts on Thailand’s manufacturing and export sectors than expected.

<u>**Discussions by the Committee**</u>

The Committee assessed the economic outlook and noted the possibility of the new outbreak and virus mutations which would prolong and intensify the pandemic both in Thailand and abroad. Despite improving vaccine procurement at the present juncture, emphasis should also be placed on the efficacy of vaccines against virulent mutants together with their adequate and timely distribution. At the same time, measures to minimize adverse economic impacts in the short term and in the post-pandemic period should be expedited. The details were as followed.

- **The Committee assessed that the Thai economy faced significant downside risks. A prolonged outbreak could cause the economy to underperform the baseline. This would squeeze business liquidity and slow down employment in the services sector.**

Furthermore, uneven economic recovery across different sectors would intensify. In the **baseline scenario**, positive developments in vaccine distribution would help contain the outbreak by the beginning of the fourth quarter of 2021. This would enable herd immunity attainment within the first half of 2022 and the Thai economy would return to the pre-COVID level by the end of the same year. However, in the scenario that **the outbreak became more prolonged than the baseline**, a new outbreak could emerge due to a more easily transmissible and deadly mutant. In this case, herd immunity would be delayed to the end of 2022 and the Thai economy would return to the pre-COVID level at the beginning of 2023. **Thus, the Committee viewed that the procurement and distribution of appropriate vaccines against new virus mutations adequately and timely was the most important issue facing the Thai economy. This would prevent a prolonged and severe outbreak.** Meanwhile, fiscal stimulus measures should be expedited. Monetary policy must remain accommodative. Adequate and targeted financial measures to assist businesses and households affected by the pandemic should be pushed forward, especially the special loan facility, asset warehousing, and debt restructuring. **All parties should accelerate various measures to produce results and support the economy through this period, especially during the next six months where uncertainties would remain high.**

- **The Committee viewed that the recurring outbreaks increased labor market fragility. Recovery in labor markets would be W-shaped and slower than the past.** Despite some improvements in the overall employment after the relaxation of containment measures against the first-wave outbreak, recurring waves of infections would increase fragility in the labor markets, particularly the services sector and among the self-employed. Recent indicators reflected that that some employers adopted a rotation system among workers and cut their working hours. The number of workers who returned to their hometowns recorded a historic high. Most dismissed workers in the services sector could not reallocate to the manufacturing sector with improving prospects due to their skill mismatch. Moreover, the number of the long-term and newly-graduated unemployed as well as persons outside the labor force continued to rise. **The Committee assessed that the government should address vulnerabilities in the labor markets in an adequate and continuous manner to reduce long-term scarring effects after the COVID-19 outbreak subsided.**
- **The Committee assessed that the temporary increase in headline inflation in the second quarter of 2021 was not a point of concern.** The increase was due to the low level of crude oil prices in the same period last year and transitory supply constraints. Meanwhile, reflation in the advanced economies would have limited spillovers to domestic inflation as imported consumer products accounted for only 16 percent of the Thai CPI basket. Additionally, producers decided to bear the rising costs of production due to difficulties of price pass-through during an economic slowdown. In the period ahead, headline inflation would edge down toward the lower bound of the target range due to the following factors. First, global crude oil prices would rise at a slower pace as oil producers were capable of expanding production capacity to meet global demand. Second, raw food prices would decrease as the risks of drought

subsided. Third, demand-pull inflationary pressures remained low due to a high level of household debt and fragile labor markets.

- **The Committee reiterated the need for structural reform policies to raise long-term potential growth of the Thai economy.** This would alleviate the impacts of the COVID-19 outbreak and the changing economic structure in the post-COVID environment due to the following factors. First, the recovery among different sectors would be highly uneven, especially the severely affected tourism sector. Second, income inequality would intensify for the unemployed and the self-employed with income reduction. Third, financial positions of businesses and households would become more fragile. Consequently, without appropriate measures, long-term potential growth of the Thai economy would decline. **The Committee viewed that all related parties should jointly support structural transformation of the Thai economy by identifying key objectives and establish policy guidelines for both the short and long term as well as push forward their implementation.** In particular, business model adjustments as well as the upskilling and reskilling of labor to suit the post-COVID environment should be facilitated. These would support a sustainable economic recovery and bolster the resilience of the Thai economy against future negative economic shocks.

Monetary Policy Decision

The Committee voted unanimously to maintain the policy rate at 0.50 percent to support the economic recovery which remained highly uncertain.

The Committee assessed that the Thai economic recovery would be slower and more uneven than the previous forecast due to the third-wave outbreak. Downside risks to the economic outlook remained significant given the new wave. As a result, the balance sheets of some businesses and households became more fragile. Additional measures should thus be more targeted and in line with the need of borrowers, helping to distribute liquidity to the affected businesses and households broadly. These measures included financial and credit measures, credit guarantees, and expedited debt restructuring. Such measures would alleviate the financial burden of businesses and households in a more targeted manner than a reduction in the policy rate. The policy rate was already at a low level and cutting it might provide limited support to the economic recovery. **The Committee thus voted to maintain the policy rate at this meeting and would stand ready to use the limited policy space at the most effective timing.**

The Committee would continue to monitor developments in foreign exchange markets and capital flows to ensure that exchange rate movements would not hinder the economic recovery going forward. Although pressures on the baht would abate in tandem with the projected current account deficit in 2021, the Committee would continuously expedite the new foreign exchange ecosystem to improve the structure of the Thai foreign exchange markets over the medium term. The Committee viewed that by encouraging Thai institutional investors to increase their portfolio investments abroad, it would facilitate capital outflows and improve the balance between capital inflows and outflows.

The Committee viewed that the continuity of government measures and policy coordination among agencies would be critical in restoring the economy from the new

outbreak. Short-term measures to accelerate the procurement and distribution of appropriate vaccines would prevent the outbreak from being prolonged and reduce economic costs. Fiscal measures would play a crucial role in driving the economic recovery amid high uncertainties. Thus, the government should accelerate the disbursement of relief and other fiscal support measures to provide adequate and continuous economic stimulus as well as address vulnerabilities in the labor markets. Meanwhile, monetary policy must remain accommodative. The new financial rehabilitation measures to restore businesses affected by COVID-19, together with other measures by specialized financial institutions, should accelerate the distribution of liquidity to the affected groups in a targeted manner, reduce debt burden, and support the economic recovery. In addition, financial institutions should accelerate debt restructuring. The Bank of Thailand would closely monitor the progress and assess the efficacy of financial and credit measures.

Under the monetary policy framework with the objectives of maintaining price stability, supporting sustainable and full-potential economic growth, and preserving financial stability, **the Committee continued to put emphasis on supporting the economic recovery.** In addition, the Committee would monitor key factors affecting the economic outlook, namely the distribution and efficacy of vaccines, the possibility of the outbreak situation in Thailand and abroad becoming more severe owing to virus mutations, as well as the adequacy of fiscal, financial, and credit measures. The Committee would stand ready to use additional appropriate monetary policy tools if necessary.

Monetary Policy Group

7 July 2021

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Key Issues from the MPC Meeting No.4/2021

23 June 2021

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Thai Economic Outlook

The most important issue for the Thai economy at present would be the procurement and distribution of appropriate vaccines adequately and timely. The economy would expand at a slower pace due to more prolonged and severe outbreak situation, and would still face significant downside risks from virus mutations.

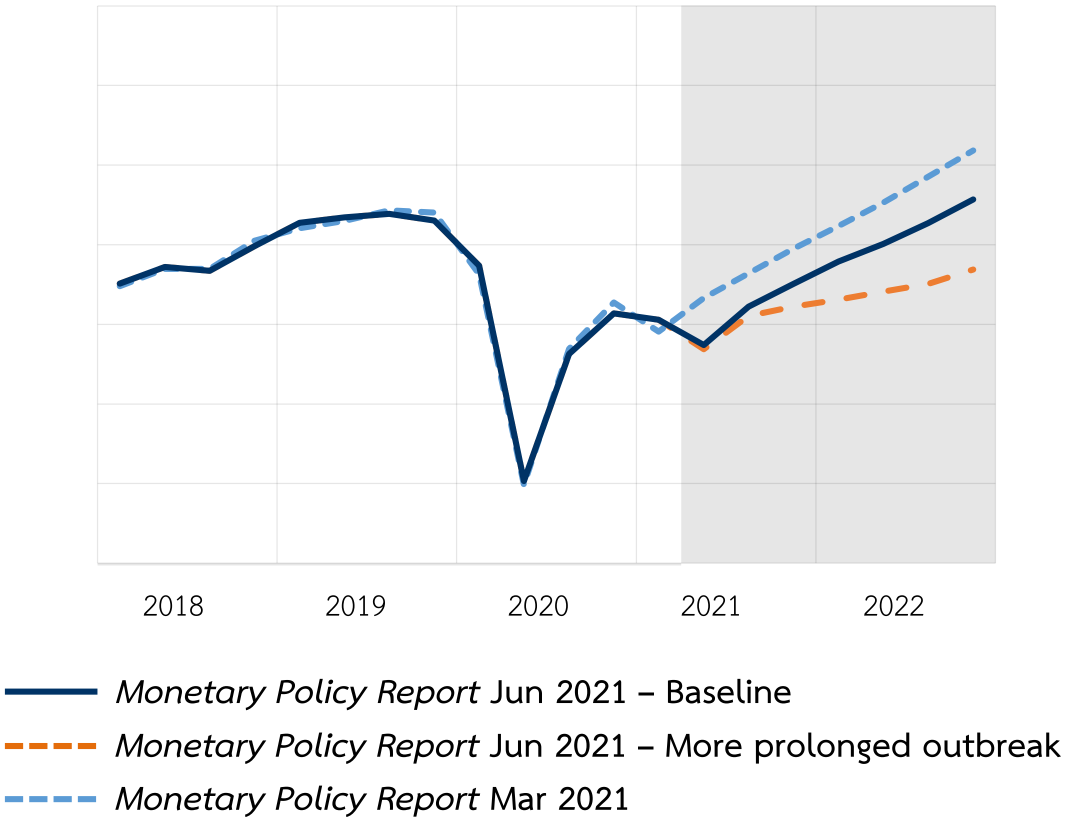
Percent	2020	2021[E]	2022[E]
GDP Growth	-6.1	1.8	3.9
		(3.0)	(4.7)
Headline Inflation	-0.8	1.2	1.2
		(1.2)	(1.0)
Core Inflation	0.3	0.2	0.3
		(0.3)	(0.4)

* Outturn, [E] Estimation

( ) *Monetary Policy Report*, March 2021

Source: *Monetary Policy Report,* June 2021

Real GDP



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Details of the economic forecasts

(% YoY)	2020	2021^E		2022^E	
		Mar 21	Jun 21	Mar 21	Jun 21
GDP Growth	-6.1	3.0	1.8	4.7	3.9
- Private Consumption	-1.0	3.0	2.5	2.7	3.4
- Private Investment	-8.4	6.0	7.0	5.5	6.0
- Government Consumption	0.9	5.2	4.1	-3.1	-1.0
- Public Investment	5.7	11.6	9.5	0.8	5.7
- Exports of Goods and Services	-19.4	5.2	8.8	13.9	7.8
- Imports of Goods and Services	-13.3	9.2	15.0	7.5	5.5
Current Account (Billion USD)	17.6	1.2	-1.5	25.0	12.0
- Value of Merchandise Exports	-6.5	10.0	17.1	6.3	4.9
- Value of Merchandise Imports	-13.8	15.2	22.7	6.8	6.6
Headline Inflation	-0.8	1.2	1.2	1.0	1.2
Core Inflation	0.3	0.3	0.2	0.4	0.3
Assumptions					
- Number of Tourists (Million)	6.7	3.0	0.7	21.5	10.0
- Dubai Oil Price (USD/Barrel)	42.2	60.0	62.3	62.5	65.5

Note: ^{E} Estimation

Source: *Monetary Policy Report,* June 2021

Important factors contributing to forecast revision

(-) Domestic demand weighed down by the 3rd outbreak

(-) Lower-than-expected foreign tourist figures from severe outbreaks at home and abroad

(+) Progress in vaccine procurement and distribution

(+) Greater fiscal support

(+) Improving merchandise exports thanks to global economic recovery

Significant risks affecting the economic outlook

- More severe outbreaks and virus mutations
- Continuity of fiscal support
- Deteriorating businesses' financial positions that possibly trigger layoffs
- More-serious-than-expected supply disruption

The manufacturing sector was somewhat affected by the supply disruption, but most supply shortages were expected to alleviate within the first half of 2022.

Sector	Domestic factors		Foreign and domestic factors		
	Migrant labor shortages	COVID-19 outbreak in factories	Container shortages and higher transportation costs	Higher steel and input prices	Chipset shortages
Auto & auto parts		√	√	√	√√
Electrical appliances		√	√	√	√√
Food	√	√	√√	√	
Electronics (IC & HDD)		√	√	√	
Rubber & plastics		√	√		
Construction materials			√	√	
Petroleum & chemicals			√	√	
Textiles & apparel	√		√	√	
Beverages				√	
Expected period of shortage alleviation	Q2/22 Many foreign workers returned to their home countries since the first wave and did not return yet.	Q3/21 There could be potentially recurring outbreaks until the new wave abates.	Q1/22 Production of containers in China could not meet global demand. Recent closures of China's major ports due to the outbreak exacerbated container shortages.	Q1/22 Prices would remain high due to low supply from India despite some re-opening of steel factories in Europe.	Q2/22 The expansion in chipset production would not meet the surge in demand this year.

Note: √ = Impact on either production costs or quantities √√ = Impact on both production costs and quantities

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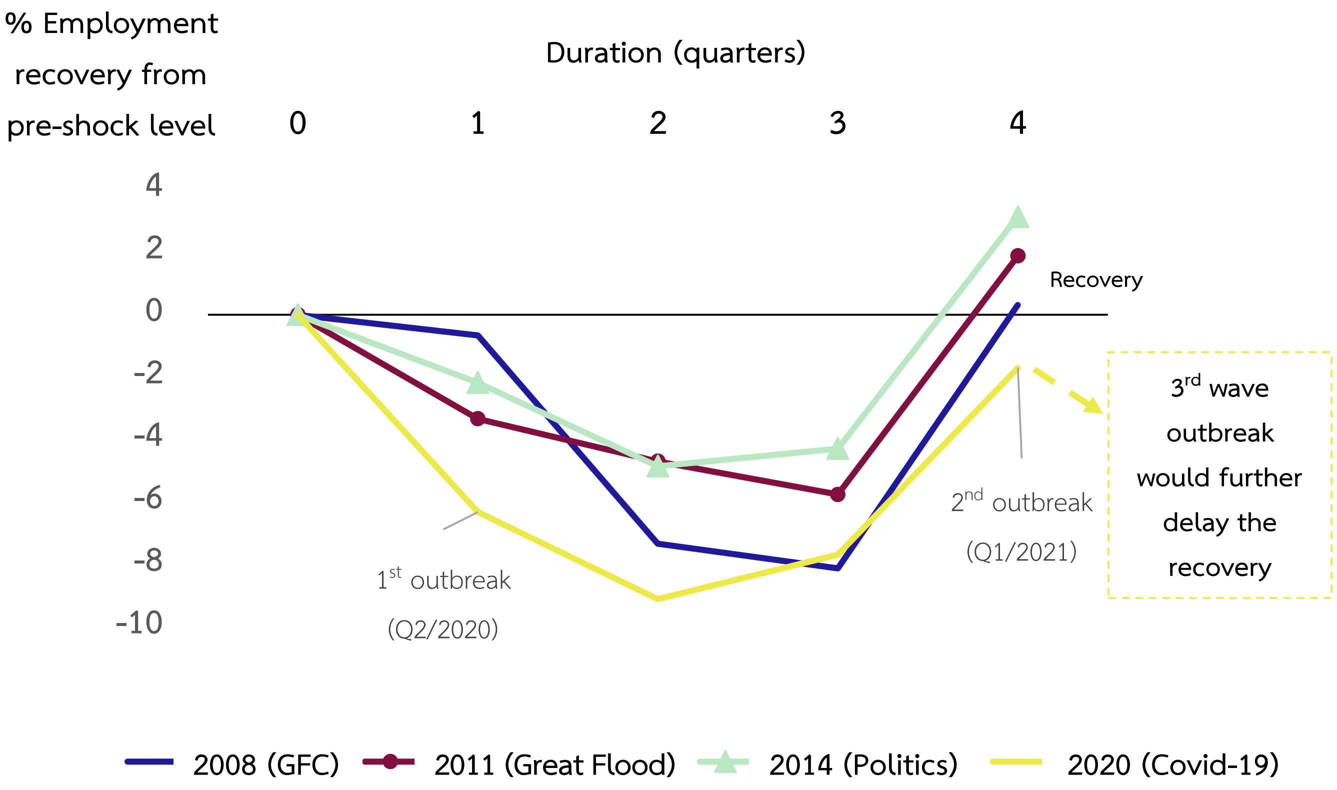
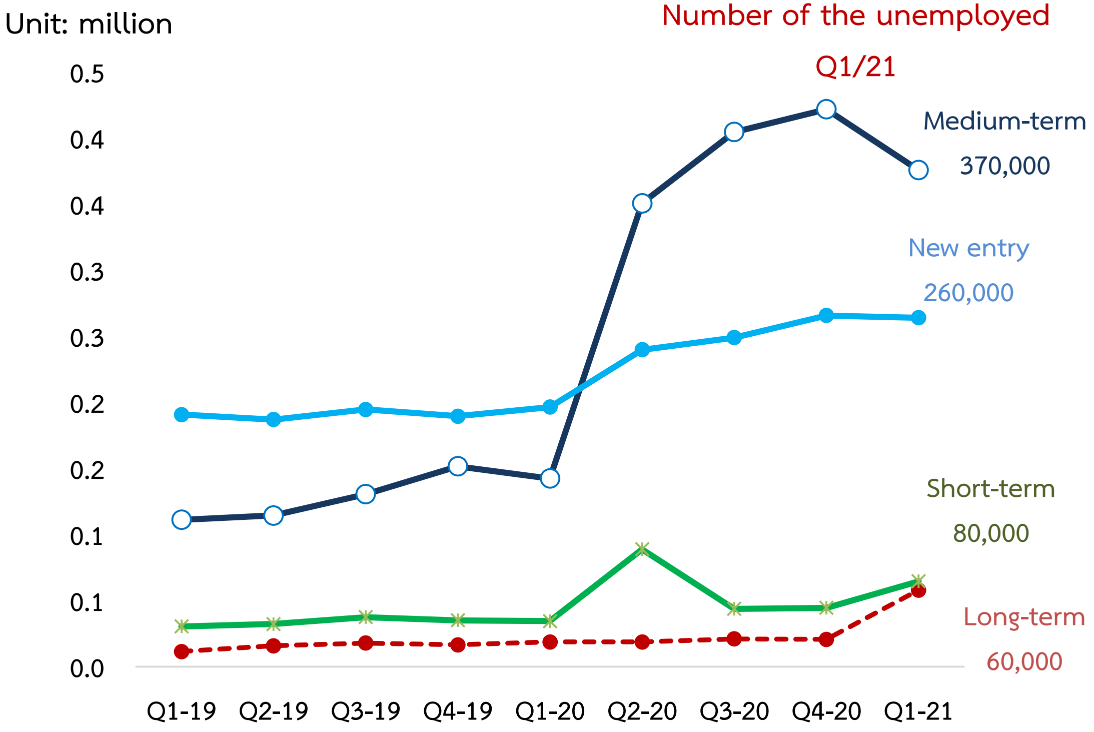
Recovery in labor markets would be W-shaped and slower than in the past. Economic scars from more fragile labor markets, especially in the services sector and among the self-employed, would be harder to resolve without timely intervention.

Recovery of private non-farm employment* from the level before shock



* Calculated from a sample of 11.4 million private sector employees outside the agricultural and construction sectors

Number of unemployed persons (seasonally-adjusted) classified by duration of unemployment



Note: The definitions for the duration of unemployment are as follows.
Short-term: less than 1 month, medium-term: 1 month – 1 year, long-term: more than 1 year
Source: Labor Force Survey, National Statistical Office of Thailand, calculations by BOT

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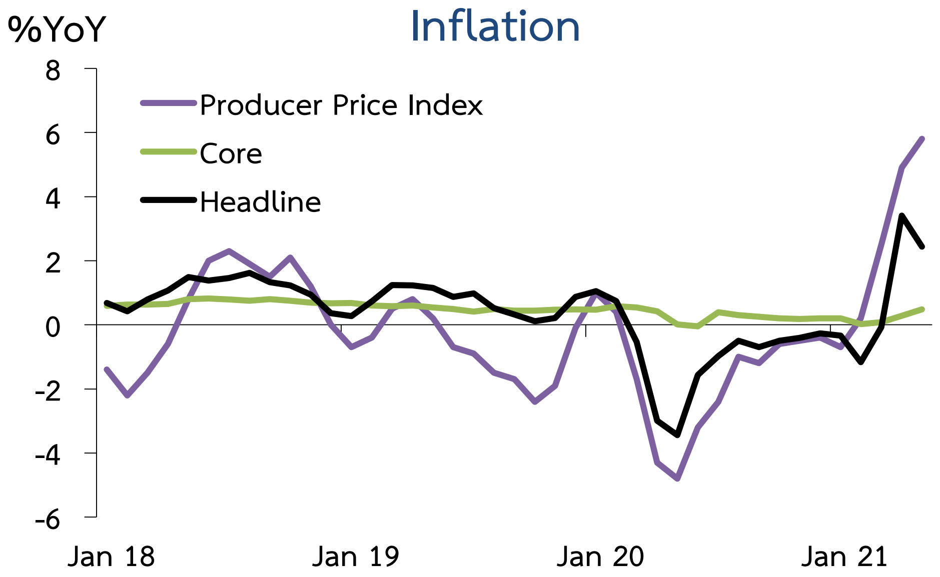
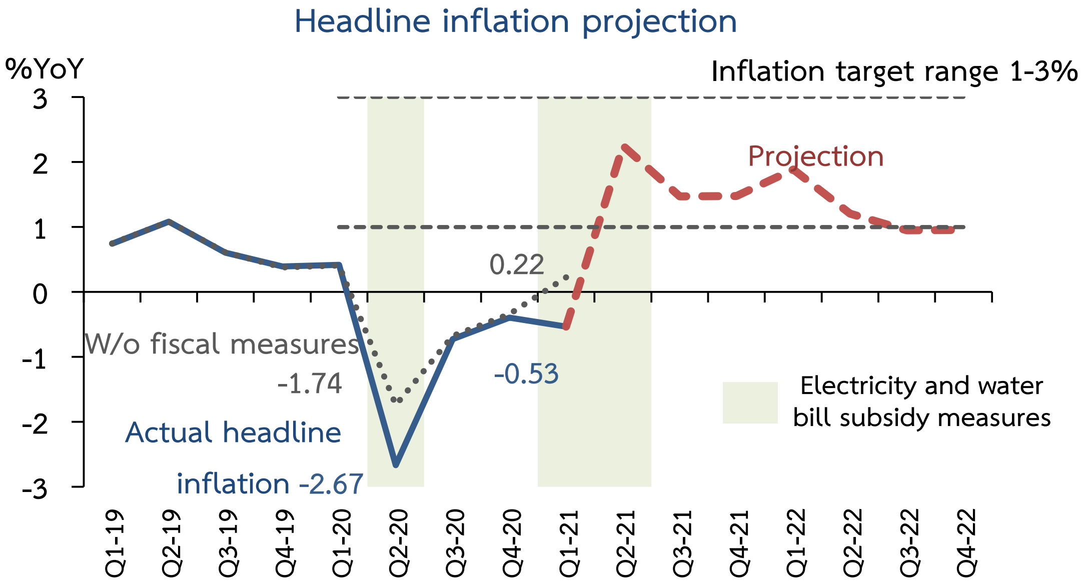
Headline inflation would rise temporarily in Q2/21 from the low-base effect before edging toward the lower bound of the target range.





Reflation in the AEs, the rise in global commodity prices, and supply shortages would have limited impact on Thai inflation

Spillover from reflation in the AEs

- Only 16% of the CPI basket is imported
- Crude oil prices would not rise significantly thanks to prospects of supply increase in the period ahead

Commodity price increases and supply shocks

- PPI increased in some industries which made up only 7% of the CPI basket
- Supply shortages would alleviate by early 2022

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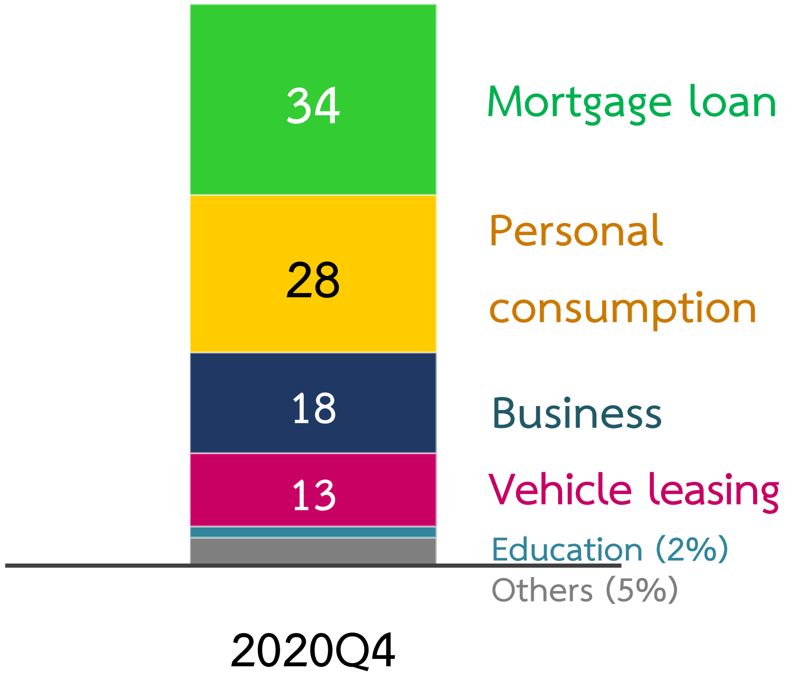
Most household debt is for consumption purposes, which is short-term and carries high interest rates. Meanwhile, household vulnerabilities increased mostly in the self-employed workers as reflected by a significant income fall.

Thai household debt classified by purpose

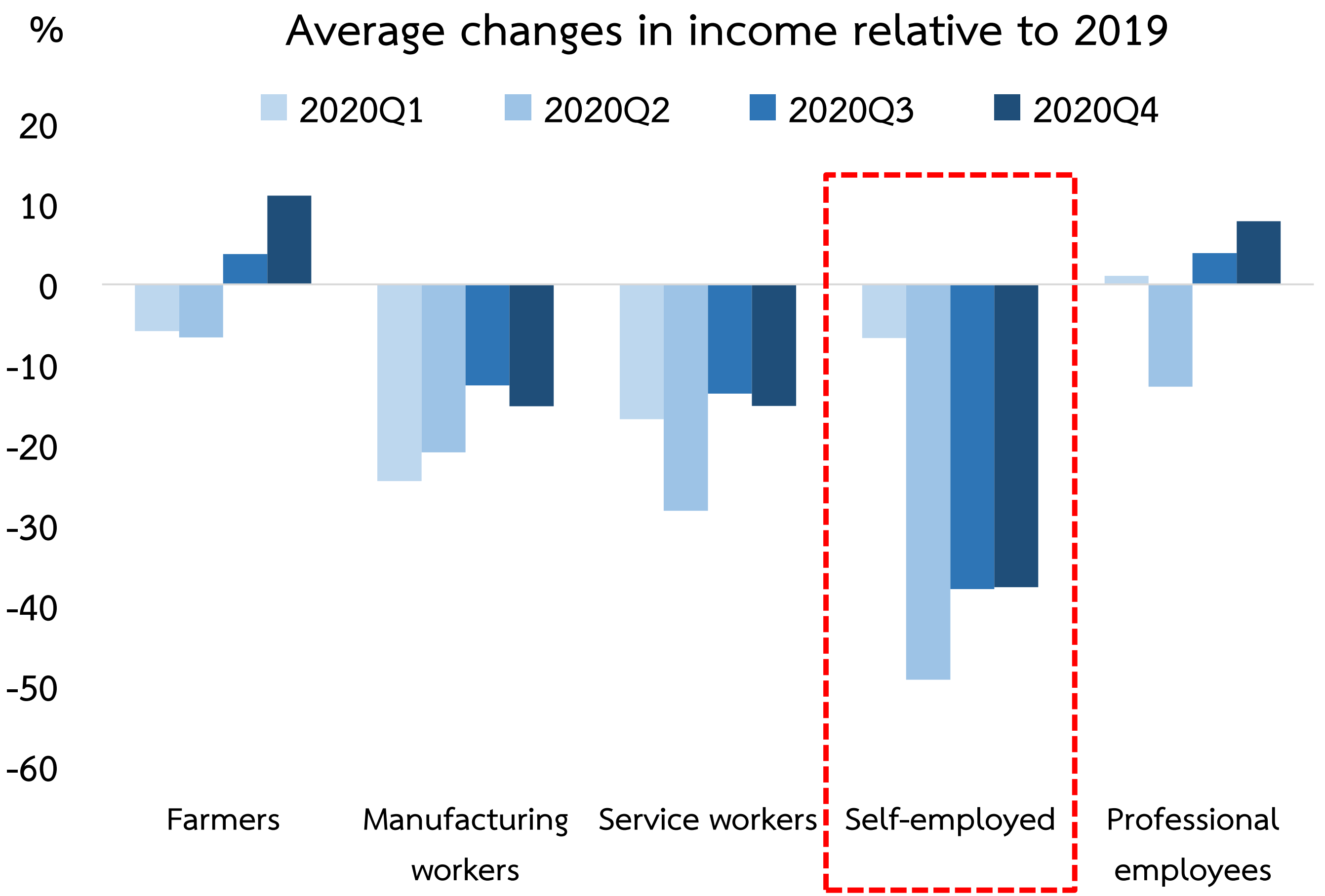
(% share of total debt outstanding)



Note: Other household debt comprises loans for purchasing securities and loans for unclassified purposes

Source: BOT

Average changes in income relative to 2019



Note: Income of the self-employed are estimates from economic activities

Source: SES and LFS (National Statistical Office), OAE, calculations by the BOT