

Thailand Business Forecast Report Q4 2013

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Abstracts

Core Views

Thailand is technically in recession with the economy having contracted for two consecutive quarters – seasonally-adjusted real GDP growth came in at a negative 0.3% quarter-on-quarter (q-o-q) in Q213, following a contraction of 1.7% in Q113. Crucially, private consumption and gross fixed capital formation are also beginning to witness some signs of slowing down. We expect cooling external demand to continue to drag on the overall economy and that full-year real GDP growth will come in relatively weak at just 4.0%, compared to the Bloomberg consensus of 4.8%.

In light of the difficulties in withdrawing the rice policy without fuelling widespread unrest and losing support from voters, we see a risk that the government may choose to kick the can further down the road, resulting in a protracted delay in bringing the budget back into balance. Our forecasts for Thailand's budget deficit to narrow only gradually, before eventually balancing out by around 2017, reflect our concerns that the government is likely to face significant delays before getting its finances back in order.

Our view that China's economic growth will continue to deteriorate as we head into 2014, and that this will weigh on external demand across South East Asia, and in turn, Thailand's export sector, remains a key factor underpinning our cautious outlook on the Thai baht in the medium term. Nonetheless, given Thailand's robust macroeconomic fundamentals – bullish outlook for automobile exports and the country's leading position as a major exporter of rice and other agricultural produce in the region – we continue to see the country running a balanced current account going forward.

Major Forecast Changes

We have revised our currency forecasts to account for the recent collapse of the Thai

baht against the US dollar and to reflect our neutral outlook on the current account. We forecast the Thai baht to average THB30.70/US\$ and THB31.00/US\$ for 2013 and 2014, respectively.

Key Risk To Outlook

Downside Growth Risks From Deteriorating Fiscal Position: In the event of a substantial decline in rice prices over the coming months, we could see the government suffering massive losses as a result of its rice policy. This could weigh on the government's ability to finance large-scale investment projects, resulting in project delays and putting downward pressure on economic growth.

Upside Long-Term Growth Risks From Political Reconciliation: Political uncertainties have resulted in depressed foreign direct investment in the economy. However, reconciliation efforts and economic reforms to distribute wealth more equally among the population could eventually help to bridge the political divide in Thailand. This would provide a significant boost to investor sentiment and pave the way for a surge in foreign direct investment inflows and robust economic growth.

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Thailand's political situation will remain highly volatile, and it is difficult to envision political stability over the next few years. In the event of prolonged social unrest, we do not preclude another military coup occurring, although this would by no means resolve matters.

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Domestic Demand Weaknesses Support Downbeat View

We expect cooling external demand to continue to weigh on Thailand's economic outlook over the coming quarters. Moreover, private consumption and gross fixed capital formation are also beginning to show signs of weakness, amplifying the downside risks for our already below-consensus view on the economy.

Monetary Policy

Monetary Normalisation To Come Only In 2015

Our short-term view is generally in line with the Bank of Thailand (BoT)'s decision to keep its policy rate on hold at 2.50% during its monetary policy in August. Money supply growth is accelerating and remains uncomfortably high for the BoT. However, we expect monetary normalisation to come much later in 2015 as a result of the relatively fragile

economic recovery.

Balance Of Payments

Foreign Capital Outflows To Weigh On The Baht

China's economic slowdown, which will weigh on external demand across South East Asia, and in turn, Thailand's export sector as we head into 2014, remains a key factor underpinning our cautious outlook on the Thai baht in the medium term. Nonetheless, given Thailand's robust macroeconomic fundamentals – bullish outlook for automobile exports and the country's leading position as a major exporter of rice and other agricultural produce in the region – we continue to see the country running a balanced current account going forward.

Fiscal Policy

Failure To Withdraw Rice Subsidies A Major Risk For Fiscal Outlook

The lack of progress in addressing persistent budget deficits, exacerbated by the growing cost of maintaining the government's expensive rice policy, risks undermining long-term efforts to address Thailand's deteriorating fiscal position. In light of the difficulties in withdrawing the rice policy without fuelling widespread unrest, we expect the government to run budget shortfalls of 3.1% and 2.2% of GDP in 2013 and 2014, respectively, before achieving a balanced budget only by around 2017.

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