



NESDB

ECONOMIC OUTLOOK

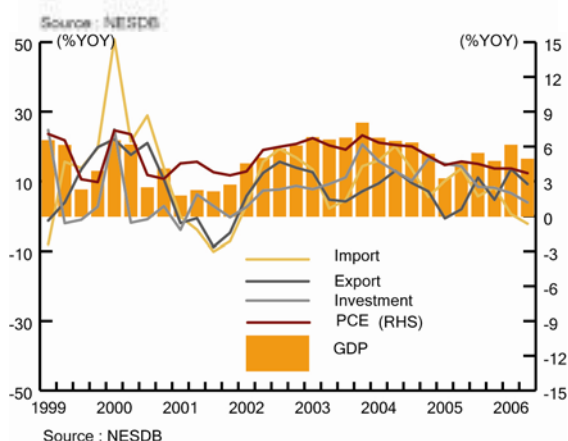
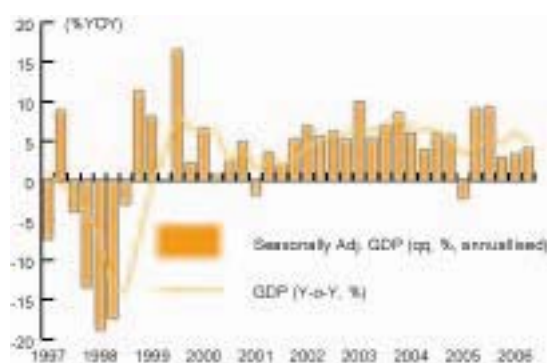
Economic Performance in Q2 and Outlook for 2006

- **In the second quarter, Thai economy expanded by 4.9 percent**, slowed down from 6.1 percent in the first quarter. This was due to a slowdown in private consumption and investment. However, overall economy in the first half showed a favorable growth of 5.5 percent.
- **Key engine of growth** continued to be exports of goods and services. Government expenditure and investment also picked up in this quarter. Meanwhile, private consumption and investment grew at a moderate pace and continued to slow down.
- **Negative factors to economic growth** in this quarter included rising oil prices, high inflation, increasing interest rate and declining consumer and business confidence in response to soaring oil price and domestic political uncertainty.
- **Upward interest rates adjustment put more evident impacts on the economy.** The response has been seen in the moderate increase in private credits, increasing fixed deposits and overall deposit as well as high financial liquidity.
- **Pressures on economic stability increased in the second quarter.** This was evident in a 6.0 percent inflation rate and a current account deficit of 1,153 million US dollars. However, the situation improved as inflation rate decelerated to 4.4 and 3.8 percent in July and August, and current account returned to record a surplus. In the mean time, unemployment rate was kept low at 1.4 percent in the second quarter and international reserves stood at 58.06 billion US dollars at the end of June 2006, equivalent to 3.3 times of short-term debts.
- **The economy is likely to grow at moderate pace in the second half of 2006**, resulting from several risk factors including the surge in oil prices, the increase in interest rates, the slowdown in the world economy as well as domestic political uncertainty. Supporting economic conditions will be from tourism sector and exports which tend to expand well, though at a slower pace than in the first half. Moreover, rising agricultural production and prices as well as subdued inflationary pressure will help restore confidences.
- **It is expected that the economy in 2006 will expand in the range of 4.2-4.7 percent** with inflation of 4.5-4.7 percent, a small current account surplus of 0.6 percent of GDP and unemployment rate of 1.8-2.0 percent.

Macroeconomic Office
Office of National Economic
and Social Development Board
962 Krung Kasem Rd.
Bangkok 10100
<http://www.nesdb.go.th>
Tel. 02-280-4085

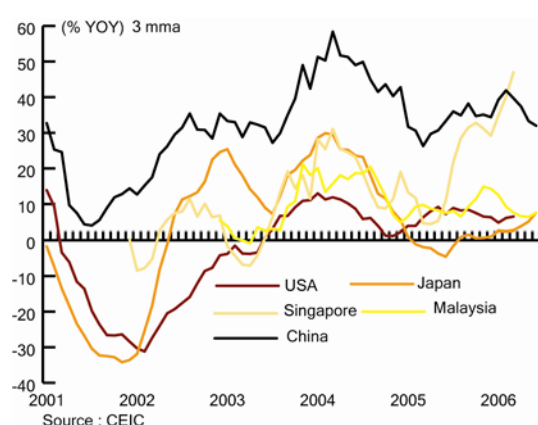
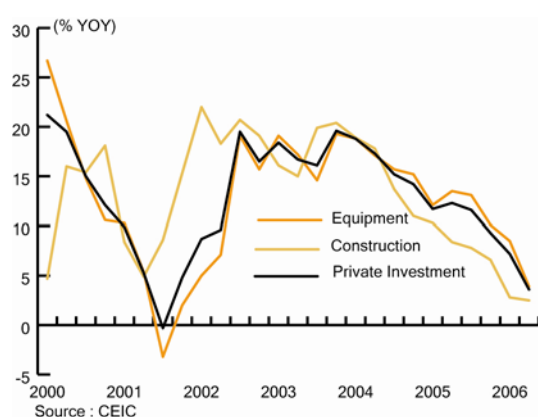
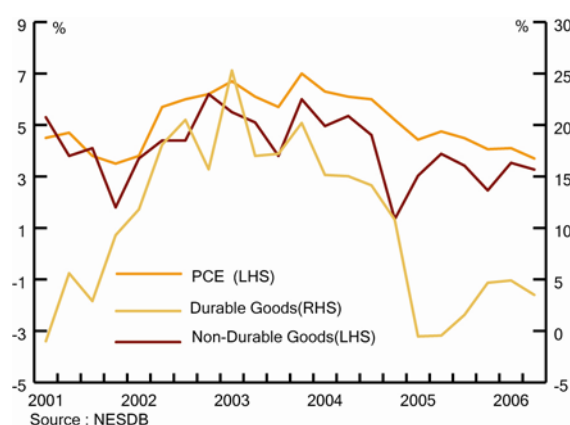
1. Economic Performance in Q2 and H1 of 2006

- 1.1 The economy in the second quarter of 2006 expanded by 4.9 percent, slowed down from 6.1 percent in the first quarter. This was primarily due to a slowdown in domestic demand, both private consumption and private investment. Net export of goods and services continued to be the key driving engine of economic growth in this quarter.



Key Themes

- ❑ **Thai economy in the second quarter grew by 4.9 percent, slowed down from 6.1 percent in the first quarter.** This was due to a significant slowdown in domestic demand, both private consumption and private investment in light of higher oil prices, interest rates uptrend and domestic political uncertainty. The key growth engine of the economy in the second quarter was net exports of goods and services which continued to show a strong growth in response to favorable condition of the world market, particularly an uptrend cycle of the world's electronics market and rising rubber prices in the world market following soaring oil prices. Imports showed a sharp slowdown due to a slowdown in private investment and a rapid rundown of inventories. In addition, both government expenditure and public investment increased in the second quarter.
- ❑ **Overall, the economy in the first half of 2006 expanded by 5.5 percent,** mainly driven by strong net exports of goods and services. Domestic demand, however, contributed less to the economic growth.
- ❑ **Domestic demand slowed down and inventories have been run down at total value of 14,702 million baht in the second quarter, led to moderate increases in imports and production. Net exports of goods and services contributed more to the economic growth.** Net export volume of goods and services increased by 9.2 percent in the second quarter and 11.3 percent in the first half, higher than 0.6 percent growth in the first half of 2006 and 7.8 percent in the latter half of 2005.
- ❑ **Private consumption slowed down from the first quarter, while government expenditure reverted to a positive growth.** In the second quarter, private consumption grew by 3.7 percent, softened from 4.1 percent in the previous quarter. The slowdown of spending were notably seen in durable goods, particularly in automobile and parts and hard-wearing appliances as well as services items including domestic tourism, health care and entertainment. This was caused by a declining purchasing power resulted from higher oil prices, rising commodities prices, interest rate increases and worsened consumer confidence. In all, private consumption



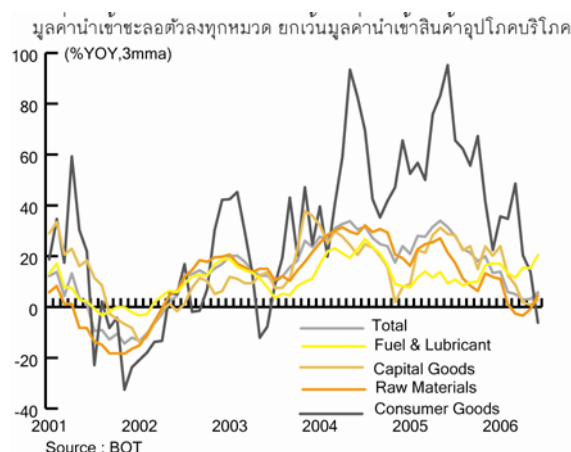
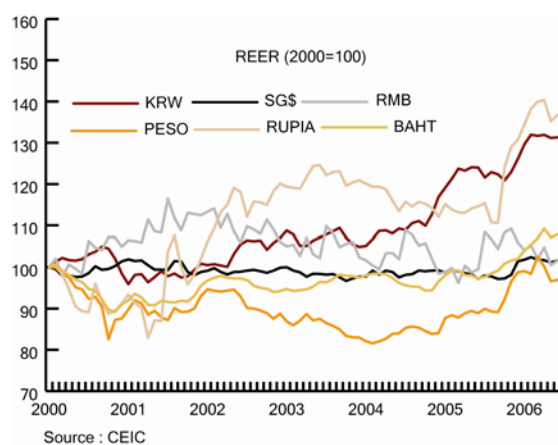
expanded by 3.9 percent in the first half. Government expenditure grew by 3.4 percent in the second quarter, picking up from a declined rate of 0.9 percent in the first quarter.

- **Total investment showed a slowdown. This was primarily due to a sharp slowdown in private investment, while public investment grew at the same rate as in the first quarter.** Total investment increased by 3.3 percent, slower rate than 6.6 percent in the first quarter. This slowdown was apparently seen in private investment, in particular machinery investment. Investment in machinery and equipment expanded by 3.9 percent, slowed down from 8.5 percent in the first quarter and led imports of capital goods to fall by 1.7 percent in terms of baht and investment in commercial cars to decline after a high surge in 2005. Investment in construction increased by 2.5 percent, comparable to 2.8 percent expansion in the first quarter, but this showed a declining trend as compared to 8.2 percent growth in 2005. Meanwhile, public investment rose by 5.0 percent, slightly up from 4.7 percent in the first quarter.

Overall, in the first half of 2006, private investment expanded by 5.4 percent, sharp slowdown from 11.2 percent in 2005. Public investment rose by 4.9 percent, also slower than 11.9 percent in 2005.

- **Export value grew robustly, attributed to higher export volume. Nevertheless, export price showed a slowdown trend.** In the second quarter, export value in terms of US dollars increased by 16.3 percent, and 18.1 percent in July. This was partly owing to an uptrend of electronics cycle as well as good performance of export of agricultural products, supported by the continued increase in rubber price following an increase in price of synthetic rubber in the light of higher oil price and increasing demand of automobile sector in China and India. In addition, demand for cassava also increased. Export volume recorded a high growth of 11.1 percent, while export price increased slightly by only 4.6 percent due to a gradual slowdown in price of manufacturing products. However, recent indicators suggested that export is likely to soften in the second half. Key issues are as follow;

- Export and import data of electronics and electrical appliances in major economies have indicated that electronics cycle has approached its downtrend and in line with the trend, Thailand's export of electronics

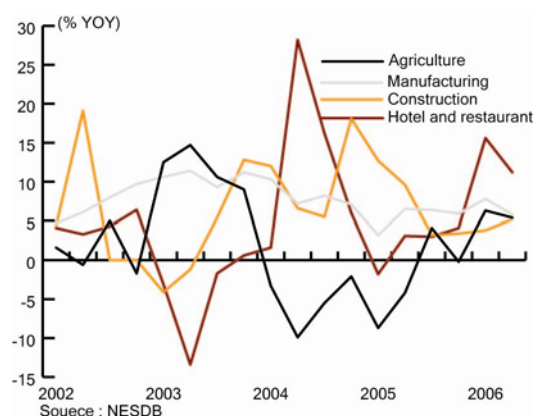
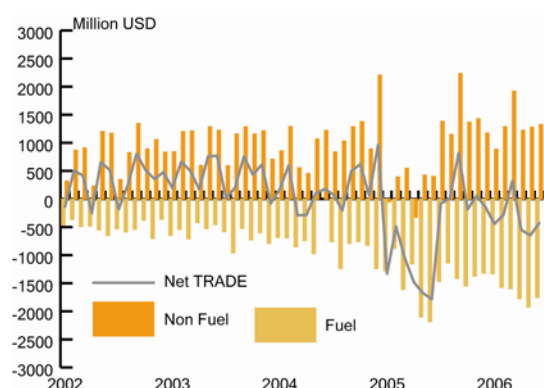
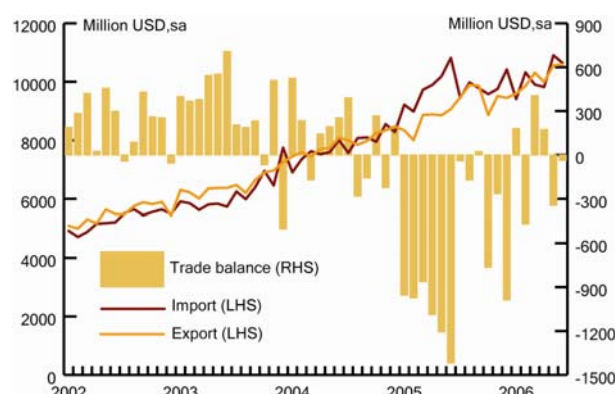


is expected to slow down in the second half of this year.

- Appreciation of the baht did not show clear evidence of impacts on Thailand's price competitiveness during the second quarter and the first half of this year since other regional currencies have also appreciated. However, real effective exchange rate has signaled a faster appreciation than other regional currencies, in line with the inflation rate. Consequently, this would render difficulties for Thai exports under situation of world economic slowdown and rising competition. Pricing to market can help reduce the impact. However, the key impact is that the exporters' revenue and profits in terms of Baht may not increase significantly or may even decrease due to the appreciation of the Thai Baht. This suggests that results on income and multiplier effects of exports on domestic spending will be moderate.

- **Import value slowed down gradually due to the declined import volume, although the overall import prices, especially oil prices, had increased.** In the second quarter, import volume dropped by 3.7 percent, while price rose by 7.2 percent. Thus, import value increased by 3.2 percent in the second quarter, slowing down from 5.4 percent in the previous quarter. Import of capital goods and fuels slowed down sharply, while import of raw materials and intermediate materials declined. Main reasons are as follows (1) high import base of the same quarter last year as a result of high stock accumulation which was as a result of expectation on a sharp increase in crude material and consumer products' prices (2) the slowdown in private investment, due to a plummeted confidence in private sectors in the light of uncertain political situations as well as an increase in interest rate (3) the complete construction of Suvarnabhumi airport, led to a sharp slowdown in demand for imports of capital goods and (4) measures on import management of products with high volume and volatility, namely oil, iron and steel and gold, consequently brought about a sharp decrease in import volume of iron and crude oil. Overall, in the first half of the year, import value increased by 4.2 percent as the import volume dropped by 3.3 percent, while price increased by 7.9 percent.

- **Trade account registered a deficit of 1,705 million US dollars**, in the second quarter of 2006 comparing to a deficit of 224 million US dollars in the first quarter. Net trade account of oil and petroleum products was in deficit of



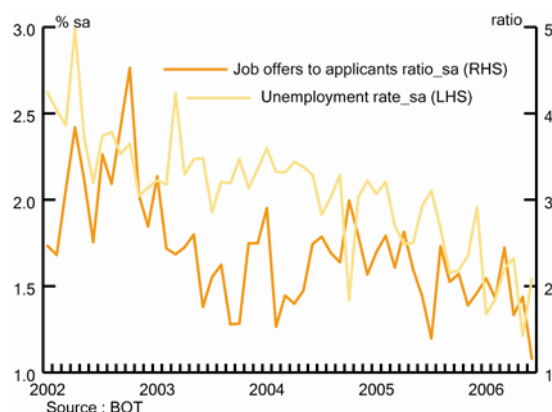
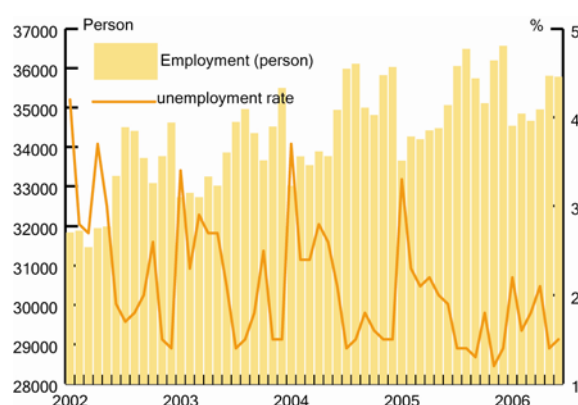
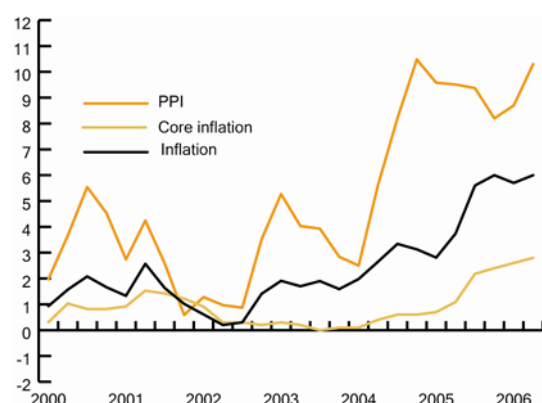
5,447 million US dollars, higher than a deficit of 4,500 million US dollars in the previous quarter, as the oil price increased. For non-oil account, the trade balance recorded a surplus of 3,742 million US dollars, lower than 4,276 million US dollars in the previous quarter. In the first half of 2006, trade account was in a deficit of 1,929 million US dollars, comprising of a deficit of 9,947 million US dollars of net trade account of oil and a surplus of 7,914 million US dollars of non-oil products account.

- **Current account recorded a deficit of 1,153 million US dollars** in the second quarter of 2006. Net services and transfer were in a surplus of only 551 million US dollars, following a normal period of low season of tourism and a period for transferring back of dividends and returns on investment of foreign investors. A surplus of net service, income and transfer, could not offset trade balance deficit and thus make current account recorded a deficit in second quarter. However, all in all in the first half of 2006, the current account recorded a surplus of 503 million US dollars.

- **Production side slowed down but still remained in a good position, production side expanded slower than demand for goods and services, thus the inventories have been run down in order to serve the increasing demand.** Manufacturing production expanded by 5.8 percent follow increased in export, but slowed down from 7.8 percent in the first quarter. Increased in manufacturing production mainly came from electronics (both hard disk drive and integrated circuits), vehicles and parts. Agriculture sector expanded by 5.4 percent, with main increasing products include major rice, cassava, sugar cane and oil palm. Hotel and restaurant sector grew by 11.2 percent following the recovery in tourism sector, number of tourist in second quarter grew by 16.2 percent.

- **Pressures on economic stability increased in the second quarter of 2006; as seen in the inflationary pressures and a current account deficits.** The inflationary pressure, however, remarkably softened in July and August and current account turned into a surplus.

- **Mounting pressures on price of products continued in the second quarter.** In the second quarter, the inflation rate was 6.0 percent and the core inflation in this quarter was 2.8 percent, which continually rose from the previous quarter. This is due to pressures on production cost responding to high oil prices, which eventually passed through to



consumers' prices. In the first half of 2006, the headline inflation was 5.9 percent and the core inflation rate was 2.7 percent. The headline inflation declined to 4.4 percent and 3.8 percent in July and August, respectively. This was a result of a slowdown of private consumption and an high base effect of inflation in tandem with floated rate of diesel petroleum and high prices of commodities in the second half of 2005.

➤ **Employment rose and unemployment rate was lower than that in the second quarter of 2005.**

The number of employed person were 35.79 million people, rose by 3.9 percent from 34.46 million people in the second quarter of 2005 to 35.79 million people in this quarter. Comparing to the second quarter of 2005, the number of employment in agricultural sector in the second quarter of 2006 expanded by 18.4 percent. On the other hand, the number of employment in manufacturing sector decreased by 3.5 percent compared with the same period last year. The employment in construction sector showed the most notable decline of 15.7 percent, reflecting the slowdown in real estate market. The employment in trade and banking sector declined by 5.0 percent. Meanwhile, the unemployment rate continually decreased to 1.4 percent in the second quarter of 2006, compared with 2.0 percent in the same period of last year. However, the ratio of job offers to applicants decreased from 2.26 in 2005 and 1.9 in the first quarter of 2006, to 1.3 in the second quarter of 2006. This ratio indicates less tight labor market and private sector has become more cautious in offering more employment.

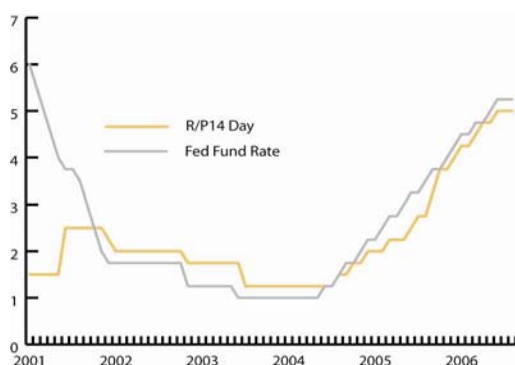
➤ **Public debts:** At the end of May 2006, public debts was 3.26 trillion Baht, approximately 42.1 percent of GDP, slightly increased from 42.1 percent at the end of March 2006 but dropped from 46.4 percent at the end of December 2005

➤ **External stability was favorable.** International reserves stood at 58.06 billion US dollars at the end of June 2006 and increased to 58.8 billion US dollars at the end of July, accounted for 3.3 times of short-term external debts and equivalent to 5.65 months import, which is considered to be a stable level.

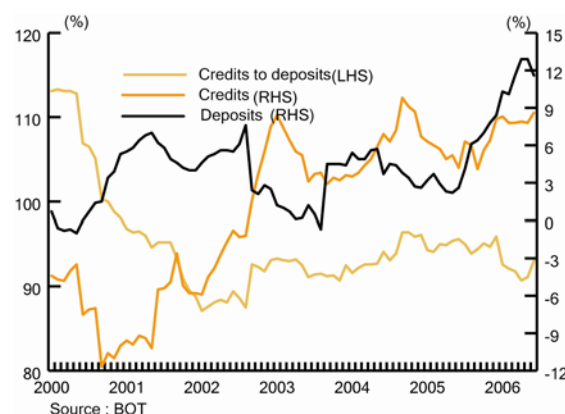
❑ **Fiscal cash balance recorded a surplus of 75,580.3 million Baht** in the second quarter of 2006. The fiscal position in the second quarter improved, compared to a surplus of 9,170.7 million Baht in the previous quarter and a deficit of 51,414.1 million Baht in 2005. During October 2005 –June 2006, the fiscal cash balance returned to a surplus of 883.7 million Baht. In the second quarter of 2006, total government revenue collection was 455.5 billion Baht, or increased by 11.2 percent. Meanwhile, the total budget disbursement was 288.6 billion Baht, or around 21.2 percent of overall budget of 1,360,000 million Baht. Such budget disbursement was lower than the target of around 24,166.1 million Baht, or about 1.8 percent. It is noted that budget disbursement between October 2005 and 26 August 2006 was 1,116.9 billion Baht, or accounted for 82 percent of overall planned budget.

❑ **Financial sector: interest rate and bond yield have been on the rising trend, credit expansion signaled a clear slowdown trend, and liquidity in the financial system remained at a high level.**

➤ **Interest rates have been increasing** The Monetary Policy Committee raised the policy rate (R/P 14 days) twice, each by 25 basis points in the second quarter, before holding the policy rate at 5 percent per annum in the 19 July 2006 meeting. Meanwhile the Fed Fund Rate was maintained at 5 percent in August. Subsequently, commercial banks have continuously raised their interest rates; the average of 12-month time deposit and the MLR rate of five large commercial banks increased by 0.75 and 0.38 percentage point from the end of the first quarter to 4.63 and 7.75 percent per annum at the end of August consecutively. Moreover, yield on short term bonds with less than 1-year to maturity rose continuously by 25 – 51 basis points throughout second quarter, in line with the policy rate.

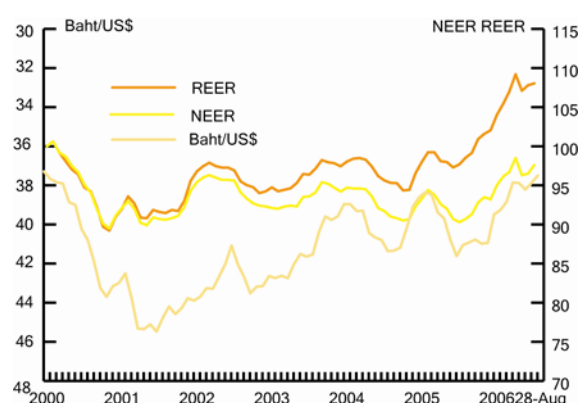


➤ **The increase in commercial banks' interest rate has resulted in an acceleration of deposits and a slowdown in credit.** Commercial banks' deposits, excluding those of new established banks, expanded by 7.6 percent, higher than the 2.6 percent growth in the first half of 2005, before the interest rate raise. Particularly, the commercial banks' time deposit expanded by 35.4 percent in the second quarter, higher than the growth rate of 27.3 percent in the previous quarter, partly due to a shift from saving deposits. Consequently, saving deposits declined by 12.9 percent from the same period of 2005. In the meantime, commercial bank and finance company credits grew at the moderate rate at 4.4 percent year-on-year. Credits extended to manufacturing sector, which constituted the largest proportion of total credits expanded by 5.2 percent, lower than the growth rate during the first half of 2005 of 13.3 percent. Credits to real estate sector began to decline, while personal consumption credits slowed down continuously from the growth rate of 11.7 percent in the previous quarter to the growth rate of 9.7 percent in the second quarter.



➤ **Credit card spending and cash advances slowed down**, while loan outstanding still grew at the continual pace at the rate of 21.3 percent. This may reflect the weakened repayment ability of household due to higher personal expenditure.

➤ **Liquidity in the banking system tended to increase** since the deposits accelerated rapidly while credits grew at a moderate rate, the credits (including investment in private securities) to



deposits ratio dropped from 95.5 percent in the same quarter of previous year to 93.0 percent at the end of the second quarter. The excess liquidity in the banking system remained high at 682 billion baht, increasing by 43.2 percent from the same period of previous year.

➤ **Overall financial stability was considered satisfactory.** NPLs in the banking system picked up slightly in the second quarter, the ratio of NPLs to the total loans stood at 8.22 percent, but there is yet no significant sign of increasing NPLs stemming from upward trend of interest rate. Thai Baht in the second quarter averaged 38.07 baht per US dollar, appreciated by 3.4 percent from the same quarter of 2005. The Baht continued to appreciate in July and August contributed by considerable capital inflows to the country, as well as the speculation on further RMB revaluation. The appreciation of the Baht at the faster rate than most regional currencies caused the average nominal effective exchange rate (NEER) in the second quarter to appreciate by 5.2 percent from the second quarter of 2005. Moreover, the accelerating inflation rate led the real effective exchange rate (REER) to appreciate by 8.0 percent.

➤ **Stock market underperformed** throughout the second quarter resulted from the net sell of foreign investors of 29 billion baht; however, the stock market condition improved in July and August. SET index closed at 692.0 at the end of August, with total market capitalization of 5.0 trillion baht. The bond market registered the average daily trading of 26.9 billion baht in the second quarter, grew by 34 percent partly due to an investment shift from the stock market. Total return index had increased throughout the quarter. The business sector has shifted their sources of financing during the upward trend of the interest rate cycle by issuing less debentures; but instead, issuing more on short term bills with a net value of 51.1 billion baht at the second quarter. The yields on long term bonds had slightly increased and began to decline in the first two month of third quarter due to increased demand, which partly resulted from expectations that long-term interest rates will contain at the low level. Consequently, the government bond yield curve flattened.

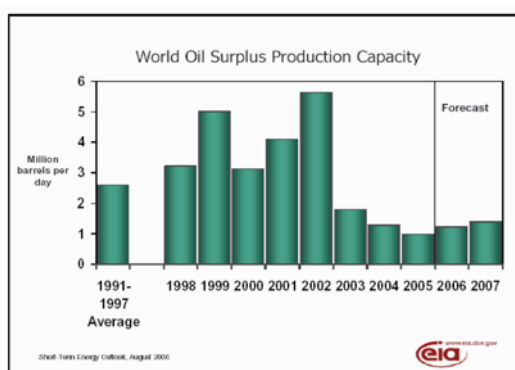
1.2 World economic growth in the second quarter of 2006: grew at a decelerating rate contributed by the slowdown in US, NIEs and Japanese economies. Inflationary pressure remained unabated; therefore, many countries lifted policy interest rate. China pursued more tightening policy to slow down the overheated economy.

- **The US economy** slowed down, due mainly to a decline in fixed asset investment, the slowdown in private consumption which was affected by the continued weakness in real estate sector. Inflationary pressure increased and trade balance was recorded a deficit at high level. **The Japanese economy** slowed down caused by less contribution from net export of good and services and the declines in residential investment, public spending and inventories. However, the contribution from domestic spending increased from the higher growth rates in private consumption and investment. Consumer price index, private credits and employment continued to expand at accelerated rates, leading to a stronger recovery in the latter half of 2006. **The NIEs economies became softer.** Singapore and Hong Kong economy grew at a moderate level following the slowdown in export particularly electronics and product export. The Taiwanese economy had a moderate growth as a result of the

sharp decline in private consumption and investment. The Korean economy slowed down in tandem with the softening consumption and construction investment. However, **the Chinese economy** had a buoyant economic growth with the main contribution from industrial production and fixed asset investment. **The Euro area economy** expanded at a higher rate, with the main contribution from Germany and France. Unemployment rate continued to decline. Indonesia and Malaysia had higher rates of economic growth. Sharp increases in public spending in Indonesia and in investment in Malaysia were the main contribution in economic growth.

- High oil price put upward pressure on inflation, particularly in US and Europe. To reduce high pressure on inflation, the Fed fund rate was increased from 4.75 percent in March to 5 percent in May and 5.25 percent in June. The ECB official rate was increased from 2.5 percent in March to 2.75 percent in June. However, pressures on inflation declined in Indonesia, Malaysia and Philippines.
- The global imbalance remained a problem. Asian economies including Japan and China experienced increasing trade surplus; while the US had a higher deficit.

2. Economic Projection for 2006: GDP growth will lie in the range of 4.2-4.7 percent growth with 4.5-4.7 percent inflation rate and a current account surplus of 0.6 percent of GDP



2.1 Economic factors/conditions in 2006

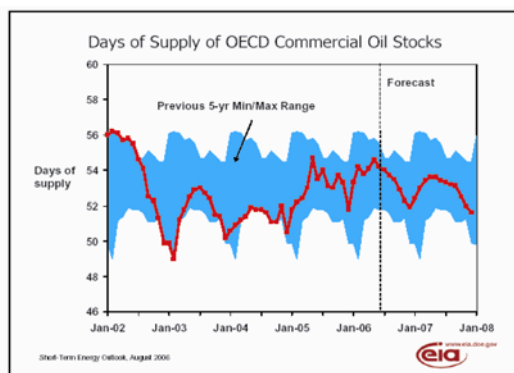
(1) Risk factors

(1.1) External factors: External risk factors are associated with high and volatile oil price as well as global economic slowdown in the second half of 2006 as a result of rising oil prices and interest rate uptrend in several countries. Besides, global imbalances remain significant risks associated to the outlook.

- Crude oil price are likely to stay at a high level due to following reasons: (1) Continuing rise in crude oil demand. International Energy Agency (IEA) revised world oil demand forecasts in 2006 to 84.78 million barrels, up by 1.19 million barrels per day or increased by 1.4 compared with 2005. This is mainly due to continuing increases in demand from China and US. (2) Tightened production capacity of both crude oil

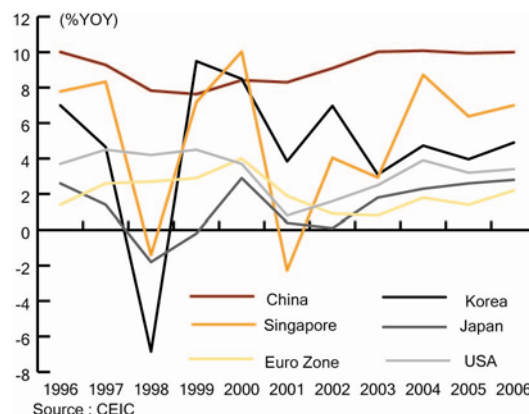
production and refinery plants capacity. At the end of August 2006, OPEC's surplus capacity was at 1.3-1.8 million barrels per day. This renders oil price to be sensitive to the supply disruptions and also to unconstructive news related to oil production, demand and inventories conditions. (3) Uncertain situations, terrorism and political conflicts in leading oil producers, in particular those Middle East countries, such as nuclear tensions between Iran and the West and unrest in Nigeria and a conflict between Lebanon and Israel. These factors also indirectly affect the confidence of international politics.

Nonetheless, some supporting factors show that oil prices will not continue their ascent far from current level owing to the following factors: (1) Expected slowdown of the Chinese, US and Asian economies in the latter half of 2006, while high oil prices continue and remain at high level. (2) The improvement of various countries in energy development which help ease price pressure. (3) Reserved amounts of crude, Middle Distillate and Gasoline in US – largest oil consumers – remain at high level above 5 years-averaged level. Total amount of OECD increased in the first half of 2006 and (4) Oil price has been at high level since the beginning of 2006 and is expected that the OPEC will determine to keep the production ceiling at the current level. Moreover, surplus capacity of OPEC increased from 0.9-1.4 million barrels per day to 1.3-1.8 million barrels per day. Thus, it is projected that oil prices will not leap from the current level.



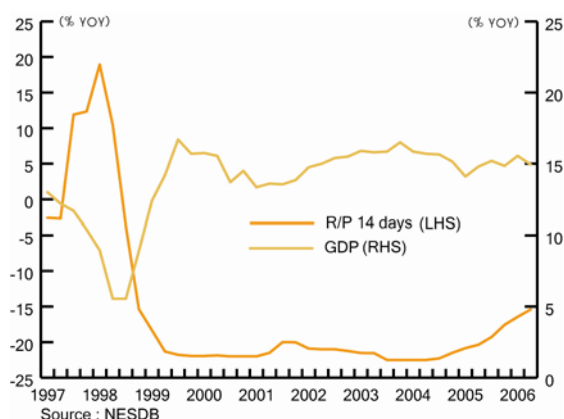
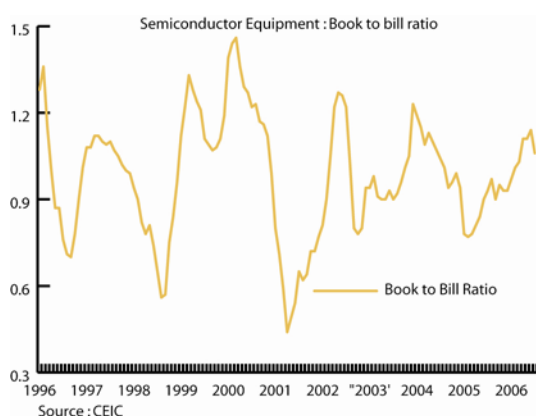
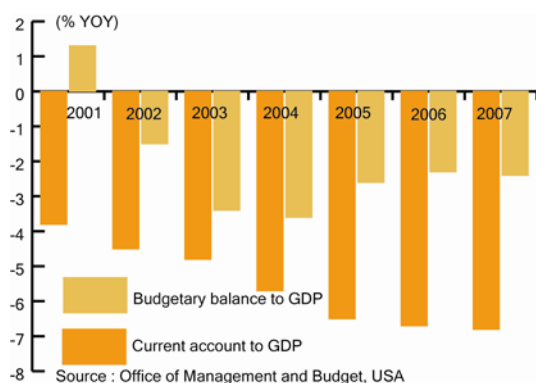
- **The world economy tended to slow down in the latter half of 2006. The main risks that could cause world economic growth to be lower than anticipated was the continued increase in crude oil, the adjustment of US economy to global imbalance which lead to fluctuations in international capital flows and exchange rate**, including the slowdown in US economy from the continued increase in policy interest rate. In addition, the real estate

market showed a weakness in many countries such as US, China, Australia and UK. However, the world economy had a strong growth rate in the first half of 2006. As a result, overall growth rate of world economy in 2006 is expected to be higher than that in 2005 from the strong recovery in Japanese economy, the improvement in Euro area economy together with the high growth rates of Chinese and US economies, which offset the slowdown in Asian economies.



However, there are five main risks on the world economy in the latter half of 2006 as follows: (1) The slowdown in the US economy, the continued weakness in real estate and the problem of US current account and fiscal deficits could cause the dollar to depreciate. It is expected that in 2006 the dollars will depreciate against the Euro and Yen currency from 1.19 US dollar per Euro in 2005 to 1.32 in 2006, and Yen will appreciate from 118 Yen per US dollar in 2005 to 105 Yen in 2006¹. (2) The slowdown in Chinese economy caused by the tightening policies to cool down the overheating economy particularly in fixed asset investment and real estate. In addition, the high trade surplus in China will lead to a stronger pressure on Chinese RMB appreciation. (3) The European economic recovery is likely to be sluggish due to a slowdown in domestic consumption. (4) Interest rates in the world market is on a rising trend to ease inflationary pressure. The Fed fund rate is expected to be adjusted to 5.5 percent (from current rate of 5.25)².

¹ and ² According to the Lehman Brothers' projection in "Global Weekly Monitor", 25 August 2006.

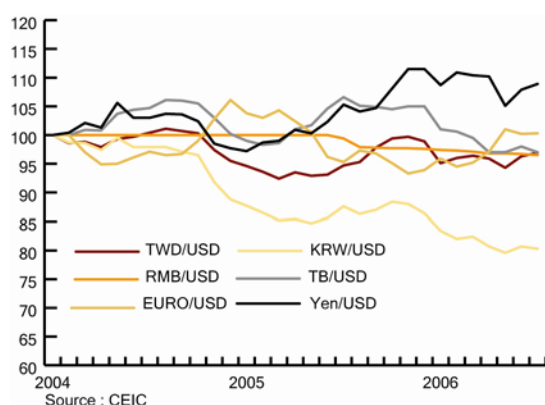


percent). The ECB official rates is expected to increase to 3.0 percent (from current rate of 2.75 percent). For Japan, the policy rate is likely to be increased to 0.5 percent (from current rate of 0.25 percent). (5) The slowdown in Asian economies in tandem with the slowdown in export which was affected by the moderate growth in US and China and the downturn cycle in electronic cycles.

- A slow down of world economy in the latter half of 2006 will affect Thai export. Particularly export of electronics products which highly increased in the first half of this year, however, the ratio of book to bill of electronics goods decreased to 1.06 in July. (from 1.12 in the second quarter of 2006). Moreover, in the latter half of this year, stringent import schemes of importing countries, such as the ending of privilege for exports of cereal, lychee/ longan canned products to the US, certificate of standard of prawn in the European market and regulations on harmful chemical in electronic appliance and parts in the European market, will affect the Thai export. As a result, export will increase only 14 percent, lower than a target of 17.5 percent.

(1.2) Internal risk factors/conditions: inflation and interest rate remain high and domestic uncertainty has an impact on consumer confidence.

- **Increasing interest rate leads to more caution in private spending and investment.** Interest rates have been rising since the beginning of 2006, particularly the MLR which was averaged at 7.75 percent at the end of August, causing credits for personal consumption to slow down from the growth rate of 14.6 percent in 2005 to 11.2 and 9.7 percent in the first and second quarter of 2006 respectively, although the housing credits started to pick up by 14.1 percent, compared to the growth rate of 9.5 percent in the first quarter. However, the average growth of housing credit expansion still signals a slowdown trend. Moreover, the lending rates are anticipated to increase further to be in line with the upward adjustment of the policy rate and the increasing cost of raising fund due to rising deposit rates. In addition, the future inflation which was expected to slow down in the second half of this year would lead to the further increase in real lending rates at the same period; partly results in the slowdown of credit expansion.
- **Appreciation in real effective exchange rate will has an impact on price competitiveness** particularly the sectors approaching the slowing trend such as



electronics and the sector which have already been losing their competitiveness to the low cost production country, namely electronic, textile, leather goods and furniture sector. Nonetheless, the baht is not expected to appreciate much further.

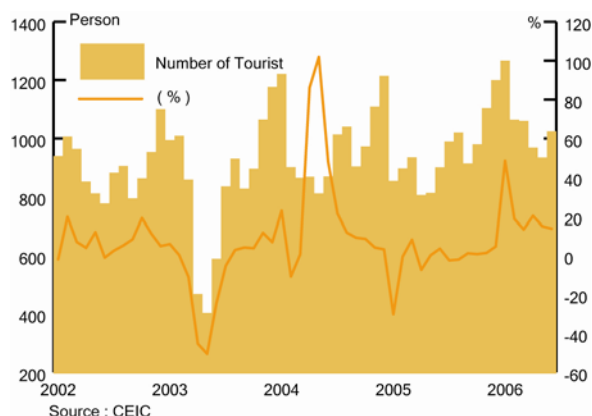
- **The political uncertainty and southern unrest have caused consumer and private confidence to plummet continuously since the beginning of 2006**, and have an impact on their consumption and investment decision. Moreover, the domestic uncertainty causes the delay in the approval of the new budget legislation which would affect the budget disbursement of capital investment and government spending during the first two quarters of fiscal year of 2007.

(2) Supporting factors/ opportunities for economic growth in the second half: Expansion of export, tourism, agricultural production and prices, self-adjustment of household spending and government measures on energy management.

- (2.1) The recovery of agricultural sector with the expansion of production while prices remain high**, coupled with the supports of products processing and implementation on alternative energy development, such as bio-fuel, aiming to create values of agricultural products including sugar cane, cassava and oil palm. In addition, major crop production is projected to increase in the second half of the year, thanks to sufficient water supply. Farm prices, in particular crop prices are expected to rise further especially those of rubber, rice, oil palm and sugar cane. In the first 7 months of 2006, average farm prices grew by 28.1 percent and crop production expanded by 5.2 percent. Thus, farm income rose significantly by 31.7 percent. GDP in agricultural sector increased by 5.9 percent in the first half of 2006. Export is also likely to expand well through the year's end. Export in agricultural products will benefit from an approximately decline in world's agricultural output of 4-5 percent as a result of natural disaster. Commodities whose exports tend to increase are cassava, rubber and corn as well as processing agricultural products.

Major Crop Production in H1/2006							
	Growth (%YOY)						
	2005					2006*	
	Year	Q1	Q2	Q3	Q4	Q1	Q2
1. Major rice	-0.3	-14.6	-10.6	14.6	2.6	6.6	22.0
2. Corn	-9.7	-27.1	-19.2	1.6	-13.5	1.1	8.8
3. Cassava	-15.4	-21.0	-10.5	-4.4	-10.7	41.6	69.3
4. Sugar cane	-37.4	-32.3	-16.8	-	-59.0	18.5	2.0
5. Oil palm	-3.5	-1.6	-6.6	-2.3	-1.6	12.6	6.8
6. Rubber	-1.0	1.0	-7.9	3.4	-1.1	-4.2	4.9

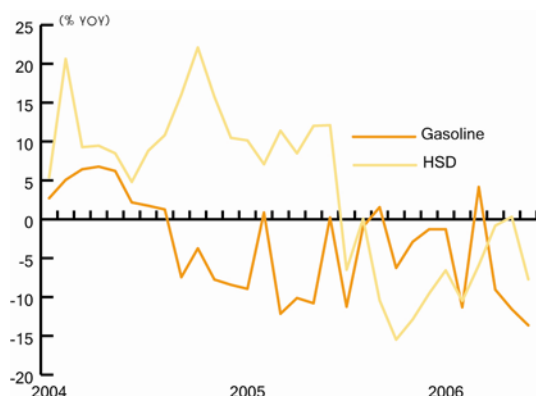
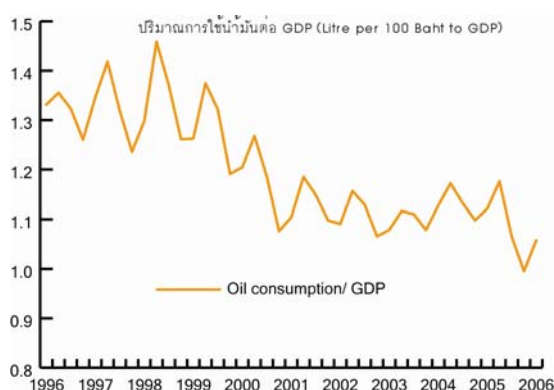
Note: * Office of Agricultural Economics



(2.2) The tourism sector continues its recovery. In the first half of 2006, numbers of foreign tourists were 6.3 million and up to 7.4 million people in the first 7 months, or rose by 19.7 percent. This contributed to a surplus of service account and thus led to a current account surplus in the first 7 months. Looking ahead, the tourism sector is likely to expand well due to favorable global economic condition, in particular Asian and emerging economies like China and India that brought about higher number of foreign tourists. Moreover, tourism development measures which focus on raising value more than quantities as well as international road show will encourage number of tourists to meet target level of 13.8 million people in 2006.

Crude oil imports (Growth)							
(%YOY)	2005				2006		
	Year	H1	Q3	Q4	H1	Q1	Q2
Volume	-5.1	-1.06	0.67	-17.83	-1.96	-1.91	-2.01
Value	33.0	37.59	46.46	13.01	28.89	39.47	8.21

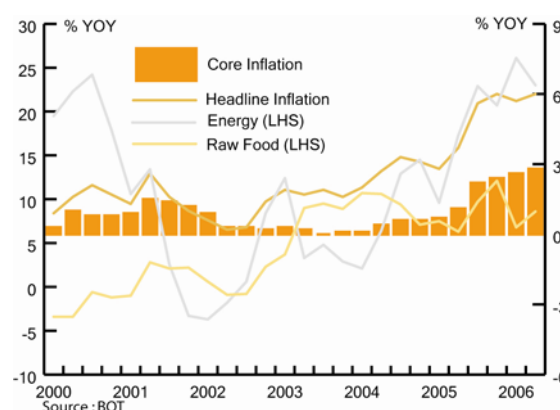
Source: Department of Energy Business



(2.3) Continuing policy implementation on energy saving and alternative energy development which in turn would reduce demand for petroleum products despite favorable economic growth. This will help save more foreign currency from oil imports and lessen pressures on current account. The result has been more apparent as petroleum products consumption noticeably slowed down in 2005, dropped by 1.9 percent in the first half of 2006, compared to 11.7 and 3.7 percent increase in the first half of 2004 and the first half of 2005. Consumption of Benzene and Diesel dropped by 2.8 and 9.4 percent. Due to higher oil price, consumers adjusted their behaviors in an efficient and economical way. Although the economy in the first half of 2006 expanded by 5.5 percent, higher than 3.9 percent in the first half of 2005, consumption of petroleum products decline. As a result, total oil consumption to GDP continued to fall. Declining oil consumption led quantity of oil imports in the first half to drop by 2.2 percent. The acceleration of alternative energy measures over the next 6 months are needed, including the preparation for private sector on ethanol production, NGV usage in taxi and bus. This will reduce a dependency on oil imports and strengthen capability on alternative energy development.

(2.4) Lessened inflationary pressure in the latter half of 2006. In July, inflation was 4.4 percent and declined to 3.8 percent in August, down from the average rate of 5.9 percent in the first half. It is expected that inflation will steadily decline in the remaining months due to (1) increasing interest rate

which will slow down household spending (2) baht appreciation which will soften pressure on cost from import products and (3) high-base of inflation in the latter half of 2005. Subdued inflationary pressure will restore consumer confidence and reduce pressure for upward interest rate adjustment further. This, as a result, will brought about private consumption and investment to expand stronger in 2007, particularly after setting up the new government, announcing new government policies and 4-year administrative plan which will elucidate political stances as well as economic policy guidelines. This will finally bring back confidences of consumer and investors.



2.2 Key Assumptions for 2006 Projection: Dubai oil price is expected to be 65-68 US dollars per barrel, up from 49.30 US dollars in 2005. Global growth is estimated to be 4.7 percent.

World Economic Growth

(%YOY)

	Year	Year	Q1	Q2	Q3	Q4	Q1	Q2	Jun	Sep
World*	5.1	4.4							4.6	4.7
USA	3.9	3.2	3.3	3.1	3.4	3.1	3.7	3.5	3.4	3.4
Eu15	2.1	1.5	2.1	2.5	2.2	1.8	1.4	1.3	NA	NA
Eu25 1/	2.3	1.7	1.6	1.5	1.8	1.9	2.2	2.6	NA	NA
Euro area	1.8	1.4	1.2	1.2	1.6	1.7	2.0	2.4	2.1	2.2
Germany	1.1	1.2	0.6	0.8	1.5	1.7	1.7	2.4	1.8	2.0
Japan	2.3	2.6	1.4	2.6	2.8	3.7	3.6	2.0	2.8	2.8
Hong	8.6	7.3	6.0	7.2	8.2	7.5	8.0	5.2	5.0	5.0
Singapor	8.7	6.4	3.4	5.7	7.6	8.7	10.8	8.1	6.2	7.0
S. Korea	4.7	4.0	2.7	3.2	4.5	5.3	6.1	5.3	5.2	4.9
Taiwan	6.1	4.1	2.5	3.0	4.4	6.4	4.9	4.6	4.0	4.0
Indonesia	5.1	5.6	6.3	5.6	5.6	4.9	4.7	5.2	5.1	5.1
Philippine	6.2	5.0	4.2	5.4	4.8	5.3	5.7	5.5	5.1	5.1
Malaysia	7.2	5.2	6.1	4.1	5.3	5.2	5.5	5.9	5.5	5.5
China	10.1	9.9	9.9	10.1	9.8	9.9	10.3	11.3	9.6	10.0

World composes of 18 Thailand's trading partners

Source: CEIC, government agencies and average from several sources

- (1) The world economy in 2006 is likely to grow by 4.7 percent, slightly accelerating from 4.4 percent in 2005. The assumption is revised upward slightly from 4.6 percent growth assumed in the June projection. The upward adjustment is due to the upward revision of key economies such as China, Euro area, and Singapore. The Chinese economy is expected to expand by 10.0 percent, revised upward from 9.6 percent in the previous forecast. This resulted from a buoyant growth rate of 10.9 percent in the first half of 2006 and the less effective tightening policies due to high liquidity and ineffectiveness of monetary policy under highly fixed exchange rate regime. In addition, the Euro area economy is expected to expand by 2.2 percent, revised upward from 2.1 percent in the previous forecast as Germany and France grew at faster rates in the second quarter. The Singapore economy also posed strong growth of 9.4 percent in the first half of the year. As a result, the projection of Singapore economy is revised upward to 7.0 percent from 6.2 percent in the previous forecast. However, the growth of the Korean economy is revised downward from 5.2 percent in June projection to 4.9 percent in September projection due to the slow down in private consumption affected by higher oil price and the overshoot policy interest rate. Overall, the upward revision outpaces the downward revision.

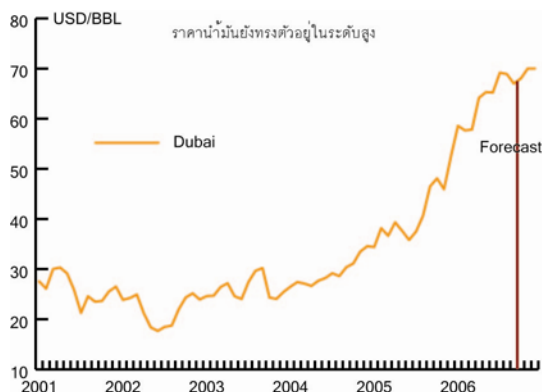
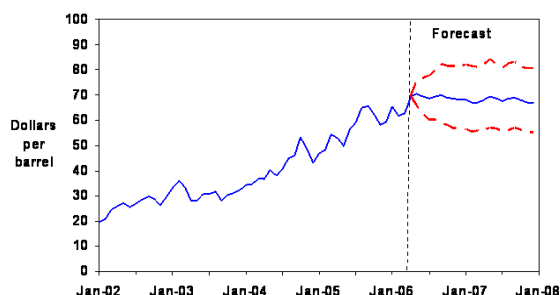
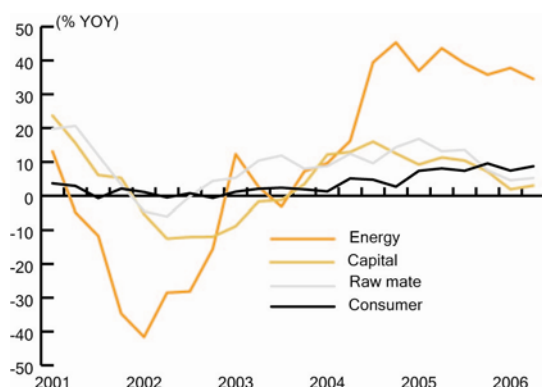


Figure 1. West Texas Intermediate Crude Oil Price
(Base Case and 95% Confidence Interval*)



*The confidence intervals show ± 2 standard errors based on the properties of the model.

Short-Term Energy Outlook, May 2006



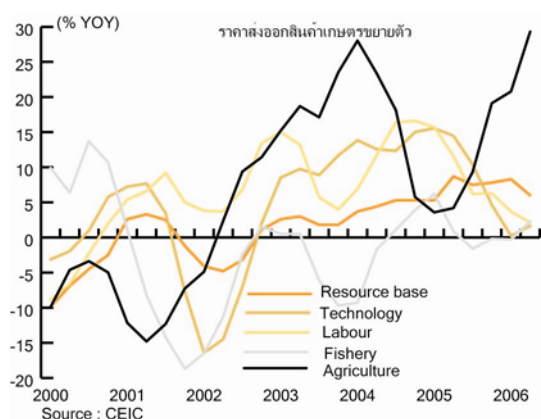
(2) Crude oil price is expected to be around 65 percent US dollars per barrel, revised up from earlier assumption of 63 US dollars per barrel.

- Oil price continues to remain high. It is expected that average Dubai price will be around 65-68 US dollars per barrel in 2006. The most likely price is 65 US dollars per barrel which is higher than 49.30 US dollars per barrel in 2005, or increased by 31.85 percent. This level is revised upward from previous assumption of 63 US dollars per barrel, within the range of 62-65 US dollars per barrel. As far as the movement of oil price throughout 2006 is concerned, the Dubai price in the first half of 2006 averaged at 61.45 US dollars per barrel. Compared to the same quarter of 2005, average price increased by 34.6 US dollars. It was 69.17 and 68.89 US dollars in July and August respectively. It is projected that average oil price will be 67-70 US dollars in the rest of this year due to the winter season.
- On 8 August 2006, Energy Information Administration (EIA), in USA announced the forecast of West Texas Intermediate (WTI) in 2006 to be on average of 70 US dollars per barrel. WTI price is generally 5-8 US dollars per barrel higher than the Dubai price.
- Currently, the NYMEX Brent futures price of 2006 is about 70 US dollars per barrel. The gap between Brent and Dubai price increases to approximately 5-8 US dollars per barrel²

(3) Export and import prices. In 2006, it is expected that commodities' prices in the global market is still on uptrend as a result of continuing rise in oil and raw materials prices as well as strong growth momentum of world economy, bringing about the higher world demand for goods. Meanwhile, the capacity utilization rates in many countries continue to increase and the excess capacity of global production will be lower than in 2005. However, consumer products' prices including steel and crude oil price start to decline. In addition, a slowdown sign of world economy in the second half of this year suggests that a slowdown in demand for goods in the world market, particularly of electronics products, which their prices have achieved the peak level. This has shown a continual slow down of export prices in all items, except for agricultural product. Since the second half of

² Refers to Global Weekly Economic Monitor by Lehman

Brother, 25 August 2006



2005 up until the first 7 months, export prices increased by 4.9 percent, lower than the growth rate of 12.6 percent and 7.7 percent in the first and second half of 2005, respectively.

Therefore, in this projection, export prices in US dollar term in the last 5 month are expected to increase faster than in the first 7 months, due to low base in the same period of previous year. Average export price is assumed to increase by 5.2 percent as in the previous projection. Import prices increase is also remained at 7.6 percent as in the previous forecast. In the first 7 months average import price increased by 7.8 percent slowing down from the previous year, particularly due to those of capital and raw material products, except continued higher crude oil import prices.

2.3 Economic projection for 2006: 4.2-4.7 percent GDP growth, 4.5-4.7 percent headline inflation, and 0.6 percent of current account to GDP.

Thai economy expanded by 5.5 percent in the first half of 2006. However, it is expected to expand moderately in the latter half of 2006 as a result of many constraints, already assessed on June 5 press release. Such constraints are (1) higher-than expected crude oil price (2) continue lower consumer and business confidences causing private consumption and investment to slow down (3) the budget disbursement of capital investment during the first two quarters of fiscal year of 2007 was affected by the postponement of the approval of the new government budget to April 2007 and (4) the slowdown in world economic growth in the latter half of 2006.

Hence, NESDB revises the upper bound growth of the range. The projection on real GDP growth is revised from the range of 4.2-4.9 percent (mean value of 4.6 percent) released in June to the range of 4.2-4.7 percent (mean value of 4.5 percent). The projected headline inflation will be at the range of 4.5-4.7 percent. The trade balance will record a deficit of 3.7 billion US dollars, lower than earlier forecast of a deficit of 6.1 billion US dollars. This was due to a higher growth rate in export and a lower growth rate in import than expected. Together with the surplus in service account of 5 billion US dollars, the current account is expected to record a slight surplus of 1.3 billion US dollars, or 0.6 percent of GDP. The projected unemployment rate will be approximately 1.8-2.0 percent.

In all, this projection is revised downward slightly from previous forecast, as better-than-expected exports of goods and services almost completely offset a slowdown of domestic demand. Therefore, the 2006 growth will be supported by stronger net exports, while domestic demand will contribute less than earlier estimated. **The slight downward revision of the 2006 economic growth forecast are as follows:**

- **Downward revision on projection of private consumption and investment growth.** Latest economic indicators in the first 7 months of 2006 showed that the domestic demand, both private consumption and investment, continues its slowdown and to a larger extent than previously expected. This is mainly due to continued higher oil prices, rising inflation and uptrend interest rates in financial market. All of which is expected to increase in the second half of the year. Both consumers' and business sentiment continued to decline as well.
- **Upward revision on export volume and downward revision on volume of import of goods and services results in higher volume of net export and service than the previous forecast.** In this projection, volume of export of goods is upwardly revised as latest data have generally indicated stronger export volume than expected. In the first 7 months, exports grew by 11.25 percent. It is assumed that the world trade volume will expand by 8.5 percent, higher than earlier estimation of 8.0 percent and up from 7.3 percent in 2005. Volume of import of goods is revised down as it is expected that more inventories both of raw materials and finished goods will be run down of stocks level. Moreover, slower-than-expected

private investment brings on a significant slowdown of import of capital goods. Correspondingly, it is expected that export volume will slowdown in the latter half following global economic trend and electronics market. However, import volume will expand higher than in the first half owing to depleted stocks already in the first half and stronger baht. In addition, there are an upward revision on service payments in tandem with higher number of Thai tourists traveling abroad in the first half of the year, which partly due to baht appreciation.

(1) The High Case Scenario of 4.7 Percent Economic Growth

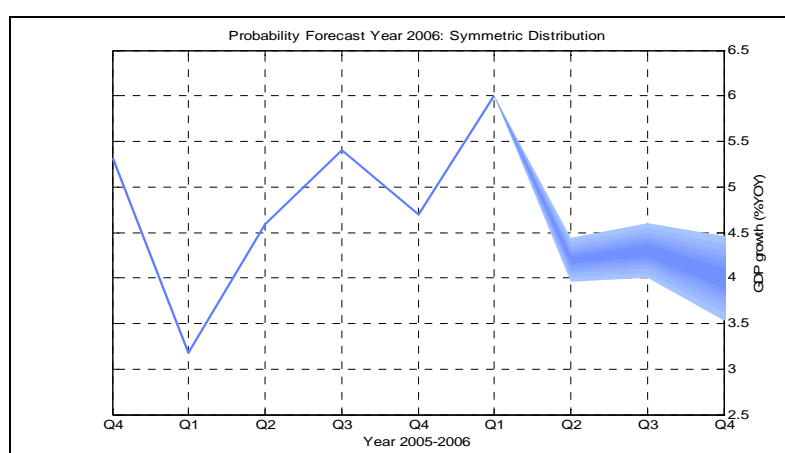
Thai economy in 2006 will achieve 4.7 percent growth under the following conditions: (1) Export growth accelerates to 15 percent from the normal trend rate of 13-14 percent. The efforts would be primarily focused to increase exports of agricultural products, in particular, rubber, shrimp, fowls, and canned seafood as electronics, transport equipment and parts. (2) The efforts to promote international tourists generating higher tourist revenue at least 50,000 million baht from the 2005 revenue base. (3) The disbursements of government budget and state enterprise capital budget are on the target. This includes the SML and provincial CEO budget. (4) Financial and fiscal measures will be consistent with economic condition which faced higher pressures from labor costs and energy prices.

(2) The Low Case Scenario of 4.5 Percent Economic Growth

In the case of reschedule of election which will affect consumer and investor confidence and the case of higher oil prices due to more severe conflicts over US and Iran, the terrorist attacks, the much lower temperature in winter in the West, the Dubai oil prices could be 70 US dollars per barrel in the remaining of the year. The averaged Dubai oil price for the whole year of 2006 will be beyond 65 dollars per barrel. This will lead to the slower growth of global economy than expected, leading export to be lower than the trend case. Meanwhile, the value of import will increase in accordance with higher oil prices, leading to a larger trade deficit than the normal trend. However, the case that the oil price will increase more than 65 dollar is less plausible as both the slowdown in world economy in the latter half of 2006 and behavioral changes in energy use toward more efficiency will reduce pressures on inflation.

3. Probability Distribution of GDP Growth Forecast

The probability that the averaged Dubai oil price for the whole year of 2006 to be higher or lower than 65 dollars per barrel and the probability that the world economic growth to be higher or lower than 4.7 percent are equal. Therefore, the probability forecast indicates that the cases of economic growth rate below and over the base case of 4.5 percent are equally likely. In other words, the probability distribution of economic growth is symmetric. NESDB projects economic growth for 2006 to lie between 4.2 to 4.7 percent with probability of 87 percent.



4. Economic Policy Management for the Remaining Periods of 2006

In 2006, the slowdowns in household consumption and private investment have become more pronounced. Moreover, higher oil price as a key risk factor might put greater impacts on the world economy than expected. The rebalancing process of the world economy could be another key risk factor associated with the outlook of the Thai economy. In addition, the downward trend of the electronic cycles will dampen export performance. Meanwhile higher oil prices and interest rates could potentially destabilize the adjustment of expenditure and investment towards a stable path. Therefore, measures which ought to be intensively implemented in order to prevent the stagnation in the latter half of 2006 and as well as to provide a smooth transitions into 2007 are as follows:

- (1) Accelerating government sector to complete the disbursement plan and commit the budget. This is in order to make preparation for the actual disbursement in the last quarter of 2006 and the first quarter of 2007.
- (2) Expediting energy measures including particularly of the readiness of private sector to produce ethanol, the usage of NGV in taxi and mass transit buses as well as speeding up the elevated train projects already approved by the cabinet.
- (3) Running a deficit budget in 2007 and prioritizing the budget allocation to education, health, energy projects and infrastructure development projects.
- (4) Implementing social measures for aging and disabled people. Emphasis will be made on providing such necessary expenditure as scholarships and pension works.
- (5) Restoring confidence of both consumer and business sector by explaining the facts about current economic situation and on-going policy implementation during the caretaker government.

Economic Projection of 2006

	Preliminary ^{1/}			Projection of 2006		
	2003	2004	2005	6 Mar 06	5 June 06	4 Sep 06
GDP (at current prices: Bil.Bht)	5,929.0	6,503.5	7,104.2	7,777.7	7,750.7	7,831.3
GDP per capita (Bht per year)	93,142	101,305	109,573.5	119,033	118,619	119,853
GDP (at current prices: Bil.USD)	142.9	161.4	176.3	194.4	201.3	206.1
GDP per capita (USD per year)	2,244	2,514	2,846	2,958	3,081	3,154
GDP Growth (at constant prices, %)	7.0	6.2	4.5	4.5-5.5	4.2-4.9	4.2-4.7
Investment (at constant prices, %)	12.1	13.8	11.4	8.7	4.7	4.3
Private (at constant prices, %)	17.7	16.3	11.2	9.3	4.9	4.4
Public (at constant prices, %)	-0.7	6.8	11.9	6.8	4.0	4.0
Consumption (at constant prices, %)	5.8	5.7	5.4	4.5	3.5	3.3
Private (at constant prices, %)	6.4	5.9	4.4	4.2	4.0	3.8
Public (at constant prices, %)	2.3	4.7	12.2	6.2	0.8	0.8
Export volume of goods&services (Volume,%)	7.0	9.6	4.4	7.8	8.7	8.7
Export value of goods (Bil.USD)	78.1	94.9	109.2	125.9	124.1	124.5
Growth rate (%)	18.2	21.6	15.0	15.3	13.6	14.0
Growth rate (Volume, %)	9.5	8.4	4.3	6.8	8.4	8.8
Import volume of goods&services (Volume,%)	8.5	13.5	9.4	7.0	4.9	3.1
Import value of goods (Bil.USD)	74.3	93.5	117.8	135.5	130.2	128.2
Growth rate (%)	17.4	25.7	26.0	15.0	10.5	8.8
Growth rate (Volume, %)	10.7	12.3	8.9	6.0	2.9	1.2
Trade balance (Bil.USD)	3.8	1.5	-8.6	-9.6	-6.1	-3.7
Current account balance (Bil.USD)	8.0	6.6	-3.7	-4.0	-1.0	1.3
Current account to GDP (%)	5.6	4.1	-2.0	- (2.0- 2.5)	- 0.5	0.6
Inflation (%)						
CPI	1.8	2.7	4.5	3.5-4.5	4.5-4.7	4.5-4.7
GDP Deflator	1.6	3.3	4.6	4.5	4.5	5.0
Unemployment rate (%)	2.0	2.0	1.7	1.8	1.8-2.0	1.8-2.0

Source: Office of the National Economic and Social Development Board. September 4, 2006

Note: ^{1/} Preliminary data 2003 - 2004 were adjusted since data from Office of the National Income Account (GDP) and the Bank of Thailand (Export/Import data) have been revised.

