

2013 Country Outlook: Thailand

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Cascade Asia Forecast:

	Q1	Q2	Q3	Q4	2013	2014
Real GDP (% , y/y)	4.8	4.5	4.2	4.0	4.5	4.0
CPI (% , y/y)	3.4	3.3	2.8	2.9	3.1	2.0
Trade Balance (% of GDP)	-	-	-	-	1.2	2.8
Policy Rate (% , eop)	2.75	2.50	2.50	2.50	2.50	2.50

Economic Outlook

GDP growth to slow down

Thailand's strong GDP growth is forecasted to decelerate to about 4.0-4.5% in 2013 from 5.7% in 2012. We expect investment to continue to drive growth but the demand surge from post-flood reconstruction in 2012 is expected to decline significantly. Weak external demand from Europe, the United States, and Japan will cause Thai exports to continue to be sluggish. Moreover, Thailand's relatively high exposure and trade linkages to China make it vulnerable to China's expected slowdown in 2013. Domestic private consumption, however, will be supported by a sizable minimum wage increase and subsidies aimed at supporting disposable income. Investment will continue to be the main driver of growth.

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Public spending to support domestic consumption

The current Pheu Thai government is pro-growth. Despite rising public debt (from 40% of GDP to 44.9% GDP in 2012), its populist policies will continue to support domestic demand through rebates, tax cuts, and minimum wage increases but to a lesser degree when compared to 2012. The government's minimum wage increase, guarantee to purchase rice from farmers at a premium, and allotment of 3% of GDP for soft loans will continue to support rural income and domestic demand. The ambitious THB 300 bn floodwater management project will also have a positive effect on domestic investment. However, shorter term programs that have boosted consumption such as tax rebates for first time home and auto buyers are set to expire in H2 2013.

Current account to stay in surplus on improved trade balance

Thailand's current account dipped to a deficit of 0.2% of GDP in 2012 due to slowed exports and a surge in post-flood reconstruction imports. Its external balance should improve and we forecast a current account surplus of 1.2% in 2013. As export growth will remain sluggish, imports are also expected to decrease as investment demand reverts back to normal levels. However, the government's mega flood management project could lead to some deterioration in the earlier part of 2013. With an improving trade balance and tourism related inflows to remain robust against the backdrop of loose monetary policies from developed markets, we forecast a slight appreciation of the THB against USD, EUR, and JPY.

Monetary Policy Outlook

Inflationary pressure remains benign; more room for rate cut

Despite a 22% minimum wage hike in 70 provinces in Thailand, inflationary pressures will be muted as global commodity prices are expected to remain steady in 2013. The Bank of Thailand surprised the market by preemptively cutting the policy rate by 25 bps, an indication of an accommodative central bank. With well-contained inflation, we believe the central bank has more room to further cut rates if domestic economic growth decelerates significantly in Q1 2013. We anticipate a possible 25bps rate cut in Q2-Q3 of 2013.

Political Outlook

Stability returning to Thailand's volatile political environment

After nearly 17 months in office, it has become increasingly clear that Prime Minister Yingluck Shinawatra is not a surrogate of her brother, former PM Thaksin Shinawatra, who was deposed six years ago in a royally-backed military coup and who lives in self-imposed exile. How well Yingluck manages relations with a habitually restless military establishment,

bureaucratic elites and palace officials will become increasingly crucial in 2013 in light of King Bhumibol's questionable health and Thaksin's urge to press for an amnesty for his return. Yingluck's successful stewardship of the Thai economy through natural and economic crises in 2011-2012 has improved her political clout. A recent political survey released in December by Bangkok University shows a comfortable margin of support for Yingluck, with her Puea Thai party at 47% compared to 33% for the opposition Democrat party led by rival and former Prime Minister Abhisit. Yingluck is poised to continue to leverage her diplomatic and political clout to push her populist economic policies in a progressively stable political environment. We do not, however, foresee Yingluck championing controversial legislation that could jeopardize short-term political capital that she has garnered with the military and royal establishment.

Low risk of a Thaksin return in 2013

Yingluck's cabinet reshuffle in late October replaced 12 cabinet members with a mixture of confidantes and technocrats underlines her efforts to consolidate the longevity of her administration and highlights her growing assertiveness in acting independently of her brother. Yingluck has taken a number of steps through the cabinet reshuffle to act in her own political interest by: (A) selectively appointing six former members of Thaksin's disbanded Thai Rak Thai party, (B) refusing to appoint Thaksin ideologue and red-shirt co-leader Jatuporn Prompan and other Thaksin allies, and (C) retaining key ministers and political allies outside of the Thaksin camp, particularly former Deputy Prime Minister and newly appointed Finance Minister Kittiratt Na-Ranong. Contrary to rumors, Yingluck is likely to avoid taking significant steps to pardon her brother through a controversial constitutional amendment to Section 68 (that safeguards the role of the king as head-of-state) or through a more likely but distant proposal for "reconciliation." Lack of movement on allowing Thaksin to return bodes well for political and economic stability in the near term.

Charges against former prime minister source of potential unrest

The Department of Special Investigation's charges against Democrat party leader Abhisit Vejjajiva for the killing of red-shirt protesters in April/May 2010 is the first of its kind against a prominent politician and former prime minister in Thailand. Red-shirts are adamant that the prosecution of Abhisit, widely viewed as "public enemy number one" by the red-shirts, is the roadmap to reconciliation after the violence in 2010.

However, the circus surrounding this hot-button issue for yellow-shirt supporters and anti-Thaksin elites has the potential to spark civil strife in the capital and commercial hubs visible in Bangkok when thousands rallied in October-November calling for the military overthrow of the Yingluck administration under now-defunct Pitak Siam (Protect Thailand) movement led by

former General Boonlert Kaewprasit. Significant headway in the prosecution of Abhisit could threaten short term stability as the Democrat party is likely to mobilize anti-Yingluck allies in defense of Abhisit, who was also found guilty in November of draft-dodging in his youth and stripped of his military appointments and pension in January.

Ultimately, the Yingluck administration exercises nominal influence over the judiciary where a criminal prosecution of Abhisit will likely stagnate. Yingluck will most likely abstain from rocking the boat further by yielding to pressure from her supporters to charge military leaders for the red-shirt crackdown.

Yingluck expected to manage a soft landing of the ICJ ruling on Preah Vihear

In April, the International Court of Justice will hold final oral hearings to reinterpret its 1962 ruling on Preah Vihear, which awarded jurisdiction of the temple to Cambodia. A final verdict will be issued in October. A verdict in favor of Cambodia is expected and would no doubt rouse Thai nationalist fervor, inciting anti-Cambodian nationalists, such as The Patriots Network, to rally their bases and lobby for the government to reject the verdict. Such a scenario would test Yingluck's hand at managing public rancor. Recent overtures by the military suggest a placid response to a ruling favoring Cambodia but ensuring cooler heads on the border has been a challenge in times past. Unlike her predecessor, the Yingluck administration enjoys warm ties with the Cambodian government, thanks in part to her brother's close relationship with PM Hun Sen, and affords greater political will for a peaceful acceptance of the ICJ's ruling.

Market Outlook

Bullish on the SET

The Stock Exchange of Thailand (SET) returned 39% in 2012 and 3% YTD and is trading at around 1430 points, which is at the upper bound of the 52-week range (1054-1451). While we do not expect the SET to be able to repeat the same level of return this year, we remain bullish that it will continue to trade higher into 2013 on improve corporate profitability, strong domestic demand, and cheap credit inflows from developed markets (monetary easing in US, EU, and Japan). However, despite the optimistic forecast, we remain watchful for signs of stock market bubbles and do not rule out the possibility if the stock market continued to grow faster than the rest of the economy. With the expectation of a gradual appreciation of the THB, fixed income markets both local-currency denominated corporate and sovereign debts, as well as long FX plays on the THB each present interesting investment opportunities in 2013.

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