

Thirachai Phuvanatanarubala: Prospects for the Thai economy

Speech by Mr Thirachai Phuvanatanarubala, Deputy Governor of the Bank of Thailand, at the German-Thai Chamber of Commerce Annual Meeting, Bangkok, 18 February 2003.

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Ambassador Andreas von Stechow , Distinguished guests,

Ladies and gentlemen,

It is a pleasure for me to be here. My task today is to assure you, as one of our most important groups of foreign investors, that the Thai economy is doing well. And for this year my task is quite easy.

2002 was a good year for the Thai economy. Despite much uncertainty in the global conditions, the Thai economy made a robust recovery with stability, both on the internal and external fronts.

You may recall that 2 years after the crisis, we started to have positive growth in 1999. GDP growth rates for 1999 and 2000 were strong at 4.4 and 4.6%. But the year after that, in 2001, the global downturn adversely affected our export and made growth for 2001 dip to 1.9%. However, we recovered in 2002 when growth for the first three quarters climbed back up to 4.9%.

For the final quarter, our initial estimate is just over 5%, which would result in growth for 2002 the whole year at 5% as well. This is a good performance in the midst of slow growth in many parts of the world.

So what has caused this?

First, there was an export recovery. Export contracted as much as -7% in 2001. But it began to recover in April 2002. The latest figure for the whole year showed the annualised growth at almost 6%. This was a dramatic turn around.

It should be noted that the export recovery did not come entirely from our traditional markets, the US and Europe. What we did see was that export to Asia increased by over 7%, somewhat higher than the average figure, with China absorbing a good 23% more of Thai goods this year compared to last.

Second, farm prices improved substantially. Prices increased by 11% boosting farm income by the same percentage for the whole year. Both these factors helped improve our domestic consumption especially the sale of automobiles, motorcycles and construction.

Third, there was a strong recovery of other domestic demand. Part of this was helped by the fiscal stimulation. In 2002 the budget deficit was at 3.6% of GDP. The other factor was the low interest rate environment that the Bank of Thailand has maintained for the past 5 years and is now beginning to bear fruits.

The accommodative monetary policy resulted in robust growth of mortgage lending as well as other types of consumer loans. Consumer confidence rose to its highest level in recent years.

Domestic investments improved too. I agree that at the moment not much of the new business investment was yet financed by bank loans. The entrepreneurs still rely more on their internal cash. But the latest investment indicators showed an annual rate of increase at a high of 23%.

Domestic demands have been helped not only by direct government spending, but also by other government schemes that injected funds directly to the grass roots. We had the Bht 74 billion village fund (approx US\$ 1.7 billion) whereby each village had been allocated Bht one million to on lend to village members, often under group mutual guarantees. We also had the micro loan scheme organised by the Government Savings Bank, the government owned bank, which lend directly to the poor.

Ladies and gentlemen,

The good news went on.

Despite the strong recovery, we have been able to keep inflation under check. Headline inflation for 2002 was 0.7% and core inflation 0.4%. The adverse affect from high oil prices has not translated into much inflation.

Our currency was also quite stable. For the whole of 2002, the bath appreciated against the US dollar by less than 2%, which was quite modest compared to other Asian currencies. The international reserves level was also ample at US\$ 38.9 billion, allowing us to aim to pay back all the loans under the IMF program by the end of July this year.

Moreover, three major credit rating agencies, S&P, Moody's, and Fitch Ratings, all assigned better outlook to the Thai economy. Japan Credit Rating Agency did in fact upgrade Thailand's sovereign rating from BBB to BBB+ last November. Such widespread improvement in confidence among consumers, entrepreneurs, and investors helped support both consumption and investment throughout the year.

We have also made a substantial progress in solving the non-performing loan problem. The Thai Asset Management Corporation, the central organization run by the government that took over Bht 700 billion of NPL's from the commercial bank system has already worked through two-thirds of their portfolio. The recovery rate was 135% of the TAMC's purchase prices, which was the banks' written down value. This means that the TAMC should not add any further burden, both to the banks and the taxpayers.

Meanwhile even though the banking system still has 15% of the NPL left on their books. However, much of this has already been fully provided for in their loan loss reserves. The banks are therefore now poised to resume lending, and the restructured debtors are once again eligible to borrow.

Ladies and gentlemen,

The big question is of course – is this sustainable?

2003 is fraught with so much uncertainty. The most important risk at the moment is from the external sector, namely, tension between the US and Iraq. If this conflict aggravates into a war, it may delay the global recovery process. If the situation prolongs and gravely deteriorates, there could be even greater risks posed to world demand and ultimately the demand for Thai exports and tourism. At the same time, a possible upward pressure on the price of oil could have some adverse impact on an oil-importing country like Thailand, affecting not only the cost of production but also consumer and business confidence.

The domestic components, however, look set to continue their strong courses. The high confidence levels by both the consumers and the businesses should ensure that domestic demands for both consumption and investment continue to expand. The repair that had been made to the balance sheets of commercial banks – and many of them are now back to making substantial profits – should allow them to once again serve the economy. The improvement in debt equity ratios of many private companies also opens the road for them to start thinking up new investment projects.

Even on the external components, the fact that Asian countries have been trading more and more among themselves can also help shield them from temporary turbulences in the American and European economies, should there be any.

Our GDP growth forecast for 2003 is between 3.5 to 4.5, with both core and headline inflation at 0.5 – 1.5. This is in fact a forecast that has taken into view of the uncertainty caused by the possible war. Therefore, if the external environment does not deteriorate much from the present trend, if the war is brief and limited in scope, our forecast has a significant upward potential, and growth could actually be higher than 4.5 percent.

But the biggest question in your mind is perhaps how does the government plan to manage its financial obligations, since a large part of the GDP growth in the past year did come from fiscal stimulus.

In this respect, I can inform you that the government has made it very clear that they plan to consolidate the fiscal deficit to no more than 3.1% of GDP for fiscal year 2003. This is a good gradual reduction from 3.6% last year.

The overall government debt is currently still at 54% of GDP, well under the cap of 60% announced in 2001. The rapid recovery of the general economy also helped boost tax revenue collection by as much as 10% in 2002, and looks set to repeat itself in 2003 as well, helping to narrow the budget deficit.

Ladies and gentlemen,

No one can plan for 2003 with absolute certainty. We are all following the news minute by minute, and even the best laid out plan for this year must contain several scenarios to cover for contingencies.

But the one certainty I can assure you is that the macro economic policies in Thailand that aim for stability and sustainable growth will continue.