Bandid Nijathaworn: Thailand's banking and economic outlook

Keynote address by Dr Bandid Nijathaworn, Deputy Governor of the Bank of Thailand, at the Australian-Thai Chamber Luncheon, Bangkok, 3 April 2009.

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Let me first thank AustCham Thailand, especially President Andrew Durieux, for the invitation to speak at today's luncheon. It has been almost four years since I last spoke at an AustCham event, so, it is a pleasure to be back. Today I will speak on Thailand's banking and economic outlook, a subject which I am sure will be of interest to all of you. In keeping with what a good luncheon speaker should do, I will keep my remarks short and to the point, so that we will have plenty of time for desserts and for questions and answers.

This week is undoubtedly an important week for the global economy, as leaders and finance ministers of the world's twenty most important economies gather in London to map out a strategy that aims to comprehensively address the current global financial crisis. Up to now, policies to tackle the crisis have been left largely to the individual economies in response to the problems that arise. But as the crisis has mutated into a major global problem, a coordinated policy response at a global level is clearly needed to ensure a synchronized recovery in all the key parts of the global economy. Without coordinated and comprehensive policy response, a synchronized recovery will not take place. And without a synchronized recovery, the world will be at risk of running into a weak, patchy, and unsustained recovery for a prolonged period. So, this week is really an important week, and what has been announced so far by the world leaders, in terms of the new resources that will be made available to aid the global recovery, is positive for the market and for the global economy.

The current global crisis is now in its 20th month. My count is since the Federal Reserve took the unprecedented step to reduce its policy interest rate sharply for the first time in August 2007, signaling the serious nature of the problem. Thailand, being a small open economy, could not escape the impact of the turmoil. The impact on Thailand, so far, has been felt through a sharp reversal of capital flows, on account of deleveraging by foreign investors, as well as through a tightening of access to foreign capital, and through a dislocation in economic activities as export and tourism receipts fell sharply. The banking sector, however, has been resilient given the low direct exposure to the toxic assets, the low reliance on global liquidity as a source of funding, and the strong capital base. The fact that the Thai banking sector remains safe and sound is no accident. It is largely the result of continuing improvement in risk management capacity of the banking sector following the Asian financial crisis, under a stronger regulatory framework and risk-based supervision. Compared to some countries at this time, the banking sector in Thailand is functioning normally, with the financial markets remaining relatively stable despite greater volatility and uncertainty in the global economy.

At the Bank of Thailand, we are optimistic that policy efforts at the global level will be successful in stabilizing the financial markets and in providing a comprehensive solution to the current crisis. Nevertheless, our view is that the adjustment that follows, and hence the process of global recovery, will probably take time. More importantly, in the Thai context, given the global nature of the crisis, and the fact that our economy has been affected mainly through contagion, it will be difficult for an economy like Thailand to achieve a sustained recovery on our own, if the global economy does not recover. Therefore, in the context of policy, the focus of policy response in Thailand should be on helping the economy and the private sector to adjust to the impact of the crisis, while ensuring that the key economic institutions and systems 6 most importantly the banking sector 6 continue to function normally, so that the economy will be in a position to move forward quickly once the crisis storm passes.

It is in this context that the Bank of Thailand has been shaping our response to the current economic downturn. The response so far includes an aggressive easing of monetary policy, ensuring adequate liquidity to the financial markets and the banking sector, helping banks to better manage the increased risk in lending by introducing a government-sponsored credit guarantee scheme for SMEs, and encouraging banks to act early in assisting customers with debt rescheduling or debt restructuring so as to ward off the pressure on asset quality and on the non-performing loans.

These are the direction and the measures we have taken in our response to the crisis, and more will be done if needed to ensure a smooth adjustment in the economy and the financial sector. Judging from what we are seeing in terms of the recent broad global developments, I am confident that the combined effects of the fiscal stimulus by the Government and the financial measures that the Bank of Thailand has put in place, should provide the essential cushion for the economy to adjust to shock, and keep the impact of the global financial crisis on the economy manageable.

As for the near-term outlook, latest monthly data still show signs of sharp corrections in the domestic economy. Exports and tourism fell by 11 percent and 23 percent, respectively, in February from a year earlier. Imports, on the other hand, fell by more than 40 percent, indicating a sharp deterioration in the domestic demand and supply conditions, and this is reflected by the continued declines in manufacturing production, capacity utilization, private consumption and investment. Domestic credit growth slowed to 6.8 percent in February while deposits grew by 6 percent. Contraction in economic activities further eased the pressure on prices, with headline inflation declined to a minus 0.2 percent in March.

Given the sharp dislocation in economic activities in the last few months, market consensus now seems to agree on a small negative growth for Thailand this year, but with an improvement in growth next year. This means the market expects the Thai economy this year to go through a period of sharp adjustment on account of the global slowdown before growth is resumed next year. This view is consistent with the current mainstream view that, with the strengthening of the policy efforts at the global level, the world economy should look better next year compared to this year. As for the Bank of Thailand, our Monetary Policy Committee in its meeting next week, will also be going over this same question in assessing the near-term outlook for our deliberation of monetary policy. Whatever growth numbers we come up with, they will be conditional upon the prospects of the global economy going forward, especially after the G-20 announcement of the new global policy.

Turning now to a more positive note, regardless of the adjustment we have to go through this year, or even next year, the Thai economy at this time is fundamentally stronger, and is in a better position to weather the crisis, compared with the situations we were in ten years ago during the Asian financial crisis. Let me give you six good reasons.

<u>First</u>, Thailand does not have any imbalances in the economy, and hence there is no bubble to speak of. <u>Second</u>, the country's external position is much stronger now with surpluses in the external current account, low level of foreign debt, and a large international reserves position. <u>Third</u>, our banking sector is sound and resilient, and is functioning normally with good liquidity.

<u>Fourth</u>, the corporate and household sectors are not highly leveraged. They have low debt and strong balance sheets. <u>Fifth</u>, the ability of the economy to adjust to external shock has improved markedly from before, given the flexibility that we now have in our economic and financial systems. The most crucial is a more flexible policy regime, especially the exchange rate. And <u>sixth</u> is the low level of public sector debt, now at 39 percent of GDP. This low debt gives ample room for the authorities to use fiscal policy to support growth. Such room will give the authorities better leverage to cope with any further fallout from the global turmoil.

The last point I want to make is to assure you that despite the ongoing global credit crunch, and the tightened conditions in the international financial markets in terms of funding access, our policy on cross-border capital flows will remain open and liberal, and our policy on access to domestic funding by non-residents will also remain unchanged. This should help reduce any fear that you may have about policy tightening in this area, and the current policy stance should help foreign-owned Thai resident companies to adjust well to the impact of the crisis.

Ladies and Gentlemen,

I hope my brief remark today has been useful in updating you on the current situations, and that it adds to the confidence that you already have in Thailand, and in the ability of our economy and the banking sector to weather the current global downturn. We are now living in an exceptional time, but our caution and right action, together with a good collaboration between private businesses and the authorities, will help see us through. Thank you for your attention and again thank you for the invitation.