FLASH

SCB Economic Intelligence Center

SCB EIC expects the MPC to continue with 3 more policy rate hikes to stand at 2% in 2023

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KEY POINTS

MPC voted unanimously to raise policy rate by 0.25% from 1% to 1.25% as expected. The Thai economic recovery has continued to gain traction. Tourism and private consumption will continue to be key economic drivers going forward and help alleviate the impact of global slowdown on the Thai economy. Headline inflation is expected to be higher than the previous projection for 2023 due to domestic energy prices. However, it is still expected to decline and return to the target range within 2023. The Committee deems that a gradual policy normalization remains an appropriate course for monetary policy given the growth and inflation outlook.

The MPC assesses that the Thai economy will likely continue growing at 3.2%, 3.7%, and 3.9% in 2022, 2023, and 2024, respectively.

The tourism sector continues to strengthen as the number of foreign tourists continues to rise. Additionally, private consumption is supported by improving economic activities, as well as a more broad-based recovery in employment and labor income. Tourism sector and private consumption will continue to be key economic drivers in 2023 and 2024, although the global slowdown would cause Thai export growth to decelerate. Nonetheless, the Committee will monitor the highly uncertain global economic outlook which could slow down more than expected, as well as the momentum of the tourism sector.

The MPC expects headline inflation to be at 6.3%, 3.0%, and 2.1% in 2022, 2023, and 2024, respectively.

Headline inflation has peaked in the third quarter. For 2023, it is expected to be higher than previously assessed on the back of the upward adjustment of electricity charges, but it is expected to return to the target range by the end of 2023. Core inflation projection is close to the previous assessment at 2.6%, 2.5%, and 2.0% in 2022, 2023, and 2024, respectively. Meanwhile, medium-term inflation expectations remain anchored within the target range. However, the Committee will continue to closely monitor risks to inflation, especially a potential increase in cost pass-through as well as domestic energy prices which remain uncertain.

The MPC assesses that overall financial system remains resilient while financial conditions remain accommodative.

Debt serviceability of businesses and households 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 as incomes have yet to fully recover. Meanwhile, funding costs in the private sector gradually rise in tandem with the policy rate but remain conducive for business financing, with credit and funding in the bond market still seeing growth. The baht against the US dollar has been highly volatile owing mainly to expectations surrounding the monetary and macroeconomic policy in major economies.

IMPLICATIONS

EIC expects the Thai policy rate to continue rising to 2% by the end of next year.

The MPC is expected to continue hiking policy rate in consistent with the outlook of the Thai economic recovery and high inflation above the target range of 1-3%, particularly in the first half of next year. EIC expects the MPC to gradually raise the policy rate 3 more times (25 bps at each meeting) during the first half of 2023 to stand at 2% so that the monetary policy can be gradually normalized to the level consistent with sustainable growth in the long term. Nevertheless, EIC views that the policy rate may not be raise continually during the latter half of next year as the global economy is expected to slowdown significantly, especially for major economies including the US which will likely enter the recession. Meanwhile, economic recession in the UK and eurozone will continue from the end of this year. As a result, global demand will drop considerably which could affect Thai exports and the outlook of Thai economic recovery. EIC assesses that the MPC will judge the pace and timing of monetary policy normalization to the level consistent with long-term sustainable economic growth. This is to ensure that policy normalization, both monetary policy and financial measures which will be completed by the first half of 2023, will not cause financial condition to tighten so rapidly that it affects the economic recovery amid the highly uncertain global economic slowdown. These measures include the temporary FIDF fee reduction which will end this year[1], and financial rehabilitation loans which will end in April next year.

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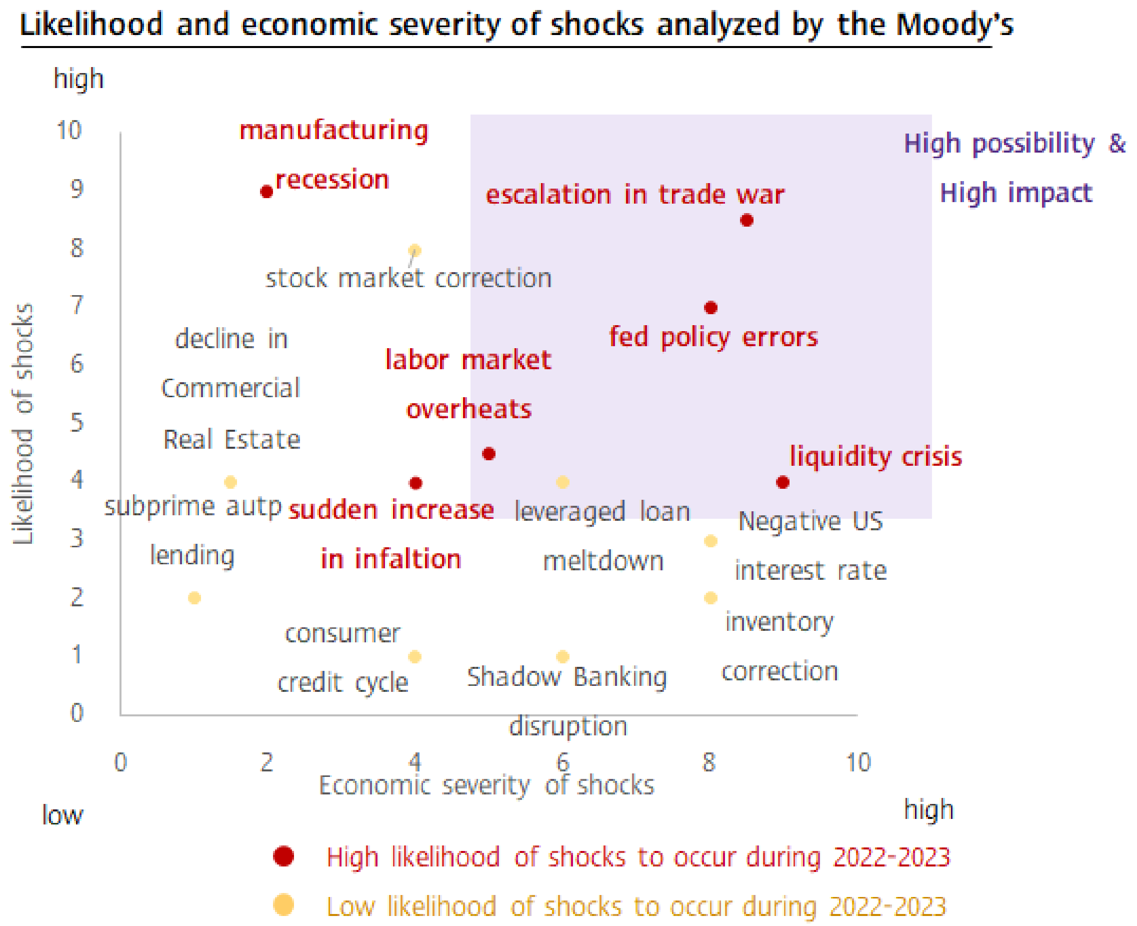
[1] In April 2020, the BOT issued a measure to temporary reduce the contribution rate from financial institutions to the FIDF from 0.46% to 0.23% of deposit base for the period of two years. This is intended for financial institutions to immediately pass on such cost savings to borrowers by further reducing their loan rates during the COVID-19 pandemic in order to relieve their debt burdens during the period when incomes of businesses and households severely dropped. However, this measure will expire at the end of this year (referring to BOT Press Release No. 33/2022). The FIDF contribution rate will thus be raised to the original rate of 0.46% from the beginning of next year. This will result in higher cost pass-through, causing the loan rates of commercial banks to increase in tandem. This will add pressure on the tightening financial conditions from the policy rate hikes and thus cause borrowing costs to increase further.

Uncertainties in the global economy remain high which will be key risks to the Thai economic recovery. EIC assesses that the global economy in 2023 could grow below 2%, close to the average growth during the past economic recession, although EIC expects the global economy not to enter the recession in the baseline projection. However, should unexpected events occur, such as the more severe international tensions or accelerating inflation, this could result in a more aggressive monetary policy tightening in major economies (figure 1) and in turn lead to a global economic recession. This will be a key risk for the Thai economic recovery and monetary policy normalization in Thailand.

Figure 1 : The global economy could face unexpected events in 2023 which could result in the economic recession



Source : EIC analysis based on data from World Bank and Moody's

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