



# Thailand

## Economic Assessment

**G**DP growth slowed to 6.6% in the first quarter of 2004, from the 7.8% burst in the fourth quarter of 2003, and decelerated further to 6.3% in the second quarter. The deceleration was largely attributable to a long drought, avian flu, rising oil costs, and tensions in the southern provinces.

For the first half of 2004, GDP grew by 6.4%, with private consumption again the main driver, making a contribution of 3.2 percentage points. Nevertheless, growth in private consumption, which accounts for more than 50% of GDP, slowed from 7.1% in the last quarter of 2003 to 6.1% and to 5.5% in the following 2 quarters, as consumer confidence was affected by the factors listed above.

Investment growth, which accounts for about 20% of GDP, decelerated from almost 20% in the last quarter of 2003 to 16.2% and to 12.1% in the next 2 quarters. Private investment recorded more stable expansion of around 17% during the first half year. Gross fixed capital formation contributed 2.9% to total GDP growth in the half.

Both the business sentiment index and the consumer confidence index have generally been positive, though slightly affected at times by the negative factors. Export demand remained buoyant in the first half but was outpaced by imports, such that net exports subtracted 2.0 percentage points from GDP growth.

On the supply side, slower GDP growth was almost entirely due to the performance of agriculture. Agricultural production fell by 2.6% in the first quarter and dropped a further 7.5% in the second, after a strong performance in the last 2 quarters of 2003. This significant slowdown was the result of a prolonged drought and the impact of avian flu on the poultry industry. Against this, prices of major crops stayed high, which supported farm incomes. The nonagri-

culture sectors grew steadily, by 7.7% in the first and second quarters of 2004. Manufacturing expansion slipped from 10.3% in the first quarter to 7.5% in the second. The services sector picked up, partly due to the low base in 2003 when the SARS outbreak hit tourism. Wholesale and retail trade grew at around 3–4%.

In the labor market, tightness was reported in several sectors, which helped push up real wages by 0.3% and 0.7% in the first and second quarters, respectively.

The Government's fiscal situation is on track. In the first 8 months of FY2004 (ending 30 September 2004), government revenues amounted to B659 billion while expenditures totaled B752 billion, putting the budget in deficit by B94 billion. After taking into account expenditures from external financing of B5 billion and a nonbudgetary surplus of B77 billion, the overall government balance was a deficit of B22 billion. Overall public debt stood at B2,850 billion as of 31 March, equivalent to 44.0% of GDP. This was down from B2,918 billion (49.7% of GDP) at end-FY2003. The ratio of central government debt to GDP also declined, from 27.4% in September 2003 to 24.8% in May 2004.

Inflation accelerated to 1.9% in the first quarter of 2004 and to 2.6% in the second. Inflationary pressures picked up due to rising oil and nonfuel commodity prices, together with the tightening of the labor market and higher capacity utilization in the industry sector. In the first 7 months of 2004, prices of agricultural products increased by 15.8%, while the rise in manufacturing product prices was contained at 2.9%. Core inflation (CPI excluding food and energy) was 0.3% in the first 7 months, still within the 2004 Bank of Thailand (BOT) inflation target. Liquidity growth measured by M2 also accelerated, to 6.4% in the first quarter of 2004, but in the second it slowed a little to 5.8%. Similarly, the pace of expansion in commercial bank credit picked up to

**Table 2.11 Selected Economic Indicators, Thailand, 2004–2005, %**

Item	2004		2005	
	ADO 2004 Update	ADO 2004 Update	ADO 2004 Update	ADO 2004 Update
GDP growth	7.2	6.4	6.2	6.6
Inflation (CPI)	2.4	2.8	2.6	2.6
Current account/GDP	3.9	4.0	3.9	4.0

Source: Staff estimates.

6.7% in April and 9.0% in June, due to increased lending to the corporate sector.

The Stock Exchange of Thailand Index has given back some of the large gains it made in 2003, when it more than doubled, declining by about 14% to mid-September from the start of the year. In the foreign exchange market, the baht averaged B40.3/\$1 in the second quarter, depreciating slightly from B39.2 in the first, and by mid-September it was quoted at around B41.3. Reasons for the softening included investors' concerns over rising oil prices and the unrest in southern provinces, foreign investors' net sales of Thai stocks, local oil companies' demand for dollars, and market concerns over higher US Federal Funds rates.

External performance remained strong through the first half of 2004. Exports grew by 20.9% in the first quarter and 24% in the second, as a result of higher exports of agricultural items and of manufactured products, such as electrical appliances, automobiles, and plastics. Export prices also climbed rapidly, by about 17% in the 6 months to 30 June. Concurrently, imports increased even faster, by 27.3% in the first quarter and 35.3% in the second. At midyear, the trade surplus was down to about \$100 million, compared with \$2.5 billion a year earlier, and contributed to a current account surplus of \$2.8 billion, from \$3.7 billion. International reserves stood at a comfortable level of \$43.5 billion at end-July, higher than the level before the Asian financial crisis in 1997–98.

External debt continued its steady decline of recent years, from \$51.8 billion at end-2003 to \$50.0 billion 6 months later, and the debt service ratio fell from 16.0% to 9.3%. Short-term debt accounted for about 23% of total external debt at midyear.

## Policy Developments

BOT raised the 14-day repurchase rate from 1.25% to 1.50% in August, concerned over the inflationary pressures caused by increasing capacity utilization, rising oil prices, and a tightening labor market. BOT had previously flagged that it might well move toward a gradual tightening of monetary policy.

With the economy reaching sustained growth supported by private investment, fiscal policy also tightened a little. In FY2004, the consolidated general government balance is expected to record a surplus of about 0.8% of GDP, larger than earlier projections, as a result of higher tax collection arising from the economic expansion. For FY2005, the Government is expected to propose a balanced budget, the first since the financial crisis.

Thailand continues to make advances on restructuring the financial and corporate sectors. The share of NPLs in total commercial bank lending was 13.1% in June 2004, slightly lower than 13.5% in January and down significantly from 16.8% in June 2003. However, Krung Thai Bank, a major financial institution, reported in July a sharp increase in its NPLs. Prudent financial sector management needs to be maintained to prevent higher levels of lending by the banks to the corporate, property, and household sectors from becoming NPLs. Further strengthening of capital markets would enable the corporate sector to secure higher levels of longer-term funding.

## Outlook for 2004–2005

GDP growth for 2004 is revised down to 6.4% from 7.2% in *ADO 2004*, on the basis of the deceleration in the first and second quarters. For 2005, it is forecast to pick up slightly to 6.6% (Figure 2.11), on the assumption that the factors that caused the deceleration in the first half of 2004 will have subsided. Domestic demand, particularly private investment, is expected to continue to underpin growth. According to BOT, industries with capacity utilization rates higher than average precrisis levels, including automobiles, electrical appliances, electronics, and steel, will step up their investments.

Inflation is now forecast at 2.8% in 2004

rather than 2.4% to reflect the recent inflationary pressures, before it declines to 2.6% in 2005. The monetary authorities expect that core inflation will rise at a slower rate, to average 0–1% and 1–2%, respectively.

With imports growing faster than exports, the trade balance may turn into deficit in 2004 or 2005. However, investment inflows, particularly FDI, may well outweigh the deficit, and the current account balance will likely remain in surplus in 2004–2005. Indeed, a recent survey by the United Nations Conference on Trade and Development (UNCTAD) indicated that Thailand was viewed as the third most attractive destination for FDI in Asia.

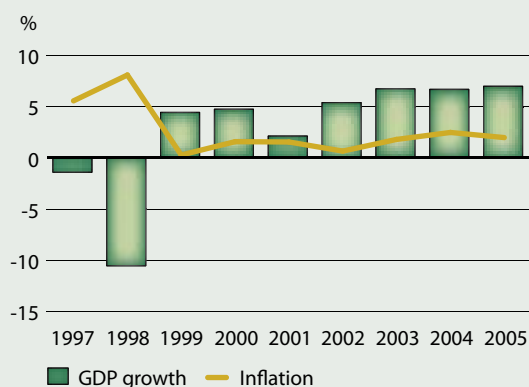
Domestic risk factors that may affect these forecasts include unrest in the south and avian

flu. A widespread recurrence of avian flu would hurt the poultry industry, which is an important segment in both agriculture and food processing, and services if the disease starts to affect larger numbers of people. Externally, the most obvious risk is that crude oil and nonfuel commodity prices could be higher than expected, lowering growth and raising inflation in the process. Other external risks include larger than expected global interest rate rises and slower economic growth among the country's major trading partners.

Other than these risks, the Government, particularly BOT, needs to monitor several vulnerable parts of the economy. Rising levels of household debt remain a concern: the average household debt went up from B68,279 in 2001 to B110,133 in the first quarter of 2004. If domestic interest rates increase, sustainability of household debt may become a serious issue that could affect the banks and consumer spending. The property sector, too, could cause problems for banks if the recent surge in activity and prices turns down and interest rates rise.

External stability could become an issue in the medium term, despite the fact that the economy has become less vulnerable to shocks over recent years, with, for example, external debt at 40% of GDP and the ratio of international reserves to short-term debt at 3.8:1 in January. Large increases in imports and investments to support high economic growth may result in a decline in the current account surplus in the short term, which could turn into a deficit further out.

**Figure 2.11 GDP Growth and Inflation, Thailand, 1997–2005**



Sources: National Economic and Social Development Board; Bank of Thailand.