"Thai Economy: The Current State and the Way Forward"
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Distinguished guests,

Ladies and gentlemen,

A very good morning to you all.

I would like to thank Nomura for inviting me here to share my thoughts on the current state and outlook of the Thai economy.

For today's talk, I have two main agendas. First, I will talk about the current state of the Thai economy where I will discuss recent developments and its prospect ahead. Second, I will talk about Bank of Thailand's roles to help transform the Thai economy into one with greater productivity, better economic prospect, and more inclusivity.

As many of you know, the Thai economy has weathered several storms over the past few years. On the external front, changes in the political landscape and macroeconomic policies of major economies have brought about not only financial market volatility throughout the region but also greater uncertainty to global trade. On the domestic front, Thailand experienced major droughts and floods that affected agricultural prices and output, and most significantly the passing of His Majesty the late King Bhumibol a year and a half ago that caused the greatest grief and sorrow among all Thais. Yet the Thai economy stood firm and was able to continue expanding steadily, thanks to both sound economic fundamentals and a well-diversified economy which underpinned Thailand's resilience against shocks. In 2017, the Thai economy recovered markedly and achieved an annual GDP growth of 3.9 percent. Merchandise exports grew 9.7 percent in USD terms, highest in the past 6 years, and was one of the main drivers of growth. The tourism sector continued to perform well, with the number of tourists reaching new highs of over 35 million. The economy is expected to continue a strong momentum this year, with GDP growth in the first quarter registering an impressive rate of 4.8 % year on year, the highest in 5 years, with private investment growth recording a 3-year high.

Nevertheless, this recent economic upturn is different from the other episodes. Indeed, the GDP outturn and macroeconomic numbers showed strong improvements over the previous years, but a closer look revealed that growth was uneven across different segments of the economy. At the same time indicators such as the unemployment rate and NPL ratios were rising slightly between 2015 and 2017. This is contrary to what you would expect to see when the macroeconomy performs better. Although both unemployment rate and NPL ratios have recently stabilized, their developments reveal that some segments of the economy did not benefit much from the economic recovery. In my view, there are at least three reasons behind these developments.

First, the recovery has primarily been driven by external demand. Hence growth benefits are felt mostly by those associated with the external sectors. The robust recovery momentum on the global scale has resulted in a strong expansion of Thai exports across product categories and export destinations. In addition, the Thai tourism sector has grown consistently with steady increases in the number and quality of tourists. Therefore, it is not surprising to see businesses associated with exports of goods and services enjoying the benefits from the improved external demand. Domestic demand growth, however, is still proceeding at a gradual pace. Despite a continuous recovery, private consumption growth remains well below that of GDP, registering within the 3 percent range. And until recently, private investment growth had concentrated mainly in the export sector. Overall, the large current account surplus of 10.5 percent to GDP last year summarizes the pattern of economic recovery and reflects the imbalance between the external and domestic demand.

Second, the rural economy has been exposed to more adverse shocks than its urban counterpart. Specifically, several populist measures including the controversial rice pledging scheme were withdrawn, together with adverse weather conditions such as severe droughts in 2016 and floods in 2017 as well as declines in global prices of key export crops especially rubber and rice, all constituted negative income shocks to farmers. In addition, rural entrepreneurs, which are mostly SMEs, tend to be less productive and might not be able to compete with larger firms who are better equipped with capital and technologies. Thus, larger and productive firms are able to reap the benefits of economic recovery and adapt to changes in the new business environment. Indeed, the difference in business performance between medium-sized and large firms in the stock market has been widening. This is evidenced by several financial indicators including the return on assets and the net profit margin. These developments partly explains why the NPL situation has yet to improve for SMEs across the board, while we see improvement in loan quality among large corporates in the same sectors.

The third reason for the uneven economic recovery is the impaired function of the spending multiplier. Usually, when recovery starts to emerge in certain segments of the economy, the multiplier effect of spending should create positive spillovers to the other parts of the economy, thereby securing a more broad-based recovery over time. However, export-oriented firms which currently spearhead the ongoing economic recovery are capital-intensive. They utilize more machinery rather than relying on labor. Thus, positive spillovers to employment are less prevailing. This partly explains why the manufacturing employment growth has been rather moderate despite strong export growth and pickup in the manufacturing production index.

Furthermore, having a high level of household debt, especially during the debt deleveraging period, dampens this multiplier mechanism. This is because households have to use additional income to service their debt obligations rather than spending on goods and services. While there are signs of household debt being deleveraged, as reflected by a continuous decline in the ratio of household debt to GDP which fell from 79.0 percent in 2016 to 77.5 percent by the end of last year, debt burden remains high especially for lower-income households.

Ladies and gentlemen,

I have been talking about factors behind the uneven economic performance of the last few years. Going forward, the economic recovery is expected to be more broad-based and I want to highlight a few of these positive developments.

First, export growth, our main growth driver, is becoming more broad-based as growth has now extended beyond larger players. In fact, export growth rate of SMEs has become more or less on par with that of larger firms. Domestic demand is also gaining traction with a steady growth in private consumption, and a pickup in private investment since the third quarter of last year especially from imports of capital goods.

Second, the government has directly stepped up various stimulus measures to support the rural economy. Last year, the government introduced the supplementary budget with a particular focus on local infrastructure development, and the Welfare Card Scheme which aimed to support daily expenditures among poorer households. This year, the new supplementary budget is allocated to vocational training as part of the second phase of the Welfare Card Scheme, development of local community enterprises, as well as water resource development to improve productivity within the agricultural sector. This, together with the increase in the minimum wage in April, will support the rural economy and the well-being of the lower-income group.

Third, the multiplier effects should improve on the back of increasing public and private investment. While some of the government infrastructure projects were deferred from last year partly due to the new government procurement system. This year progress should have a better outlook since many projects have gone through the bidding and procurement processes, with material progress underway. These projects include, among others, 4 of the 5 dual-track railway projects that would greatly improve upon the logistics network between major cities and industrial estates in central and northeastern Thailand. We can expect to see these dual-track railways up and running from 2019 and 2020 onwards. Our Mass Transit System is also being upgraded with 3 new metro lines in Bangkok that will extend from key stations in the cities to residential areas in outer Bangkok. Two of these projects, particularly the Green and Orange lines, are under construction and should be completed by 2021 and 2023, respectively. Other infrastructure projects in construction include the Bangkok-Korat high speed train and the expansion of the Suvarnabhumi Airport which are also expected to be completed in a few years. On the private side, private investment is expected to gain further momentum as evidenced by growing imports of capital goods as well as investment spending in machinery and equipment. This is in line with private credit growth which has picked up since the beginning of 2017.

Given these outlooks, we expect the growth momentum to be more balanced with a stronger contribution from domestic demand. In our March forecast, the GDP growth for both 2018 and 2019 was projected at 4.1 percent. These figures are likely to be revised up given better-than-expected growth outturns in the first quarter this year. Headline inflation in April and May has turned up above the lower bound of our target, which is set at 2.5±1.5%, mainly due to the recent pickup in energy prices. Yet inflationary pressure remains soft overall and we must continue to closely monitor inflation developments once these supply-driven fluctuations fade. Over time, improvement in domestic demand and rising energy prices are expected to bring about higher inflation, although it is likely that headline inflation would still remain below the midpoint of the target over the year. For now, an accommodative monetary policy stance would be maintained to foster a strong economic growth and facilitate the return of inflation to the target. Going forward, the Monetary Policy Committee will closely monitor the strength of growth momentum, inflationary pressure as well as underpricing of risks in the financial system that could lead to financial fragility and financial stability concerns.

Ladies and gentlemen,

So far, I have given you an overall near-term summary of the Thai economy. Let me now move on to the second part of my talk which looks further into the backbone of Thailand's economic growth engine over a longer horizon. In particular, I want to focus on Bank of Thailand's roles to help transform the Thai economy into one that is more efficient, more productive, and more inclusive.

But before doing so, let me give you a quick summary on a broader perspective regarding the new economic platforms in Thailand which have emerged over the past few years. Chief among them is the new investment platform in the Eastern Economic Corridor or the EEC in short. The EEC, as many of you know, is an economic zone specifically designed to bring about large infrastructure upgrades and provide extensive investment incentives for high value-added industries. The continuity of this investment platform is ensured regardless of any political changes now that the EEC Act has come into effect since May. Last year, we have seen the value of net investment applications under the Thailand Board of Investment privilege program grew by 23 percent, almost half of which are investment in the EEC. The high speed train project to connect U-Tapao Airport with major cities within the EEC and two main airports in Bangkok has been announced with the TOR of this project now available for potential bidders. The TOR for Laem Chabang seaport upgrade will also be announced in a few months' time.

In addition to the EEC Act, various legal amendments and process improvements were implemented over the past couple of years to improve the ease of doing business in Thailand and ensure that laws can be adjusted to accommodate new business practices in a timely manner. With these reforms, Thailand's position in the World Bank's Doing Business Ranking improved from 46th in 2017 to 26th in 2018, and we should continue to see further improvements in the ease of doing business in Thailand going forward.

Another important development, which provides a strong foundation for digital economy, is the nationwide broadband internet project. Over the past years, the project has brought fiber optics network to almost 25,000 villages in remote parts of the country, enabling access to free-WiFi hotspots as well as home broadband at affordable prices. As such, human capital development can improve greatly through better access to online information, remote education, and online healthcare services. Business opportunity can also be greatly expanded with greater access to online marketing platforms and more cost-effective communication tools. This new and expanded online connectivity is a critical milestone which will bring economic opportunity and productivity to people in the rural area whose potential has been limited by the previous lack of supportive infrastructure to connect with the modern world.

Ladies and gentleman,

Let me now turn to Bank of Thailand's initiatives to help uplift Thailand's long-term competitiveness. Thailand is transitioning to a new era of digital payment system and financial technology in which the Bank of Thailand is fully committed to foster.

First and foremost, electronic payment infrastructures must be put in place to realize the full potential of digital economy. Under the National e-Payment Masterplan, last year the Bank of Thailand together with the Ministry of Finance and the Thai Bankers' Association launched our new faster payment system – PromptPay – which propelled the wider adoption of e-payment in Thailand. PromptPay is an instant payment platform that links bank accounts to various forms of identification including national ID numbers and mobile phone numbers. With PromptPay, funds can be transferred to a recipient's preferred bank account in real time and at virtually no cost. This new technology has significantly boosted the usage of mobile banking, and has potential to lead to significant growth in e-commerce in Thailand as well as to radically change the way government welfare payments are distributed. In just over a year since the launch of PromptPay, there are over 40 million IDs registered on the platform and more than 2.7 million transactions a day. The increasing usage of PromptPay also served as a catalyst that eventually led to the announcements of most commercial banks two months ago, to eliminate transfer fees for all transfers through mobile and online banking. All in all, PromptPay provides a crucial payment infrastructure which opens the door to many other digital payment services.

Another initiative of the Bank of Thailand to promote digital payment services is the Thai standard QR code for payment. The Standardized QR Code makes e-payment seamless across platforms regardless of which bank or non-bank service provider merchants and consumers are using. In just eight months since its implementations, more than two million merchants in Thailand now accept e-payment through QR code, and this figure will continue to grow. Having a common standard for QR code will indeed generate benefits beyond payment convenience. The common standard will help ensure that no incumbent service providers has an advantage of locking merchants with their QR formats, and allow new and innovative payment service providers to easily enter the market. The standard will also help facilitate the move towards information-based lending for SMEs as their payment transaction information can be consolidated. Given that the payment standard was developed together with five global credit card companies using EMVCo, it could serve as a platform to enhance financial connectivity in the region. Thai banks and payment service providers have begun to work with partners in our neighboring countries to facilitate cross-border payments using the standardized QR code.

This standardized QR code was a product that went through the Bank of Thailand's regulatory sandbox. Going forward, there are a few high-impact technologies or applications which are being developed and tested in the Bank of Thailand's regulatory sandbox. The first one is an extension of our standardized QR code to include other means of payment, including credit card. This could bring down the number of fraudulent transactions, and markedly reduce the merchant discount fees for credit card payments.

The second one is the blockchain technology which we are working closely with the financial industry to apply them to various banking applications. 'Thailand Blockchain Community Initiative' was officially announced at the Bangkok FinTech Fair in March of this year. This initiative is a collaboration between 14 Thai banks and 7 leading businesses and state-owned enterprises to utilize blockchain technology in financial services, starting with a pilot project to offer blockchain-based letters of guarantee. This project is expected to become operational in the second half of this year. On a longer horizon, the blockchain technology is also planned to be applied to supply chain finance to improve authentication efficiency which would facilitate real sector activities. Other blockchain related projects in the pipeline include scriptless bond issuance which would significantly speed up saving bond allocation to retail investors from 15 days to 2 days, as well as granting more flexibility for bond issuers. The proof-of-concept of this project is almost complete, and production is expected to begin in the very near future. Another project in the pipeline is the "Project Inthanon" in which the Bank of Thailand and banks will co-develop a new way of conducting interbank settlement using wholesale central bank digital currency or CBDCs. Like other central banks, our goal is not to immediately bring CBDC into use, but rather to explore its potential and implications for back office operations. These efforts should pave way for faster and cheaper transaction and validation due to less intermediation process needed compared to the current systems.

So far, I have discussed the Bank of Thailand's role as a catalyst for digital infrastructure development and as a facilitator of innovation. One should not forget that our core mandate is being a regulator to safeguard financial stability. To this end, we proposed the new Payment Systems Act which became effective earlier this April. The Act unifies previously fragmented payment laws and regulations under a single Act, and empowers the Bank of Thailand with the authority to both regulate and oversee development of Thai payment systems in a manner conducive to new payment innovations. Beside the Payment Systems Act, supervisory practices are also being updated to improve and safeguard cyber security risks. The updated guidelines on management of information technology risks of financial institutions were released in December last year to ensure that banks have appropriate governance structure in place and can swiftly respond in the event of cyberattacks. Our efforts also extend to ensuring safety of the payment system, and awareness among both financial service providers and consumers.

Let me now turn to another area that is important for our region, which is the promotion of regional financial connectivity. Over the years, the Bank of Thailand has made multiple arrangements with regional central banks to support the use of local and regional currencies in trade and investment. This will reduce transaction costs and mitigate exchange rate risks under today's volatile financial market conditions. In addition, direct exchange rate quotations for currency pairs involving the Thai baht are now available including the Chinese Yuan, the Malaysian Ringgit, the Indonesian Rupiah, and, most recently, the Japanese Yen.

On top of promoting local currency usage, the Foreign Exchange Regulation Reform implemented last year would further complement regional financial connectivity by making foreign exchange-related transactions more flexible and accessible. To give a few examples, foreign exchange transaction form was completely abolished; qualified companies are now allowed to conduct foreign exchange transactions and hedging based on their own risk management practices without having to request for approval on a transactional basis; commercial banks are also allowed to provide loans in Thai baht to non-residents investing in the region; and the coverage of qualified investors allowed to directly invest abroad has been expanded to include retail investors within a wider range of wealth.

All in all, the outlook and prospect of digitalization and regional financial integration look very promising and the Bank of Thailand will continue to facilitate timely development of new financial innovations while also safeguarding financial stability in an efficient and business-friendly manner to ensure a smooth and successful transition of the Thai economy.

Ladies and gentleman,

I have now come to the end of my talk and let me give you a brief summary of what I have said today. The Thai economy continues to expand at a good pace with merchandise exports and tourism so far being the main drivers of growth. Although growth benefits have not spilled over to other segments of the economy as much as we would like to see, domestic demand is improving and we expect a more robust and more balanced GDP growth this year. On a longer horizon, Thailand is undergoing major transformation with the emergence of several promising economic platforms and the ongoing transition towards a new era of digital financial and payment services, all of which will unlock Thailand's economic potential, uplift productivity, and bring about more inclusive growth. The Thai government and the Bank of Thailand, in its various capacities, are committed to making these achievements possible.

Thank you very much for your attention.