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SCB EIC expects the MPC to continue hiking policy rate 2 more times and keep it steady at 2% throughout 2023

25 January 2023

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KEY POINTS

The MPC votes unanimously to raise the policy rate 0.25% from 1.25% to 1.5%.

The Thai economy will continue to gain traction with continued recovery in tourism and private consumption thanks to the return of Chinese tourists. Meanwhile, merchandise exports will slow down this year but are expected to improve in 2024 in line with the global economic recovery. Headline inflation is expected to decline, whereas core inflation remains at a high level with increased risks from demand-side inflationary pressures due to the economic recovery. The Committee deems that a continuing gradual policy normalization is an appropriate course for monetary policy consistent with the growth and inflation outlook.

The MPC assesses that the Thai economy will continue expanding.

The tourism sector will exhibit a faster recovery following the return of Chinese tourists. This will contribute to a more broad-based improvement in employment and income of services sector and self-employed workers, which account a significant share of total employment. Such improvements will support the continued expansion of private consumption. Meanwhile, growth of merchandise exports will moderate this year, but is expected to resume in 2024 in tandem with global growth. The Committee assesses that downside risks to the global economy have decreased given the improving outlook in both advanced economies and China.

The MPC expects headline inflation to decline but risks of rising demand-side inflationary pressures must be monitored.

Supply-side inflationary pressures continue to dissipate along with a decline in global energy and commodity prices. Core inflation is expected to remain at a high level for some time before gradually decreasing. Meanwhile, medium-term inflation expectations remain anchored within the target range. However, there is a risk that core inflation would remain high for longer than expected owing to a potential increase in pass-through given elevated costs. Moreover, the tourism recovery could increase demand-side inflationary pressures.

The MPC assesses that financial system remains resilient but overall financial conditions are less accommodative.

Debt serviceability of households and businesses has improved in line with the economic recovery. However, the financial positions of some SMEs and households remain fragile and sensitive to the rising living costs and debt burden. Funding costs have risen in tandem with the policy rate increases as well as the expiration of reduction in the Financial Institutions Development Fund (FIDF) contribution. However, bank lending and bond issuances continue to increase. The baht against the US dollar has appreciated owing to expectations of a less aggressive tightening of the Fed as well as China's relaxation of international travel restrictions which would benefit the Thai tourism sector.

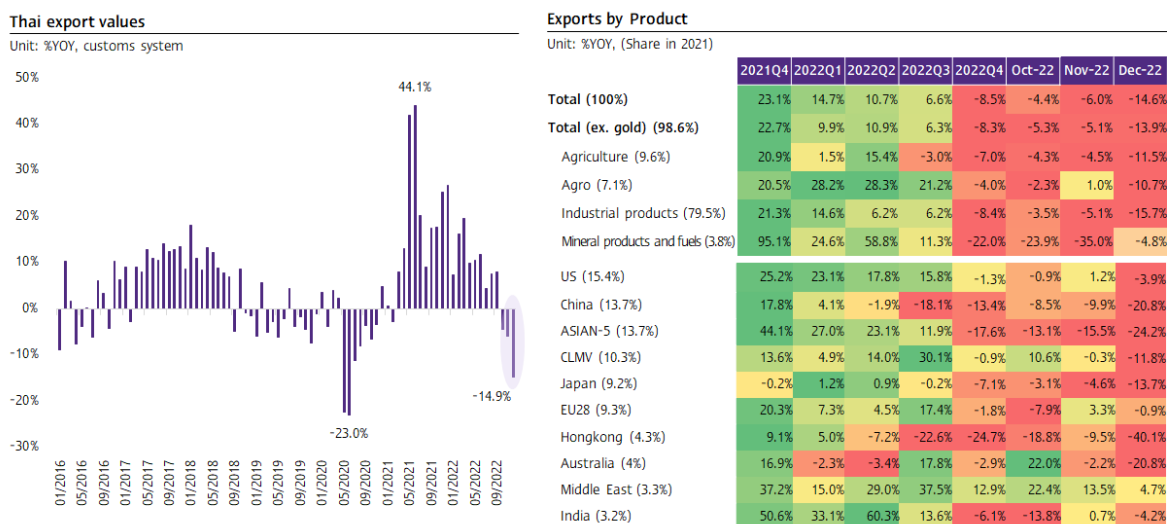
IMPLICATIONS

SCB EIC expects the MPC to continue hiking policy rate 2 more times to stand at 2% this year.

The MPC will likely continue raising policy rate at the meetings in March and May 2023, 0.25% at each meeting, and is expected to keep the policy rate steady at 2% throughout this year. The policy rate can therefore be gradually normalized to the level consistent with sustainable growth in the long term. SCB EIC expects the Thai economy to expand 3.4% in 2023 with key drivers coming from tourism and private consumption. A faster-than-expected China reopening will result in an increase in Chinese tourist arrivals this year, which would benefit businesses in tourism and related services. Such improvement will support private consumption to continue expanding. However, the outlook for Thai merchandise exports may not so bright as seen in a drop in Thai export value in Q4/2022 (Figure 1) in line with the global economic slowdown. This year's exports could also face additional pressures from the new import tariffs implemented by key trading partners¹ including EU and India, some of which are effective this year. Thai export value is thus projected to expand by only 1.2% in 2023.

¹ The European Union has announced the two new environmental taxes, namely (1) Carbon Border Adjustment Mechanism, which will affect Thai exports of key products to the EU including steel, machinery, electronic circuits, rubber products, and computers; and (2) Regulation for Deforestation-Free Products, which covers Thai exports to the EU including palm oil, wood, rubber products. Meanwhile, Indian government plans to increase customs duty on 35 items which will likely cover key products exported to India including plastic products, gems, and jewellery.

Figure 1: Thai export value dropped in Q4/2022, while the outlook for Thai exports may not be so bright in 2023 given the global economic slowdown



Source : SCB EIC analysis based on data from Bloomberg

Headline inflation will likely slow down in 2023 but will still be above the BOT target range.

Headline inflation grew 6.1% in 2022 (Figure 2). SCB EIC expects headline inflation to gradually fall to 3.2% in 2023, which will still be higher than the target range of 1-3%. This is because domestic energy and food prices remain high with core inflation accelerating. Core inflation is projected to slightly speed up to 2.7% from 2.5% in 2022 driven by a more broad-based passthrough to prices of goods and services in other categories as businesses have also passed on the rising costs to prices of consumer products along with the economic recovery. Domestic demand recovery could also increase demand-pull inflationary pressures. Moreover, Thailand’s inflation could face risks from several factors including China’s reopening, global climate change, COVID-19 outbreak, and geopolitical issues, which could increase upside risks to inflation.

Figure 2 : Thailand's inflation grew 6.1%YOY in 2022 but will likely slow down to 3.2%YOY in 2023

Consumer price index classified by product's type

	%YoY	Share	2021	Oct-22	Nov-22	Dec-22	2022
Total		100%	1.2%	6.0%	5.5%	5.9%	6.1%
Food and Non-Alcohol		40.4%	-0.1%	9.6%	8.4%	8.9%	6.9%
fresh food		20.6%	-1.0%	10.5%	8.1%	8.9%	6.8%
- Meats		3.5%	2.3%	26.4%	23.5%	19.9%	21.1%
- Prepared Food: at Home		8.7%	0.4%	9.5%	9.7%	9.9%	7.5%
- Prepared Food: Food Away From Home		6.7%	0.5%	8.8%	9.2%	9.3%	7.0%
Apparel & Footwears		2.2%	-0.3%	0.2%	0.3%	0.3%	0.0%
Housing & Furnishing		23.2%	-1.7%	3.6%	3.5%	3.5%	4.7%
Electricity, Fuel, Water Supply		5.5%	-7.3%	13.2%	13.2%	13.0%	20.8%
Medical & Personal Care		5.7%	0.2%	1.6%	1.9%	1.8%	1.1%
Transport & Communication		22.7%	7.7%	4.8%	4.9%	5.7%	9.1%
Recreation, Reading, Education and Religion		4.5%	-0.4%	1.3%	1.4%	1.4%	0.2%
Tobacco & Alcoholic Beverages		1.4%	0.3%	1.9%	1.4%	1.3%	2.0%
Core Consumer Price Index		67.1%	0.2%	3.2%	3.2%	3.2%	2.5%

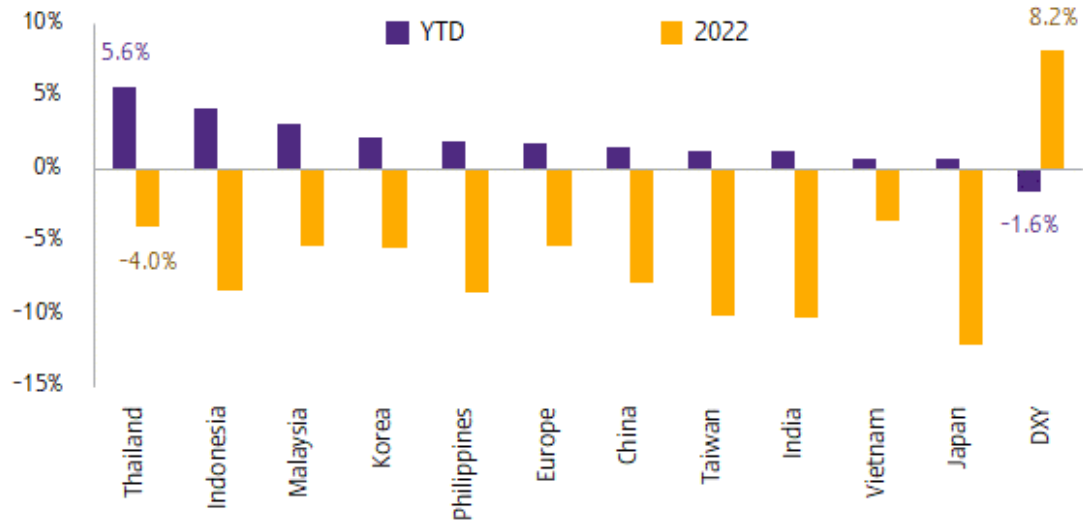
Source : SCB EIC analysis based on data from the Ministry of Commerce

Thai baht will likely continue to strengthen in 2023 to the range of 31.5-32.5 baht per USD at the end of the year. Since the beginning of 2023, the baht strengthened rapidly, outperforming other regional currencies, as a result of USD depreciation and the positive Thai economic outlook given that it will benefit much from China's reopening. The baht thus strengthened 5.6% since the beginning of the year (Figure 3) and will likely continue to strengthen this year in line with improving Thai economic fundamentals propelled by tourism recovery and current account surplus. As a result, capital inflows to the Thai financial markets will likely continue supported by improving investor confidence. Moreover, USD will likely weaken this year due to a less aggressive tightening of the Fed and economic risks. The baht will likely stay in the range of 32.5-33.5 baht per USD in the first half of this year and is expected to strengthen in the latter half of the year to the range of 31.5-32.5 baht per USD.

Figure 3 : Since the start of 2023, the baht appreciated 5%, the strongest in the region

Change in currencies against USD

Unit: % (As of Jan 25, 2023)



Source : SCB EIC analysis based on data from Bloomberg

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