Regional Macro

Thailand: An investment-led rebound

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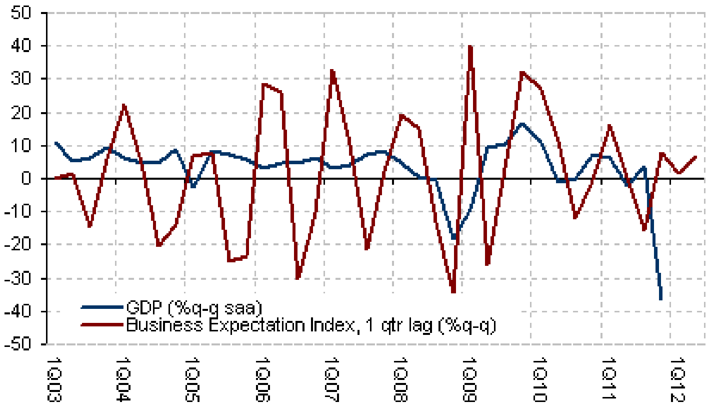
2011 Real GDP / Inflation: 0.1% / 3.8%
2012(f) Real GDP / Inflation: 4.5% / 3.5%

For 2012, we expect Thailand to stage a strong V-shaped economic recovery (Fig 1) in the wake of last year's devastating floods, led by investments in large-scale reconstruction efforts.

Nonetheless, inflationary pressures remain elevated on the back of rising oil prices as well as the recent hike in minimum wage.

At this juncture, Bank of Thailand is unlikely to cut rates in the near term in view of an improved economic outlook as well as increased inflationary pressures.

Fig 1. Leading indicator points to a strong recovery



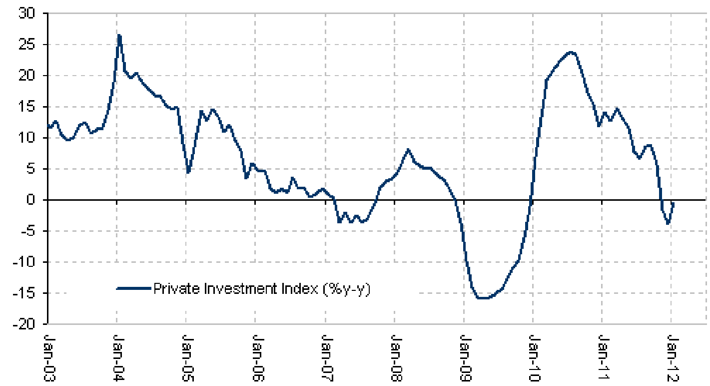
Source: CEIC, PSR est.

A strong economic rebound in 2012

We expect the Thailand economy to rebound to around 4.5% in 2012, from 0.1% in the preceding year on the back of a strong recovery in domestic demand as well as a low base effect. This takes into account the following factors.

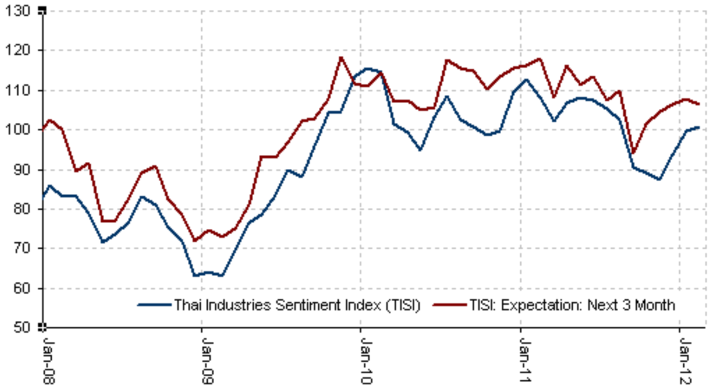
- First, government expenditure and private investment will increase due to large-scale reconstruction efforts. Specifically, the government plans to undertake a THB 300bn water management and flood prevention schemes around the Chao Phraya River basin. Businesses will purchase new machinery and equipment while households will also contribute to residential investment when they reconstruct their homes. In January, private investment grew by 0.64% m-m saa, reversing from four consecutive months of sequential contraction on the back of healthy domestic cement sales (to facilitate reconstruction efforts) as well as machinery investment. On a y-y basis, private investment declined at the slowest pace in 3 months (-0.4%) (Fig 2). Looking ahead, private investment is likely to continue to expand, following a sustained improvement in the Thai Industrial Sentiment Index which climbed to a 6-month high in February (Fig 3).

Fig 2. Private investment is recovering



Source: CEIC, PSR est.

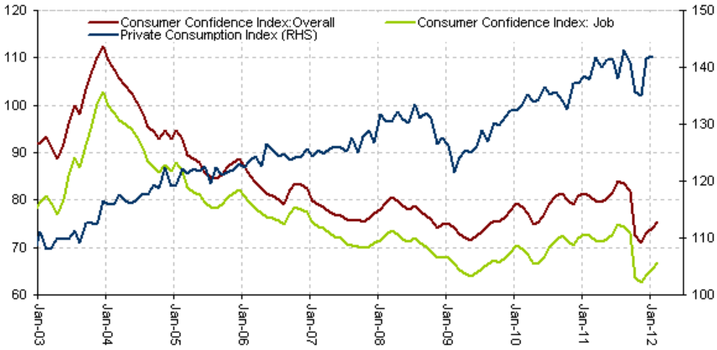
Fig 3. …and is likely to continue to expand.



Source: CEIC

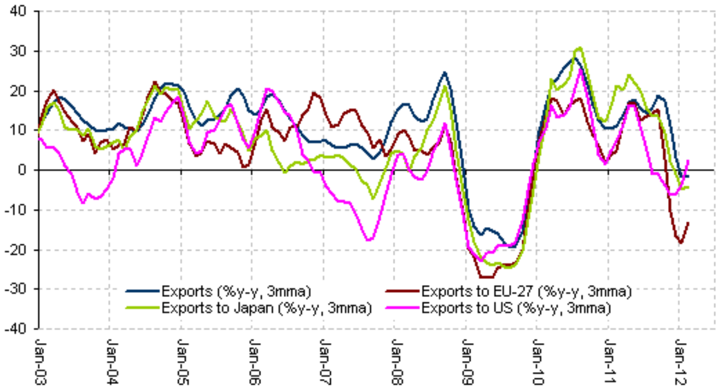
- Second, private consumption expenditure will register gains as consumer confidence recovers and labour market normalises in the aftermath of the severe flood disaster. Specifically, private consumption grew by 1.6% m-m saa in January while consumer confidence improved for the third consecutive month, up almost 6.3% in February from last November's trough. Consumer confidence on the overall economy as well as the labour market has also recovered around 8% since the devastating October Thai floods (Fig 4). Furthermore, household consumption should stand to benefit from a slew of government assistance measures such as direct compensation and tax allowances.

Fig 4. Household consumption has picked up and is expected to receive a boost from increased consumer confidence and improving labour market.



Source: CEIC

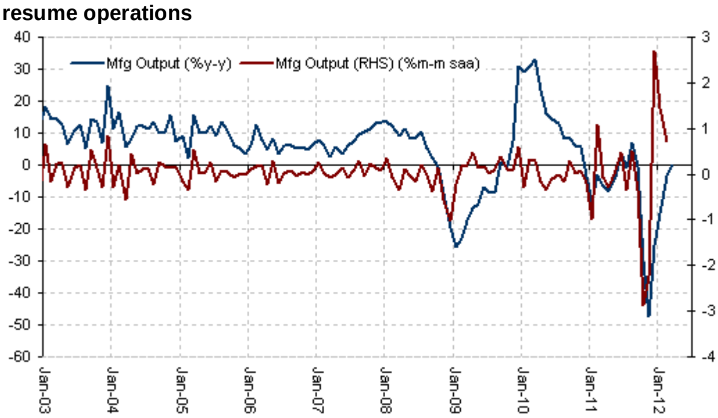
Fig 6. …though weak external demand still pose significant headwinds to exports.



Source: CEIC, PSR est.

- Third, a modest recovery in exports, barring strong external headwinds. According to Bank of Thailand's recent business survey, manufacturing industries that are severely hit by the floods (such as the autos and electronics) are expected to gradually resume to pre-flood production levels by 3Q12, consequently leading to a recovery in exports. In Jan-Feb, manufacturing production continued to decline by 9.2%, albeit at a slower pace compared to 4Q11 (-34%) as flood-hit factories begin to slowly resume production (Fig 5). On the external front, exports grew at a tepid pace of 1.1% in Jan-Feb, reversing from the contraction of 2.9% in 4Q11 as global demand improved. Looking ahead, exports have and should continue to benefit from the resilient ASEAN demand as well as improving US demand. Manufacturing production will rebound as plants resumed operations and supply-chain disruptions eased in the wake of the Thailand floods.

Fig 5. Manufacturing production picked up as factories gradually resume operations



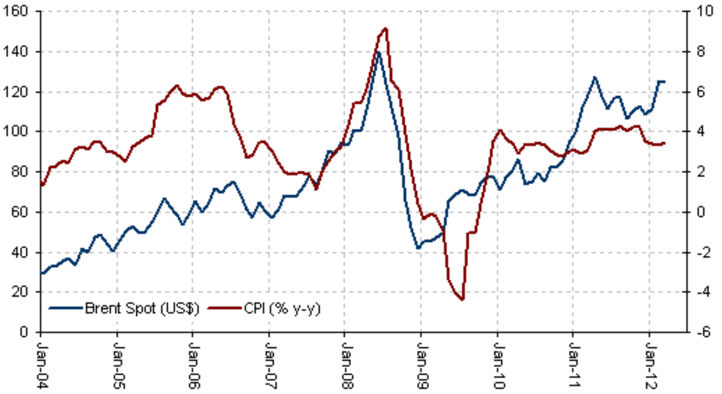
Source: CEIC, PSR est.

Though we project a strong economic rebound from 2011, our 2012 real GDP growth projection (4.5%) is lower than Bank of Thailand (BoT)'s forecast (5.7%). We are of the view that (i) there might be hiccups in the implementation of the government's massive flood infrastructure investment, (ii) minimum wage hikes could pose supply constraints to firms (particularly small and medium enterprises) and (iii) economic growth will be dampened by rising oil prices. Furthermore, risks to growth for export-dependent Thailand are skewed to the downside. Specifically, weaker-than-expected external demand (Fig 6) as well as a delay in the recovery of manufacturing production could crimp growth.

Inflationary pressures remain elevated

Headline inflation is projected to register 3.5% in 2012, compared to 3.8% in the preceding year. In 1Q12, headline inflation moderated to 3.4% y-y, from 4.0% in the preceding quarter (Fig 7). However, wage pressures -particularly in the formal sector- may rise following the government's decision to increase the daily minimum wage to THB300 in Bangkok as well as six other provinces, and by an average of 40% in the rest of the country with effect from this April. Nonetheless, to some extent, these pressures will be mitigated by Thailand's relatively large informal sector and a steady stream of cheap migrant labour. In addition to these wage pressures, upside risk to the inflation forecast remain. Thailand -a net importer of oil and an oil-intensive economy- will see a significant rise in inflation should oil prices continue to surge as a result of possible escalation of geopolitical tensions in the Middle East.

Fig 7. Upside risks to inflation persist

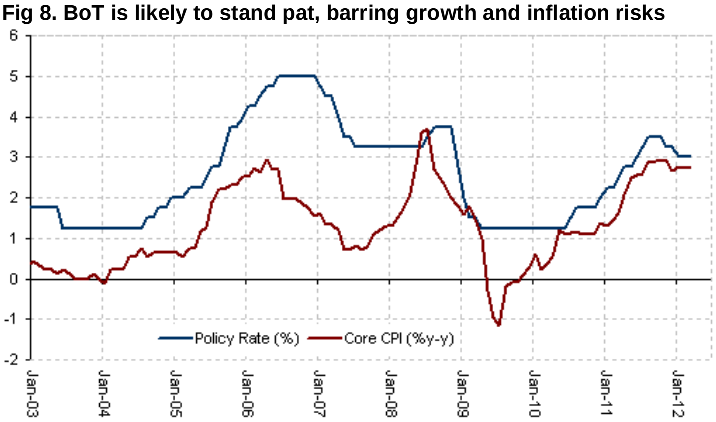


Source: CEIC, PSR est.

BoT to tread a fine balance

BoT is likely to hold its benchmark one-day bond repurchase rate at 3% in the near term, in view of an improving macroeconomic outlook (with risks abated for now) as well as large fiscal injection into the economy. Monetary policy rhetoric has turned slightly hawkish, though BoT stood pat at the March monetary policy meeting. Specifically, BoT noted that while (i) downside risk relative to the previous meeting in January has eased and (ii) economic recovery from the Thai floods is proceeding well, (iii) inflationary pressures- arising from rising global oil prices and the minimum wage increase- has edged up. Nonetheless, should growth falter, there is still some room for BoT to undertake rate cuts to stimulate the economy as core inflation (which excludes energy and fresh food) is at 2.7% in 1Q12, still within the target range of 0.5-3.0% (Fig 8).

Fig 8. BoT is likely to stand pat, barring growth and inflation risks



Source: CEIC

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