

## ***Thailand***

Thai real GDP is expected to grow by 4.3 percent this year, down from 5 percent in 2006, before rising slightly to 4.6 percent in 2008. Both last year and so far this year growth has been principally supported by robust net exports, while domestic demand growth has remained weak due to declining consumer and investor confidence, political and policy uncertainties, and higher oil prices. Net export growth was however slower than in 2006 and this is the main reason for the slower pace of GDP growth this year. Exports of goods and services are expected to grow by 6.5 percent in real terms (8.5 percent in 2006), while import growth should pick to around 2.5 percent (1.6 percent in 2006). Inflation has slowed to around 2 percent this year, a 2.7 percentage-point decline from last year. Growth is forecast to increase modestly to 4.6 next year as domestic uncertainties begin to clear up and domestic demand picks up. However there remain many downside risks related to both global environment (oil prices and external demand) and the domestic political and policy environment.

Private investment growth has slowed from last year. Weak domestic and foreign demand, policy uncertainties, less crowding-in from public investment, and the rapid appreciation of the baht, which has affected export growth, have delayed capacity expansion by firms. High oil prices and greater global uncertainty related to the US sub-prime crisis are not helping either. Foreign direct investment is likely to have contracted this year for the first time after 2003 and overall private investment growth will likely register no growth this year, the lowest since 2000. Capacity utilization, which has been rising since 2004, is now approaching pre-1997 crisis levels.

Clearer policy direction from the new government after the December 2007 elections should help improve investor sentiment and raise investment growth next year. Even though actual investment has been weak, Board of Investment (BOI) investment promotion applications and approvals for both local and foreign firms have reached record highs this year. This may indicate improved investor sentiment and a potential investment recovery next year. However, the extent of actual investment will also likely depend on reduced perceptions of policy uncertainty. These had increased this year after the December 2006 introduction of capital controls to stem baht appreciation – even though most of these have now been relaxed – and the January 2007 Cabinet approval of amendments to the Foreign Business Act (viewed as making foreign investment more restrictive than before).

Public investment growth has also been low this year. Investment budgets have increased only marginally and tighter governance rules have slowed disbursement. The Central Government's investment budget increased by only 4.5 percent in 2007 (compared to 8.7 percent in 2006). In addition, several new measures to make public procurement more transparent and accountable have also tended to slow disbursements.. Disbursement of the government and state-owned enterprises are expected to be around 70 percent and public investment is projected to rise by 6.8 percent in nominal terms and 4.5 percent in real terms this year (10 percent and 4.5 percent in 2006). The carry-overs from this year will be spent next year, and the central government investment budget for 2008 has been raised by 8 percent. But there could still be delays in decisions on large investment projects as the new government will assume office only around February next year. Due to the delay in the disbursements, the fiscal balance is in deficit this year by 0.8 percent of GDP compared to the planned 1.8 percent budget deficit. The deficit will likely be much less next year as revenues collection are projected to be stronger in line with higher GDP growth (although the budget has been programmed to be in deficit).

Exports of goods and services remain the key driver of growth this year and will remain so next year. Growth in exports of goods and services in real terms this year has decelerated from last year's 8.5 percent to 6.5 percent due to the slow increase in agricultural price, appreciation of the baht and the deceleration of US demand, which is Thailand's largest export market (15

percent of total exports). Growth of merchandise export is projected to be 7 percent in real terms and 14.5 percent in value (9 percent and 17.4 percent in 2006). Political uncertainty and the 2006 New Year's Day bombings have also affected tourism numbers and receipts. Tourist arrivals increased by only 2.8 percent in the first 9 months of this year. Looking forward, real merchandise export growth is expected to slow slightly down to 6.6 percent in real terms, in line with modest growth in world demand and a still strong baht. Tourism receipts should recover as elections take place and political uncertainty declines. Exports of goods and services in real terms could reach a slightly stronger 7.2 percent growth in 2008.

The current account surplus will reach a record high this year, but should decline next year as import growth speeds up. Import growth has slightly increased this year to 8 percent in value terms (7 percent in 2006), mainly from the imports of raw materials, and is expected to speed up to 15 percent next year as investments picks up. As a result, the current account this year will reach almost US\$12 billion or 4.9 percent of GDP. Next year, the current account surplus will decline to around US\$5.7 billion or 2.2 percent of GDP. The large current account surplus this year has contributed to the accumulation of Thailand's international reserves to almost US\$80 billion by the end of September 2007 and also to the baht's appreciation. The baht would likely remain strong next year as the current account remains in surplus and as less political uncertainty attracts more investment inflows.

Some reforms have been undertaken this year but other measures have adversely affected investors' confidence. The Japan-Thailand Economic Partnership Agreement (JTEPA) was signed in April this year. Moreover, the Privatization and Corporatization Act and the Deposit Insurance Act have been approved by the Cabinet and will likely be passed by the National Legislative Assembly this year. The National Productivity Master Plan, aiming to raise productivity at the both the sectoral and aggregate levels, has been drafted by a high-level national committee and approved by the Cabinet. However, the still undecided amendments to the Foreign Business Act and remaining capital controls have dampened foreign investors' confidence. Boosting investor's confidence through the improvements in the business climate, which includes the reduction of regulatory burden and further liberalization of certain services industries, will be key to Thailand's future growth. In addition, policies to improve the productivity of the service sector which would help unleash the large potential growth of the services sector needs to be undertaken to provide an additional engine of growth for Thailand.