"The Thai Economy: The Current State and The Way Forward"

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Mr. Shingo Sato, President of the Japanese Chamber of Commerce,
Members of the JCC Board, JCC members,
Distinguished guests, ladies and gentlemen,

A very good evening to you,

First of all, I would like to thank the Japanese Chamber of Commerce for inviting me again to share with you my thoughts on the prospect of the Thai economy. Last year, I truly enjoyed the exchange of views, ideas, and information with all of you and certainly hoped many of you did so too.

With more than 5,000 Japanese firms actively operating in Thailand across various industries, Japan is certainly one of Thailand's most important business partners in both the real and the financial sectors. Indeed, as Thailand is trying to move towards more innovative and high value-added industries, it is encouraging to see Japan continuing to be at the top among countries that applied for privileges under the new BOI investment promotion scheme in 2016. This would not happen if Japanese professionals already on the ground like yourselves did not have strong confidence in the long-term prospect of the Thai economy.

Ladies and gentlemen,

My talk this evening will consist of two parts. In the former part, I will briefly discuss the current state of the Thai economy, paying special attention to its resilience and growth momentum. In the latter part, I will share with you my thoughts on the way the Thai economy is moving forward as well as opportunities for Japanese businesses.

Let me start with the first part, by reviewing what we went through last year. I believe you all agree with me that 2016 was full of unexpected events and turns. On the domestic front, we faced with a severe drought early in the year followed by a historic flood in the South around the end of the year, and of course the passing of His Majesty the late King Bhumibol, which caused all Thai people the greatest sorrow. Also, the government's crackdown of illegal tour operators led to temporary yet significant effects on the tourism industry which had been a major growth driver of the economy in the past few years. On the external front, we saw the Bank of Japan's adopting a negative interest rate policy in January of last year, an unease over the fate of European financial institutions, the Brexit vote, and the unexpected outcome of the U.S. presidential election.

Yet the Thai economy was able to weather these storms, one after another, and ended up with a 3.2 percent growth with all stability intact. The resilience reflected the underlying strength of the economy which owed partly to preemptive policies to create shock absorbers for the economy such as ample international reserves and ample banks' capital base and loan loss provision. In addition to these buffers, the government responded swiftly once adverse shocks occurred especially with additional fiscal measures, including, soft loans for farmers and low-income earners and allowing travelling and shopping expenses to be tax deductible temporarily.

So, what about 2017—when uncertainty appears to loom even larger than last year especially on the global front?

Against the backdrop of improving global economy, risks to global growth continue to run high. The number one risk, in my assessment, is the direction of global trade and investments after the U.S. Presidential election. Yet there are others that cannot be ignored. These include China's highly leveraged corporate debt problem and financial stability concerns, political developments in Europe, the deep-rooted problems in the European banking sector, and geopolitical risks in Northeast Asia and the South China Sea. All these factors could result in significant financial market volatility and easily derail the global economic recovery.

Even so, I believe the Thai economy and the Thai financial system will remain resilient to withstand these challenges. As you have seen, the impacts of adverse external shocks on Thai financial markets have so far been limited, unlike many emerging market economies, thanks to our robust external position. We have international reserves greater than three times of short-term external debt. Compared with more than 30 percent on average in emerging markets in this region, foreign ownership of Thailand's public sector bonds amounts to less than 9 percent[1]. Thailand is, therefore, relatively less prone to capital flight, should foreign investors change their sentiments and expectations. Moreover, Thailand's corporate sector has relatively low external debt financing. External corporate debt amounts to around 13 percent of total corporate debt, with a majority belonging to large corporations for financing overseas investment, and these firms tend to manage exchange rate risks well.

On top of these external buffers is the fact that our growth engines in 2017 are firmer and more balanced than last year. Most importantly, both exports and to a lesser extent private investment have shown signs of a more broad-based and sustained pickup in recent

[1] Including Bank of Thailand bonds

months. Given that the export recovery is now a regional phenomenon, we expect the trend to continue. On exports of services, the tourism sector, which was temporarily affected by the crackdown of illegal tour operators in the fourth quarter of last year, has recovered faster than expected.

At the same time, fiscal stimulus remains an important growth driver with the additional mid-year budget and the implementation of the medium-term public infrastructure investment program. Apart from improved government disbursement, the government has proposed the supplementary budget for fiscal year 2017 amounting to 190 billion baht, which is over 1% of GDP on top of the originally planned budget deficit of 2.6% of GDP. In addition, fiscal policy will continue to be expansionary with a budget deficit of 2.9% of GDP proposed for the fiscal year 2018.

Despite the continued sizable budget deficit, there are fiscal buffers to cushion against unexpected difficulties ahead. The public debt to GDP ratio currently at 43 percent is projected to stand well below the sustainability ceiling under the ongoing fiscal reform.

In coordination with the expansionary fiscal policy, monetary policy remains accommodative to reinforce the economic recovery. The Monetary Policy Committee (MPC) has decided to keep the policy interest rate on hold at a low level since April 2015. Yet the MPC deems that monetary conditions should remain conducive until the economic recovery becomes more broad-based and more robust. For the future, the MPC's decision on monetary policy will be carefully balanced between accommodating economic recovery and avoiding financial stability risks that could result from an extended period of low interest rates.

Ladies and gentlemen,

To wrap things up before I move to the second part of my talk, the Thai economic recovery has become more **broad-based** with a **firmer momentum compared with last year** while our economy has **relatively strong buffers** compared to emerging-market peers in the region.

Now let me turn to **the way forward for the Thai economy**. With the short-term trajectory of the Thai economy holding up well thanks to the first two 'arrows' as in the Abenomics terms, namely fiscal stimulus and monetary easing, **Thailand's long-term future depends critically on the success of the third arrow of 'structural reforms'**. This brings me to the second part of my talk tonight on the way forward for the Thai economy, and how we and our partners like Japanese businesses may work together towards sustainable economic prosperity.

While dealing with short-term issues, we need to pay attention to long-term challenges that could restrain our competitiveness, productivity, and growth potential. The rising trend of disruptive technology will also come into play as it brings both opportunities and threats. To tackle these long-term challenges, structural reforms are underway to upgrade and unlock our economic potential in the long term.

The government has made structural reform a national agenda and has launched several important initiatives. One of our main focuses is to upgrade **connectivity infrastructure** within Thailand and within the region, including roadways, railways, waterways, power lines, air networks, and digital networks. This strategy will establish Thailand as a center for regional transportation and logistics, connecting the Indian Ocean with the Pacific Ocean, as well as connecting Thailand with South China and neighboring CLMV countries.

Beyond building physical infrastructure, the government is pushing forward to **restructure the Thai economy towards a high-value and innovation-driven economy under the 'Thailand 4.0' theme**. This policy focuses on promoting targeted industries, including the **'new S-curve'** industries. As many of you are well aware, the Board of Investment (BOI) revised the criteria for investment promotion privileges to be based on the value added content of the project rather than on its location as in the past. Thailand's economic model will be geared towards sophisticated high-valued manufacturing, innovative manufacturing, and modern services. This can be done by focusing on promoting technology, creativity, research and innovation, especially with respect to IT-based services.

In addition, the government is undergoing an overhaul of **the legal frameworks,** which need to catch up with the fast changing world, and new business practices. In my view, legal reform is the area that has not been well appreciated or perhaps well communicated to the foreign investor community. Let me take this opportunity to inform you of some significant legal amendments. In so doing, I would like to briefly categorize the **ongoing legal reform into three broad groups**.

<u>The first group is to improve governance and distribution of economic opportunity</u>. For instance, the amended **Securities and Exchange Act** will boost governance and fairer trading environment in the Thai capital market with more effective enforcement mechanism to punish market misconduct as well as broader coverage of wrongdoings to prevent malpractices. The new bill on the **governance of state-owned enterprises**, or SOEs in short, aims to tackle the governance within the SOEs system, as government agencies involved with SOEs often assume multiple, and sometimes conflicting, roles – namely, being policymaker, regulator, operator, and owner at the same time. The bill will set principles to dismantle these distinct roles into separate governing entities. The revision of the **Trade Competition Act** will ensure a fairer and more competitive environment among business. Lastly, the **Business Securities Act** helps improve credit access for small and medium sized firms to funding by allowing inventories, machineries, and intellectual property as collateral.

The second group of legal amendments aims to enhance productivity. There are four laws that might be of your interest. The **Licensing Facilitation Act** helps acquiring permits easier and more transparent for all businesses. The **Royal Decree on Review of Laws and Regulations** requires that all laws and regulations be reviewed once every five years to ensure that necessary adjustment be made to accommodate dynamic changes in business practices. The **Payment System Bill** is meant to replace the old governing laws and regulations that are dispersed under many different authorities, especially electronics and digital payments, and allow the Bank of Thailand to be the sole regulator in this field. The **Eastern Economic Corridor Bill** will establish a special economic zone across three provinces to attract investment in industries of the future with extensive infrastructure investments to support transport, logistics, and public utilities.

The last group of legal reform is to strengthen long-term sustainability. The **Fiscal Responsibility Bill** will impose fiscal discipline through improvement in public spending transparency and governance of overall fiscal management. More importantly, future governments will find it very difficult to conduct open-ended populist policies, as the law will require the government to calculate costs and identify sources of fund ex-ante. The introduction of the **Inheritance Tax Act** and the **Land and Building Tax Bill** will augment prudent spending by expanding the government's ability to collect revenue and ensure a better tax structure to deal with future liabilities, promote greater fiscal balance, and reduce wealth inequality.

All these developments will promote administrative efficiency and improve ease of doing business in Thailand. Putting the aforementioned laws into practice will change Thailand's business and financial landscape regardless of which political party steps into power after the next election. They will contribute to better governance and equality, higher productivity, and long-term sustainability of the country. However, I should point out that, as for all reform initiatives, effectiveness in execution will be the bottom line of their success.

Ladies and gentlemen,

As for the Bank of Thailand, we also play an important role in **upgrading Thailand's financial infrastructure and regulatory reform** within our responsibility**.** In the pursuit of the digital economy, the government aims to involve all stakeholders to transform Thailand to a **less-cash society** under the **National e-Payment master plan**. In conjunction with the Ministry of Finance and the Thai Bankers' Association, we have recently launched the **PromptPay** system, which is an electronic faster payment system. It helps facilitate payment transactions and save costs for businesses and consumers. This morning I also witnessed the signing of an agreement with two banks; consortium to roll out EDC machines to 560,000 shops and government agencies all over the country to promote the use of debit cards on a nation-wide basis.

The Bank of Thailand also aims to **promote competition, innovation, and digital financial services among financial service providers** (including **FinTech**). This move will benefit financial institutions, businesses as well as Thai citizens. In addition, we will encourage niche players to help narrow gaps in access to financial services. In this regard, we have recently announced the regulatory regime using a "Sandbox" approach. **The Regulatory Sandbox** will allow FinTech firms and financial institutions to test the viability of their products and services in a well-defined space and duration, without being fully subject to all regulatory requirements that are normally applicable. This approach helps us assess risks arising from the proposed products and services, and provide sufficient consumer protection.

The Bank of Thailand also recognizes that **regulatory reform** is crucial for competitiveness of firms operating in Thailand. To this end, we are in the process of streamlining regulations using **the Regulatory Guillotine** concept to review and simplify many sets of regulations, starting with those governing capital flows and foreign exchange transactions. This reform is currently in the process of public consultation.

Lastly, in addition to **upgrading our physical, financial, and legal infrastructure through structural reforms, the ability to reach out to regional economies given Thailand's strategic position** will be important. For our part, the Bank of Thailand promotes greater **'financial' connectivity**, for example through promoting local currency usage in the region and regulatory harmonization, particularly with CLMV, our neighboring countries with high growth potential. Such initiatives will lower financial transaction costs, spur more trade and investment and deepen regional financial integration.

Ladies and Gentlemen,

I hope my talk tonight has provided you with an overview of where Thailand is heading in both the near future and the longer term. In the world of volatility and uncertainty, you can be assured that the Bank of Thailand will do our best to minimize adverse impacts from unexpected shocks that may prevent us from reaching our goal of sustainable and inclusive economic growth.

Again, it is my great honor to be here with our partners who have supported Thailand's economic and financial advancement. Going forward, we are confident that Japan, Thailand, and the region will collectively benefit from broader and deeper linkages both economically and financially. Thank you very much for your friendship, commitment, and contribution to the Thai economy. I look forward to our enhanced collaboration for many years to come.