



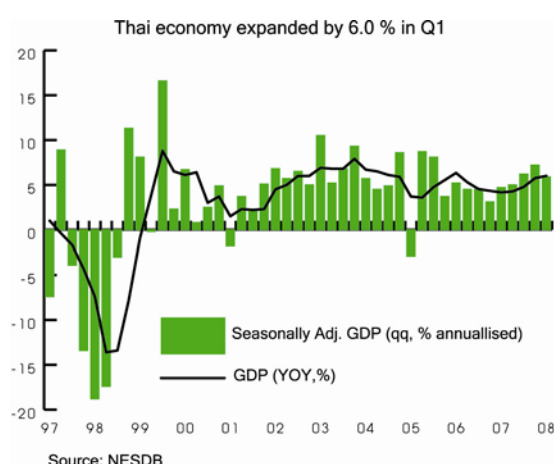
# **ECONOMIC OUTLOOK**

## **THAI ECONOMIC PERFORMANCE IN Q1 AND OUTLOOK FOR 2008**

- ❑ **The Thai economy has continued on an uptrend trajectory, expanding by 6 percent in the first quarter of 2008**, gaining better momentum from the 4.8 percent growth in 2007. The recovery in domestic demand helped balance the growth components of the economy while the contribution from net export is smaller than that of last year owing to more robust growth of imports than that of exports. State-owned enterprise budget disbursement improved during the first quarter. The disbursement rate of government budget was closed to the target of 23.5 percent.
- ❑ **Overall economic stability remained sound, but inflationary pressure has started to build up.** In the first quarter, headline inflation rose to 5 percent, substantially higher than 2.9 percent in the previous quarter, fueled by elevating oil and food prices. Current account remained in a surplus of 3,068 million USD, but narrowed from the surplus of 4,689 million USD in the first quarter of 2007. Unemployment rate continued to be low at 1.6 percent.
- ❑ **Money market rate remained unchanged but real interest rate declined noticeably**, caused mainly by rising inflation. Deposits were still in its downward trend. Liquidity consequently declined, yet remained high. Thai baht in nominal term appreciated against USD. In real effective term, it, however, weakened. On average SET index continued to improve despite some short term volatilities caused by rapid capital flows of foreign investors
- ❑ **Budget balance and cash balance continually registered deficits**, under the stance of expansionary fiscal policy in order to stimulate economy. Public debts to GDP stood at 36.35 percent at the end of February 2008, slightly declined from 37.97 percent at the end of 2007.
- ❑ **In the first quarter, favorable factors to the Thai economy** included upward adjustment of salary and minimum wages, increase in farm income supported by rises in prices and production, solid expansion of the economy of Thailand's trading partners, decline in real interest rate, and improvement in consumer and business sentiment since November of last year.
- ❑ **The Thai economy is projected to register 4.5-5.5 percent growth in 2008**, unchanged from the previous forecast despite higher oil prices and inflation rate. The forecast has been maintained for the following reasons: (i) a higher-than-expected growth in the first quarter contributed by faster-than-projected recovery in private consumption and investment while the export performance remained robust, (ii) implementation of various additional measures to ensure continuity of the recovery of private consumption and investment as well as to reduce impacts of high oil prices and inflation on the group of needy and SMEs. Those measures consist of tax incentive in order to boost up consumption and investment, setting target for loan expansion to the SMEs and low-income people, upward salary adjustment for low-ranked government officers as well as upward lift of minimum wage. (iii) Other supporting factors include implementations of budget deficit policy and urgent policy in order to strengthening the economy, low interest rate, and increase in employment.
- ❑ **Risks management in order to support further recovery of the economy** concerns: (i) rising inflationary pressure and its impact on needy groups and SMEs as headline inflation is anticipated to increase to 5.3-5.8 percent, pushed by higher prices of oil, commodities, food and raw materials. Meanwhile, weakening Thai baht would also add pressure on domestic prices, (ii) world economic slowdown will put constraint on Thai exports (iii) current account surplus has narrowed and is expected to register a surplus of only 2 percent of GDP, and (iv) improvement of energy efficiency is imperative and should be continuously promoted.

## 1. Economic performance in Q1 and year 2008

**1.1 The Thai economy in the first quarter of 2008 grew by 6.0 percent, higher than an average rate of 4.8 percent in 2007. The satisfactory growth rate indicated that Thai economy is on the path of recovery, supporting by recovery in domestic demand, exports expansion and the increase in number of tourisms that boosted services revenues.**



Export (%YOY)		Exports of goods						2008
		Year	Q1	Q2	Q3	Q4	Q1	
Agriculture	Value	15.8	14.2	17.6	2.6	28.8	45.9	
	Price	10.3	10.6	2.8	3.1	26.5	26.5	
	Volume	5.0	3.2	14.4	-0.5	1.8	15.3	
Fishery	Value	11.1	20.6	15.8	4.5	7.0	-2.5	
	Price	5.1	6.0	7.0	2.7	4.9	11.0	
	Volume	5.7	13.7	8.2	1.7	2.0	-12.2	
Manufacturing	Value	19.1	18.8	18.4	13.8	25.4	20.5	
	Price	4.9	3.8	5.0	4.4	6.3	7.8	
	Volume	13.6	14.4	12.7	9.0	18.0	11.8	
Total	Value	18.1	17.9	18.0	12.6	24.0	21.1	
	Price	2.0	4.7	5.1	4.5	8.5	9.9	
	Volume	11.8	12.7	12.2	7.8	14.3	10.2	

Source: BOT

### Key Highlight

- ❑ **The Thai economy in the first quarter expanded by 6.0 percent, higher than that of 5.7 percent in the last quarter of 2007 and the annual growth of 4.8 percent.** Growth was supported by a broader base expansion, including (i) an accelerating growth of manufacturing sector from 5.7 percent in 2007 to 9.7 percent in this quarter which was in tandem with the continued expansion of exports sector, and the recovery of private investment and consumption (ii) the improvement in agricultural production (iii) a stronger expansion of hotel and restaurant sector due to the rapid increase in number of foreign tourists (iv) a better performance of financial sector than last year that was supported by credit expansion, high interest rate spreads and the increase in incomes from investment in bond and securities market.
- ❑ **The stronger expansion of manufacturing production was driven by the recovery in private investment and consumption as well as continued expansion of export quantity.** In the first quarter, private consumption and investment grew by 2.6 and 6.5 percent respectively, picked up the pace from 1.5 and 0.5 percent increase in 2007. However, domestic demand is still running below aggregate supply, thus containing inflation from the demand side while inventory built up. Export quantity increased by 6.9 percent while revenues from services sector increased at a satisfactory rate, in line with a stronger increase in tourism number of 13.3 percent as compared to 4.6 percent rise in 2007.
- ❑ **Overall, growth components in Q1 become more balance between the contribution of domestic demand and that of net exports.** The adjustment was supported by the rapid domestic demand expansion which helped offset the slowdown in the quantity of net exports.
- ❑ Export quantity continued to slow down but was compensated by impressive increase in export prices, and thus resulted in strong expansion of export values. In the remaining months, however, export quantity is likely to trend down in light of a weaker global economic expansion. This will dampen export values, though export prices are likely to continue on the uptrend which is in part

supported by agricultural prices. However, the share of agricultural exports of which prices are rising, accounts for a little less than 10 percent of total exports. Moreover, export of agricultural products tends to fluctuate and vary with supply condition. Therefore, contribution of agricultural commodities in driving export expansion is limited and unlikely to sustain. In addition, agricultural production increasingly faces with higher costs of oil, raw materials and labor, which will render competition in the world market more difficult. The situation, therefore, has stressed on urgent need of productivity improvement.

- Growth of the fast growing manufacturing products which accounts for a larger share in exports continued to slow down. They are, for example, computers and part thereof, air conditioners, auto and parts thereof, plastic products, jewelry, rubber products and paper products.

- Import accelerated both in terms of quantity and prices and resulted in trade deficit. In the first quarter, import values increased by 34.5 percent, accelerated from yearly average rate of 9.6 in 2007, and turned trade balance into a deficit of \$ 109 million, the first deficit in 6 quarters. The main contributors for the acceleration in import values are as follows:

- The strong expansion of demand for capital in tandem with the recovery in private investment. Demand for imported capital goods picked up from a very low base in 2007, a period of investment contraction and a reduction in demand for capital goods. In the first quarter of 2008, the quantity of imported capital picked up by 32.8 percent while its import prices increase moderately by 4.9 percent.
- The import values of fuel and lubricants increased rapidly by 68 percent. This is attributable to the rise in prices of 48 percent and the rise in import quantity of 9.7 percent, the first increase in 4 quarters. The steady increase in crude oil price of 63.5 percent raised value of crude-oil imports by 79.4 percent. The implied increase of quantity of crude oil import was driven by an increase demand of refinery in Thailand and thus

resulted in a reduction of the import quantity of refinery products.

- The expansion of exports and domestic demand together with the increases in import prices resulted in a strong expansion of import value of raw materials. In the first quarter, import prices of raw materials increased by 9.4 while import quantity increased rapidly by 26.0 percent.
- Import value of consumer goods picked up by 37 percent due to the expansion in import quantity of 30.7 percent. The steady baht appreciation as compared to baht value in 2007, together with deposit interest that remained lower than in 2007, encouraged consumers with high purchasing power to increase their spending on imported consumer goods.

		Import of goods					
		2007					2008
		Year	Q1	Q2	Q3	Q4	Q1
Consumption goods	(%YOY)						
	Value	13.80	7.2	9.7	10.3	27.2	37.3
	Price	3.6	1.5	2.6	5.1	5.3	5.0
Raw materials	Volume	9.8	5.6	6.9	4.9	20.8	30.7
	Value	15.1	15.3	12.2	13.4	19.4	26.0
	Price	5.8	5.7	5.9	5.4	6.2	9.4
Capital goods	Volume	8.7	9.0	6.0	7.6	12.4	15.2
	Value	3.7	-6.6	7.2	7.6	6.4	39.4
	Price	2.2	1.6	1.9	2.3	2.9	4.9
Fuel and Lubricant	Volume	1.5	-8.1	5.1	5.2	3.4	32.8
	Value	2.8	-4.0	-2.9	-3.3	22.1	68.0
	Price	8.1	-0.6	0.4	2.7	31.0	48.0
Total	Volume	-5.0	-3.4	-3.3	-5.8	-6.8	13.5
	Value	9.6	5.9	7.3	8.4	16.6	34.5
	Price	5.4	3.4	3.4	4.1	10.5	15.6
	Volume	4.1	2.4	3.8	4.1	5.5	16.3

Source: BOT

- **The disbursements of central government and state-enterprises budgets in the first quarter were closed to the targets.**

- The total disbursement of budget registered at 368,952 million baht which is equivalent to 22.2 percent of the budget and closed to the target of 23.5 percent. The disbursement of investment expenditures amounted to 76,744 million baht while current expenditures with debt-repayment and was at 292,173 million baht and disbursement of carry-over was at 32,972 million baht.
- Disbursement of state enterprises budget was at 54,952 million baht, higher than 35,305 million baht in the same period last year.
- Overall, the budget disbursement in the first quarter followed its normal path. Compare to the same period last year (of 407,395 million baht), however, the large disbursement of the

same period last year was attributable to the **delay in an implementation of Budget Act** in 2007 and thus the budget that should have been disbursed if without delay was postponed and added up into the January-March quarter. Together with higher price level, real government consumption declined by 0.1 percent in the first quarter of 2008 while public investment increased by 2.0 percent.

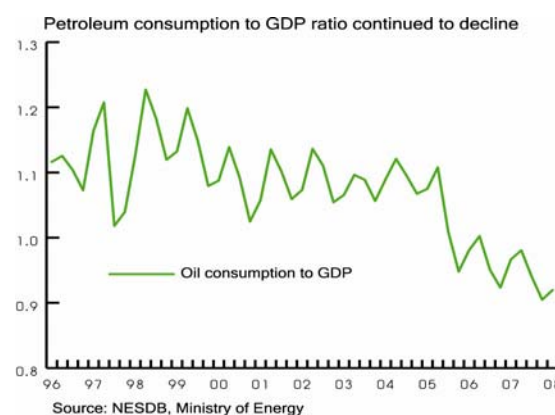
- The faster pace of credit expansion indicated that the continued interest rate cuts in 2007 started to have more impacts on real economic activities. In the first quarter, commercial banks' credit expanded by 11.1 percent, compare to 3.8 percent increase in 2007. Combined with credit extended by other depository financial institutions, credit extended to private sectors increased by 5.9 percent. Except for construction sector, credit extended to private and other business sectors increased at a faster pace. As lending rates had been kept unchanged since the second half of 2007, the reduction in real interest rates was attributable to higher inflation rate. In addition, spread between 12-month deposit and MLR had increasingly widened from 325 bps at the end of 2006 to 468 bps at the end of April 2008.
- Economic stability remained in check but the surge in oil prices continued to put upward inflationary pressures and eroded current account surplus.
  - In the first quarter, the unemployment rate remained as low as 1.6 percent, equal to that of in the same period last year. Employment picked up by 1.3 percent in response to the expansion of economic activities
  - However, inflation rate accelerated to 5.0 percent in the first quarter from 2.9 percent in the last quarter of 2007 (and accelerated further to 6.2 percent in April which raised an average inflation rate in the first 4-month to 5.3 percent, of which 2.7 percentage points was contributed by the surge in prices of foods and beverages). The broader inflation base resulted in upward pressures on core inflation which continued to pick up the pace from 0.8 percent and 1.1 percent in the third and fourth quarter of 2007 respectively to 1.5 percent in

the first quarter of 2008 and 2.1 percent in April.

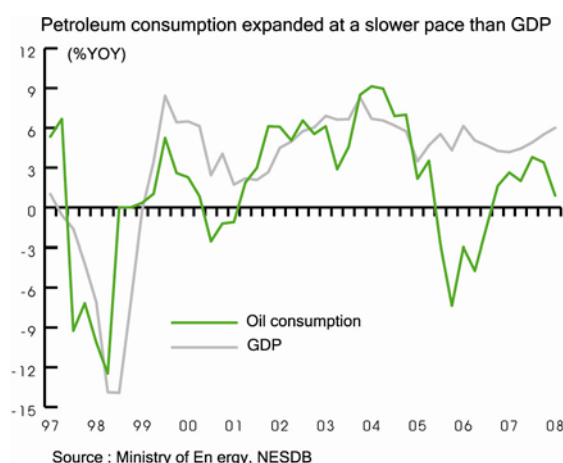
	Contribution to Inflation			
	2005	2006	2007	4 months 2008
Total	4.5	4.7	2.3	5.3
Food	1.8	1.6	1.5	2.7
Rice	0.0	0.1	0.2	0.2
Meat, poultry and fish	0.4	0.2	0.0	0.6
Vegetables and fruits	0.8	0.8	0.6	0.5
Transportation & Communication	2.2	2.0	0.5	2.0
Public Transport fare	0.6	0.8	0.1	0.1
Oil	2.4	1.6	0.3	2.3
Non-Food	2.7	2.9	0.7	2.5

Source: MOC

- Trade balance recorded a deficit of \$ 109 million which was the first deficit in 6 quarters, but service account surplus was higher than normal trend due to the strong expansion in tourism sector in combination with the increase in investment incomes. Current account continued to record a surplus of \$ 3,068 million but lower than a surplus of \$ 4,689.3 million in the first quarter of 2007.
- **The overall energy efficiency continued to improve with the adjustment in energy structure to be more balance.**
  - The ratio of petroleum used to GDP continued to decline in particular after the lifting of oil subsidy in 2005, which indicated an improvement in energy efficiency. In 2007, the ratio stood at 0.95 declined from 0.9625 in 2006 and reduced to 0.9184 in the first quarter of 2008.







% YoY	2007				2008 Q1
	Year	H1	Q3	Q4	
Total petroleum	2.7	2.3	3.8	2.4	0.9
Benzene	1.69	2.11	4.39	-1.71	-1.92
Octane(91+95)	-6.1	-0.2	-4.7	-18.78	-26.42
Gasohol	37.79	12.91	46.23	77.03	111.95
Diesel	2.13	0.73	5.61	1.81	-0.37
HSD+LSD	-1.22	-1.17	1.78	-4.15	-10.23
B5	1360.62	1081.61	1768.31	1391.93	787.29
LPG	14.3	12.59	13.59	18.15	17.59
NGV	117.61	102.92	113.29	139.8	190.52

Source : EPPD

Recent indicators, in particular in 2006, showed that the structure of energy consumption become more balance. Over the past 2-3 years, consumption behaviors have been shifted towards alternatives energy, in particular, gasohol, bio-diesel and natural gas and resulted in the reduction of energy costs.

- Consumption of alternative energy continued to increase. Gasohol and bio-diesel consumption rose sharply (from their low base level) by 111.9 percent and 787.3 percent respectively. Similarly, natural gas consumption expanded by 190.5 percent in contrast with the continual reduction in consumption of diesel, fuel oil and regular gasoline of 0.4, 15.4 and 4.2 percent respectively. This reflected the shift in consumer behaviors towards low-cost alternative energy. In addition, energy employed in production becomes more balance. For example transportation and electricity sectors that were highly dependent on gasoline, diesel, and fuel oil have increasingly employed natural gas in their production. In this respect, and in order to strengthen energy efficiency, the government is required to manage energy structure to be free from distortion and promote appropriate use of energy types among different user groups. The sharp increase in the use LPG in transportation would make a good example of further analysis.

- **Labor productivity** increased by around 4 percent in the first quarter; roughly estimated by the difference between the economic growth and employment growth.

- **In 2008, export continued to expand at a satisfactory rate due to the diversification in the structure of export markets.** The shift in market structure reduced sensitivity of the Thai economy to fluctuation in the global and industrialized economies.

- The market structure has increasingly diversified with a higher dependency on new markets in contrast with the decline in a share of Japanese and U.S markets.

(% share)	2538	2540	2545	2549	2550	2551 Q1
United State	17.8	19.4	19.8	15.0	12.6	11.7
Japan	16.8	15.1	14.6	12.6	11.9	11.3
EU (15)	15.1	15.9	15.0	13.0	12.8	12.8
ASEAN (3)	21.7	21.8	19.9	20.8	21.3	21.6
Middle East	4.5	3.3	3.6	4.4	4.9	4.8
Australia	1.4	1.6	2.4	3.4	3.8	4.0
China	2.9	3.0	5.2	9.0	9.7	9.9
India	0.5	0.5	0.6	1.4	1.7	1.7
Hong Kong	5.2	5.9	5.4	5.5	5.7	6.1
South Korea	1.4	1.8	2.1	2.1	1.9	1.9
Taiwan	2.4	2.7	2.9	2.6	2.2	1.7
South Africa	0.4	0.4	0.5	0.8	0.9	0.9
Others	9.9	8.3	8.0	9.3	10.6	11.6

Source: BOT

- Emerging economies become important export markets for the Thai economies, in particular the fast growing China, Eastern Europe and Asia. These economies, particularly Asia, are now the main growth engine for the World economy and their share in global GDP has increased steadily.
- Thailand remained competitive in electronics and mobile industries and parts due to the production base expansion of multi-national corporations and the shorter product life cycle of electronics products resulting from technological advancement that has encouraged a faster product development. The development of products with high digital contents also beneficial. For automobile, exports to Australia have increased following FTA arrangement while exports to the Middle East edged up due to higher petroleum revenues.
- Thailand has been beneficial from the sharp increase in prices of major agricultural commodities following the increase in oil prices that resulted in a heated future markets

Net trade balance

Billions US\$	2548	2549	2550					2551	
			พ.ค.	Q1	Q2	Q3	Q4	Q1	Apr.*
Trade balance (Custom basis)	-7.3	0.9	12.5	3.5	1.4	2.9	4.6	-1.2	-1.8
- Oil	-17.5	-20.1	-20.1	-4.3	-5.1	-5.4	-5.4	-6.8	-2.4
- Non-oil	10.1	21.1	32.6	7.7	6.5	8.3	10.0	5.6	0.6

Source: BOT

\* data from Ministry of Commerce

Note: Trade balance under Balance of Payment basis was deficit 109 Million dollar in the Q1/2008.

of commodities. This is partly attributable to a strong increase in demand for energy crops and the reduction of wheat in the world market as a result of supply disruption, as well as, the restriction on rice exports in Vietnam. **□ Risk**

#### factors and Concerns

- The steady increase in oil prices have adversely affected living costs and hinder to the recovery of household spending. Up to date, high oil prices pushed an upward pressures on production cost and living costs through its direct effects on energy and

transportation costs and its indirect effects in terms of higher commodity prices, in particular foods and beverages which are necessary consumption commodities with high transportation cost component. These consumption items are affected by both higher transportation costs and the steady increase of rice prices. The burdens on low-incomes group and rural people tends to be higher than that of country average as indicated by the increase in inflation indexes for low incomes group and rural people by 5.6 and 8.3 percent respectively, a faster pace than country average inflation rate. This is explained by bigger share of spending on foods to total expenditure of these groups in oppose to that of country average.

- As trade balance turned to deficit, current account surplus softened. In the first quarter, current account continued to register a surplus with the contribution of a strong expansion of services revenues that compensated the shortfall in trade balance. Nevertheless, current account surplus substantially lower than that of in the first quarter of 2007 and need specifically attention under following conditions

(i) The resurgence of oil import quantity in the presence of high oil prices (partly due to the expectation that oil prices would rise further and raise demand for stock accumulation) resulted in a deficit of oil balance of \$ 7.2 billion in the first 4-months. Therefore, it is necessary to continuously promote those measures for energy saving as well as the use of alternative energy.

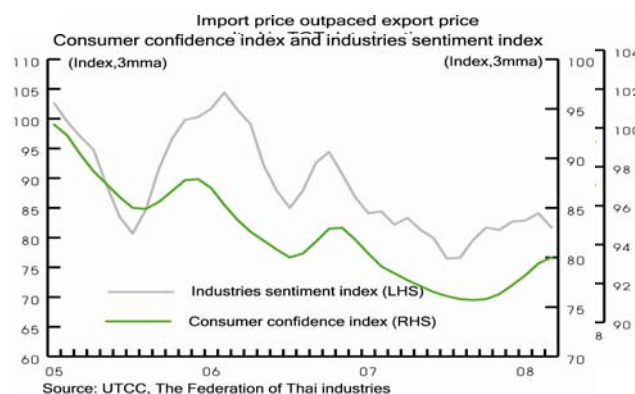
(ii) The imports for consumer goods increased substantially in the presence of baht strengthening, which is mostly demand for luxuries from high income consumers. Low deposit rate also helped stimulate the demand.

(iii) The sharp increases in imports of steels and gold under expectation that prices will continue to trend up in line with oil prices. This situation is similar to the development in 2005 which finally led to the inclusion

these commodities into the list of import management scheme.

- (iii) The expansion in imports of capital goods is likely to continue in line with investment recovery. Despite the significance of this import category to the expansion of investment, measures for capital efficiency strengthening in particular among the SMEs must be implemented and promoted.
- (iv)(v) The deterioration in terms of trade. Although, agricultural prices has increased sharply, the steady rise in oil prices drove an average import prices to grow at a faster pace than that of exports. Relatively, oil

has its larger share in total import than that of agricultural in total exports and thus export volumes must be increased to satisfy the same bills of oil imports. This is the impetus of trade deficit and will dampen national income.

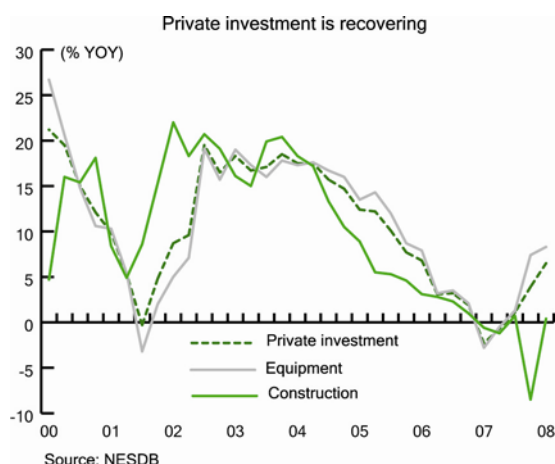
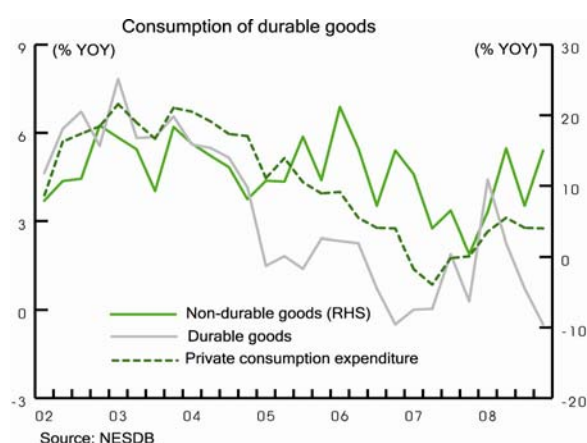
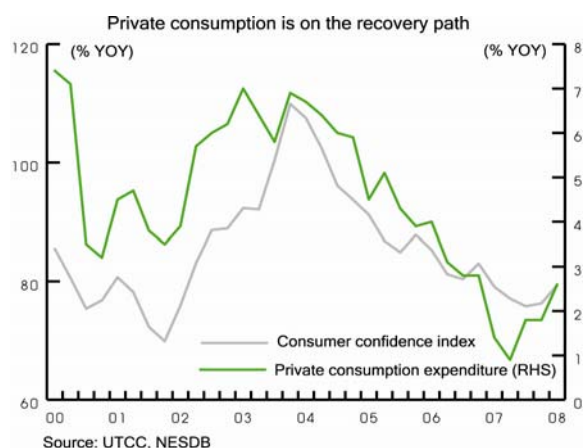


The reduction in current account surplus, without sufficient compensation from capital inflows, it would lead to deficit of balance of payment and put depreciation pressures on the baht currency. However, the stronger economic recovery would provide impetus for capital inflows and thus relief the pressure on balance of payment.

- Consumer confidence index that had increased continually since November 2007 started to decline in April. Consumer and investor sentiments are the important conditions for economic recovery to gain its momentum. However, the sentiments are eroded by various developments including the social and political disparities, the continued rising trends of oil prices and inflation. Therefore, in order to restore confidences, it is necessary for the government to hasten the measures to

relieve the negative impacts of high oil prices.

### Economic Condition in the first quarter of 2008 by sectors:



- **Household consumption expanded more strongly, supporting a continuing expansion.** In the first quarter of 2008, household expenditures expanded by 2.6 percent, accelerated from 1.6 percent in the fourth quarter of 2007. This noticeable improvement was underpinned by higher farmers' income, upward adjustment of government officers' salary and minimum wage, a lower real loan rate, and restoring of consumer confidence since November 2007. But constrained by accelerating inflation rate, recovery of household expenditures had not yet been full-fledged

**The expansion on household expenditures was driven by an increase in spending on durable goods,** semi-durable goods and food expenditure at 10.9, 3.3 and 3.4 percent respectively. However, the remarkable growth in durable goods expenditures was based on the significantly contraction of 7.5 percent in last year, impacted by an enormous decrease on consumer confidence. However, the consumption on goods and services declined by 2.7 percent, reflecting the consumer caution on their spending for luxury and indulgence. Hence, in spite of rapidly increase in total private consumption which favorably supported the economic growth, the expansion was still fragile.

- **Private investment continually recovered, in particular investment in machinery and equipment** - private investment expanded by 6.5 percent, noticeably accelerated from 3.9 percent in the previous quarter and merely 0.5 percent in 2007, partly due to low real loan interest rate and near-full production capacity utilization in various industries such as beverage, paper, petrochemical product, tire, hard disk drive, integrated circuit, washing machine and air-conditioner etc. In addition, there are some other supporting factors such as the improvement in investor sentiments as political uncertainty subsided. This strong recovery is also explained by the low base effect as the investment contracted in the first quarter of last year led by weak investor sentiments.

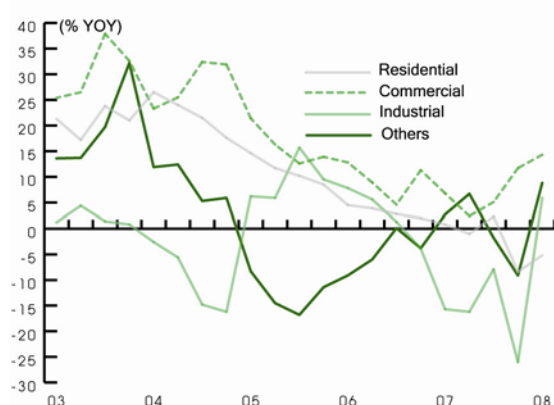
**Investment in machinery and equipment expanded** at 8.3 percent, as was reflected in the 20.0 percent increase in capital imports (in year 2000 price). The imports of electrical machinery, agricultural machinery, computer parts and equipment exhibited strong growth. Commercial



Total capacity utilization					
Year	2007				2008
	H1	Q3	Q4	Q1	
(%)					
Capacity Utilization	74.6	74.1	73.9	76.3	76.3
Beverage	81.6	81.4	76.5	86.8	87.2
Pulp and paper products	91.0	90.3	91.2	92.2	88.7
Chemical products	95.9	90.4	101.0	101.8	92.1
Petroleum products	88.2	87.5	90.8	87.1	87.2
Construction materials	78.4	78.4	80.6	76.1	79.7
Vehicles and equipment	72.6	68.9	75.7	76.9	78.0
Electronic products	79.3	72.2	81.5	91.1	80.9
Exports <30% of production	79.8	78.8	81.0	80.5	81.8
Exports 30 – 60% of production	69.6	71.4	65.9	69.7	81.0
Exports >60% of production	71.1	70.0	69.7	74.6	67.6

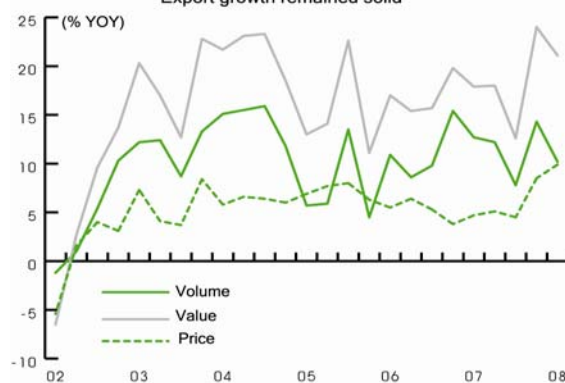
Source: Bank of Thailand

Private investment in construction



Source: NESDB

Export growth remained solid



Source: Bank of Thailand

Export of Agriculture

Year		2007				2008	
		Q1	Q2	Q3	Q4	Q1	Apr
Rice	Value	34.3	13.7	40.0	17.0	59.4	108.1
	Price	9.5	17.3	10.1	7.3	4.2	13.6
	Quantity	22.7	-2.9	27.0	7.7	53.2	82.7
Rubber	Value	4.5	5.0	2.8	-6.4	17.9	33.6
	Price	7.1	8.1	4.9	-7.2	27.0	33.8
	Quantity	-3.0	-2.6	-2.0	0.6	-7.3	0.0
Cassava	Value	23.2	51.8	34.6	-0.9	13.1	13.5
	Price	24.6	-5.6	8.1	40.7	55.8	58.9
	Quantity	3.8	61.1	24.4	-29.7	-27.4	-29.3
Corn	Value	48.7	71.1	50.3	296.3	-9.5	229.7
	Price	-7.0	29.3	-10.0	-41.5	38.5	15.0
	Quantity	22.7	53.4	38.4	395.3	-34.4	181.1

Source : MOC

sales also showed an impressive growth of 7.5 percent, after its average reduction of 5.9 percent in year 2007. Private investment in construction expanded slightly by 0.4 percent from its contraction of 8.5 percent in the fourth quarter of 2007, attributed to the acceleration on investment in commercial building construction, industrial plants construction and other constructions which increased by 14.3, 5.9 and 8.8 percent respectively, suggesting further investment in machinery and equipment imports in the future. On the other hand, housing construction remained weak at a new drop of 5.2 percent, caused by a decline in regional housing construction (which equal 70 percent of total housing construction). Due to higher spending on necessity led by inflation surge and rising prices of construction materials, some consumers have postponed their decision on housing purchase. Moreover, it is expected that home buyers are still waiting for the new tax package and generous lending offered by the Government Housing Bank to be in effect.

- **Export growth remained solid while export volumes had a tendency of slowdown.** In the first quarter of 2008, export value in US dollar terms accelerated notably at 21.1 percent growth and export volumes slowed down from 14.3 percent growth in the fourth quarter of 2007 to 10.2 percent while export price rose by 9.9 percent, comparable to that in the previous quarter. According to the latest data, export growth remained strong with an increasing value of 27.0 percent in April, resulting in 23.0 percent growth of export value during the first 4 months this year. However, in baht terms, export value and price increased at smaller rates of 10.3 and 0.1 percent respectively. April saw export value growth 13.9 percent, and resulted in 11.6 percent growth for the first 4 months.

- **Export of agricultural commodity continued its growth as a result of the rapid increase in its export price and its accelerating export volume.** Export of agricultural commodity grew significantly by 48.5 percent, compared to 28.8 percent growth in the last quarter of 2007 with its increasing volume and price of 15.3 and 26.5 percent respectively. Major agricultural exports which recorded strong expansions are rice and corn while the export price profited from the

rapid increase in global commodity prices. Consequently, all the major agricultural exports experienced high price surges, including rice, corn, tapioca and rubber.

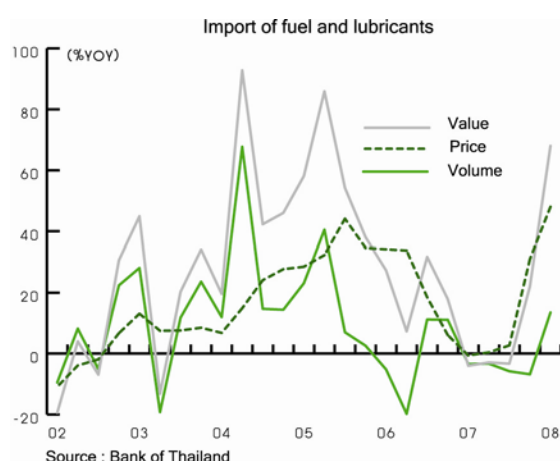
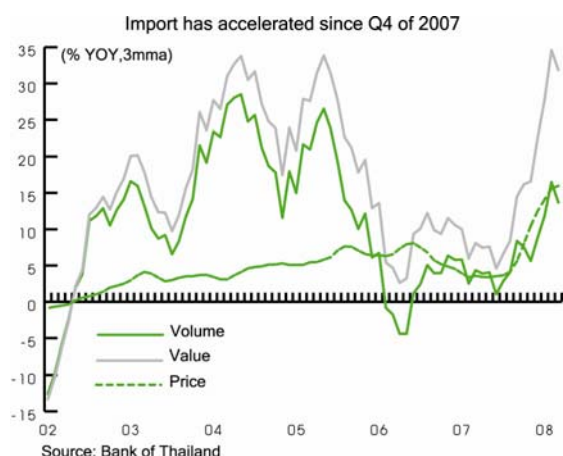
- **Export volume of manufacturing products substantially slowed down in spite of a strong expansion.** Export volume of manufacturing products has continued on a decelerating trend, increasing by 11.8 percent, slowed down from 18.0 percent in the fourth quarter of 2007. Nevertheless, its export price rose by 7.8 percent, producing an escalating export value of manufacturing products in the first quarter with 20.5 percent growth. Main drivers of manufacturing exports were air-conditioner and parts, refrigerators and parts, computers and parts, vehicle and parts, gems and jewelry, plastic, rubber products, paper products and toiletry products. On the contrary, integrated circuit, shoes and furniture experienced a sharp drop in export value. Meanwhile value of metal products export slowed down.

Key export markets (%YOY)	2007					2008	
	Year	Q1	Q2	Q3	Q4	Q1	Ratio
Major Market	11.2	12.3	12.9	2.7	17.7	11.7	51.3
US	-1.2	1.9	-1.7	-9.1	5.3	7.1	11.7
Japan	10.6	15.5	12.3	3.0	12.2	6.1	11.3
EU (15)	15.6	22.2	24.0	10.4	7.7	11.7	12.8
Asean (5)	20.1	11.6	18.8	8.3	42.2	20.3	15.6
Other Market	25.8	24.0	24.7	23.1	30.6	32.0	48.7
Hong Kong	21.2	6.1	8.6	28.6	39.4	46.3	6.1
Taiwan	-1.4	32.4	-4.7	-22.3	-5.4	-26.7	1.7
South Korea	11.1	14.1	13.7	5.2	12.1	13.9	1.9
Middle East	29.1	20.2	31.4	31.8	32.2	23.9	5.0
India	47.2	64.2	61.6	56.7	17.2	24.4	1.7
China	26.5	20.1	34.9	25.9	25.5	34.2	9.9

Source: MOC

- **Main export market has a tendency of softening but others markets continued to expand well.** Volume of Thai exports to EU and U.S.A. increased by 11.7 and 7.1 percent respectively, while volume of exports to Japan and ASEAN (5) tend to slow down with 6.1 and 20.3 percent growth as compared to 12.2 and 41.8 percent growth in the fourth quarter of 2007. Exports to the US market continuously increase in two consecutive quarters, partly due to low base in last year export when it was affected by sub-prime problem in the U.S. economy. Export products to the U.S. market such as computers and parts, rubber, and yarn and man-made filament increased in the first quarter. In addition, export to other markets continued to grow satisfactorily, for instance, exports to India (24.4 percent growth) China (34.2 percent growth), South Asia (25.5 percent growth), Africa (64.8 percent increase) Indochina (4) (58.4 percent rise).

- **Imports accelerated both in value and volume terms.** Import value grew at a remarkably rate of 34.5 percent, compared to 6.6 percent in the



fourth quarter of last year and average growth rate of 9.6 percent in 2007. The price and volume rose by 15.6 percent and 16.3 percent, respectively, attributable to growth in all import categories in particular oil imports of which price and volume picked up significantly. According to the latest data available, imports in April continued to expand by 44.4 percent, and imports in the first 4 months of 2008 consequently increased by an average 37.1 percent.

■ The strong import growth in **raw materials** was seen in gems and jewelry, iron, steel and products, crops and yields, fertilizer and pesticide, and chemicals. Meanwhile, a rise in import of **capital goods** was contributed mainly by an increase in import of computer and parts, machinery and parts, electrical machinery and parts and scientific equipments. The imported **consumer goods** which increased strongly included electrical appliances, cloths, shoes, watches and parts, and milk and dairy products, for instance. An increase in **fuel and lubricant** imports was due primarily to the import of crude oil of which price rose remarkably.

□ **Term of trade deteriorated.** Import prices in US dollar term increased by 15.6 percent, a faster pace than 9.9 percent increase of export prices. This led terms of trade to deteriorate consecutively from the latter half of 2007, jeopardizing national income and rendering trade account vulnerable.

□ **Trade balance registered a deficit of 109 million US dollars** (or 3,834 million baht). Nevertheless, service balance recorded a large surplus as a result of increases in tourist receipts, remittance of investment earnings, as well as private and state enterprise transfers. Accordingly, current account in the first quarter registered a surplus of 3,068 million US dollars (99,657 million baht), which was equivalent to 4.3 percent of GDP.

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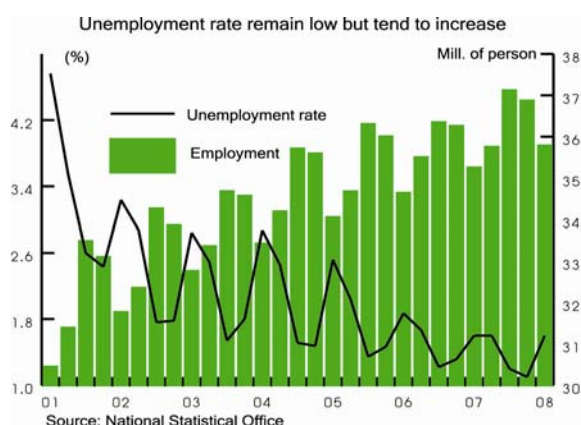
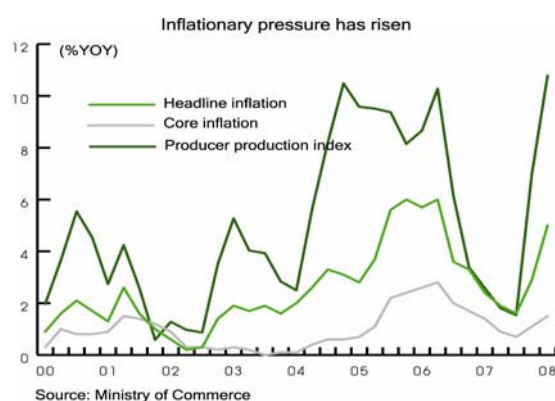
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#### □ **Production side: Better expansion with broad base**

- Agricultural sector expanded by 3.5 percent in the first quarter of 2008, slightly picked up from 2.9 percent in the fourth quarter of 2007. Production of major agricultural products which increased included corn, cassava, sugar cane, palm and rubber. Crop prices significantly increased, especially the prices of energy crops, cereal and grain, and food crops. Greater demand for alternative energy sources especially from energy crops, and supply constraint of grain have underpinned such price movement. Price rises while production continued to expand supported farm income growth of 21.1 percent.
- Industrial Sector expanded continuously by 9.7 percent, slightly picked up from 8.0 percent in the fourth quarter of 2007. The said expansion derived from greater growth of export-oriented industries and domestic-used manufacturing such as the manufacturing of petroleum products, bicycle, and passenger car. Supporting factors for the solid growth were increasing demand for energy-saving car, higher farm income, and innovation that support manufacturing of E20-alternative-energy cars for market. Relating to the export-oriented industries, the strong expansion was seen in canned sea food products, HDD products, air conditioners, and washing machines. The expansion was considered as a result of more efforts placed on branding for export, and expansion of made-to-order business to serve foreign orders. However, the leather product manufacturing contracted further, and has led some manufacturers to switch from being producers to importers for trading instead. In overall, in this quarter, the capacity utilization rate was at 76.3 percent, compared to 74.6 percent in the first quarter of 2007.
- Construction sector in the first quarter of 2008 expanded by only 1.1 percent, slowed down from 5.2 percent in the fourth quarter of 2007 and 2.1 percent. The slowdown was the result of the deceleration of government construction. However, private investment in construction expanded, especially commerce building construction. Dampening factor for construction has been a continuous increase in prices of construction, especially higher price of steel marked by 37.0 percent jump.
- Hotel and restaurant sector expanded by 8.8 percent in the first quarter of 2008, slightly picked up from 7.2 percent in the fourth quarter of 2007, and 4.9 percent growth for the whole year of 2007. The expansion was in accordance with better performance of tourism, especially reflected in the 13.3 percent rise in number of foreign tourists while the rate of occupancy marked at 68.6 percent. The rise supported a solid increase in tourism income by 27.8 percent in this quarter. Considering by nationality, the number of tourists from European and American countries, as well as China increased impressively. These are groups of tourists who have spent increasingly during their stay in Thailand.
- Financial sector grew by 9.1 percent in the first quarter of 2008, slightly picked up from 8.7 percent in the fourth quarter of 2007 and 5.7 percent for the year. The expansion was generated by loan expansion for business sector, smaller reserve requirement after completion of the requirement to conform with International Accounting Standards (IAS 39) since the end of 2007, and higher interest spread receipts.

□ **Economic stability:** Unemployment rate remains low but inflationary pressure has mounted while current account recording smaller surplus.

- **Inflation rate rose rapidly.** In the first quarter of 2008, headline inflation was 5.0 percent higher than 2.9 percent in the forth quarter of previous year, mainly due to jump in prices of food and non-alcoholic beverages as well as transportation and communication cost which increased at accelerating rates of 6.8 and 9.2



	Employment growth (%YOY)					
	2007 Avg.	Q1	Q2	Q3	Q4	2008 Q1*
Employment	1.6	1.8	0.7	2.1	1.7	1.3
Agriculture	1.0	2.8	-0.5	1.2	0.6	0.5
Non-Agriculture	2.0	1.2	1.5	2.9	2.5	1.8
Manufacturing	2.1	0.2	1.3	5.4	1.7	0.4
Construction	-0.1	1.6	1.5	-4.9	1.0	-2.0
Hotel and Restaurant	3.0	4.3	2.0	4.0	1.8	1.9
Unemployment rate	1.4	1.6	1.6	1.2	1.1	1.6

Source: NSO

\* Monthly Average

percent respectively. Substantial increases were seen in food category such as cooking oil, meats, rice and flour, fruits and vegetables eggs and dairy products. In the category of transportation and communication, fuel prices were significantly lifted up by 26.8 percent.

**Core inflation** continued to accelerate. In the first quarter, core inflation was 1.5 percent compared with 1.1 percent in the fourth quarter of 2007. This was mainly due to higher prices of various products such as food ingredients and processed food, construction materials and transportation fares

**Producer price index**, in the first quarter, continued to rise by 10.8 percent increasing from 7 percent of the previous quarter. In addition, the price index went up in all categories. Raw materials, intermediate goods and final goods increased by 16.5 13.8 and 9 percent respectively. The strong increase in prices of raw material category was mainly accounted by the up surge of food prices such as rice and starch products (noodles) as a result of a huge increase in price of paddy rice. Chicken price as well as prices of other major agricultural products also went up. The rises in producer price index suggest further pressures will be passed to consumer prices, and thus higher cost of living for all walks of life. That said high inflation rate is still anticipated in the remaining months.

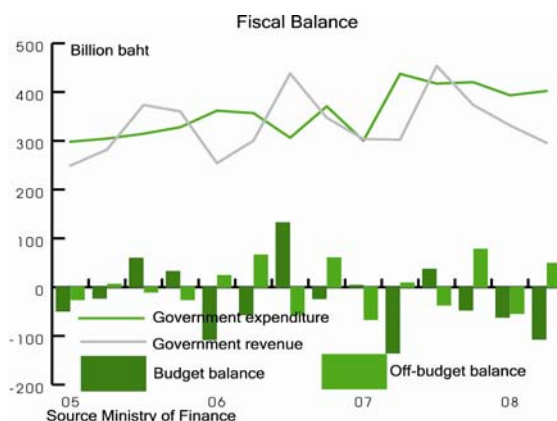
- **The average employment in the first quarter of 2008.** There were 35.78 million people employed in the first quarter which increased by 1.3 percent from the same period last year. Numbers of employment in agricultural sector were 12.48 million people, increased by 0.5 percent. Numbers of employment in non-agricultural sector were 23.30 million people with an increasing rate of 1.8 percent. The higher rate of employment was witnessed in industrial and hotel and restaurant sector, with an increasing rate of 0.4 and 1.9 percent, respectively. The increases were in accordance with the tourism revitalization. For construction sector, its employment rate reduced by 2.0 percent in response to slowdown in its growth. The



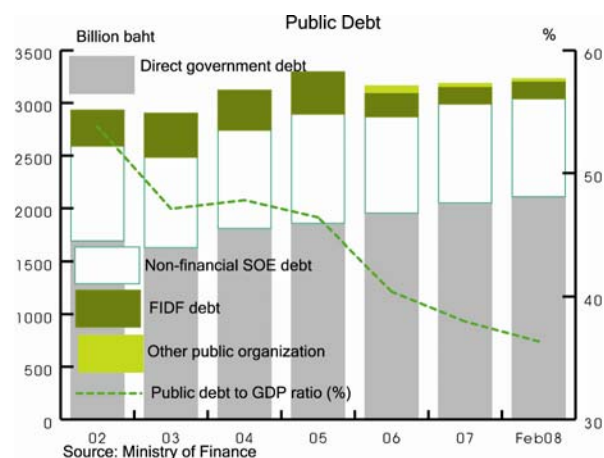
unemployment rate was as low as 1.6 percent. In the first quarter of 2008, insured persons were marked at 8.82 million people, increased by 1.3 percent comparing with the same period last year. However, some indicators depicted that the sound economy growth did not fully generated employment as expected because the growth sectors were concentrated more in the capital-intensive industries. This was implied from the proportion of the unemployed to new job-applicants which remained at 0.88 times, as compared to 0.80 times in the first quarter of 2007

- Fiscal balance remained in deficit in response to budget deficit policy.** In the second quarter of fiscal year 2008 (January – March 2008), the total of government revenue was 295,782.07 million baht, decreased by 2.2 percent compared to the same quarter of the last fiscal year, whereas the government expenditure was 402,207.49 millions baht, decreased by 8.0 percent. Therefore, budget balance recorded a deficit of 106,425.42 millions baht, decreased by 28,539.48 millions baht, or dropped by 21.1 percent from the same period of the last fiscal year. Including a surplus of the non-budget balance of 46,684.14 million baht, budget cash balance before borrowings was 57,741 million baht, decreased 68,793 million baht, or declined by 54.4 from the same quarter of the last fiscal year.

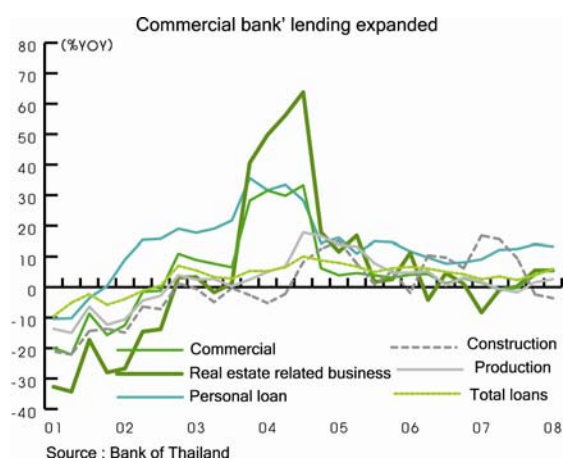
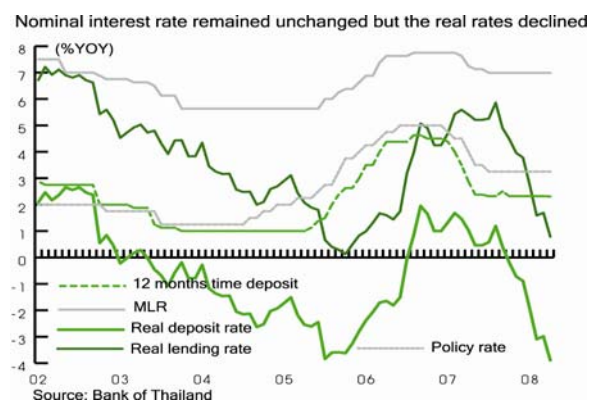
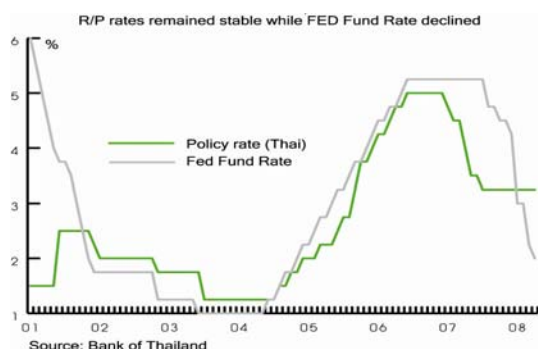
During the first half of the fiscal year 2008 (October 2007 – March 2008), budget balance recorded deficit of 168,133.88 million baht. Combining with a deficit of the non-budget balance of 5,254.02 million baht, cash balance registered a deficit before borrowings around 173,387.40 million baht. Comparing with deficit target of fiscal year 2008 of 165,000 million baht, deficit during the first half of the year has already surpassed the target around 8,387.4 million baht. Government bonds and T-bills in total of 85.447 million baht, together with the withdrawal of treasury cash balance of 87,939.52 million baht, have been issued finance the deficit budget.



- Public Debt** At the end of February 2008, public debt stood at 3.33 trillion baht, increased from the outstanding of public debt at the end of the year. This is mainly because of an increase in direct government debt especially domestic debt to balance the deficit budget as well as an increase of FIDF's debt of non-guaranteed by the government. However, ratio of public debt to GDP slightly decreased to 36.35 percent, down 37.97 percent at the end of the December 2007.



- Financial conditions:** Money market interest rates remained unchanged but real interest rates declined. Bank deposits and credits, both household and commercial, expanded. However, liquidity remained high. The Thai baht continued to appreciate in nominal terms, but depreciated in real effective terms. SET index was volatile due to the fluctuation in foreign capital movement.



- Policy rate was kept unchanged** at 3.25 percent during the first quarter, even though many countries had lowered their policy rate in response to the recovery in domestic economy while upward pressures on core inflation had increased. The Federal Reserve Board lowered Fed Fund Rate 3 times from 4.25 percent in December to 2.25 percent in March and cut further to 2.0 percent at the end of April due to higher risks to economic growth. Euro zone and Japan maintained policy rate at 4.0 and 0.5 percent respectively. In the first quarter, most Asian Central Banks tended to maintain their policy rates and cautiously monitored the proceeding impacts of the sub-prime crisis, which in turn will affect the export market especially to United States and Euro area. The accelerating inflation rate heightened policy alert in the upward direction. On the other hand, the opposed pressure also increased from widening of interest rate differential between Fed Fund Rate and domestic policy rate.
- Commercial banks' deposit and lending rates were on hold in line with the policy rate. However, real interest rate declined due to inflation acceleration.** Average 3-month and 12-month time deposit rates of five major commercial banks have remained at 2.13 and 2.32 percent respectively in the first quarter. The MLR lending rate was averaged at 6.99 percent per annum. Adjusted by accelerate inflation rate at 5.3 percent in March, the real 12-month time deposit rate turned to negative of 2.99 percent while the real lending rate declined to 1.69 percent. In April, inflation rate continued its raise at 6.2 percent, has decelerated the real 12-month time deposit rate and the real lending rate to negative of 3.89 percent and 0.79 percent respectively.
- Commercial banks' deposits and credits accelerated.** Commercial banks' deposits grew by 2.5 percent at the end of the first quarter compared to that of 0.1 percent at the end of the fourth quarter of 2007. The growth was due to increasing in special saving

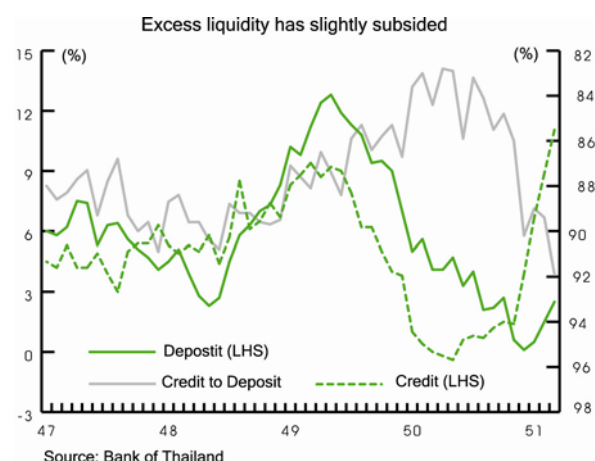
products with high deposit rates offered by commercial banks. Deposits increased rapidly in the account with less than 1 million and more than 50 million baht. Commercial banks' credits expanded 11.1 percent compared to that of 3.8 percent at the end of December 2007.

In terms of credit extended by depository corporations<sup>1</sup>, it expanded by 5.9 percent compared with 4.0 percent at the end of fourth quarter of 2007. The increase was seen in most sectors. Household credits expanded by 8 percent, slightly picked up a pace from the previous quarter. Loans to corporate sector expanded by 2.9 percent from 0.7 percent at the end of December 2007. Increasing commercial credits showed investors' confidence in economic growth and prospect. Considering by sectors, loans to manufacturing, wholesale and retail, real estate, and agricultural sectors have increased at 3-13 percent, whereas loans to construction sector has declined. Furthermore, loans to financial intermediation expanded by 93.2 percent. Due to central bank provided soft loans to SME's via financial institutions in order to strengthening SME's productivity. Loans to personal consumption slightly increased from the previous quarter and expanded by 13.3 percent from March 2007. This was mainly attributed to increased of housing loans and purchase and hire purchase loan, which continually growth in high pace since mid 2007.

Credit card spending slightly decreased from the preceding quarter, but cash advance increased. Therefore, credit card outstanding balance expanded from the first quarter 2007 by 5 percent.

- **Liquidity in commercial banking system has increased.** Accelerating of commercial bank credit led credit to deposits ratio increased from 94.8 percent at the end of December 2007 to 96.5 percent at the end of

March 2008, however still indicating ample level of liquidity. Besides excess liquidity in banking system, estimated as disposable liquidity, was approximately 1,035 billion baht at the end of March, higher than 822.2 billion at the end of December 2007. This was due to the increasing of financial institutions' investment in the repurchase market with net lender position.

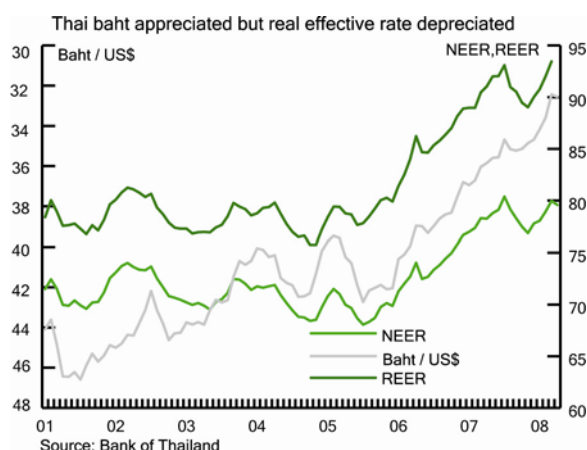


- **NPLs declined.** NPLs in financial institutions (excluding BIBF and credit fanciers) at the end of the first quarter 2008 equaled 249.4 billion baht, which is 3.76 percent of total credits. It declined from 3.95 percent from the previous quarter.
- **Listed companies earning reported high growth.** Listed companies on SET showed net profit 152.4 billion baht, which is 33 percent more than the same period in 2007. The increased profit due to rise in total sales and gains from exchange rates. 384 companies posted net profit, while 71 companies reported net losses. Most profitable sectors were energy and banking sectors. Thai commercial bank also reported high earnings, with net profit of 31 billion baht compare to net loss of 7.5 billion baht at the fourth quarter of 2007. That partly because their burden on higher provision for loan loss under the application of International Accounting Standard (IAS39) almost had overcome as they make full provision since the end of 2007. Furthermore,

<sup>1</sup> Depository Corporations comprises of all depository corporations excluding the Bank of Thailand, namely, domestically-registered commercial banks, branches of foreign banks, international bank facilities, finance companies, specialized banks, thrift and credit cooperatives, and money market mutual funds.

they gained high profit from return on investment and exchange rate.

- Thai baht continued to appreciate in nominal terms as compared to the US dollar but real effective exchange rate weakened.** Average exchange rate in the first quarter was at 32.38 baht per US dollar, appreciated significantly by 4.45 and 8.88 percent from the fourth quarter last year and the same period of last year respectively. The appreciation was mainly attributable to various underlying factors including the impact of sub-prime crisis, especially to financial institutions, that caused US dollar to depreciate further, and the increase in balance of payment surplus. In the first quarter, the movement in Thai baht against the US dollar and other major currencies was volatile. Considering the movement of Thai baht against other currencies, it appreciated against other major and regional currencies but depreciated against Japanese Yen and Philippine Peso. Therefore, average nominal effective exchange rate (NEER) and real effective exchange rate (REER) appreciated by 0.88 and 1.96 percent respectively. In April, an average exchange rate was at 31.53 baht per US dollar, depreciated by 0.39 percent from March. Result from market speculation on Federal Reserve Board decision to hold policy rate at 2 percent until the end of the second quarter which trigger appreciation in US dollar. At the same time, increased in import volume had created demand for US dollar from Thais' importers.

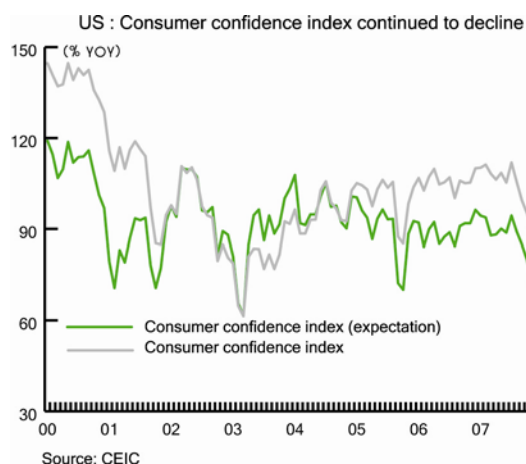


- SET index and trading volume decreased.** Average daily trading value was 18.8 billion baht, declined from 19.4 billion baht in the fourth quarter last year. SET index closed at 817.03 points, down from 858.1 points at the end of the fourth quarter last year. Net sale of foreign investor was recorded at 13.9 billion baht. In the first quarter, the market became more volatile. SET index plunged to 728.58 points at the end of January, from unexpected interest rate cut by Federal Reserve Board which directly affects investor confidence. During February through to March, SET slowly rose to 845.76 points (highest point in the first quarter), fueled by foreign net buy from 3 main factors: 1) Lifting of the Reserve Requirement on Short-term Capital Inflows by Bank of Thailand 2) implementation of new tax policy to boost economy and 3) increase in oil price.
- Bond trading accelerated.** Daily average outright trading increased from 47.3 billion baht in the fourth quarter last year to 62.8 billion baht in the first quarter. Net buy of foreign investors was recorded at 29 billion baht. Bond price index increased slightly. Government bond yields declined, particularly those of medium-term maturity. In April, daily average trading volume was at 84.2 billion baht, with the net buy from foreign investor of 6.7 billion baht.
- Corporate funding** (excluding short-term bond) in the first quarter was at 72.7 billion baht compared to 66.3 billion baht in the fourth quarter last year and 42.5 billion baht in the same period last year. Fund raised by both financial and non-financial sectors registered 18.8 and 286 billion baht respectively. The issuance of private placement accounted for 58 percent of total transaction.



## 1.2 The world economic performance in Q1/2008

In the first quarter, the world economy slowed down as economic activities in most major economies softened. Although the economic growth rate was the same as that in previous quarter, growth components suggest that the U.S economy remains on down trend. For example, residential investment still experienced steady contraction, reflecting the lingering impacts of sub-prime crisis. Its spillover effects had broadened to European financial system and eroded consumer and investor confidences. Similarly, Japanese economy continued to slow down due to contraction in residential investment while the Chinese economy was weakened by the slowdown in exports. Nevertheless, contributed by a strong expansion of intraregional trade and domestic demand recovery, growth in Asian region remained solid.

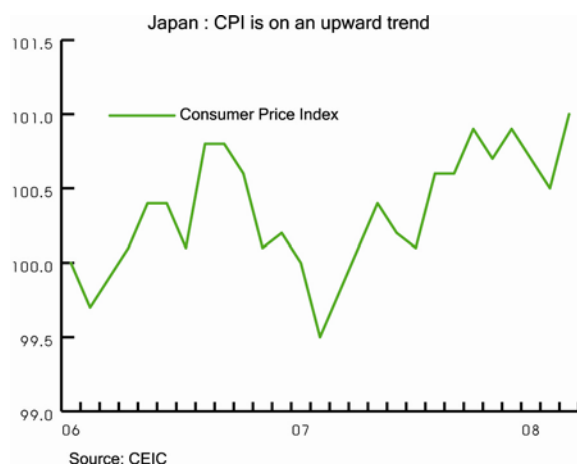


□ **The US Economy** grew by 2.5 percent, unchanged from previous quarter (and 0.6 percent qoq, annualized). The moderate rate of economic growth was mainly driven by the expansion of net exports, household consumption and inventory accumulation. These factors offset the continual contraction of investment, in particular that in residential sector. The glut in housing market was reflected in various indicators such as housing starts that declined steadily since Q2 of 2006 as well as the reduction of new home sales of 21.8 percent in Q2 compare to 10.2 percent in Q1. This situation continued to put downward pressure on home prices and eroded collateral values of existing loans. Household consumptions, on both durable and nondurable goods, softened while retail sales slowed down from 12.2 percent growth in previous quarter to only 0.1 percent, in line with the reduction in consumer confidence that reached its lowest level since 2003. In addition, the slowdown in domestic demand dragged on production as reflected in a reduction of ISM index which registered at 48.6 in March and a reduction of manufacturing new orders. In terms of stability, inflationary pressure picked up as headline inflation accelerated to 4.1 percent due to the surge in primary commodity and oil prices. Core inflation stood at 2.4 percent compare to 2.3 percent in previous quarter.

□ **Euro-zone economy** grew by 2.2 percent in Q1 (0.7 qoq, sa), slowed down from 2.6 percent in the last quarter of 2007. The base of growth increasingly broadened. Growth rates in Germany and France were stronger than in Q4 of 2007 and higher than market expectations due to a strong expansion in their exports. Spain and Netherlands slowed down due to weak domestic demand which was the result of financial market fluctuation and credit standard tightening. Exports softened in line with the slowdown in the world economy and exchange rate appreciation. Price pressures steadily heightened and drove average inflation rate from 2.9 percent in Q4 of 2004 to 3.4 percent, which is above the policy target. Against these developments, the ECB maintained its policy rate at 4.0 percent.

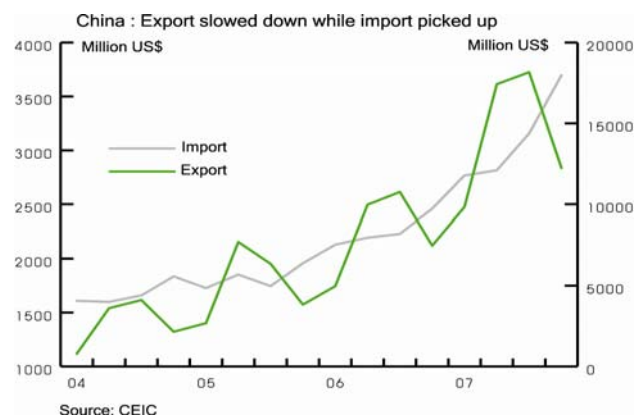


□ **Japanese economy** decelerated from 1.7 percent growth in Q4 of 2007 to 1.0 percent growth in Q1, the continually deceleration since Q2 of 2007. Residential investment continued to decline although housing construction showed signs of recovery. Investment prospects remained weak as indicated by the contraction in non-residential investment for the first time in 5 years. Business profits decreased and business confidence softened. New orders for industrial machinery are likely to contract while private consumption remained fragile as consumer turned to pessimistic about general economic situation and inflation acceleration. Export growth, the main driver for economic expansion in Q1, remained solid in particular exports to China and other Asian countries. However, imports increased at a faster rate and subtracted growth contribution from net exports. Inflation accelerated and drove an average inflation rate to 1.0 percent in Q1. This, encouragingly, may imply the end of prolonged period of deflation. Against these developments, the BOJ kept its policy rate unchanged at 0.5 percent. However, as the core inflation remained at zero rates, it is likely for the BOJ to cut its policy rate if economic development deteriorated further.



□ **Asian Economy** grew solidly due to previous episodes of monetary policy expansion and the recovery of domestic demand, in particular, investment expansion that contained the negative trade effects from the downturn of the U.S economy. Export to intra-regional and new markets expanded at a satisfactory rate while imports increased at a faster rate in line with the recovery in domestic demand. Inflation pressure heightened but partially had been offset by the appreciations of regional currencies. Nevertheless, which was driven by the increases in oil and food prices, the steady rise in inflation is likely to render policy decision in the region more difficult.

■ **Chinese economy** also slowed down from 11.2 percent in Q4 of 2007 to 10.6 percent in Q1 consistent with the slowdown in industrial production from 18.3 percent in the first quarter of 2007 to 16.4 percent in this quarter. On expenditure side, export growth remained buoyant with an expansion rate of 21.4 percent (the export growth rate accelerated from 6.5 percent to 30.6 percent in February before softened to 21.8 percent in April). Imports increased at a faster rate and eroded growth contribution from net exports. However, the growth of aggregate economy remained solid due to the resumption of domestic demand expansion, which partially offset the slowdown of growth contribution from net exports. Retail sales increased by 20.6 percent, picked up the pace from 20.2 percent in Q4 of 2007 quarter. Investment in durable goods increased by 24.0 percent. Higher food costs resulted in an accelerated rate of inflation. Core inflation was at 8.0 in Q1 (and 8.5 percent in April), compare to 6.3 percent in previous quarter.



- South Korea's economy** grew by 5.7 percent in Q1, equal to previous quarter (on qoq basis, the economy grew by 0.7 percent, the slowest pace in 3 years). Consumption cooled down from 4.1 percent growth in Q1 2007 to 3.5 percent. Companies started to scale back their spending. Investment expansion slowed down significantly from 7.2 percent to 0.9 percent over the same period. Exports continued to grow at a satisfactory rate of 12.1 percent but slowed down from 17.0 percent of previous quarter while imports growth slowed down from 14.4 percent to 9.5 percent. Therefore, net exports increasingly contributed to growth in Q1. Unemployment edged up to 3.1 percent in March as manufacturing sector layoff workers. These indicators indicated that the Korean economy had entered a slowing period. Signs of a slowdown emerged in the pace of accelerated inflation and the slowdown in the global economy. Inflation hit a 3 years high of 3.9 per cent in March while consumer sentiments turned pessimistic for the first time in a year and manufacturers' confidence declined from a three- month high. Against these developments, the Bank of Korea kept interest rates at 5 percent.

## 2. Economic Projection for 2008

### 2.1 The world economic outlook

For the rest of 2008, the spillover from the sub-prime crisis and the slowdown in the U.S. economy will continue to hamper the global growth. The impacts of housing market deterioration and tight credit condition on the real U.S. economy are likely to become more materialize in Q2 while the latest indicators suggested that the impacts of financial and U.S. economic fluctuations on other industrialized economies are larger than previously expected. The Asian economies are weathering but not fully decouple from the slowdown in industrialized nations. Taking into account the latest developments, growth of the world economy is forecasted to slowdown from 4.9 percent last year to 3.8 percent in 2008. Meanwhile, the increase in inflationary pressures increasingly restrains domestic demand expansion and limits the room for exchange rate policy intervention.



World economic projection

	2549	2550					2551 f	
		Q1	Q2	Q3	Q4	Year	Jan08	Apr08
World	4.9	4.6	5.0	5.3	4.7	5.0	4.1	3.8
USA	2.9	1.5	1.9	2.8	2.5	2.2	1.2	1.0
Eurozone	2.9	3.1	2.5	2.6	2.2	2.6	2.0	1.4
Japan	2.2	2.8	1.6	1.9	1.8	2.1	1.6	1.4
Singapore	8.2	6.4	8.7	8.9	5.4	7.7	6.0	4.0
Korea	5.0	4.0	4.9	5.2	5.7	4.9	4.5	4.2
Philippines	5.4	7.1	7.5	6.6	7.4	7.3	6.0	5.8
Malaysia	5.9	5.5	5.7	6.7	7.3	6.3	5.5	5.0
China	11.1	11.1	11.9	11.5	11.2	11.4	10.0	9.3
Vietnam	8.2	7.7	8.8	8.7	9.3	8.4	8.0	7.3

Source: CEIC , Public agencies and average value from many sources

## 2.2 Economic Projection for 2008: Private consumption and investment are set to expand more solidly from the low base of last year and help compensate for the slowdown in net export. Energy and food pressures will keep inflation elevated. Current account will remain in surplus, though probably a smaller one than that of last year.

### 2.2.1 Main Themes

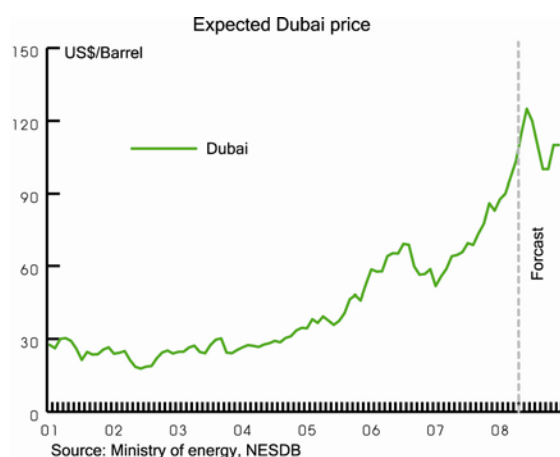
- ❑ **The higher than expected economic growth in the first quarter and favorable factors supporting the recovery of domestic demand will boost the economic momentum in the rest of the year.** In the first quarter, private consumption and investment continued to improve. In the rest of the year, private consumption and investment is foreseen to recover on the back of favorable factors including (i) the low level of interest rate, (ii) an increase in income base, primarily made of rising agricultural price of main crops (rice, rubber, cassava, and palm oil) will benefit farmer to have higher farm income. The salary raise for government servants and state-owned enterprise employees which will be fully effective in 2008 and the additional increase which will be in effect in July will also increase income and support the recovery. The increase in minimum wage of 1-7 baht per day since January 1 and the additional increase in July will be another source of income increase, (iii) the government measures to stimulate and strengthen the Thai economy. These measures include (1) tax stimulus measures to increase people's purchasing power, promote household savings, and help the underprivileged group (2) tax measures to encourage investment and increase competitiveness (3) soft loan provided to boost local economy and to promote productivity enhancement of small and medium-sized enterprises (SMEs).
- ❑ **However, there remain downside risks which must be efficiently managed in the remaining of the year.** This includes (i) the upsurge in oil prices, food prices, and cost of living. In light of tight labor market condition

and high capital utilization rate, inflationary pressures could be mounted easily unless the productivity is increased. (ii) smaller current account surplus led by the rapid increase in import and the substantial deficit of oil trading. (iii) deterioration of consumer and business confidences appear to kick in considering from their decline in April amid rising cost of production and rising conflicts over constitutional amendment. (iv) the impacts of the world economic slowdown on exports is likely to be more manifested in 2008.

- ❑ **The assessment of strong growth in the first quarter, favorable and risk factors in the remaining of 2008 indicates that the Thai economy looks set to pick up pace from 2007. The composition of economic growth will be more balanced as contribution from domestic demand will be larger than that in 2007 and help offset for the decline of contribution from net export.** The growth of export volume is likely to remain on a satisfactory pace in spite of the expected slowdown. However, the import volume will increase more rapidly and thus dampen the contribution of net export volume.

### 2.2.2 Key Assumptions for 2008 Projection

- ❑ **The global economy is expected to grow by 3.8 percent, softening from 4.9 percent in 2007.** The assumption on the world economic growth is revised downward from the assumption of 4.1 percent employed in the previous forecast. The downward revision was mainly due to the reduction in economic growth in the US, Japan, Europe, China, South East Asia and Asia. The downward revision may be explained as follows:
  - (1) The latest economic indicators showed that the impact of sub-prime problems on the US economy will be more severe than expected. This induced export of Japan, Europe and Asia to slow down in 2008. In addition, government stimulus measures to encourage investment in many countries will lead to higher import growth. As a result the contribution of net export on economic growth will be less.



Crude oil price and retail oil prices

U.S. dollars per barrel and baht per liter	2006	2007					2008	
	Year	Q1	Q2	Q3	Q4	Year	Q1	22 May
Oman	62.6	55.7	65.2	70.7	83.41	68.75	92.34	129.12
Dubai	61.5	55.4	64.8	70.1	85.10	68.83	91.50	128.98
Singapore 95	73.2	68.3	85.7	81.7	95.79	82.88	105.1	140.55
Singapore HSD	76.5	69.7	81.3	86.5	102.60	86.87	114.4	173.10
Retail Benzene 95	27.6	25.8	29.6	28.8	31.69	29.18	33.05	39.09
Retail Diesel	25.6	23.4	25.2	25.9	28.45	25.66	29.36	35.94

Source: Energy Policy and Planning and Office

- (2) The sharp increase in oil price will dampen the prospect of economic growth in most countries.
- (3) The hike in inflation rate fueled by high oil and food prices will be passed through to other commodities' prices on a wider spectrum. This secondary effect will be built-in the core inflation and set to increase. With higher core inflation, the conduct of expansionary monetary policies to boost domestic demand will be under a considerable scrutiny and caution.

□ **Dubai crude oil price in 2008 is expected to increase from the average of 68.83 dollars per barrel in 2007 to be around 110-120 U.S. dollars per barrel in 2008, revised upward from the previous forecast of 80-85 U.S dollars per barrel<sup>2</sup>** The Dubai crude oil price was averaged at 91.50 U.S. dollars per barrel during the first quarter and at 97.97 U.S. dollars during January to May 22, 2008, up considerably by 67.10 percent from the same period of last year. On May 22, the Dubai price jumped to 128.98 U.S. dollars. The upward revision of assumed oil price was a result of the higher than expected of crude oil price in the first five months, the expected tight oil market and the depreciation in U.S. dollars. However, crude oil price is likely to be slightly leveled off in the latter half of the year as the world economy softens and the U.S. dollar is likely to stabilize.

□ **Export price in terms of U.S. dollars will increase by 7.0 percent while import price will increase by 11 percent.** These unmatched increases are expected to deteriorate term of trade. That said as the prices of oil import and raw material import increase, Thailand will need more of export revenue to finance import as the prices of

<sup>2</sup>

EIA revised the WTI crude oil price upward from the April forecast of 101 U.S. dollars per barrel to 110 U.S. dollars per barrel in 2008, higher than 72 U.S. dollars per barrel in 2007. The WTI price will slightly decline to 103 U.S. dollars in 2009. Lehman Brothers forecasted the Brent crude oil price to increase from 72.60 U.S. dollars in 2007 to 103 U.S. dollars in 2008 and 83 U.S. dollars in 2009.

imports are relatively more expensive. Given that the agricultural products which have enjoyed high rise of their prices account only a little less than 10 percent of total exports. Their price surges are, therefore, not sufficient to cover oil import bills.

**2.2.3 Economic outlook for 2008: Thai economy is expected to grow at 4.5-5.5 percent with 5.3-5.8 percent of headline inflation and a current account surplus at 2 percent of GDP**

- (1) In the press release on the 25th of February 2008, Office of National Economic and Social Development Board (NESDB) projected that the Thai economy will grow at 4.5-5.5 percent with 3.2-3.7 inflation rate and a current account surplus at 4.1 percent of GDP
- (2) In this release on the 26<sup>th</sup> of May 2008, NESDB maintains the 2008 economic growth projection at 4.5-5.5 percent despite higher-than-expected oil prices and inflation rate. The overall growth is, however, likely to be contributed by different growth components from those projected in the previous forecast. Moreover, the economic growth will ease slightly towards the end of the year as the high base effect kick in saying that the recovery of domestic demand will not be able to completely offset the foreseen dampening contribution of net export volume. Maintaining of the previous overall growth forecast of 4.5-5.5 percent is underlined by the following reasons:
  - i. Higher-than-expected economic growth in the first quarter will offer a springboard for further growth as the stronger economic momentum is priced in over the coming quarters
  - ii. Thai exports remain solid with a better performance than expected in both manufacturing and agricultural products
  - iii. Number of foreign tourists is expected to expand in line with its target at 15.7 million with 4.3 million already traveled to Thailand during the first quarter,

increased by 13.3 percent from the same period of last year.

- iv. Other supporting factors such as upward salary and minimum wage adjustment, implementation of tax measures to boost up consumption and investment, credit measures for grassroots economy and higher prices of agricultural products will enhance consumption and investment to grow at least at the rate that was previously projected

**2.2.4 Projected growth components in 2008.**

On the demand side, growth contribution is expected to be more balance in 2008, with a larger growth contribution from domestic demand in contrast with a smaller contribution from net exports.

- (1) Total consumption expenditure is projected to increase by 4.7 percent, a faster pace than that of 2.7 percent in 2007. Although, oil prices and inflation are higher than those in previous projection (on February 25), the current projection keeps the growth of private consumption unchanged at a rate of 3.8 percent due to additional supporting factors mentioned above (fiscal stimulus package, financial package, upward salary and minimum wage adjustment and, higher prices of agricultural products). Public consumption expenditure is projected to expand by 10.0 percent reflecting back-loaded disbursement in the latter half of 2008.
- (2) Investment is forecasted to pick up the pace to 8.5 percent growth, stronger than 1.4 percent in 2007 and higher than 6.7 percent in the previous projection. Private investment is projected to grow by 9.3 percent (upward revision from 7.0 percent in previous forecast) and 6.0 percent for public investment. The upward revision is attributable to (i) the strong than expected expansion of investment and imports of capital goods in the first quarter and (ii) the contribution from additional government measures such as



- Tax measures to support community enterprises and SMEs (which are including personal income tax exemptions for unregistered partnerships under Community Enterprises Act with their earning revenues of less than 1.2 million baht a year, corporate income tax exemptions on the net profit of 150,000 baht for corporations and partnerships with their registered working capital of less than 5 million baht
  - Tax measures for investment stimulation and competitiveness strengthening. These are including a greater rate of capital allowance for machinery, corporate incomes tax exemption for expenditures on energy-saving machine installation, capital allowance for software, the reduction of specific business tax rate from 3.0 percent to 0.1 percent for property businesses, and a reduction of fee for transfer and mortgage of property from 2 percent to 0.01 percent.
  - Housing credit program from Government Housing Bank is expected to stimulate residential investment.
- (3) Value of exports in dollar terms is projected to increase by 13.3 percent, upward revision from 12.2 percent in previous projection but lower than 18.1 percent in 2007. The projection for exports quantity is revised upward to 6.3, in line with its strong expansion in the first 4-months. However, growth of export quantity is likely to slow down in the second half of 2008, in tandem with the downward trend of the world economy. In addition, export price is revised upward due to higher oil and agricultural prices. Exports of rice, cassava, foods, electronics, and cars and parts, are expected to grow solidly.
- (4) Import value is forecasted to expand at an accelerate rate from 9.6 percent in 2007 to 22.0 percent, upward revision from 15.4 percent in previous projection due to the recovery of investment and consumption reflected in import surge in the first 4 months.
- The upward revision of import value is the result of both import prices and quantity upward adjustment in line with recent strong expansion of import values.
- (5) Trade balance is forecasted to register a surplus of \$ 1.5 billion. Combined with surplus in services account, current account balance is projected to register a surplus of around 2.0 percent of GDP, downward revision from 4.1 percent in previous projection.
- (6) Inflation rate is likely to pick up the pace to 5.3-5.8 percent, higher than 3.2-3.7 percent in previous projection. This revision takes into account upward pressures from (i) higher costs of oil, raw materials (ii) higher foods and agricultural prices (iii) upward salary and minimum wage adjustment and (iv) stronger domestic demand for goods and services.

#### 2.2.5 Projection conditions for High and Low case

- (1) The high case scenario of 5.0 percent expansion or higher. The Thai economy in 2008 is projected to expand at a rate of at least 5 percent under following conditions (i) global economy grow at a rate of at least 3.8 percent. Export sector is capable to adjust to higher cost of production as well as to maintain its current position in the world market. With this condition, the export sector is likely to generate incomes from exports and tourisms by another 13.0-15.0 and 8.0-9.0 percent respectively (ii) budget disbursement of at least 85 percent of planned budget for government and state-enterprises. Disbursement priory is given to vocation development projects for low income group and social infrastructure development projects (iii) consumer confidence is fully restored following its reduction in April (iv) a better oil market condition due to the OPEC production expansion. With this condition, crude oil price is likely to decline to the level not higher than yearly average of \$ 110-115 per barrel in 2008.

- (2) The low case scenario. The Thai economy in 2008 is projected to expand at a slower pace than 5.0 percent under following conditions (i) the world economy slows down at a faster pace than expected with the growth rate of less than 3.5 percent. Under this condition, the spillovers from NPLs and oil prices increases hinder global economic expansion and thus restrain exports growth of the Thai economy (ii) budget disbursement rate fall below 80 percent and (iii) yearly average crude oil prices (Dubai) rises to higher than \$ 120 per barrel.

**Base on the assessment of supporting and risk factors including higher – than – expected growth in the first quarter of 2008, It is projected that the Thai economy is likely to register 5.0-5.5 percent expansion.**

## 2.3 Production side:

Agriculture, manufacturing, tourism and real estate sector tend to expand comparing with a rate in 2007. For financial sector, higher growth in credit expansion is expected. Nevertheless, many financial institutions are now entering the transition period, as they have to adapt to the new rules and regulations, such as the BASEL II and new deposit insurance act. Production side outlook is as follows:

- (1) Agriculture sector** is expected to improve especially in key products, for example:

**(1.1) Rice:** Production of rice tends to improve due to adequate supply of water and favorable price. High price is expected as a result of higher demand from foreign market. In addition, the competitors such as Vietnam and India have revised down its export target in order to maintain its homeland food security, while government already approved the “Thai rice strategy” in order to improve quality and varieties of “Thai rice product”. This strategy aims to strengthen consumer confidence which will lead to better farmer income. Moreover, Thai rice product is gradually delivered into

market. The said product is expected to increase by 12.0, compared to a rate in 2007.

**(1.2) Cassava:** Output of cassava is likely to increase as result of greater domestic demand from alternative energy use, especially Gasohol 91 and 95. Moreover, Ministry of Energy targets the Ethanol production in 2008 for 1.3 million liters per day, increasing from 0.5 million liters per day in 2007. The said target leads to higher demand for cassava in order to serve Ethanol production. Besides, foreign countries, especially China and Korea, also greatly demand for cassava chips and pellets from Thailand. Hence, cassava price is expected to remain at high level.

**(1.3) Rubber:** With greater global demand and price speculation in the commodities forward market, both output and price of rubber are expected to increase. In addition, many industries such as tire and rubber glove, have increased their natural rubber usages, which responsive to both domestic and international vehicles production

**(1.4) Fishery** In 2008, the growth in fishery production will decrease in accordance with the extent of king prawn production which accounts for approximately 20 percent of overall shrimp production. Key contracting cause is production factor including higher price of animal food and gasoline. Thailand export still confronts a threat of trade barrier performed by importing countries such as USA. However, a positive factors in 2008 are consequences from dealing with trade partner, such as special profit according to GSP received from EU. Moreover, a deal of Japan-Thailand Economic Partner Agreement (JTEPA) is also a positive consequence that can lower the tariff rate, beneficiary for Thailand in exporting frozen fresh and processed shrimp with decreased rate from 5.0 percent to 0.0 percent. In this regard, Thailand export in 2008 is expected to increase continuously.

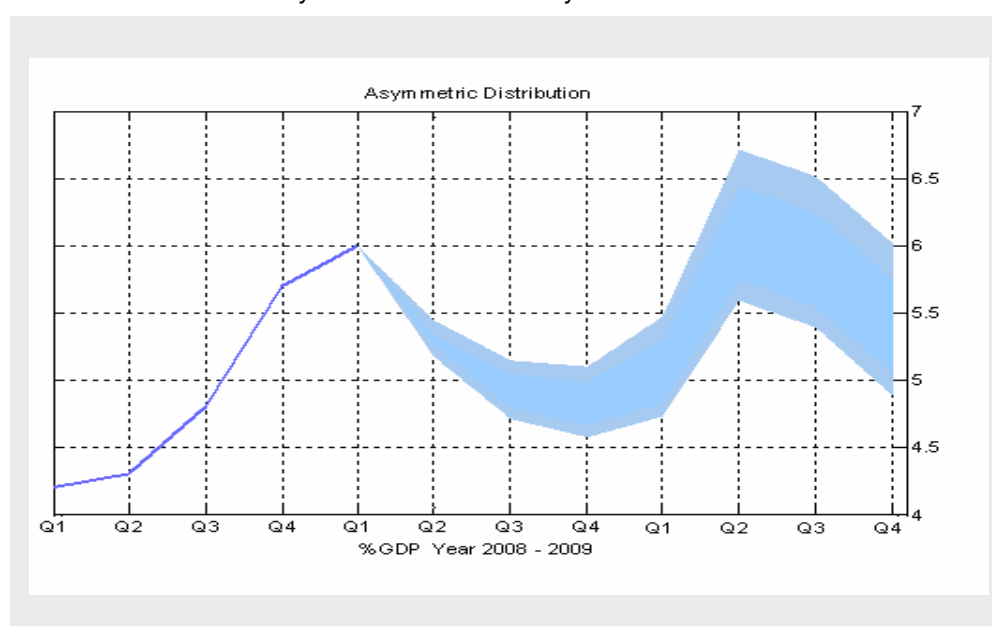
**(2) The industrial sector.** Export-oriented production tends to slow down due to a downward trend of key trading partners' economies. Nonetheless, production for domestic consumption will benefit from an upward trend of domestic consumption and investment. Particularly, main industries - such as electronics, automobiles, petrochemicals, chemical products, especially motorcycles, as well as alternative-energy car, - are on a positive trend. In 2008, challenging factors will be the fact that small entrepreneurs need to improve their standards and quality of products due to continuously changing in structure of global production with strong competition from low cost producers (e.g., China, India and Vietnam) while oil price is also likely to increase. Therefore, development of labors' skill is strongly required because various industries still face with lack of skilled labors.

**(3) The construction sector.** In 2008, the construction sector will be on a positive trend, particularly residential construction in Bangkok and vicinities. This is because of changing consumer behavior encouraged by surge in oil prices. Demand for construction along the route of mass transit system is likely to substantially increase. Office building and manufacturing constructions are also on an upward trend. This upward trend is stimulated by economic recovery, concrete solution in mass transit system and low rate of interest. Furthermore,

measures for economic stimulation in real estate sector, enforced in March 2008, also support the trend by providing privilege for real estate business with lower tax rate decreasing from 3.0 percent to 0.1 percent and with lower fee rate for transferring registration and mortgage decreasing from 2.0 percent to 0.01 percent. The measures will be supporting factors for recovery of construction and related businesses.

**(4) The tourism sector In 2008.** The target of foreign tourists is set at 15.7 million people, increased by 9.8 percent or from 14.3 million people in 2007. Revenue is expected to be around 600,000 million baht, an increase from 506,435 million baht in 2007. During 2008-2009 government launches "The Year of Tourism in Thailand" with the approaches to develop tourism quality and standard as well as to promote new geographical tourism such as "The Royal Coast", "Thailand Riviera". Besides, the government also promotes the quality tourist market such as the old age group, health care-oriented group, conference participants and exhibitors as well as ecological and cultural tourists. Moreover, the government targets to upgrade Thailand to be "World Class Destination" by creating value of service standard and safety for tourist, responsive to national competitiveness.

Probability Forecast in 2008: Asymmetric Distribution



### 3. Economic Policy Management for 2008

In the remaining period of 2008, the government should continue to properly manage economic risks and reduce the impact of downside risks on the Thai economy. Such risks include (1) higher than expected oil price which affects higher costs of production of business sectors and higher costs of people's standard of livings and (2) the slowdown in the global economy that affects export sectors. The economic management in the short-run should focus on reducing the impact of oil price on low income households and small and medium entrepreneurs, promoting energy savings and efficiencies, accelerating uses of alternative sources of energy to meet targets. Meanwhile, government should expedite implementing the long-term measures to upgrading Thailand's competitiveness. First, government should control the implementation of infrastructure development projects as planned, particularly transport and logistic systems and Bangkok Mass Transit. Secondly, government should closely monitor the implementation of measures to increase production efficiency and of the management of small and medium enterprises. Thirdly, the economic restructuring should be pushed, particularly increasing value creation of products, improving production efficiency, upgrading product standard and food safety, and promoting agricultural product processing. Fourthly, the rules and regulations that affect investment and business operation should be clear. Lastly, government should set strategies and mechanisms to regulate and promote international capital flow, both short-term capitals and direct investment in order to have capital inflows at the desirable levels that benefit the country. Management guidelines are as follows.

- 3.1 Driving measures on energy savings and energy efficiency improvement continuously as well as accelerating the use of NGV in transport sectors to meet the targets. In addition, government should continue promote the uses of alternative energy as planned (i.e plans for E10/95 E10/91 E20/95 B2 and B5)
- 3.2 Increasing government measures to expand the coverage of social welfare to the underprivileged, elders and retirees in order to reduce the impact on standard of livings. As now, 755 million elders out of 6.33 million elders receive social pension. In addition, 229,985 disabled out of 1.098 million disabled receive social pension.
- 3.3 Stabilizing prices of agricultural products by focusing on improving efficiency, developing production and upgrading product quality. In addition, government should build mechanisms that cause farmers to receive high fair prices.
- 3.4 Driving the measures of SMEs credit expansions to meet the target would help SMEs to survive and prosper with efficiency improvement. SMEs funding supports include the 5000 million baht SME fund to help SMEs affect from baht appreciation and the 40,000 million baht fund to help SMEs to upgrade efficiency, technology and production process.
- 3.5 Accelerating budget disbursement in fiscal year 2008 to achieve target of 94 percent disbursement rate of government budget(particularly the budget for well-being strategy and projects to increase potential of communities, including those to reduce poverty and strengthening SME). The target rate of disbursement of SOE's investment budget is set to be 90 percent. This scheme of implementation must be carried out in line with the implementation of provincial and provincial cluster development plan.
- 3.6 Management of median prices of public projects to be in line with changes in inflations. This will prevent the delay of project implementation and support the revival of investment. (prices of construction materials increased by 15-20 percent since 2007).
- 3.7 Building up investors' confidence by implementing policies to build the foundation of Thai economy and enhance competitiveness in long-run. Government should keep the continuity of policy implementation of public investment projects to improve infrastructure, particularly the mass transit

system in Bangkok and the vicinity areas. The approved projects should be expedited for construction in 2008. The development of logistic systems, the amendment of law and regulation that will be hurdles of private investment growth, and the implementation of “the 2008-2009 years of investment” should be expedited.

- 3.8 Promoting tourism sector to strive for the slowdown in 2007 under the campaign of “the 2008-2009 years of tourism for Thailand”

### Economic Projection of 2008

	Actual Data			Projection 2008	
	2005	2006	2007	Feb 25_f	May 26_f
GDP (at current prices: Bil. Bht)	7,095.6	7,830.30	8,485.2	9,231.9	9,418.6
GDP per capita (Bht per year)	109,440.9	120,763.40	128,563.6	139,877	142,705.6
GDP (at current prices: Bil. USD)	176.2	206.6	245.5	286.7	292.5
GDP per capita (USD per year)	2,715	3,186.40	3,720.0	4,344	4,431.9
GDP Growth (at constant prices, %)	4.5	5.1	4.8	4.5 - 5.5	4.5 - 5.5
Investment (at constant prices, %)	10.6	3.8	1.4	6.7	8.5
Private (at constant prices, %)	10.6	3.7	0.5	7.0	9.3
Public (at constant prices, %)	10.8	3.9	4.0	6.0	6.0
Consumption (at constant prices, %)	5.3	3.0	2.7	4.7	4.7
Private (at constant prices, %)	4.5	3.2	1.4	3.8	3.8
Public (at constant prices, %)	10.8	2.3	10.8	10.0	10.0
Export volume of goods & services (%)	3.9	8.5	7.1	5.9	7.3
Export value of goods (Bil. USD)	109.4	127.9	151.2	169.3	171.3
Growth rate (%)	15.2	17.0	18.1	12.0	13.3
Growth rate (Volume, %)	4.3	8.3	7.2	6.0	6.3
Import volume of goods & services (%)	8.7	2.6	3.5	6.6	10.0
Import value of goods (Bil. USD)	117.6	126.9	139.2	161.1	169.8
Growth rate (%)	25.8	7.9	9.6	15.4	22.0
Growth rate (Volume, %)	8.9	0.2	1.5	6.9	11.0
Trade balance (Bil. USD)	-8.3	1.0	12.0	8.1	1.5
Current account balance (Bil. USD) <sup>1/</sup>	-7.6	2.2	14.9	11.6	6.0
Current account to GDP (%)	-4.3	1.0	6.1	4.1	2.0
Inflation (%)					
CPI	4.5	4.7	2.3	3.2 - 3.7	5.3 - 5.8
GDP Deflator	4.5	5.0	2.7	3.2 - 3.7	5.5 - 6.0
Unemployment rate (%)	1.8	1.5	1.4	1.5	1.5

Source: Office of National Economic and Social Development Board. May 26, 2008

Note: <sup>1/</sup> Reinvested earnings has been recorded as part of FDI in Financial account, and its contra entry recorded as income on equity in current account.



## Global Economy in 2008

**The U.S economy: Latest indicators in April showed that the U.S economy remained weak.** Although, real GDP in Q1 grew at a stronger rate than market expectation, the main contributor was private inventory accumulation. The economy remained in the period of financial and real economic corrections to the sub-prime crisis. The dynamics of real recession have not yet been reverted as indicated by, (i) turbulences and low confidences in financial system which revealed in widening spreads between returns on financial securities and yields on treasuries, (ii) housing market correction has not yet bottomed out. Case – Shiller index plunged further at a faster pace, (iii) production activities remained weak as shown in the decline of Industrial production index by 0.7 percent, the largest drop in 2.5 years, and (v) private consumption remained sluggish as house price deflation, rising jobless, escalating inflation, and credit standard tightening took a toll on consumption which had resulted a slip by 0.2 percent of retail sales.

In order to stimulate the economy and resolve liquidity problems, the U.S administration has implemented various measures, which are including (i) continued cutting policy rate by the Federal Reserve Bank (Fed) Up to April, the Fed Fund rate has already been lowered by 200 bps, as well as lowered. Moreover, the spread between the discount rate and fed funds rate has been reduced from 100 bps to 25 bps. (ii) In March 2008, under Term Securities Lending Facility (TSLF), Fed allowed financial institutions to borrow up to \$ 200 billion by using mortgage-backed securities as collateral. In May 2008, Fed authorized an expansion of collateral to include AAA-rate Asset Backed Securities. (iii) Fed extended amounts of outstanding under the Term Auction Facility (TAF) to \$100 billion in March and to \$ 150 in May. (v) Fed further raised existing temporary reciprocal currency arrangements with European Central Bank (ECB) and Swiss National Bank (SNB) to \$50 billion and \$12 billion respectively. (iv) Tax rebates of totally \$ 150 billion, and (vi) the Federal Housing Administration has been permitted to underwrite a broader range of mortgages as well as to raise Federal Home Loan Mortgage Corporation and Federal National Mortgage Association lending limits by \$ 200 billion.

These measures have led to improvements in investment sentiment and a better credit market condition. Led by banks, the equity markets increased by 11.0 percent from their lowest level. Financial institutions have increasingly recognized the scale of financial losses and are taking remedial steps as witnessed in the recent capital raisings<sup>1</sup>. The new lending facilities for securities dealers reduced counter-party risks while a program to allow banks to swap illiquid mortgage backed securities for Treasuries freed-up funds for lending. These policy initiatives have allowed mortgage rates to decline moderately. Junk-bond spreads have narrowed from a peak of 862 bps in March to 692 bps while the high-grade bond spreads have narrowed from the peak of 305 bps to 268 bps over the same period. These developments, together with the surge in inflation and previous measures, implied that Fed is now less likely to reassure the economy by mean of aggressive interest rate reduction.

While financial markets have improved moderately, the majors leading indicators suggested that the real economy tends to trend down further. New orders decreased while consumer confidence index continued to decline to its 5-year low. In addition, the retrenchment in house prices becomes deeper than market expectation, its effect on lenders and financial markets could further aggravate real economic activities. Supported by tax rebates package and continual

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<sup>1</sup> For example, Citigroup, Merrill Lynch, JP Morgan and Wachovia

interest rate reductions, the economy is likely to gain more ground but its growth momentum remained subject to credit condition that has been tightened further by financial institutions. Therefore, the processes of economic recovery tend to be slow. Taking into account all these developments, the US economy is likely to grow by 0.8 percent in 2008, slightly lower than 1.2 percent in press release on November 25 and down from 2.2 percent in 2007.

**The impacts of financial turbulence and the slowdown of the U.S economy on other industrialized economies** are larger than previously expected: The U.S recession continued to drag on economic performances of other industrialized countries.

**The Eurozone** is facing with growing divergences in economic performances across its member economies. Germany is beginning to feel the pinch from financial and U.S fluctuations. Spain and Italy seems to entered severe economic corrections. In April, the Purchasing Managers' Index was particularly weak, registered the first decline in new orders since May 2005. Service sector PMI grew at a slightly slower pace with a faster growth in Germany contrasted with weakness in other member countries. The manufacturing PMIs slowed for the third month in April due to the slowing global demand and a stronger Euro. The economic sentiment index decreased from 99.6 in March to 97.1 in April, the lowest level since August 2005. Overall, economic indicators in April pointed to economic deceleration while the Inflationary pressures is likely to drag on consumer spending and the strength of the Euro put downward pressure on exports. European Bank has attempted to ease tight credit condition by opening up its financing window. However, the already weakening real economy is aggravated by the rise in inflation which recorded 3.6 percent in March, its highest level since an establishment of Eurozone in 1999. Therefore, the ECB is facing with policy dilemma in reconciling price stability and solid economic growth. However, as the policy rates have been kept unchanged since September 2550, policy makers increasingly concern about the deterioration in real economic activity. Against this background, the ECB is likely to cut its policy rate by 25-50 bps in the second half of the year, when inflation receded and the slowdown become more materialized. All in, with the deterioration in economic activities, growth for the Eurozone in 2008 is expected to slowdown from 2.0 percent in 2007 to 1.4 percent this year while the inflation rate is forecasted to accelerate from 2.1 percent to 2.8 percent over the same period.

The deceleration in **the Japanese economy** is likely to continue in 2008. Industrial production output decreased sharply and reflected the impacts of the slowdown in the U.S and Eurozone economies as well as the Yen appreciation. Domestic demand remained weak. In April, sentiment among merchants fell for the first time in three months while consumer confidence recorded its lowest level in five years. While a fall in shipments to the U.S has been cushioned by strong exports to Asia, the latest data showed that Japan's exports to Asia increased 1.9 percent in March, the smallest increase since May 2005 as growth of shipments to China slowed to 3.2 percent from 14.9 percent. With these developments, the BOJ is likely to refrain from interest rate hike. In addition, the latest downgrade economic forecast by BOJ indicated the potential interest rates cut if economic conditions deteriorate sufficiently. The economic growth for the year is likely to slowdown to 1.4 percent from 2.1 percent last year.

**Other major Asian economies** are weathering but not fully decouple from the slowdown of industrialized economies. Recent indicators indicated that export quantities slowed down in some Asian NIEs, ASEAN-4 economies and notably India and China, in particular exports to industrialized countries and thus domestic demand and intraregional trades are likely to play more significant roles in driving growth. However, the inflationary pressures have escalated across countries and are likely to slash domestic spending. Therefore, growths in major Asian economies are likely to slowdown in 2008, led by China and India which are expected to grow at the rate of 9.3 and 7.9 percent, down from 11.4 and 9.2 percent in 2007. Asian NIEs and ASEAN-5 are likely to slowdown to 4.0 percent and 5.8 percent, from 5.6 percent and 6.3 percent in 2007 respectively.

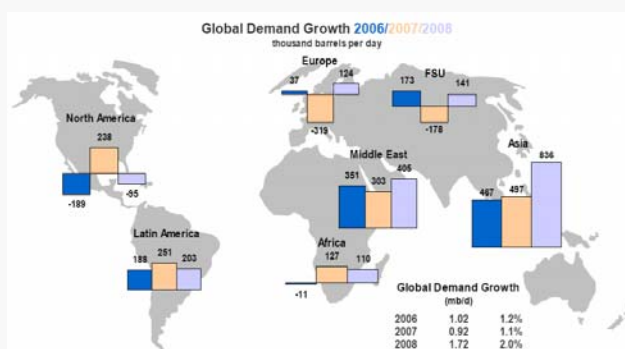
## Oil price in 2008

During the first five months of 2008, oil prices increased substantially as a result of tight market condition and a continued depreciation of U.S dollar that encourages hedging and speculation against the further depreciated value of USD. Over the upcoming months, oil prices are likely to continue its upward trend. Given that oil market condition will remain tight while there is possibility that US dollar will continue on its downward trend, these developments will give investors and also speculators more incentive to reallocate their portfolios toward oil and other commodities to guarantee their investment return and hedge against risks. In addition, the persistence of high oil prices could additionally heated by political tension in several oil producing countries such as Nigeria and Argentina. An increase in oil demand from OECD countries in order to replenish their declining stocks over the past months is also in favour of further rises in oil prices. World oil demand will also likely to grow faster, particularly in the emerging economies such as China, India, and oil-exporting countries. The average of Dubai crude oil price in 2008 is project to be around 110-120 U.S. dollars per barrel, much higher than the average of 68.83 U.S. dollars in 2007. Underlying factors for expected surge in oil price in 2008 are as follows:

**(1) World oil demand has continued to grow.** The International Energy Agency (IEA) forecasted that the global oil demand will be 87.2 million barrels per day, with the increase of 1.3 million barrels per day from 2007 (or increase by 1.5 percent). The oil demand growth will outpace the supply growth. The oil supply in 2008 is expected to be 86.68 million barrels per day, increase by 1.38 percent. As suggested by the forecast, the level of oil production will be fall short of the projected oil consumption by 0.52 million barrels per day. Especially, high oil demand in emerging economies will continue to be the main drivers of the growth in global oil demand. For example, oil demand in china in 2008 is expected to be 7.89 million barrels per day, increase from 2007 by 4.7 percent, partly from the increase of oil import to support the Olympic in August. Oil demand in Non-OECD Asia will be 18 million barrels per day, increase from 2007 by 7.27 percent. Oil demand in Middle-East countries in 2008 will be 7 million barrels per day, increase from 2007 by 6.1 percent. The increase of their production will only to cater their own demand, if the further production increase is agreed upon.

Barrel/Day	2005	2006	2007 Year	2008				
				Q1	Q2f	Q3f	Q4f	Year
Quantity	84.6	85.3	84.66	86.08	86.79	87.41	86.71	86.68
Non-OPEC	50.4	51.1	49.24	49.17	49.49	50.05	50.59	49.83
OPEC Crude oil	29.7	29.7	35.43	32.28	32.59	32.22	31.1	32.05
NGL	4.5	4.6	4.53	4.62	4.71	4.86	5.01	4.8
Supply-Demand	0.7	0.6	-1.34	-1.22	0.49	0.51	-1.69	-0.52

Source: EIA



- (2) **The U.S dollar looks set to move on the depreciating trend.** Underlying factors for the depreciation will be the continued slowdown in the US economy and further emergence of damages in financial sectors. This will induce the Hedge Funds and institutional investors to diversify portfolios from debt instruments denominated in U.S. dollar to future markets of commodities such as future markets of oil, steel, gold and agricultural products. Moreover, the depreciation will induce an attempt by oil exporting countries to maintain oil price at high level in order to compensate for revenue reduction in terms of local currency.
- (3) **Weather tends to fluctuate.** Global Warming will force the climate and weather to fluctuate while the natural disaster will be more frequent and more severe, if happen. These factors will directly affect the world crude oil production, particularly in the second and third quarters which are rainy seasons. Hurricanes and other natural disasters in the America and Africa, if occur, will cause the refinery to be temporarily closed and cause oil prices to rise.

#### Factors determine the oil prices over the upcoming periods

##### Upside risk factors consist of:

1. Commercial stock of many countries especially OECDs have been declined while spare capacity remains low
2. Higher cost of production due to the lack of labor and refineries from unconventional sources
3. Global oil demand continue to grow which is partly due to price subsidy in several countries
4. U.S. dollars depreciation
5. Speculation
6. Hedging

##### Spike risk factors consist of:

1. Climate changes/weather
2. Political unrest in oil producing countries, and geopolitics

##### Downside risk factors:

1. World and US economic slowdown
2. Period of refinery maintenance has passed
3. Increase in oil production from non-OPEC countries
4. Slowdown in demand during autumn (prior to driving season)

**In the first half of 2008 upside risks and spike risks have been more pronounced than the download risks which are expected to be stronger forces in the latter half, especially in the situation of global economic slowdown**



## **A phenomenon of rice price in Asian**

The sharply increase in rice price has become an important issue in Asia as its role is both rice producer and rice consumer. According to consumption baskets that were compiled across the region, rice accounts for 60-70 percent of cereal consumption. Therefore, the recent increase in rice price has caught investor's attention.

### **1. The key determination factors for the increase in rice price**

The key factors behind the surge in price of grains and rice are as the follows:

- Supply shock: World rice production has decreased since 2007 and continued into 2008 due to bad weather condition. In particular, drought in Europe in late of 2007, drought in Australia and, flooding and freezing weather in China in early 2008.
- Supply substitution: Grains in general have been competing for production resources with other crop and manufacturing productions.
- Demand substitution: The increase in rice price was partially attributable to the increase in demand for energy crop which could lead to production substitution in the long run.
- Cost pressures: Rising cost of oil, gas and other inputs (included fertilizers, fuel for farm machinery and farm machinery) raised production costs of rice and reduced profits. This situation restrained production expansion. Combined with the increase in demand for energy crop, it leads to production substitution which scarified rice production for energy crop production.
- Speculation: Concern over long term supply fluctuation resulted in higher stock accumulation and market speculation on rice price.

These factors raised concerns over supply shortage and resulted in export restriction in major exporting countries such as Egypt, India and Vietnam and thus drove rice price in the world market.

### **2) Trend of rice price**

In the medium term, output of agricultural production in the next harvesting season is expected to increase in Brazil, Uruguay, Bangladesh, India, Indonesia and Thailand. To some extents, the increase in output is expected to reduce price pressures. According to the report by FAO, in 2008-2009, output from major rice and wheat exporting countries is likely to increase. This development will reduce price pressures. However, some other factors are likely to drive rice price in long run to increase further, in particular, the increase in oil prices and supply side factors such as land water and energy. Theses factors will stronger affect agricultural production than other sectors. Thus cost management and production adjustment to changing environments are important issues.

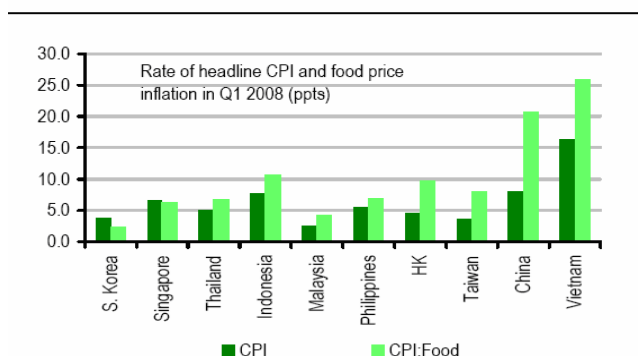
As food prices increase, the reduction in consumption is unlikely large. Therefore, food prices are likely to increase sufficiently to induce production resources from other sectors. This situation will help maintain food production but also requires the improvement in production technology. Otherwise it would lead to misallocation of production resources to low productive sectors. Therefore, the important issues in the near term are including (i) the change in food and agricultural prices in relative to other commodities and (ii) income transfers from food consumers to food producer both in domestic economy and in foreign countries.

### 3) Impacts on the economy

The emergences of food price inflation in Asian countries are mostly driven by the increase in prices of other commodities such as meat, fruits and vegetables rather than cereals or grain. However, over the past 6-9 months, food price inflation was higher than average inflation. In the case of Thailand, an average inflation rate rose sharply due to the increased oil and food prices at an accelerated rate in the first quarter.

Food price inflation erodes household purchasing power. However, its impacts vary across different groups of people.

#### CPI and CPI-Food inflation



Source: Haver

- The impacts on low-income households are greater than that of high-income households. This is attributable to the fact that the ratio of food consumption in total consumption basket is higher for household with low-income than that of high-income households. In the case of Thailand, this ratio is higher for low-income group than that of country average. In addition, food price faced by rural households are usually rise faster than that faced by urban households due to embodied transportation costs in food prices.
- As Thailand and Vietnam are food exporting country, they are beneficial from incomes transfer (from food importing countries) which is generated by food prices increase. Meanwhile, Philippines, Malaysia, Indonesia, Hong Kong, Singapore, Taiwan and Korea are negatively affected as they are food importing country and their trade balance for food items was in deficit last year. Classified by income level, however, Hong Kong, Singapore, Taiwan and Korea are high income country. Therefore the impacts of high food prices are unlikely to generate social problems. However, with lower income per-capita, the impacts on Philippines should be relatively strong.