

Thailand: expect a rate cut next week

In spite of government pressures on the BoT, we believe weak economic fundamentals warrant a 25bp rate cut next week



Source: istock

A weaker currency?

The Thai baht (THB), the darling of investors this year with an 8.3% appreciation against the USD, will lose some of its lustre if the Bank of Thailand (BoT) cuts rates to support growth, as we expect it to do next week at the policy meeting on September 27.

The BoT has been defying pressure from the government to ease policy. And in a press interview yesterday, Governor Veerathai Santiprabhob, downplayed concerns about the stronger currency. Attributing THB strength to the large current account surplus, investor confidence and reduced political risk, he said a rate cut would not necessarily lead to a weaker currency.

33.3

Our end-2017 USD/THB forecast

spot - 33.1 , consensus - 33.3

Our forecast is against the tide

Our forecast of one 25bp BoT policy rate cut next week puts us outside a consensus that's solidly behind an on-hold policy. We believe the balance of economic risks remains tilted toward weakness. Despite GDP growth in the first half of the year, underlying economic fundamentals remain weak. All the boost to growth came from inventories even as manufacturing growth remained anaemic. De-stocking will be a drag on future output.

Problem of a strong THB

Exports are on a recovering trend, but that's still not the case for manufacturing. The strong THB threatens the export recovery while it also dampens inflation pressures. CPI inflation remains close to zero and well below the BoT's 1-4% policy target. There is need to stem the THB appreciation pressure to preserve export competitiveness and, with a relatively strong current account surplus, the BoT is in a position to accommodate any THB weakness stemming from lower interest rates.

There is no denying there is not much room for policy rates to go much lower if the BoT needs to preserve some policy space for future. The low in the policy rate was 1.25% during the 2008-09 crisis, and the benefits of one 25bp rate cut may not be significant (as the Governor noted).

This means the stimulus to the economy will still need to come from fiscal policy or accelerated implementation of infrastructure development projects. Sadly, the anaemic contribution of government investment and construction components of GDP offer little evidence of this happening anytime soon.