

Prasarn Trairatvorakul: Connecting Thailand to the new investment frontiers – contribution of monetary and financial policies

Speech by Dr Prasarn Trairatvorakul, Governor of the Bank of Thailand, at “Thailand Focus 2013 – connecting to new investment frontiers”, Bangkok, 28 August 2013.

* * *

Good morning,

Distinguished Guests; Ladies and Gentlemen,

I would like to thank the Stock Exchange of Thailand and Phatra Security and Bank of America Merrill Lynch as co-organizers for the invitation to address our distinguished audience on the topical issue of “Connecting Thailand to the New Investment Frontiers”. I also would like to extend a very warm welcome to our foreign guests and to thank you for your continued interests in Thailand and the region. Today I would like to discuss the roles of monetary and financial policies in supporting the Thai economy as we prepare ourselves for the new investment frontiers.

Economic outlook and headwinds from volatility in global financial markets

As you know, much has happened recently with events taking a complete 180 degree turn from the beginning of the year. It did not seem long ago when the EMEs were the fascination and destination of choice for international investors. But since May, global market sentiments have turned with the expectation of a scale back of the Fed’s asset purchases. This coincided with the concern over regional slowdown, initially starting with China, but lately moving to other South and South East Asian economies. Since the unprecedented sell-offs in May, there have been some recent corrections to the initial overreactions. Nevertheless, capital movements and asset prices continue to be volatile and pose headwinds to growth and financial stability.

The summer period provided a brief respite and provided investors with more time to be selective, not treating all EMEs as one single asset class. Economic fundamentals became a primary consideration for assessing in which market to remain invested. We trust that Thailand will continue to receive the attention of foreign investors because of our sound fundamentals and attractive prospects. These, notwithstanding the current soft patches as the economy consolidates and work on its long term competitiveness agenda.

Role of monetary and financial policies in safeguarding stability

Long before the Subprime and the Eurozone crises, Thailand had our own economic crisis of 1997. We experienced a setback that took us more than half a decade to recover. Since then we learnt the virtue of moderation and prudence. Firms had to deleverage, banks recapitalized, regulatory standards, governance reforms and bank lending practices have improved markedly. The government’s fiscal framework was also strengthened following the fiscalization of the costs of financial sector restructuring.

Years of hard work and reform efforts paid off and laid the foundation for a more diversified and competitive economy. The availability of policy space both in the fiscal, monetary and financial policies, helped ensure a much needed domestic source of growth when global trade collapsed in 2008. Timely government stimulus helped shore up domestic demand. An accommodative monetary policy and a strong and well capitalized banking system provided a favorable environment whereby firms and household could continue to finance the consumption and expansion to support domestic demand. The Thai economy was able to navigate through short term sell offs and the sharp reversal of capital flows. The

recent turbulence in fact provided a reality check on the importance of policy consistency and the fundamentals of the economy.

Monetary and financial policies in Thailand have strongly relied on prudence and pragmatism. A credible monetary policy framework helped anchor inflation expectation, thereby fostering continued growth and stability. A flexible exchange rate regime also supported the efficient allocation of resources and competitiveness of the economy. A strong external position helped cushion against sharp reversals of capital flows.

One can never put a price on the comfort with which a strong international reserves position brings. Imagine if we had to raise domestic interest rates to defend the currency that is weakening because of capital outflows. All of this at a time when the global economy is weak and the domestic economy needs the support of accommodative macroeconomic policies!

Financial liberalization and regulatory reform efforts under the Financial Sector Master Plan provided opportunity for Thais, particularly small-scale firms, to have better access to finance. A competitive banking system and a vibrant capital market also helped strengthen investors' confidence through efficient resource allocation and appropriate pricing of risks.

The availability of policy spaces in fiscal, monetary and financial policies provided a cushion for the economy to withstand, shocks both domestic such as our own flood, and external from the risks of a global slowdown. You may be reading market commentaries on the rise in household debt and credit growth in Thailand. Let me remind you that those were the very issue raised by the Bank of Thailand. Successive Monetary Policy Committee statements have pinned these as issues of concern to the MPC even though there were calls for a reduction in policy rates. Our traditional bias towards conservatism and our strong belief in looking beyond shorttermism, kept us steadfast in our mission to be the voice of conscience and moderation. Through these repeated messages, the banking system and the property sectors, through their own reevaluation of risks and returns, have put on their own brakes and are now proceeding more cautiously. The economy overall is also benefiting from the slower pace of activities which were they to continue, would risk the build-up of imbalances in the property sector or household balance sheet.

Connecting Thailand to the new investment frontier

To enable Thailand to enjoy the benefits from the new investment frontier requires the continued pursuit of sound macroeconomic and financial policies. It also requires improvement on the supply side, ie the investment in infrastructure, education and innovation to raise the competitiveness of the country. This is a forward looking chapter that is unfolding. There is need for deeper collaboration between the public and the private sectors to position Thailand as an anchor or a hub for the region.

Strategies for the **private sector** to ensure a durable growth strategy can best be summarized in terms of three moves; **Move up, Move out and Move in.**

1. Let me elaborate further. "**Move Up**" is a reminder for our firms and enterprises to raise their productivity to support the competitiveness of the Thai economy and in preparation for the upcoming economic integration. Moving up the value chain will enable us to differentiate our products, enhance its value, and to enable us to command the margins for our trade. Competing through cheap prices is no longer a viable and sustainable model, both for the firms themselves and for the resource-constraint economy. Our labour force is in much need of productivity upgrades through relevant education, training and apprenticeship. Although these are long drawn processes, the rewards and returns for the economy is more durable. Increasingly, we are seeing large Thai corporates working in close cooperation with the education bodies, in the recruitment and training, to ensure the necessary and relevant supply of skills for their businesses.

2. The next strategy is “**Move out**” beyond the boundaries and the comfort of one’s own home market. Thai corporates can no longer wait for the transfer of knowledge and technology through FDI. They need to venture abroad to secure the resources, know how, franchise value or distribution channels.

Recognizing this, the Bank of Thailand has gradually relaxed capital flows regulations, initially on outward direct investment and more recently on portfolio investments for Accredited Investors. We plan to continue to broaden the scopes of investment with freer mobility for Thai residents in investing overseas. The BOT is also working closely with the Ministry of Finance and other agencies on appropriate tax incentives to facilitate the setting up of treasury center to enable large corporate to conduct in house financial transactions more efficiently and with lower transaction costs.

With the opening up of the New Investment Frontier, this is probably the most exciting times for Thai corporates to invest abroad to secure resources both raw material and know how, expanding customer base, acquiring distribution channels, and broadening markets.

3. The last area of “**Move in**”, aims to create a more attractive business environment for foreigners to turn to Thailand as an important spring board for investment in the new frontier markets. Thailand has a geographical location advantage to become an investment hub for the ASEAN Economic Community, particularly the new frontier markets. To become a magnet for the region, Thailand needs to maintain its ranking in the ease of doing businesses in such areas of rules of law, governance and strong regulatory frameworks. The Thai capital market has also worked hard to promote its role as the funding centre for new frontier markets. Recently the Government of the Lao PDR successfully issued Thai baht-denominated bonds amounting to THB 1,500 million to finance its investment projects. The quota have also been doubled to THB 3,000 million for next year. I am confident that the subsequent sessions in this two-day forum will offer you a clear picture on the opportunities and prospects this region has to offer.

While the private sector works hard to “Move Up”, “Move Out” and “Move In”, the focus of the **public sector** is on infrastructure, both physical and intangible, to raise the competitiveness of the economy, elevate its workforce capability and enhance its return on capital.

Recognizing the short lived, though timely, nature of consumption-led stimulus, the government is embarking on a major infrastructure investments in logistics, communication, water management and transportation. A strong and efficient logistic system will significantly help reduce transportation and logistic costs which are major impediments to our longer term growth. These projects will help unlock the bottleneck and raise overall competitiveness as well as crowd in private investments.

Infrastructural projects will also strengthen Thailand’s position as a hub for our Greater Mekong Sub-region (GMS) neighbors, and is expected to accelerate the integration of these economies as we approach the 2015 ASEAN Economic Community. Projects such as the North-South and East-West corridors will further facilitate integration as well as efficiency of transportation and logistics in the region. As the Western economies progress in the recovery from the global financial crisis, we in Asia should step up our preparations to avail ourselves of the benefits once the global economy is back on its track.

This is a good occasion for our foreign participants to share in the opportunity and prosperity of the region. Foreign investors can participate as co-financing and co-investment partner e.g. through becoming Public-Private Partnership (PPP), Joint venture (JV) or by investing in infrastructure bonds or primary shares. In the area of banking and finance, the country will shortly be welcoming new foreign participants, both as a strategic partner to an established Thai bank, as well as new entrants in the form of subsidiaries.

In addition to tackling the infrastructure constraints, the government has articulated an ambitious goal of pushing Thailand towards an innovative economy. The Government raised

the goal of R&D expenditures as share of GDP from 0.2 to 1% by 2016, and moved to establish IT parks. This is still small in comparison to our neighbours such as Singapore and Korea, but is a step in the right direction. The challenge, of course, remains in the implementation and execution phase.

Given that our long-term growth strategy hinge largely on the infrastructure and human capital investment which takes time to bear fruit, the urgency to start now is all the more important. Postponing such reforms to a future date may risk running up to a scenario like Europe where the economic engine is being put through a major overhaul and restructuring, at the same time while the plane is still flying through a turbulent storm at 30,000 feet! Foreign investors have an important role to play in ensuring that Thailand press ahead with these reform efforts. As the voice of reason and conscience, foreign analysts, credit rating agencies and fund managers have not hesitated to let us know whenever we seem to be slipping in our reform path or policy inconsistency!

Concluding remark

To conclude, these are exciting times for all of us. In the wake of the great unwinding, as public agencies, the Bank of Thailand can undertake the necessary monetary and financial policies to stabilize the market and attenuate the effects of short-term volatility or market fickleness. But the task for long-term development lies with everyone. All of us have a role to build the road to sustainable growth, for the country and the region. I thank the Stock Exchange of Thailand and co-hosts for this occasion to bring together investors and government agencies to renew our focus on investments and opportunities for the future.

Thank you for your attention.