Veerathai Santiprabhob: Monetary and financial sector policy – moving forward

Speech by Dr Veerathai Santiprabhob, Governor of the Bank of Thailand, at the Foreign Correspondents' Club of Thailand (FCCT), Bangkok, 1 June 2016.

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Members of the FCCT Executive Committee,

Distinguished guests,

Ladies and gentlemen,

Good evening to you all,

It is my pleasure to be here with you tonight. Although this is my first time speaking at the FCCT, I can feel the vibes of active journalism, which underpins the club's foundation and its long history in the community of journalists in Thailand. As one of the oldest press clubs in Southeast Asia, I would like to thank you for your continued commitment and contribution to the Thai economy and the Thai society. Public perception and expectation indeed play a large part in establishing credibility and effectiveness of economic policy. As public opinion influencers, journalists greatly contribute to achieving desired policy outcome.

As we progress half way through the year, today I would like to share with you the Monetary Policy Committee's latest economic assessment and monetary policy stance to support the current economic recovery and safeguard stability of the Thai financial system. After that, I will turn to the Bank of Thailand's financial sector development policy, with a view to facilitating Thailand's economic transition towards strong, sustainable and inclusive growth.

Let me start by talking about recent developments in the global financial markets. We started off this year with heightened volatility in the global financial markets, mainly due to concerns over the China's economic slowdown, declining oil and commodity prices and monetary policy divergence among major central banks. Lately, the global volatility has subsided as the Chinese government has shown a strong commitment to limiting the possibility of hard landing with additional fiscal and credit stimulus while restructuring the economy. Commodity prices have also begun to edge higher. Financial market participants expect monetary policy in major countries to remain highly accommodative, despite an increased possibility of another rate hike by the US Federal Reserve in the next few months.

While relative calm has returned to the global financial markets, I must stress that the global financial environment remains fragile. Development on China's economic restructuring and concerns over its corporate debt, the possibility of Brexit, and major central banks' policy divergence are among the most significant factors that can trigger new bouts of volatility. Investors' sensitivity to unexpected news and events could also amplify the volatility.

Amid the fragile global financial climate, the Thai financial markets have been relatively resilient compared to those of other emerging markets, thanks to Thailand's strong external position. Current account position last year registered a surplus of 9 percent of GDP, and is projected to remain at that level in 2016. Our international reserves have been at a healthy level, standing at around three times of the short-term external debt and 1.3 times of the total external debt. Foreign holdings of the Thai government and Bank of Thailand bond outstanding are less than 9 percent, compared with more than 30 percent in some other emerging markets in the region. External debt of the corporate sector has been relatively low, and mostly belongs to large companies, which manage their exchange rate risk sufficiently well.

While Thailand's financial strength serves as a buffer against external shocks, it is important that the private sector is not complacent and should continue to be prudent in their financial risk management. Global financial volatility can definitely trigger two-way movements of currencies and asset prices. As a small open economy, Thailand cannot escape, but to find effective ways to live with the global volatility.

On the Bank of Thailand's part, under the flexible exchange rate regime, currency movement serves as the first line of defense against unexpected external events. We continue to be prudent in using an appropriate mix of policy tools to help prevent excessive volatility of the currency and asset prices. In addition, to build market resilience in the longer run, we embrace on financial market developments, as deep and liquid markets would better absorb large swings in capital flows. We also plan to further relax capital flow regulations to allow more balanced flows in and out of the country, which would enhance stability against short-term speculative flows.

Ladies and gentlemen,

Moving from the financial side to the real side, let me share with you the Monetary Policy Committee's latest assessment to summarize where the Thai economy stands at the moment.

This year, the Thai economy is projected to gradually recover, driven mainly by government spending and the tourism sector. Government spending, mainly through small investment projects, has lent support to the recent economic recovery. Contribution from large-scale infrastructure projects is expected to become more evident in the latter half of this year. Meanwhile, tourism has been an important growth driver, with a broad-based improvement in a number of tourists from China and other regions. In 2016, we estimate that more than 32 million foreign tourists, improving from 30 million last year, will choose Thailand as one of their destinations.

In addition, the Thai economy has benefited from expansion of investment in certain sectors, notably those related to telecommunication and alternative energy. Exports of goods to CLMV countries, which now account for around 10 percent of our total exports, has supported economic growth and has potential to grow further, despite a decline in export volumes of oil in recent months due to temporary factors. Overall, the Monetary Policy Committee forecasts that the economy will grow at 3.1 percent in 2016, picking up from a growth rate of 2.8 percent in 2015 and 0.9 percent in 2014.

However, I must admit that overall momentum of the Thai economic recovery remains slow at this stage. Exports of goods, excluding gold, continue to contract, largely attributable to weak external demand, notably from China and Asian trading partners, as well as structural constraints of the Thai industries and changes in global trade structure.

Weak exports have mainly weighed on private investment which only saw a modest expansion. Private consumption, particularly which of rural agricultural households, has been dragged by high indebtedness, low income growth and severe drought. ***Amid gradual economic recovery, employment conditions remain intact.*** Flexibility in the labor market has allowed workers to move from the agricultural sector to other sectors. There have been no extensive layoffs, despite a reduced number of working hours.

In recognition of lower-than-potential growth and low inflationary pressure, the Monetary Policy Committee has maintained an accommodative policy stance to support the economic recovery. At its latest meeting a few weeks ago, the Committee decided to maintain the policy interest rate at 1.50 percent. In the Committee's view, current monetary conditions have eased further as bond yields remained low, and commercial bank lending rates declined. Therefore, the policy interest rate should be kept on hold to preserve limited policy space, which can be deployed if unforeseen events emerge in the future. Moreover, maintaining the policy interest rate would not add risks to financial stability. Under a prolonged period of low interest rate environment, some tentative signs of search-for-yield behavior, such as higher demand for risker financial instruments, have emerged and thus warrant close monitoring going forward.

Ladies and gentlemen,

As the Thai economy gradually recovers and inflationary pressure remains subdued, monetary policy will ensure that monetary conditions are adequately supportive to growth. At the same time, we must not forget to chart a course towards the country's long-term economic development. As the Thai economy is in need to upgrade growth potentials and increase competitiveness, the Bank of Thailand will contribute to this process of economic transformation by taking a proactive role in the financial sector development policy.

Ongoing in this sphere, there are at least three development plans under implementation, namely, the Financial Sector Master Plan, the Payment Systems Roadmap, and the Capital Account Liberalization Master Plan. Although the three plans have different objectives, they complement each other and together form a strong foundation for the country's financial sector development. I will highlight a few key elements we hope to get out of these plans.

The first one is the Financial Sector Master Plan (FSMP) Phase III.

Approved by the Cabinet in March this year to set out strategic directions for the next five years (2016 – 2020), FSMP III is aimed to promote a competitive Thai financial sector, to support more diverse needs at fair and undistorted prices, as well as promote regional trades and investments, with proper supervision to ensure macroeconomic and financial stability. In short, this plan's motto is to promote a "competitive, inclusive, connected, and sustainable" financial system.

After five years, the Bank of Thailand expects to see growing financial innovation with more diverse players, both banks and non-banks, especially those offering digital financial services. These services will allow a new segment of customers to gain access to financial services through new channels. SMEs entrepreneurs, for example, could pitch their ideas to a wider group of investors, through crowd funding and peer-to-peer lending platforms. New ideas would have a higher chance of being translated into businesses, thus promoting innovative spirit among the Thai entrepreneurs. Financial innovation will also promote competition and drive higher efficiency in the banking sector.

At the same time, we expect most Thai individuals to have access to basic financial services at a fair price and have an appropriate level of financial literacy. Financially deserved enterprises should receive adequate funding, using proper financial instruments. We expect to improve households' financial literacy, leading to more prudent financial management and lowered households' indebtedness. For financial institutions, we encourage them to improve the level of consumer protection and quality of financial professionals, and to incorporate more sustainability practices into their core business operation.

On the road to enhancing regional connectivity, under the ASEAN Banking Integration Framework, we encourage banks to further extend their regional presence to support expanding economic activities, or use Thailand as a springboard to expand their business in regional countries, leveraging on Thailand's established legal framework, financing facility, infrastructure, logistics and IT capability. In addition, the use of local currency in regional trade and investment has been promoted to lower business transaction costs and mitigate volatility of the major currencies. We hope that policy to strengthen financial connectivity with our neighbors will facilitate closer economic integration for the shared benefits of the region.

The second plan is the Payment Systems Roadmap.

The plan is aimed to promote safe and efficient electronic payment services with new technologies and innovation, with a view to reducing transaction costs, improving governance standards, and being supportive of expanding economic activities. In particular, integrated payment channels, such as mobile phones, internet, debit/ credit cards, and e-money along with a competitive fee structure, will support e-Commerce/ m-Commerce and benefit both businesses and consumers alike. The Bank of Thailand will also continue to work with regional regulators to advance payment systems connectivity to support international trades, labor movements, and tourisms.

Under this roadmap, the Bank of Thailand has worked closely with the government to advocate the idea of digital economy by taking a lead in the National e-Payment Plan to promote Any ID infrastructure and debit card usage. Development of a new payment infrastructure as the "open architecture" to allow network interoperability among various types of players will lower payment fees and discourage the use of cash, thus resulting in much lower operating costs and higher efficiency for the corporate and banking sectors. As fundamental parts of infrastructure development, we adopt international best practices on the security and prudential standards to ensure confidence as the country moves from a cash-based economy towards a digital economy.

The third area of financial sector development policy is the Capital Account Liberalization Master Plan, Phase II.

The plan aims to deepen Thailand's financial markets by allowing greater flexibility and diversification in products and services offered to residents and non-residents, and to support the growth and development of the Thai economy. So far, a number of regulations on foreign-exchange management have been relaxed for greater flexibility and lower transaction costs.

This year, the Bank of Thailand plans to further relax foreign-exchange regulations by allowing qualified investors to invest in securities abroad directly within a certain limit without the need to go through local intermediaries. We also plan to allow securities companies to buy and sell foreign currencies with their clients within the scope of their brokerage business. Lastly, foreign corporations located in neighboring countries are to be permitted to borrow direct loans in Thai baht from domestic financial institutions to invest in Greater Mekong Subregion (GMS).

We have also started to see the results of the increased flexibility, which helps Multi-National Companies to establish Treasury Centers (TC) and International Headquarters (IHQ) in Thailand. As of now, there are 13 companies holding Treasury Center licenses, of which 4 have been granted in the past 3 months, with one more awaiting approval from the Ministry of Finance. Many more have also made inquiries which I am very glad to see.

Ladies and gentlemen,

Let me now turn to the concluding part of my talk tonight.

Amid the volatile global financial climate, Thailand's strong external positions will serve as buffers against financial shocks. The private sector's prudent financial management and policymakers' credible policy will allow us to successfully ride with the global tides.

In the real sector, the Thai economy is expected to maintain its gradual recovery path, driven mainly by government spending and tourism. Exports of goods, on the other hand, is subject to a slowdown in trading partners' economies and structural constraints of the Thai industries. Inflationary pressure remains subdued, but the headline inflation will gradually rise in line with a recent pick up in oil prices. Against this backdrop, monetary policy stance will remain adequately accommodative to support economic activities, while safeguarding financial stability.

Over a longer horizon, the Bank of Thailand is committed to creating financial infrastructure and nurturing the financial eco-system to help lift up growth potentials of the Thai economy. We aim to promote financial innovation, financial inclusion and financial literacy, as strong foundations for sustainable economic development. With regard to the payment systems, the new infrastructures are being built to support the transition towards the digital economy. Rules and regulations on exchange-rate management are to be relaxed further for greater flexibility of investors and multinational companies. We believe these policies would put Thailand on a strong foothold to serve as a regional connector to support closer economic integration.

Last but not least, let me once again thank the FCCT for organizing this forum. The road ahead for the Thai economy indeed brings new opportunities as well as challenges, urging us to adjust ahead of the changing conditions. Being among policymakers, businesses, and journalists who gather here tonight, I hope we will continue to work together on the route to enhancing competitiveness and sustainable development of Thailand.

Kob Khun Krub.