SCB EIC cuts the Thai 2024 GDP growth forecast to 2.7% an a anticipates the MPC to lower rates within H1 following the lower neutral rate.

1 March 2024

SCB EIC cuts the Thai 2024 GDP growth forecast to 2.7% an a anticipates the MPC to lower rates within H1 following the lower neutral rate.

KEY SUMMARY

SCB EIC revises the Thai economic growth forecast for 2024 to 2.7% due to a moderation in economic momentum and the slow recovery of the manufacturing sector, which can be attributed to structural challenges.

SCB EIC revises down the Thai economic growth forecast for 2024 to 2.7% from 3%. While the overall economy in 2024 is anticipated to continue its recovery, propelled by accelerated growth in various demand-side factors, particularly exports and private investments, there are notable challenges. The momentum from the public sector will continue to weaken , resulting from delays in the 2024 Budget Act. Additionally, the high level of accumulated inventory, which was a critical issue in 2023, is unlikely to drop in 2024, revealing structural issues within the Thai manufacturing sector. Particularly, Thai exports are facing diminished competitiveness and limited adaptability to changing global product demand patterns and long-term supply chain dynamics. Consequently, the manufacturing sector's recovery trajectory in 2024 is hindered, which does not align with the demand-side of the Thai economy, shedding light on substantial structural challenges within the manufacturing sector.

Weak manufacturing conditions challenge Thai economic growth.

Regarding the supply side of the Thai economy in 2024, SCB EIC projects that the manufacturing sector will revert to an expansion fueled by strong consumer goods recovery. However, the growth is expected to stall, as numerous industries grapple with all-rounded demand-side and supply-side pressures , including (1) Higher penetration of imported products, especially from China. (2) Slow recovery of overseas demand coupled with lower export competitiveness on a global scale, partially from a cost disadvantage. The lower competitiveness is reflected upon the tepid growth of Thai exports over the past decade and the continual decline of Thai exports share since 2020 despite the robust expansion of export volume from other countries in the region.

(3) Delays in the 2024 Budget Act. (4) High accumulated inventory. (5) Geopolitical risks, particularly in the Red Sea area, which may escalate and hurt Thai exports.

Structural challenges within the manufacturing sector also lower Thailand's potential economic growth.

Thailand's potential economic growth continues to drop following more severe structural challenges in the manufacturing sector. SCB EIC estimates that the pre-COVID-19 potential GDP growth (2017 – 2019) for Thailand stood at 3.4%, while the long-term potential GDP growth (2024 – 2045) should drop to 2.7%, declining from the previous estimate of 3% as of December 2023. A major contributor to this decline is the greater decrease in Thailand's total factor productivity, exacerbated by the deepening structural challenges in the Thai manufacturing sector. These challenges arise from the close interdependence of the Thai economy to the Chinese economy and the Chinese supply chain amid global geopolitical conflicts, limited adaptive capacity to long-term global supply chain, and slow adjustments to changing global product demand patterns.

SCB EIC foresees 2 policy rate cuts by the MPC in April and June to 2%, aligning with the lower neutral rate.

SCB EIC evaluates that the MPC will cut the policy rate to 2% during H1/2024 to sustain a neutral monetary policy stance. This is because by considering the structural factors that determine the appropriate interest rate, Thailand's neutral rate drops to 2.1% (from 2.5%). Therefore, these policy rate cuts will not only help maintain a neutral stance while fostering long-term economic growth at a sustainably lower rate but also further alleviate the high debt burden, particularly for vulnerable businesses and households that are disproportionately impacted by elevated interest rates. Beyond that, the anticipated rate cuts should strengthen Thailand's economic confidence, especially amid limited momentum from the public sector this year.

SCB EIC revises the Thai economic growth forecast for 2024 to 2.7%, attributing a weakened economic momentum and the slow recovery of the manufacturing sector.

SCB EIC revises down the Thai economic growth forecast for 2024 following a weakened economic momentum and the slow recovery of the manufacturing sector. In 2023, the Thai economy experienced a disappointingly low expansion of 1.9%, slowing from the 2.5% growth in 2022. Consequently, by the end of 2023, the overall level of Thai economic activity lagged below the pre-COVID crisis level by approximately -0.4%, reflecting a slower recovery than initially assessed by SCB EIC. Thailand is thus positioned among the slowest economies in returning to its pre-COVID benchmarks. For the year 2024, SCB EIC estimates that the Thai economy will expand by 2.7%, declining from the previous projection of 3% (Figure 1). Accelerated growth in various demand-side sectors, particularly exports and private investments, should build upon the momentum generated by private consumption, tourism, and services, which were the driving forces in 2023. Nevertheless, the growth momentum from the public sector should weaken in Q1/2024, owing to delays in the 2024 Budget Act.

Furthermore, the high level of inventory, which has been accumulating since 2023, is unlikely to drop in 2024 , stemming from Thailand's limited adaptability to changing global product demand patterns and global supply chain. This significant factor contributes to the ongoing slow recovery of the Thai manufacturing sector this year. Consequently, the manufacturing sector's growth does not align with the demand-side of the Thai economy, highlighting more severe structural challenges in the Thai manufacturing sector.

Figure 1: Thai economic outlook for 2024 by SCB EIC

Economic forecast (Base case)	Unit	2023	2024F DEC23	2024F MAR24
GDP	%YOY	1.9	3.0	2.7
Private consumption	%YOY	7.1	2.6	2.4
Government consumption	%YOY	-4.6	3.3	1.4
Private investment	%YOY	3.2	4.4	3.8
Public investment	%YOY	-4.6	2.2	1.1
Goods exports value (USD BOP)	%YOY	-1.7	3.7	3.1
Goods imports value (USD BOP)	%YOY	-3.1	4.3	4
Foreign tourist arrivals	Million persons	28.0	36.2	36.2
Headline inflation	%YOY	1.2	1.5	0.8
Core inflation	%YOY	1.3	1.0	0.6
Policy rate (year-end)	%	2.5	2.5	2
Current account	% of GDP	1.3	2.0	1.5

Source: SCB EIC analysis based on data from the National Economic and Social Development Council, Bank of Thailand, and Ministry of Commerce

Regarding demand-side economic components, SCB EIC predicts that the majority of these components will experience a slower growth rate compared to the previous projection.

- **Private consumption** should continue to expand from recovery in the tourism sector due to an increasing influx of international tourists, particularly Chinese tourists. As such, the projection for the number of international tourist arrivals is maintained at 36.2 million. Additionally, domestic tourism should continue to improve. However, despite such positive trends, the overall growth in private consumption for 2024 is projected to slightly drop from the previous estimate to 2.4%. This adjustment is attributed to the high base in 2023 and the high debt burdens of vulnerable households, exerting pressure on overall spending in the country.

- **Merchandise exports** should expand by 3.1%, a decrease from the previous estimate of 3.7%. Thai exports should still receive support from the ongoing expansion of global economic activities from last year, mainly driven by the manufacturing sector which has a closer connection to international trade than the service sector does. However, challenges loom on the horizon as global trade volume is likely to expand at a lower rate than initially expected, influenced by events such as the attacks by Houthi rebels on cargo ships in the Red Sea and drought in the Panama Canal, both of which are critical shipping routes worldwide. Other notable challenges affecting Thai exports include global economic polarization and the implementation of recently added trade protectionist measures. Furthermore, Thai exports are also affected by long-term structural factors in global manufacturing sector following changing global product demand patterns and global supply chain as Thailand has limited adaptability to such changes. Indicators for such limited adaptability include the weak reading of the adaptation effect index and the relative change of world market share published by the International Trade Centre, with negative readings in many of Thailand's key industries, especially electronics and automotive.
- **Private investment** is expected to experience robust expansion by 3.8% this year, as indicated by a significant increase in project approvals from the Board of Investment. However, the growth in private investment is projected to be lower than the previously forecasted rate, primarily due to the slower recovery in exports. The manufacturing sector also continues to grapple with high accumulated inventory. Furthermore, this revised outlook aligns better with the forward-looking business sentiment characterized by ongoing concerns regarding liquidity, interest burdens, and heightened production costs.
- **Public spending** is expected to improve at a slower rate than previously forecasted, influenced by the accelerated disbursement during the first quarter of the 2024 fiscal year (Q4/2023). which causes spending to reach near-normal levels despite encountering pressure from the 2024 Budget Act delay. Consequently, the budget that could be reimbursed in the remaining period of the 2024 fiscal year budget will be lower than previously anticipated. Nevertheless, public spending growth in 2024 should improve compared to the previous year, in line with the increasing operating budget. Moreover, disbursement is expected to proceed almost normally despite challenges from the 2024 Budget Act delay.
- **Public investment** should increase slightly this year as government agencies should be able to expedite investment budget disbursements following the enactment of the 2024 Budget Act. The disbursements are set to commence in early April (Budget Bureau proposing and the Cabinet acknowledging on 27 Feb 2024). This timeline demonstrates a shorter delay than initially anticipated, which was expected towards the end of April or May. Furthermore, the low base resulting from the

low investment budget disbursements in Q4/2023 is expected to provide further support to public investment growth in 2024.

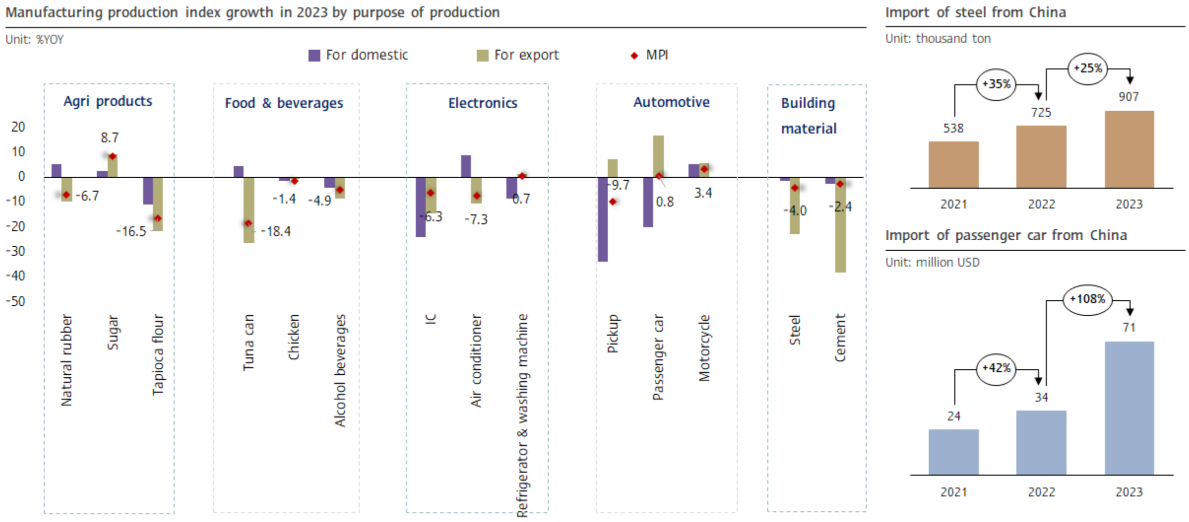
Beyond the moderating demand-side momentum that is exerting pressure on the Thai economy to recover at a slower pace than initially estimated, there are also challenges stemming from weak supply-side conditions. In 2023, the manufacturing sector in Thailand experienced a significant contraction, reflected in the reading of the 2023 Manufacturing Production Index, which contracted by -5.1%. Such a contraction was fueled by sluggish domestic and overseas demand, coupled with various sectors, namely automotive, electronic parts, and steel, which face higher penetration and pressure from Chinese imports. Consequently, the factors led to a reduction in the overall output of the manufacturing sector. Looking ahead to 2024, SCB EIC anticipates that the manufacturing sector should return to growth on the back of robust consumer goods recovery. However, the rate of recovery is expected to be slow, as various sectors within the manufacturing industry continue to contend with all-rounded demand-side and supply-side risks (Figure 2), including

(1) Increasing penetration of imported products, particularly from China with steel, automotive, and electronics seeing a decline in domestic sales share due to the ongoing surge in imports from China.

(2) The slow recovery of overseas demand and a decline in the competitiveness of Thai exports in the global market pose significant challenges. Noteworthy products experiencing diminishing competitiveness include **shrimp, chemicals, and plastic products,** which face cost disadvantages and contend with tax exemption policies for imported products. As such, Thai exports have witnessed tepid growth over the past decade. Moreover, the Thai exports share in the global market has declined since 2020 in spite of the robust expansion of exports from other regional players. Currently, the value of Thai exports is lower than that of peers, although the Thai export value experienced higher growth in the previous decade (Figure 3).

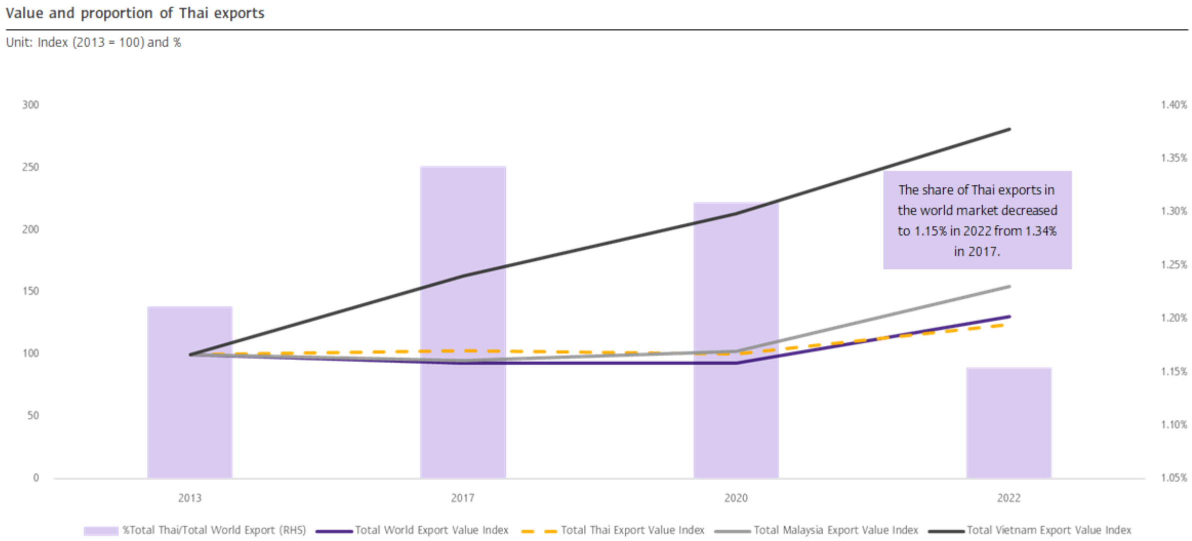
(3) Government budget delays subject the **cement industry** to uncertainty risks in demand as government construction projects may face delays.

Figure 2: Thailand's industrial production in 2023 was hampered by sluggish demand both domestically and internationally while some industries, such as steel and automotive, facing pressure from influx of Chinese products



Source: SCB EIC analysis based on data from the Office of Industrial Economics and Ministry of Commerce

Figure 3: The proportion of Thai exports in the world market continued to drop in recent periods, meanwhile, the value of Thai exports stabilized at a subdued level. In contrast, exports from other countries in the region exhibited robust expansion during the past decade.



Source: SCB EIC analysis based on data from Trademap and CEIC

(4) High accumulated inventory. The automotive and parts sector faces the highest risks due to the expected continuation of sluggish domestic demand. This situation is a cause for concern for the Thai manufacturing sector in both the short and long term, and

(5) Geopolitical conflicts. While the manufacturing sector is currently seeing limited impact, escalated conflicts in the Red Sea area could potentially hamper **Thai exports to Europe** (Figure 4).

Figure 4: Thailand's manufacturing sector should return to expansion this year thanks to recovering consumer goods demand. However, supply-side risks warrant monitoring, including high inventory build-up from changing global supply chain and production structure, labor shortages, and geopolitical issues. Such risks may hamper the production capacity of certain industries.

Key directions and factors affecting production capacity in 2024

Production capacity returning to expansion

- **Stronger recovery of domestic and overseas demand**

Seafood, Meat, Beverages, Fresh & frozen fruits, Plastic products, Electronic parts, Electronics, Electrical appliances, Chemicals, Cement

Production proportion as of 2023: 40.0%

Production capacity contract / continue to contract

- **Production shortage**

Sugar, Tapioca starch, Natural rubber

- **Vulnerable demand**

Automotive & parts, Hard disk drive

- **Foreign products/ manufacturers enter the domestic market**

Steel

Production proportion as of 2023: 20.3%

Other risks

Demand Risk

- Penetration of imported products, particularly from China
  Steel, automotive, electronics seeing a decline in domestic sales share due to the ongoing surge in imports from China
- Competition for global market share
  Shrimp, chemicals, plastic products witness cost disadvantages and contend with tax exemption policies for imported products
- Government budget delays
  Cement facing uncertainty in demand as government construction projects may be delayed

Supply Risk

- High accumulated inventory
  Automotive & parts with the highest risks following continued sluggish domestic demand
- Labor shortages
  Seafood, particularly tuna faces high risks
- Geopolitical conflicts
  limited impact on production, though warrant monitoring of conflicts in the Red Sea area that will hurt exports to the EU
- Volatile weather conditions / global warming
  Tuna and agriculture decreasing output and heightening output volatility

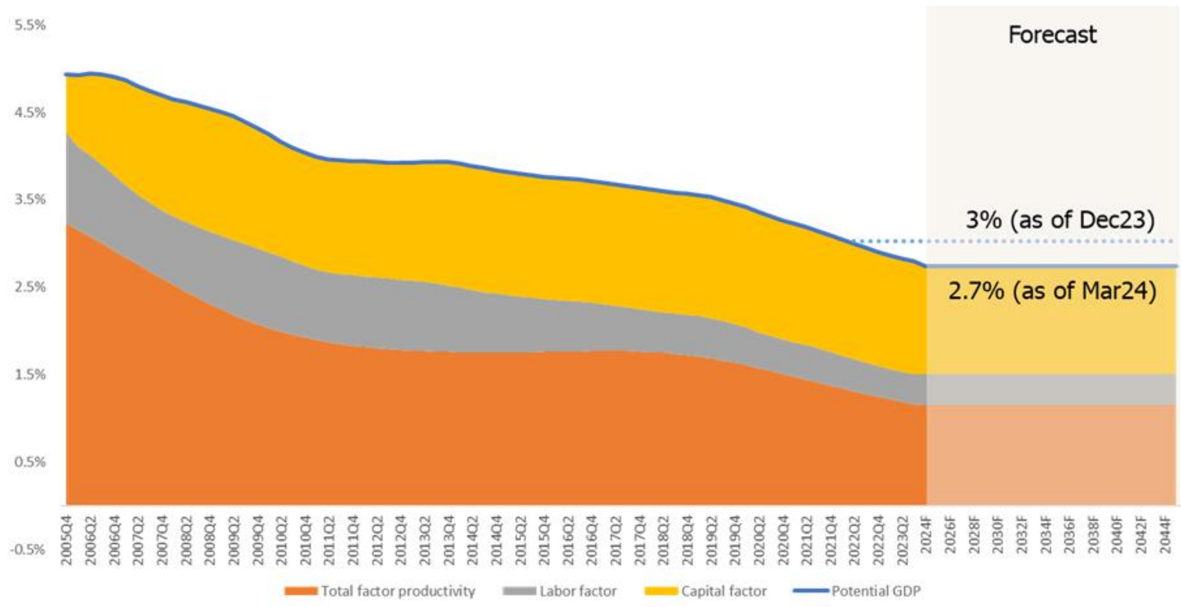
Note: In formulating the manufacturing sector outlook, SCB EIC took into account various key manufacturing sectors that collectively contribute to approximately 60% of the total manufacturing sector.

Source: SCB EIC analysis based on data from the Office of Industrial Economics

Lower potential GDP growth in Thailand reflects more severe structural challenges.

SCB EIC observes a continuous decline in Thailand's potential GDP growth in recent periods, following more severe structural problems. The estimated pre-COVID-19 potential GDP growth (2017-2019) for Thailand should stand at 3.4%, while the long-term potential GDP growth (2024-2045) should drop to 2.7%, declining from the previous estimate of 3% as of December 2023. A major contributor to this decline is the greater decrease in Thailand's total factor productivity (Figure 5), exacerbated by the deepening structural complexities within the Thai manufacturing sector. These challenges arise from the close interdependence of the Thai economy to the Chinese economy and the Chinese supply chain amid global geopolitical conflicts, limited adaptive capacity to long-term global supply chain, and slow adjustments to changing global product demand patterns.

Figure 5: Forecast of Thailand's potential GDP growth and components



Note: Adapted from the study titled Estimating potential output, output gaps and structural budget balances (Claude et al, 1995)

Source: SCB EIC analysis based on data from the National Economic and Social Development Council

Notable factors contributing to the continuous reduction of Thailand's potential GDP growth in recent periods can be categorized into 3 components as follows:

- **Total factor productivity:** Total factor productivity is identified as the primary factor responsible for the decline in Thailand's potential GDP growth in recent periods. The factor reflects the consequences of low investment in technology and R&D, along with worsening labor reallocation.
- **Capital:** Prolonged periods of low domestic capital accumulation have resulted from the private sector's lack of confidence in investments, thereby slowing capital growth. Additionally, there have been low investments in Thai infrastructure across various sectors.

- **Labor:** Thailand is currently grappling with the challenges posed by an aging society, leading to a reduction in the proportion of the working-age population. This demographic shift has a direct impact on the available workforce. Furthermore, the Thai labor market faces a skills gap, with workers lacking the necessary skills demanded in global markets, and skilled labor migrating to work abroad.

Moreover, scarring effects stemming from the COVID-19 crisis have a lasting impact on the components influencing Thailand's potential GDP growth, with a particular focus on productivity. These effects include the temporary exit from the labor market and disruption of the education system during the COVID-19 pandemic. As such, labor reallocation, wages, and labor productivity experienced enduring effects in the long run (Figure 5). This trend aligns with findings from an empirical study conducted by the IMF (2023), which indicated that developing countries faced more severe implications than advanced economies.

The MPC should cut the policy rate in April and June to 2% to align with the lower neutral rate.

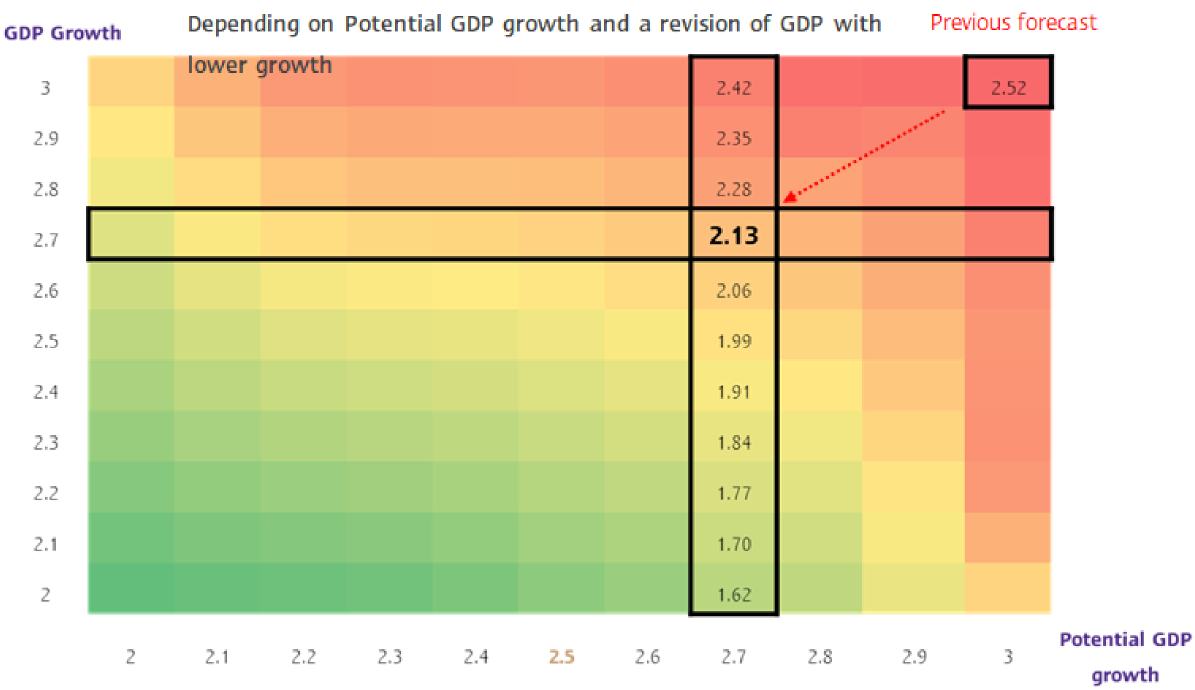
Thailand's lower potential GDP growth causes Thailand's neutral rate to drop accordingly. SCB EIC evaluates that Thailand's potential GDP growth in the long run should drop to 2.7% (from 3%), causing the neutral rate to drop accordingly. Moreover, following the release of Thailand's Q4/2023 economic results, SCB EIC views that the neutral rate now stands at 2.1%, declining from the previous estimate of 2.5% (Figure 6).

As such, SCB EIC assesses that the MPC will implement 2 policy rate cuts this year to uphold the neutral monetary policy stance. This is because by considering the structural factors that determine the appropriate interest rate , Thailand's neutral rate already dropped below 2.5%. Thus, the rate cuts will help maintain a neutral stance while fostering long-term economic growth at a sustainably lower rate. The anticipated policy rate cuts should be implemented gradually, with the first reduction of 25 bps expected in April, followed by another 25bps cut in the June meeting. Subsequently, the rate is anticipated to remain at this level throughout the year.

Figure 6: Thai policy rate should undergo 2 rate cuts this year, resulting in a reduction to 2% to align with the lower neutral rate

Sensitivity analysis: possibility to reduce Thailand's policy rate to maintain a neutral stance

Unit : %



Note: Adapted from the studies 1) Revisiting Thailand's Monetary Policy Model for an Integrated Policy Analysis (Amatyakul et al, 2021) and 2) Measuring the Natural Rate of Interest after COVID-19 (Holston et al, 2023)

Source: SCB EIC analysis based on data from the National Economic and Social Development Council and Bank of Thailand

As for the Thai economic outlook this year, growth should slow to 2.7%, closely aligning with the lower potential GDP growth in the long run, while prevents the output gap from being negative. However, this growth reflects a slow economic recovery undermined by structural problems in the manufacturing sector while domestic demand continues to see robust expansion. Furthermore, **ongoing policy rate cuts, effective at stimulating demand, may not be deemed necessary.** Instead, the rate cuts are perceived as a policy mechanism "recalibration" of the long-term Thai interest rate base in response to the changing structure of the Thai economy. **In terms of the headline inflation forecast for 2024, the rate is anticipated to be lower than the target range, standing at 0.8%** (previous estimate at 1.5%). Similarly, core inflation in 2024 is projected to decrease to 0.6% (previous estimate at 0.8%), following the implementation of government measures aimed at reducing the cost of living throughout 2024, particularly in terms of energy costs.

SCB EIC evaluates that the 2 policy rate cuts this year serve multiple purposes. These cuts are not only aimed at maintaining a neutral monetary policy stance that aligns with the lower potential GDP growth following accumulated structural challenges with severe implications in recent periods but also further alleviate the high debt burden, especially for vulnerable businesses and households that may be disproportionately affected by elevated interest rates than other groups. Furthermore, the cuts should strengthen Thailand's economic confidence, especially in the face of reduced support from the public sector this year following an approximately half fiscal year delay of the 2024 Budget Act.

Author

Economic Intelligence Center (EIC), Siam Commercial Bank

ECONOMIC AND FINANCIAL MARKET RESEARCH

SOMPRAWIN MANPRASERT, Ph.D.

First Executive Vice President, Chief Economist at Economic Intelligence Center (EIC), Siam Commercial Bank and FEVP, Chief Strategy Officer at Siam Commercial Bank.

THITIMA CHUCHERD, Ph.D.

HEAD OF ECONOMIC AND FINANCIAL MARKET RESEARCH

POONYAWAT SREESING, Ph.D.

SENIOR ECONOMIST

ASAMA LIAMMUKDA, Ph.D.

ECONOMIST

NATHAPONG TUNTICHIRANON

ECONOMIST

NATNICHA SUKPRAWIT

ECONOMIST

NICHANAN LOGEWITOOL

ECONOMIST

PUNN PATTANASIRI

ECONOMIST

VISHAL GULATI

ECONOMIST