

Tarisa Watanagase: Thailand's weathering the global downturn

Address by Dr Tarisa Watanagase, Governor of the Bank of Thailand, at a Luncheon with EU Ambassadors, Bangkok, 3 February 2009.

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Your Excellency Ambassador Hotek,
Excellencies, Honourable Guests,
Ladies and Gentlemen,

I am delighted to join this luncheon gathering of prominent Ambassadors of the Council of European Union in Thailand, under the presidency of Ambassador Ivan Hotek of the Czech Republic. Indeed, I would like to extend my sincere appreciation to Ambassador Hotek for his kind invitation for me to update Excellencies from the EU countries on recent economic developments in Thailand and the prospects for 2009.

Let me begin with the overview of Thailand's economic performance.

The Thai economic performance was satisfactory for 2008 as a whole. GDP is estimated to grow by around 3.6 percent, driven by the growth momentum during the first three quarters of the year. Notably, from October 2008 onwards, economic developments have been deteriorating. During the fourth quarter of 2008, exports weakened considerably, falling by 9.4 percent from the same quarter of the previous year. Since October, exports showed large reduction in manufacturing products, especially high-technology products.

On the domestic side, demand as well as consumers' and investors' confidence have deteriorated as evidenced by several indicators reported by the Bank of Thailand, including the Business Sentiment Index, which fell to the lowest level at 34.4 in November last year. In light of this, businessmen and the press started to become concerned about the potentially higher unemployment, which exacerbated confidence further.

Turning to economic stability, inflation pressure has dissipated starting August 2008. Headline and core inflation rates, which were at 9.2 and 3.7 percent respectively at their peaks in July 2008, fell to 0.4 and 1.8 percent at the end of the year. As for the financial sector, our banking system is healthy in terms of profitability and capital base. I will return to touch on the financial sector later on.

Economic stability on the external front is also very strong. For 2008, the current account recorded a small deficit of 0.2 billion US dollar. Our international reserves amounted to 111 billion US dollar, which is 4 times of short-term external debt. The exchange rate remains competitive and stable. For 2008, the capital account recorded an overall surplus of 12.8 billion US dollar, of which foreign direct investment or FDI was 9.9 billion US dollar. FDI from Europe accounted for about 11 percent of total FDI.

Excellencies,

For the prospect of the Thai economy this year, the Bank of Thailand sees a growth rate of 0-2.0 percent and 2.0-4.0 percent next year. I wish to emphasize that the growth performance depends not only on how fast the global economy recovers, but also on how fast confidence within the country could possibly pick up, which will help ensure the recovery of domestic demand.

On the prospect of global economic recovery, the consensus forecasts of world growth for 2009 have been continuously revised downward as the severity of the financial crisis hits the financial markets and the real sectors of industrialized economies. The latest IMF forecast expects the global economy to be stagnant this year and some economies in Asia to record negative growth.

As a result, it is most likely that international trade and investment cannot be a major driver of growth for a large number of economies. Intra-regional trade, which has strong ties in Asia, is also likely to decelerate. Most economies will have to turn inwards to look for domestic demand as a source of growth. This is why room for policy maneuver and domestic confidence are important at this juncture.

Amid the tremendous challenges that we face, I am cautiously optimistic that Thailand will be able to weather the storm relatively well. Allow me to share with you the reasons behind this.

First, the growth momentum of domestic demand has been cushioned by supportive monetary and fiscal policies, and declining costs of production. As Excellencies have already followed recent policy initiatives, there continues to be room for the Government to pursue fiscal initiatives for stimulus and social safety net protection as the public debt is low, accounting for about 37 percent of GDP.

As for the monetary policy, the Monetary Policy Committee has already cut the policy interest rate twice by a total of 1.75 percent from 3.75 to 2 percent. These were significant reductions by the history of Thai monetary policy. The cuts aim to shore up confidence by sending a strong message that monetary policy can now focus on supporting growth now that inflation is not a threat. They also help shore up domestic demand. Nevertheless, we are mindful that, at this juncture, monetary policy easing may transmit slowly to support economic growth.

Second, the Thai private sector has strong underlying strengths to withstand economic and financial volatility. Both business and household debts are low. Our production and service sectors, now adversely affected by the global slowdown, were able to build up profits earlier as a cushion. The agricultural sector continues to show signs of growth. Although agricultural prices have adjusted downward, agricultural production cost such as fuel and fertilizer have also declined, which helps reduce the burden of farmers.

Third, the banking system is liquid and resilient. Banks have ample liquidity because they do not rely on inter-bank funding but rather predominantly on domestic deposits. But the Bank of Thailand remains vigilant. We maintain close dialogue with the top management of banks concerning important external developments and stand ready to provide liquidity should such a need arise.

Unlike the crisis of 1997 when the banking system failed to function as financial intermediary of economic activities, our banking system today has remained resilient in the aftermath of US financial turmoil. The Thai banking system's foreign investment exposure was only about 1 percent of its total assets as of end-2008, of which investment in toxic assets was only a small portion. All sub prime-related CDOs have either been unwound or losses provided for in line with international accounting standard.

In the past several years, the Bank of Thailand put great emphasis on robust stress testing and risk management on the part of banks, with an aim to strengthening the banking sector while the economy was still good and the sector profitable. More recently, our financial and legal infrastructures have also been strengthened particularly through new legislations, including the Bank of Thailand Act, the Financial Institutions Business Act, and the Deposit Protection Act. Our accession to the Basel II Accord at the end of last year will further enhance banks' risk management and financial sector stability. Moreover, the second3 phase Financial Sector Master Plan, which will be announced this year, will also increase competition and further enhance financial efficiency and resiliency.

Banks also deserve credits. They have made significant improvements in their risk management. The fact that they did not make significant investment in those high-yielding sub-prime related assets in spite of their abundant liquidity is a testimony in itself. I'm glad to say that our efforts to reform and strengthen the risk focus have paid off.

Excellencies,

In summary, the Thai economy has achieved significant structural improvements since 1997. Our economy has strong fundamentals, underpinned by price and financial stability. Nevertheless, it is perhaps inevitable that we may yet see more negative impacts from the present international financial market turmoil before the improvement, since no one knows how much deeper or longer this global downturn will be.

What we need to do now is to ease some of the pain currently experienced, build up safeguards and prepare for the eventual upturn. In Thailand, policymakers on all fronts together with the private sector are doing just that.