

Exclusive Analysis: Thailand Market Update

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- **Consumer confidence bounced back to pre-flood levels**
- **BOT revised its 2013 forecast as inflation outlook remains benign**
- **Strong baht appreciation leads to policy debate on capital inflows**
- **SET up 7.04% YTD; Government bond yields at lowest level this year**

Consumer confidence bounced back to pre-flood levels

Consistent with our view that domestic private consumption will be a key driver for Thailand's economic growth in 2013, the consumer confidence index in all categories continued to register higher for a fourth straight month in January. It reached a 16-month high on better economic prospects, a low interest rate environment, as well as increased minimum wage and improved farm incomes.

Confidence Index Categories	December 2012	January 2013
Consumer Confidence	80.2	81.7
Overall Economy	70.6	72.1
Job Opportunities	71.7	72.9
Future Income	98.3	100

Source: Thai Consumer Confidence Index, University of Thai Chamber of Commerce Economic and Business Forecasting Center

While a score under 100 generally indicates consumers are more pessimistic and a score over 100 indicates an expectation that conditions will improve, we welcome the steadily improved trends in consumer confidence particularly with the index on future income reaching 100 for the first time in 16 months. Although the actual Private Consumption Index (PCI) contracted by 2.9% in January, concerns over a sluggish global economy, slower domestic GDP growth, domestic political instability and a high cost of living appear to have eased somewhat. We expect the improved consumer confidence to increase private consumption, which will provide the much-needed cushion for a slow down in external demand going forward.

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BOT revised its 2013 forecast as inflation outlook remains benign

In its January monetary policy report, the Bank of Thailand (BOT) revised its 2013 GDP forecast for Thailand up to 4.9% from 4.6% citing strong continued growth in domestic spending. More specifically, the first-car tax rebate scheme, a personal income tax cut, and ongoing investments both for repairs and replacements in some industries and to accommodate strong domestic demand are among the key drivers of the optimistic revision. With improved economic prospects in the US and the Euro Zone as well as Japan's inflation-targeting scheme, external demand for Thai exports is expected to recover gradually and regain its role as a driver of growth in H2 2013. Meanwhile, although inflation accelerated to 3.63% y/y in January driven by increased fresh food prices, the inflation outlook for the year remains benign at 2.8%, within BOT's range of 3%. The inflationary pressure is expected to cool further to 2.6% in 2014. However, we remain cautious and believe that the fragile global economy and slower pace in domestic investment demand will continue to be the main sources of downside risk to Thailand's economic growth.

January Inflation Report: Bank of Thailand's Forecast Summary

(in annual % change)

Indicator	2012	2013	2014
GDP growth	5.9 (5.7)	4.9 (4.6)	4.8
Headline Inflation	3.0* (3.0)	2.8 (2.8)	2.6
Core Inflation	2.1* (2.1)	1.7 (1.7)	1.6

Note: *Outturn

() Inflation Report 2012

Source: Office of the National Economic and Social Development Board and calculations by Bank of Thailand

Strong baht appreciation leads to policy debate on capital inflows

As we expected, the Thai baht rose sharply with approximately 2.5% appreciation against the USD in January due to strong capital inflows and positive return outlook in Thai capital markets. However, the currency depreciated slightly last week on speculation that the Bank of BOT may implement measures to cool down capital inflows and upward pressure on the currency.

The pace of appreciation and the potential negative consequences on exports and tourism sectors have led to a policy debate within the government, academic, and business

communities. Some have called for a rate cut, a view advocated by the Ministry of Finance, as a means to reduce carry trade capital inflows while others have argued for more capital controls. We believe that an expansionary policy could further fuel the potential for a bubble in the asset markets as well as increasing inflationary pressure when combined with government fiscal stimulus programs.

It is not an ideal remedy to curve capital inflows from the perspective of the central bank. Given that the BOT has recently revised its forecast for GDP growth upward and its optimistic views on domestic demand and improved global economy, it is unlikely that a rate cut will be implemented in the next meeting. However, with the Finance Minister, Kittiratt Na-Ranong sending a formal letter to the BOT urging a rate cut to match the historically low global interest rate environment, we cannot rule out the possibility of a rate cut down the road if the baht's appreciation has material impact on the export and tourism sectors—especially with the current benign inflation outlook.

SET up 7.04% YTD; Government bond yields at lowest level this year

Thailand's stock market extended the rally from Q4 2012 and has returned 7.04% YTD. The index climbed above the 1500 mark on Friday in line with the rise in global markets in response to better-than-expected trade data from China, Japan's easing bets, and improved outlooks in the US and Germany. However, the index declined slightly as investors took profits ahead of the Chinese New Year holiday. We believe stock prices will continue the upward movement with improved corporate profitability, cheap credits, and strong inflows in 2013. However, the prices will be volatile and heavily influenced by headlines on the global economy and domestic policy.

The yield on Thailand's 10-year note fell to the lowest level this year after global funds scooped up US\$1.1 bn more sovereign debt than they sold last week. Thailand's policy rate of 2.75% is an attractive carry trade profile when compared with 0.25% in the US and 0.1% in Japan. The relatively higher yield will continue to drive capital inflows into the asset.

Country	Year to Date Capital Inflows (USD mn)
Taiwan	1,589
Indonesia	957
Philippines	802
Thailand	192
Vietnam	170

Source: Duetsche Bank/Tisco Securities

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