

## Thailand: 2Q GDP Grew Stronger than Expected at 4.4% While Inflation Hits a 5-year Low of 1.1% in August

Alvin Liew  
(65) 6539 3923  
[Alvin.LiewTS@UOBgroup.com](mailto:Alvin.LiewTS@UOBgroup.com)

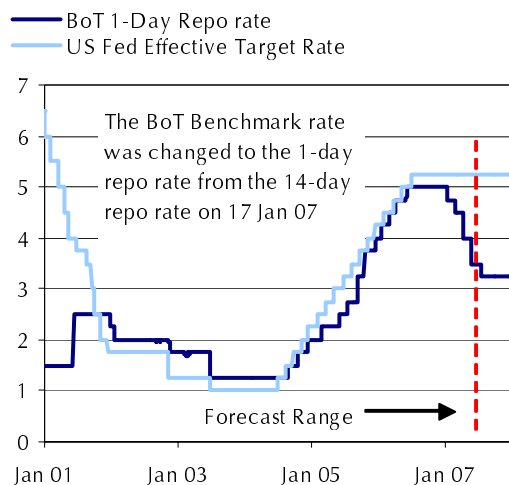
In Thailand's 2nd quarter economic report released on 3 Sep, the country's 2Q GDP expansion surprised markets (Median: 4.0%), coming in at 4.4%/y/y (although UOB was expecting a slightly higher outcome of 4.6%), from a revised 4.2% in 1Q. While much of the growth in 2Q remained attributed to the resilient export sector (with net exports contributing 2.5%age points of the 4.4% growth), fixed capital investment growth turned marginally positive in the month (0.2%) but this was solely due to the 3.1% expansion of government investment although the decline in private investment did moderate to 0.8% in 2Q from 2.3% in the previous quarter. In comparison, private consumption expenditure which has been trending down since 2Q06 weakened further in 2Q07, expanding by only 0.9% reflecting the current state of consumer confidence languishing at 5-year low. On a seasonally-adjusted q/q basis, 2Q GDP accelerated by 1.3% much to the market's surprise following the 1.2% expansion in 1Q.

From a sectoral perspective, the agricultural sector increased production markedly in 2Q (by 9.7% from 1Q's 3.3%) while manufacturing recorded weaker growth in the same quarter (4.4%) similar to regional economies like Philippines, Malaysia and Singapore. The weakness in manufacturing was also reflected in the moderation of exports growth in 2Q although it still remains the key economic driver for the Thai market. While consumer and investment sentiments remain entrenched in multi-year lows, we feel that this is probably the bottom of the cycle. Although a recovery may not be readily presented in the 3rd quarter (due to lingering domestic uncertainties and volatile external financial market developments), we may yet see a recovery of investments by the 4th quarter driven by more public investments and partial return of private foreign investments ahead of the scheduled elections.

The year long political stalemate had taken its toll on private consumption and this was aptly reflected by the weaker than expected inflation data in August yesterday, coming in at a 5-year low of 1.1%/y/y (down significantly from 1.7% in July). This was very much lower than our expectations of August inflation at 2% given the regional price developments and the low basis effect from the removal of the oil subsidy in mid-2006. We have subsequently lowered our inflation forecast for 2007, expected to come in at 2.1% (from 3.1% previously well within the official forecast range of 1.5%-2.5%). While the extremely benign inflationary environment has again sparked calls/speculation for further rate cuts by the BoT, we remain convince that the central bank has reached its neutral monetary policy stance. The next BoT MPC meeting is in Oct and we remain convince the bank will hold rates steady unless the US Fed cuts rates during its Sep meeting. 3.25% for the BoT is getting precariously low and cutting prematurely will leave it very little space for any downward maneuverability should the Fed cut rates aggressively later in the year. And we maintain that the authorities recognize that it is the political situation, not the cost of funds that is dampening consumption spending and capital investments.

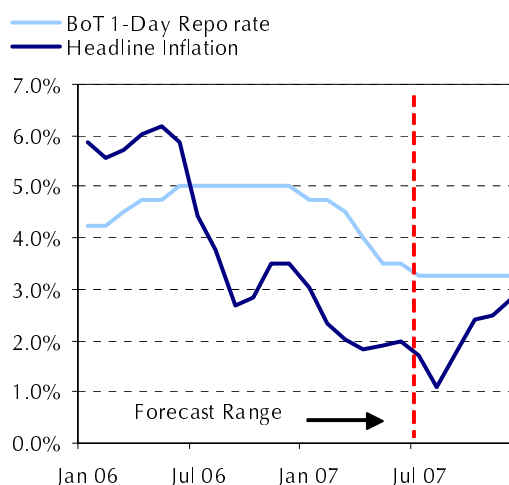
Returning to the Thai output data, with GDP growth averaging 4.3%/y/y in 1H07 the government is confident that the later half of the year will also expand at least by the same rate in 2H. We share in their sentiments, citing the lower base for 3Q and 4Q, as well as the expectation of more visible investment recovery in the final quarter of 2007. Therefore, we maintain our full-year 2007 GDP growth at 4.5% (which is at the top end of the BoT forecast) unless we see a drastic deterioration in outlook for Thailand.

The US Fed Rates and BoT's Official Rate Widest Gap Now Since 14 May 2001 Expected to Remain for 2H07



Source: CEIC, UOB

Inflation Now Likely to Remain Benign in 2H07 Trending Only Slightly Higher Later in the Year



Source: CEIC, UOB

GDP by Expenditure

At Constant 1988 Prices	Weight 2006	% y/y change		2006				2007	
		2005	2006	1Q	2Q	3Q	4Q	1Q	2Q
Consumption									
Private	53.6	4.3	3.1	3.9	3.3	2.8	2.5	1.3	0.9
Government	9.0	13.7	3.4	7.4	5.7	4.3	-4.2	11.1	7.4
Capital Formation									
GFCF	23.3	11.1	4.0	6.6	4.0	3.2	2.4	-1.5	0.2
Private	17.4	10.9	3.9	7.0	3.3	2.9	2.3	-2.3	-0.8
Government	5.9	11.3	4.5	5.3	6.4	3.8	2.5	1.1	3.1
Exports	68.7	4.3	8.6	14.4	9.0	4.7	7.0	6.9	6.7
Goods	56.0	4.3	9.0	13.9	9.2	4.9	8.7	8.5	7.9
Services	12.7	4.3	6.9	16.4	8.2	3.8	0.0	0.5	1.8
Imports	54.3	9.3	1.6	1.9	-1.7	5.2	1.0	0.2	3.7
Goods	44.6	8.8	-0.8	-2.9	-3.7	3.9	-0.5	0.1	3.0
Services	9.7	12.1	14.3	29.6	10.3	11.5	8.0	0.9	7.2
GDP	100.0	4.5	5.0	6.1	5.0	4.7	4.3	4.2	4.4

Source: NESDB, UOB