

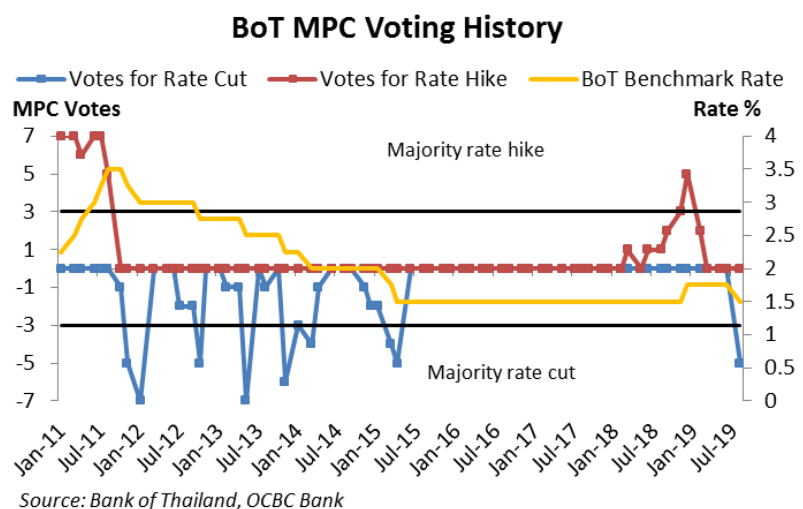
BoT surprises with rate cut as exports take centre-stage

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- The Bank of Thailand surprised markets with an unexpected interest rate cut of 25bp.
- MPC members voted 5-2 to cut key interest rate, despite a unanimous vote to stand pat in the last meeting.
- The BoT's statement noted that the economy is facing structural problems, while inflation is projected below the lower bound target.
- We think that the BoT may not shy away from further monetary easing, especially if exports continue contracting.

1. Bank of Thailand surprised markets with an unexpected rate cut

The Bank of Thailand has unexpectedly reduced its benchmark interest rate by 25bp to 1.50%, catching the markets by surprise. Only two economists on the Bloomberg poll were predicting a rate cut; the remaining 27 economists (including ourselves) were all expecting the BoT to keep rates constant at 1.75%. 5 of 7 MPC members voted for a rate cut in this meeting, citing growing headwinds to economic growth, and deemed a more accommodative monetary stance as necessary. The other two members viewed that given the already low interest rate environment, further reduction in interest rates is unlikely to provide additional support to growth.



Thailand

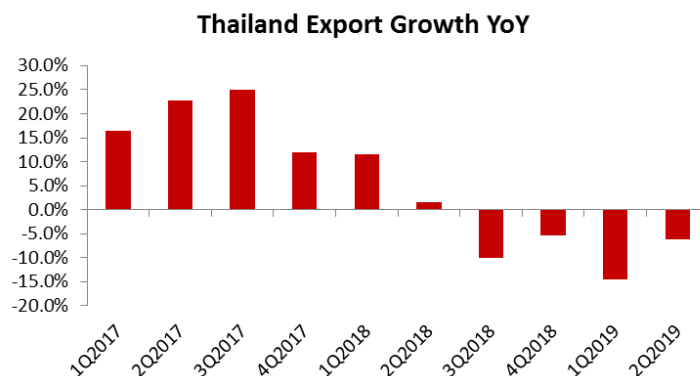
7 August 2019

2. Contracting exports is a growing concern

The BoT press release made references on contracting exports and its resulting impacts thrice:

- A contraction in merchandise exports has started to affect domestic demand.
- The contraction in exports has resulted in the Thai economy expanding below potential.
- Non-farm income and employment have declined, especially in the export-related manufacturing sector, leading to lower private consumption.

The BoT appeared to be placing an increasing amount of attention on the country's exports, which have contracted -10.4% in 1H 2019. Further contractions in trade flows – an increasing possibility given escalating US-China tensions and a disruption in the electronics supply chain from the Japan-South Korea tensions – may likely spur the BoT into reducing interest rates further.



Source: CEIC, OCBC Bank

3. Despite the surprise rate cut, the THB remains stable

The BoT has continued to voice concerns over the baht's strength, and efforts have been made to blunt the demand for the THB. In June, the BoT said that the baht appreciation may not be consistent with economic fundamentals; in its latest statement, it expressed concerns that the baht appreciation may affect the economy to a "larger degree" amid intensifying trade tensions. The issuances of Thai government bonds have decreased since June, presumably an effort to rein in the baht's strength – but the USDTHB pair has continued to trade largely within 30.5-31.0, with 30.5 the strongest for the USDTHB YTD. The surprise rate cut has so far failed to push the USDTHB pair above 30.88 at time of writing. More may need to be done if the BoT wishes to dampen the appeal of the baht, given the currency's status as a regional safe haven due to its current account surplus.

Thailand

7 August 2019

4. BoT will likely make its next decision based on exports and inflation

Given the increasing focus on exports, we expect the BoT to make its decision based on the evolution of its export growth. Two more export data releases are expected before the next meeting on 25 September. Headline inflation is also expected to play a role in their consideration, given that they have now projected headline inflation to be below the lower bound target of 1.0% this year. MPC members have noted, however, that there “remained a need to preserve policy space”. We think that there is a chance that the BoT may continue to ease interest rates further from here as it tries to soften the baht and stabilise the export sector. We see the possibility of one more rate cut to 1.25% before the end of 2019.

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