May 21, 2020
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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 19/82-1

10:00 a.m., September 30, 2019

1. Thailand—2019 Article IV Consultation

Documents: SM/19/220 and Correction 1; and Correction 2; and Supplement 1; SM/19/221; and Correction 1

Staff: Leigh, APD; Sun, SPR

Length: 1 hour, 25 minutes

Executive Board Attendance

M. Furusawa, Acting Chair

Executive Directors	Alternate Executive Directors
	I. Mannathoko (AE)
M. Raghani (AF)	
	R. Morales (AG), Temporary
N. Ray (AP)	
	B. Saraiva (BR)
	P. Sun (CC)
L. Villar (CE)	
	A. McKiernan (CO)
R. Kaya (EC)	
	P. Rozan (FF)
	K. Merk (GR)
	P. Dhillon (IN), Temporary
	A. Korinthios (IT), Temporary
T. Tanaka (JA)	
	El Qorchi (MD)
	W. Abdelati (MI), Temporary
	N. Jost (NE), Temporary
	J. Sigurgeirsson (NO)
A. Mozhin (RU)	
	R. Alkhareif (SA)
A. Mahasandana (ST)	
P. Inderbinen (SZ)	
	J. Freeman (UK), Temporary
	P. Pollard (US), Temporary

S. Bhatia, Acting Secretary
S. Maxwell, Summing Up Officer
A. Lalor, Board Operations Officer
L. Nagy-Baker, Verbatim Reporting Officer

Also Present
African Department: X. Li. Asia and Pacific Department: T. Dao, K. Kang, K. Kashiwase, L. Leigh, S. Nadeem, C. Rhee, M. Saenz Castegnaro. Legal Department: J. Pampolina, A. Rosha. Monetary and Capital Markets Department: P. Grippa, S. Kumarapathy, A. Lopez Mejia, J. Morsink, S. Ogawa. Strategy, Policy, and Review Department: V. Klyuev, Y. Lu, Y. Sun. World Bank Group: A. Aviles. Alternate Executive Director: K. Chikada (JA), F.

Sylla (AF), K.Tan (ST). Senior Advisors to Executive Directors: Z. Abenoja (ST), A. Muslimin (ST), L. Johnson (AP), Z.Mahyuddin (ST), J. Shin (AP), T. Sitima-wina (AE), N.Thiruvenkadam (IN). Advisors to Executive Directors: K. Badsi (MD), O. Bayar (EC), S. Belhaj (MD), E. Boukpessi (AF), E. Cartagena Guardado (CE), D. Crane (US), H. Koh (GR), K. Kuretani (JA), U. Latu (ST), R. Pandit (ST), A. Park (AP), A. Srisongkram (ST), M. Sylvester (CO), A. Urbanowska (SZ), S. Yoe (ST), F. Antunes (BR), A. Sode (FF).

1. THAILAND—2019 ARTICLE IV CONSULTATION

Ms. Mahasandana and Mr. Srisongkram submitted the following statement:

On behalf of the Thai authorities, we would like to thank the IMF Article IV and FSAP mission teams for the constructive engagement and candid discussions which centered on policies to achieve sustained and more inclusive growth and to address structural challenges in the Thai economy.

The authorities share staff's assessment of the economic outlook and risks, and medium-term structural challenges. The authorities also welcome staff's policy recommendations, albeit with notable divergence in a few areas.

Recent economic developments and outlook

Thailand's economic growth has slowed down amidst intensified trade tensions, led by a contraction in exports which has weighed on domestic demand. The authorities expect the economic expansion to continue, albeit at a slower pace, and project a lower GDP growth of 2.8 percent for 2019 compared to 4.1 percent growth achieved in 2018. Headline inflation is projected to be slightly below the lower bound of the 2.5±1.5 percent target range due to structural factors including technological advancements, expansion of e-commerce, growing price competition as well as a low global inflation environment. Risks to the growth outlook remain tilted to the downside mainly from external uncertainties including protracted trade tensions and geopolitical situations.

The authorities have employed an accommodative macroeconomic policy mix to sustain growth momentum while also pushing ahead with various structural reforms to address structural bottlenecks and improve productivity to ensure sustainable growth over the longer term.

Monetary policy

Consistent with the data-dependent approach, the Monetary Policy Committee (MPC) decided to cut the policy rate by 25 bps from 1.75 to 1.50 percent at the August meeting. Given heightened global uncertainties and observable signs of domestic slowdown and inflation projected to be below the lower bound of the target range, the MPC assessed then that a more accommodative monetary policy stance was appropriate to sustain the growth momentum. The policy rate was kept unchanged at its September 25 meeting as the MPC viewed that the current monetary policy stance is sufficiently accommodative to support the continuation of economic growth and the rise of headline inflation toward target.

The authorities noted staff's recommendation for further easing to support growth and inflation but emphasized that future policy actions need to be carefully calibrated based on assessment of risks and policy options. While the primary objective of monetary policy framework is inflation, supply side developments have weighed down and delayed the return of inflation to its target range. Further monetary easing to meet the growth and inflation objectives in the near term may put financial stability and future growth at risk in the longer term.

While there are no immediate systemic risks in the Thai financial system, elevated household debt and search-for-yield behavior warrant close monitoring. The BOT has deployed several macroprudential measures, such as the recent tightening of the LTV ratio which helped curb speculative activities in the housing market. However, not all pockets of vulnerabilities are within the BOT's regulatory reach particularly non-bank financial institutions. The authorities agree on the need to further strengthen the macroprudential toolkits, though such efforts may take time.

Exchange rate policy and capital flows

The authorities underscore the need to remain vigilant of the adverse impact of volatile capital flows, especially given waning domestic growth momentum and more challenging global environment.

The authorities reiterate their commitment to exchange rate flexibility as evidenced by the more than 17 percent appreciation of the Thai baht both in USD term and NEER term during the past 3 years. The Thai baht appreciated by almost 6 percent against the US dollar year-to-date. The continued appreciation followed the baht's perceived safe haven status in spite of significant decline in current account (CA) surplus (from around 11 percent of GDP in 2016 to 6 percent in 2019), and the shift in investors' sentiment as major central banks rotated towards an easing bias. This has necessitated occasional foreign exchange intervention (FXI) especially during periods of intense inflows to forestall the risks of further inflow amplification of the exchange rate.

The authorities viewed that recent episodes of the baht's sharp appreciation were not warranted by economic fundamentals, and could pose risks to macroeconomic stability. To follow staff's recommendation to let the exchange rate act as shock absorber would risk disrupting real-sector adjustments as such recommendations do not take into account the impact of foreign exchange market dynamics and the fact that exchange rate can become a shock amplifier in an environment of excessive global liquidity.

In dealing with the multi-faceted challenges from global financial conditions, small open economies like Thailand require integrated policy package and tools to address various areas and sources of risks in foreign exchange markets. Staff's argument that a policy rate cut would also attenuate short-term exchange rate pressures might be sub-optimal, given the blunt nature of the instrument and possible unintended consequences on financial stability. The authorities believe that measures to address the source of pressure would be a more effective policy alternative. The measure to lower the ceiling on the end-of-day outstanding balance of baht accounts for non-residents (NBRA/NRBS) neither prevents nor limits the quantity of inflows into Thai financial markets and NR's purchase of domestic securities. On the other hand, it aims directly at transactions that are not supported by underlying economic activity. The measure was necessary to help the economy navigate through the risk from volatile capital flows in the short run, while the ongoing macroeconomic adjustments and reforms to further liberalize outward flows would take some time.

The authorities will continue to engage with staff in the policy discussion on capital flows and encourage the Fund to undertake studies on the spillover effect of policy implementations from advanced economies that may have impact on small open economies.

The authorities reiterate the view that the disclosure of FXI data would be counter-productive at this juncture. Such information, even with a lag, can undermine the effectiveness of central bank foreign exchange operations as it could be exploited for speculative purposes. The current publication of Thailand's international reserves data every two weeks has already provided sufficient information on their FX operation.

External Balance Assessment

On the external balance assessment (EBA), the authorities welcome staff's focus on structural factors and concur that macro- and structural policies are key to addressing the CA gap. Thailand's CA gap has narrowed from recent decline in trade surplus as well as the ongoing structural balancing efforts. Going forward, the authorities expects the CA surplus to narrow further over the medium term as private and government investments pick up pace.

The authorities maintain that the EBA results must be communicated with caution given the model's inherent limitations, particularly implications being drawn regarding currency valuation. It is critical to acknowledge the inherent limitations of the model, including its narrow and CA-centric focus of external imbalances as it does not account for capital account transactions which have larger impact on the exchange rates. In Thailand's case for instance, the EBA model does not seem to account for the fact that the baht has already appreciated significantly over the years as the model continues to suggest large REER undervaluation given that the CA gap remains positive. In addition, given the large unexplained residuals in many country cases, including Thailand, the model results must be interpreted carefully and take into account country specificities in order to draw appropriate policy implications.

Financial Sector

The authorities welcome the FSAP's assessment that the Thai financial system remains sound, with strong and independent supervisory agencies and frameworks. Financial stability risks are contained while pockets of vulnerability remain under close monitoring.

The authorities broadly agree with the FSAP recommendations which were consistent with their ongoing efforts to buttress financial sector resilience. Many enhancements are well underway including SFI regulations, strengthening crisis management and banking resolution, as well as the macroprudential toolkits. Currently, the Thai authorities are discussing the possibility of setting up a financial stability advisory body consisting of regulators of significant financial intermediaries.

The authorities have different view from staff's recommendation regarding institutional arrangement. They stress that there are merits to each institutional arrangement design which must be considered within the country's context. There is no one-size-fits-all, but rather one that is 'best suited' to the country's working culture and constraints, and shaped through experiences. The current institutional arrangement in Thailand has been purposely designed based on our experiences, particularly by drawing upon lessons learned during the 1997 financial crisis which arose partly from the lack of interagency coordination and oversight. The current governance structure of each committee is focused on the desired outcomes. The setup of the Financial Institution Policy Committee (FIPC), in particular, has proven to be practical and effective in the Thai context.

The presence of the MOF representative on the FIPC brings a broader perspective and policy recommendations that take into account potential impact on the overall economy, while not compromising the operational independence of the supervisory agencies. Furthermore, the MOF representative facilitates the decision-making process involving the MOF and the Cabinet.

The authorities underscore the merits of cross directorships of supervisory agencies especially with increased interconnectedness within the financial sector, given that most of the largest players in the capital market in Thailand such as securities companies and asset management companies are subsidiaries of commercial banks. This inter-agency coordination promotes collective accountability and timely engagement of the authorities in decision-making and crisis management should the situation warrant. The authorities welcome staff's acknowledgement that the current arrangement of the supervisory agencies does not undermine each agency's operational independence.

Fiscal Policy and Structural Reforms

The fiscal stance is expected to remain expansionary for FY2020. On September 3, 2019, the Cabinet approved a budget envelope of 3.2 trillion baht for FY2020, an increase of 6.7 percent over last year with the same level of fiscal deficit coming in at 2.6 percent of GDP. Higher spending is expected to be driven mainly by the replenishment of the treasury balance as pension and medical expenses for government officials were underestimated in 2018. The draft budget bill will be tabled to the Parliament in mid-October.

The authorities are positive that fiscal spending will largely be on track. Disbursement for current spending and approved investment projects from FY2019 can continue to be disbursed despite the delay in the budget approval process. Most investment outlays would not be materially affected since it is set to be disbursed in the latter half of 2020. Macro-critical infrastructure projects under the EEC are implemented through PPP with most of the financing to come from the private sector. The construction of two out of the five EEC main projects should begin in 2020, while the rest are in the bidding and negotiation process.

Our authorities remain steadfast in implementing the structural reform agenda to ensure long-term fiscal sustainability and uplift potential growth. Regarding fiscal reforms, on the expenditure side, the government has set out a plan to revise the eligibility criteria for low-income earners so that the welfare program is better targeted to the lower income group. A group of subnational committees will be set up to closely monitor the eligibility to the program. On the revenue side, the government has embarked on a number of tax reforms to increase revenue, for example, the enforcement of the new Land and Property Tax Law and the revision of the taxation of investment income from bonds through mutual funds. The E-payment Law, which will be effective from the beginning of 2020, will prevent local online vendors from avoiding income tax payment.

There has also been continuous effort on pension reforms to enhance its sustainability. The authorities agree that pension reform will be critical to longer-term fiscal sustainability in light of aging demographics and would help strengthen social safety net to close the savings-investment gap. The government is discussing the National Pension Fund (NPF) draft bill to make participation of private sector employees in pension schemes mandatory. At the same time, the government is conducting a study on the extension of retirement age from 60 to 63 years for government and state enterprise officials in order to prepare for potential labor-shortages from population aging in the medium-term. Meanwhile, productivity in the medium term will also be enhanced through the new investment particularly in the EEC projects, as well as the ongoing government training schemes to re-skill and up-skill the labor force.

The authorities are committed to fighting corruption. The new Public Procurement Act (2017) entailed major overhauls to create a more efficient and transparent procurement process. This includes a shift to an electronic platform (eProcurement) with features that permit increased public scrutiny through appeal and complaint mechanisms. Businesses are more aware of the process as reflected by significant increases in the number of appeal and complaints. In term of cost saving, in 2018, the public sector saved more than 7 percent of procurement budget in actual bidding price when compared to the budget allocation.

The private sector has long been a part of the fight against corruption in Thailand. In 2016, the Collective Action Coalition Against Corruption (CAC) launched an initiative to call on Thai firms to support and implement the government’s National Anti-Corruption Strategy. So far, 953 companies are signatory to this declaration, of which 397 have been certified.

Final Remarks

The Thai authorities would like to express their appreciation to the Fund for its long-standing support through policy dialogue and technical assistance to accelerate structural reforms and fortify macroeconomic and financial stability. The authorities look forward to future engagement and continued support from the Fund. They would like to also thank the Fund in facilitating the upcoming technical assistance mission on external sector statistics in November.

Mr. De Lannoy, Mr. Fanizza, Mr. Etkes, Ms. Quaglierini and Ms. Korinthios submitted the following joint statement:

We thank staff for the high-quality report and Ms. Mahasandana and Mr. Srisongkram for their helpful buff statement. We broadly share staff's recommendation for accommodative fiscal and monetary policies, because the country has policy space to deploy. Higher public investment could help to improve the country's long-term growth and reduce its external surplus.

We add a few comments for emphasis:

We agree that Thailand should use the available fiscal space to raise investment in support of potential output. We concur on the recommendation for additional 5-percentage points of GDP in public investment in macro-critical projects over the next three years, building on the improved public investment management capacities. Boosting public investment remains a priority considering its recent decline as percentage of GDP.

Concerning monetary policy, we support staff's recommendation of considering further easing, but we believe that the Central Bank should adopt a data dependent approach and pay attention to not fuel vulnerabilities in the financial sector. We note that staff and authorities do not agree on the need to strengthen monetary policy transmission (p.13). We would appreciate staff's comments on the sources for this difference in view. We also support staff on the importance of flexible exchange rates as defense against external shocks. Besides, we concur with the suggestion to encourage authorities to publish FXI data, but we believe that the authorities should do it gradually and with a lag, in a way that does not hamper the effectiveness of FX interventions. Could staff elaborate on the recommended frequency and granularity of the FXI data to be published?

Regarding financial stability, we appreciate the Financial System Stability Assessment's recommendations. Thailand's financial system seems to be well positioned to cope with most shocks. At the same time, the report highlights that pockets of vulnerability remain. On two points we are less persuaded. First, on revising the institutional set up of supervisory agencies, we see value in the continuity of the current model which has worked well so far and ensured proper coordination between the Central Bank and the Ministry of Finance. Second, on CFMs, we understand that the measures for non-residents baht accounts are targeted and aimed at short-term volatile capital flows.

We welcome Thailand's active FinTech policies. Indeed, harnessing new technologies for enhancing efficiency and inclusiveness of the financial services are key for inclusive growth. Moreover, we believe that FinTech should be evaluated together with cyber protection measures to make sure that the new services do not undermine financial stability.

On institution building, we congratulate the authorities for their efforts to strengthen the anticorruption framework during recent years. Particularly, we welcome the recent adoption of the Organic Act on Anti-Corruption, the improvements in the procurement law, and we encourage consistent implementation looking ahead.

Mr. Villar and Mr. Cartagena Guardado submitted the following statement:

We thank staff for the comprehensive report and Ms. Mahasandana and Mr. Srisongkram for their informative buff statement.

Thailand continues with a robust policy framework, good growth rates, low inflation, prudent fiscal management, strong external position and ample buffers to external headwinds. Going forward, the country faces challenges to address longer-term demographic changes and the sluggish domestic demand. We broadly agree with the Staff's assessment although we also understand the concerns raised by the authorities about some of the recommendations and we want to highlight the following points.

Sequencing and the adequate policy mix are important. Staff recommends a set of policies that include front loaded fiscal impulse, taking advantage of the fiscal space and maintaining growth, monetary policy easing to address external rebalancing, and exchange rate flexibility as defense against external shocks. We also notice that measures on fiscal stimulus and monetary easing are being executed since the previous Article IV, but the authorities have expressed caution regarding the impact on household debt and financial stability that could arise from further easing the monetary policy and from continued large capital inflows.

We concur with the authorities that the policies need to be calibrated based on the assessment of risks and the integrated policy framework that assimilates country experiences, complementarities and tradeoffs among the different economic policies. We share staff recommendations on continue addressing systemic risks and high household indebtedness through macroprudential tools, such as the recent tightening of the LTV ratio. However, we concur with the authorities that some of the vulnerabilities are beyond the BOT's regulatory reach and that efforts to strengthen the macroprudential toolkit may take time, including the time required to harmonize the regulatory framework for commercial banks and SFIs, and to guarantee the availability of comprehensive data about household debt, including from institutions that are not regulated by the BOT, like thrift and credit cooperatives (TCC) and credit unions (CUS). Capital inflows regulations may play an important role in the transition period and help mitigating exchange rate appreciation that may not be warranted by economic fundamentals. Can Staff elaborate on the sequencing and mix of recommended policies, and if the integrated policy framework may apply considering authorities' views?

FSAP finds a stable financial system. We welcome the strengthening of the financial system achieved by the authorities, reflected in the findings of the 2019 FSAP which did not identify major risks to the financial sector. We concur with the Staff that the country's financial system is well positioned to cope with most shocks and welcome the additional measures that will be adopted in line with the FSAP. The authorities consider that the current financial oversight architecture has worked well and that the representation of the Ministry of Finance does not compromise independence, while FSAP recommends otherwise. We concur with the authorities with regards to institutional arrangements that there is no one-size-fits-all and that the design of institutional arrangements must be considered within the country's context. History is very important in building institutions and local authorities may have a better feeling of what work well for their economy. Further staff comments regarding the current governance structure and recommendations to transform it will be welcomed.

Fragmentation and low coverage of the pension system remains a challenge. We concur with Staff that demographic changes will threaten fiscal sustainability in the medium term and that this will require measures of revenue mobilization to be considered, with the advantage that some of the current revenues, as VAT, are lower than in other neighboring countries. We welcome the joint efforts of IMF-Thai authorities to design the broader pension system reform strategy in forthcoming Fund TA and wish the National Pension Committee success in the formulation of the national strategy for the pension system.

We wish authorities success in the foreseen reform agenda that focuses on enhancing labor productivity and competitiveness, raising potential growth and improving inclusiveness.

Mr. de Villeroché, Mr. Rozan and Mr. Sode submitted the following statement:

We thank staff for the quality of their documents and Ms. Mahasandana and Mr. Srisongkram for their insightful buff statement. While we welcome Thailand's economic resilience, we broadly share staff assessment on the need for a more supportive macroeconomic policy stance. This would strengthen growth, help to bring inflation closer to target and reduce external imbalances. On the longer term, a ramp up of investment in human capital, technology and infrastructure will help to boost potential growth, competitiveness and inclusiveness. The challenge posed by ageing should be tackled in priority with growth enhancing measures and fiscal reforms to boost future public revenues. While we agree with the thrust of staff appraisal, we would like to make the following comment for emphasis:

We fully support staff's recommendation to implement a fiscal stimulus through a front-loaded increase in public investment. Given the existing fiscal space, the large current account gap and the low level of inflation, the case for a well calibrated fiscal expansion is strong. We also support staff call to improve public investment management notably by modernizing the procurement framework. Could staff comment the recent budgetary measures announced by the authorities and mentioned in the buff statement, elaborating on its economic impact and whether it answers staff call for further fiscal easing?

We thank staff for its annex on ageing which provides valuable estimates of future fiscal costs and identifies key weakness in terms of coverage of the current system. As a general principle, we disagree with the view that future ageing fiscal costs should be dealt with the building of excessively high fiscal buffer today. Such strategy can entail a macroeconomic cost through lower investment and growth that compounds over the years. This could lead to a form of dynamic inefficiency (as identified by Samuelson or Diamond in overlapping generation models) where current and future generations are worse off. Instead the government should invest in the future through infrastructure and human capital and provide a sufficient safety net to limit excessive private precautionary savings. While we encourage staff to further reflect on this trade off in future Article IV, we would be interested to have staff elaboration on the best strategy to deal with the fiscal cost of ageing?

Regarding monetary policy, we also fully support staff's recommendation to ease monetary policy until inflation sustainably return to its target. We also support staff' call for a complementary role of countercyclical macro-prudential policy. Such measures should be preferred to "leaning against the wind" stance that leads excessively restrictive monetary policy. On the financial sector, we commend the authorities for their strong oversight and we concur with the main recommendations of the FSSA, notably to improve the crisis management framework and to enhance the effectiveness AML/CFT framework. We thank staff for its annex on private debt burden and we found the recommendation to introduce a personal insolvency regime particularly relevant.

Thailand's current account surplus, while reduced compared to last year, is substantially higher than warranted by fundamentals confirming the need for more expansionary policy mix. Regarding staff analysis of the EBA, we are still skeptical regarding the various ad-hoc adjustments made to the model result and we would prefer that staff refrains from such adjustment aiming at lowering the CA gap. We are also very skeptical of additional adjustments to the CA norm to take into account ageing. Demographic variables are already included in the model and fully capture ageing effect. Could staff elaborate on the decomposition of the current account surplus by institutional sectors (government, households and firms)?

Regarding structural reforms, we support staff main recommendation on the need to increase physical and social infrastructures in order to strengthen potential growth. Given the low level of education attainment for a middle-income country, an ambitious strategy in this domain appears key. Strengthening the business and investment climate through continuous reforms will also help improve productivity. The low level of R&D spending warrants endeavors in this domain. We commend the authorities for the recent change in the anticorruption framework and we encourage them to step up reforms in this domain along the lines discussed by staff.

Mr. Ray and Mr. Shin submitted the following statement:

We thank staff for the comprehensive set of reports and Ms. Mahasandana and Mr. Srisongkram for their informative buff statement. Thailand's economy has maintained macroeconomic stability, underpinned by a robust policy framework, amid external headwinds. Risks remain tilted to the downside in both the short and the medium term. We broadly agree with the staff assessment and have the following comments for emphasis and clarification.

We see the merit in the judicious use of fiscal policy, with careful consideration of spending efficiency and long-term sustainability. An infrastructure push, if not managed and monitored properly, could erode successful delivery of large-scale projects like the EEC and create risks to fiscal sustainability. In this regard, we suggest that such a scale-up go in tandem with the country's absorptive capacity, closely following the lessons from PIMA. Looking further ahead, age-related spending needs and the risks of contingent liabilities from SOEs could add fiscal pressures. Could staff elaborate further on their judgement that there is "some" fiscal space in Thailand?

A cautious approach seems warranted in managing FX policy and liberalizing the capital account, given recent global liquidity conditions and the shallow Baht market. We have sympathy with the authorities' concerns that some emerging markets are exposed to the potential systemic risks arising from volatile capital flows and policy spillovers from major countries. As a small open economy with the experience of currency crisis, Thailand could provide an interesting case study for the ongoing work on the "Integrated Policy Framework". In that regard, the assessment on the recently introduced adjustment to the ceiling on non-residents Baht accounts would need to be made in such a holistic approach and considering the macroeconomic effects of the policy change. Staff's view would be welcome. Based on the lessons from the Integrated Policy Framework, we suggest staff provide more practical advice, taking fully into account country specific factors.

Further efforts need to be made to address remaining financial vulnerabilities envisaged by the recent FSAP. We welcome the staff's assessment that the banking sector is resilient to severe shocks, based on the stress tests and sensitivity analysis. The Specialized Financial Institutions (SFIs) and Thrift and Credit Cooperatives (TCCs) play an increasingly important role in providing credit to households. Under this circumstance, enhancing the macroprudential framework with broader coverage of financial institutions would be a key priority. On the institutional arrangements for supervisory agencies, we share the view that there is no ‘one size fits all’ and that it is important to consider the country’s context and experiences and to focus on the outcome – in this case the effective operational independence of the supervising agencies – rather than the form.

A comprehensive package of reforms to enhance labor productivity is needed to raise potential growth. We share staff’s view that investment in human capital across the regions would help unlock growth potential and more open immigrant policy need to be considered.

Mr. Beblawi and Ms. Abdelati submitted the following statement:

Thailand is to be commended for having built a robust policy framework that underpins its resilience to external adverse shifts. In particular, the recently enacted fiscal responsibility law adds to its tradition of prudent and judicious management of public finances. We equally commend the progress made in further strengthening financial supervision and macroprudential policies. In the context of ongoing trade tensions, the strong fundamentals have attracted strong capital flows, which complicate the management of macroeconomic policies. We thank Ms. Mahasandana and Mr, Srigongkram for their informative buff Statement. We share some of the staff’s recommendations, see merit in some of the authorities points of difference, and seek further clarifications in some instances.

Staff points to weak domestic demand, and in particular low investment compared to the three main regional peers, as well as weaker consumption growth as the debt overhang weighs on credit growth. Indeed, investment has not been consistently the highest among the four peers, and was among the two lowest during 2014-2017, which also coincides with a higher current account balance since 2014. One reason mentioned is that of outward investment to Asian countries, to take advantage of lower labor costs. We also see considerable outward investment to Europe and the Americas during the same period, which presumably is not related to lower wages. We would appreciate staff views on whether this is related to building of global value chains during that period. In general, we would like to see more staff analysis of the factors behind the trend of low productivity growth.

We broadly share the authorities’ and staff views on the merits of expansionary fiscal policy to maintain the growth momentum and appreciate staff’s chart on the fiscal space available to do so. This calls for timely implementation of front-loaded increases in public investment, including the macro-critical Eastern Economic Corridor projects. We also support the plan to further strengthen revenue mobilization in the medium-term to finance development programs and social protection needs. We would appreciate staff's comment on the adequacy of the social assistance program implemented over the last two years amounting to about 0.5 percent of GDP, and what share of the most vulnerable household are covered by some form of social assistance.

We share the authorities' view on maintaining their monetary policy which is data dependent and carefully calibrated based on an assessment of risks and policy actions. We also support the authorities' call for caution in interpreting the results of the external assessment. We agree that structural policies are key to address external imbalances, and that the exchange rate should not be overburdened with the adjustment. We also take note of the large unexplained residuals in the current account approach. We would welcome staff's clarification to the three points raised by the authorities, namely that more could be done to account for Thailand specific factors in the assessment model, such as population aging, and that it does not reflect the large real appreciation realized over the past few years.

We take note of the authorities' concern that the recent appreciation of the baht is a result of spillovers from monetary policies of AEs that could pose stability risks. Indeed, EM financial markets are dwarfed by the size of cross-border flows, and a fully flexible exchange rate could become a shock amplifier when faced with self-fulfilling expectations and herding behavior in the market. While welcoming the Fund's ongoing work on the Integrated Policy Framework, the authorities see it necessary to use targeted measures that directly address the sources of risks, rather than using the policy rate to respond to short-term challenges from capital flows. They have legitimate concerns regarding the potential impact of a low interest rate on financial stability, but we also see merit in staff's view that macroprudential policy tools should be used to address these. In this regard, further strengthening the macroprudential framework, as recommended by the FSAP team, would be important.

The FSAP assessment is reassuring overall as stress tests confirm that the system can withstand an adverse scenario similar to that of the Asian Crisis. We share the concerns staff raise with respect to the private sector debt overhang, where, at nearly 80 percent of GDP, household debt causes the stronger drag on growth than corporate debt in the medium term. We also support staff's analysis and recommendation for dealing with the debt overhang in a multipronged approach. Besides their cautious approach regarding using the policy rate to stimulate growth, how did the authorities react to the analysis and recommendations of Appendix VII, and which parts are likely to be pursued in the near term?

Ms. Pollard and Ms. Crane submitted the following statement:

We thank staff for the papers and Ms. Mahasandana and Mr. Srisongkram for the informative buff statement. As Thailand's growth has softened, it is all the more important for the authorities to undertake a package of macroeconomic and structural measures to boost domestic demand to support growth and address persistent external imbalances. We particularly welcome staff's use of an alternative scenario to demonstrate the benefits of stepped-up fiscal stimulus and monetary easing. We also appreciated appendix 3 on structural changes, inflation dynamics and macro imbalances, which provides insights on deflationary pressures and helps make the case for a strong policy package. In addition, while the financial system is broadly resilient, continued efforts are needed to address remaining pockets of vulnerability highlighted in the FSSA. We agree with the thrust of the staff appraisal and would like to highlight several points.

Supporting Domestic Demand. We urge the authorities to use available fiscal space to support domestic demand. We appreciate staff's concrete recommendations in this area, including a front-loaded boost in public investment, improvements in public investment management building on the recently-approved procurement law, and improved targeting of social assistance and training programs for low-income earners. We are encouraged by the authorities support for fiscal expansion and public investment projects. We take note of their intention to improve revenue administration, with a focus on a more efficient and growth-friendly tax system, to help finance longer-term social protection needs.

External Sector. We welcome that Thailand's large current account surplus has narrowed, while underscoring staff's assessment that Thailand's external position remains substantially stronger than warranted by medium-term fundamentals. We share staff's qualitative assessment and appreciate the detailed estimates for staff adjustments to the EBA CA gap but continue to question the adjustment for political uncertainty, noting political uncertainty is not unique to Thailand. Further we are confused by staff's assertion that population aging and a weak social safety net are Thailand-specific factors not accounted for in the EBA model. Could staff explain why the demographic variables in the model and the proxy variable for social spending do not capture Thailand specific factors?

Further efforts are needed to address Thailand's persistent external imbalances. We concur with staff's advice on allowing the exchange rate to play its role as a shock absorber, limiting intervention to smoothing disorderly market conditions. We underscore staff's advice to publish foreign exchange intervention data with an appropriate lag. We welcome staff's analysis of the tightening of a capital flow management measure related to limits on non-resident baht accounts and note staff's view that the measures are unlikely to have a material impact on net capital flows due to a still large current account surplus. We encourage the authorities to adopt a comprehensive package of macroeconomic, financial and structural policies which can be a more durable solution to dealing with capital flow volatility, as recommended by staff. We welcome Thailand's ongoing gradual liberalization of capital outflow regulations.

Financial Sector. We welcome the FSSA's findings of substantial improvements in financial sector supervisions and regulation since the 2008 FSSA. We agree with staff that high household indebtedness and weakness in some corporations and SMEs are vulnerabilities that merit attention. We encourage the authorities to focus on further steps to strengthen oversight frameworks for the growing non-bank sector and to address gaps in the crisis management framework. Finally, we take note of some difference of views regarding institutional arrangements related to financial stability oversight. Experience has shown that it is important to keep certain functions – e.g., monetary policy and institution-specific enforcement decisions – free from political influence. On the other hand, regulatory coordination can clearly benefit from political level policy oversight and direction. In this vein, we welcome the reference in the buff statement to the possibility of setting up a financial stability advisory body consisting of regulators of significant financial intermediaries.

Mr. Lopetegui and Mr. Morales submitted the following statement:

We thank staff for a well-written report and Ms. Mahasandana and Mr. Srisongkram for their informative buff statement. Thailand's economy remains resilient to external headwinds, thanks to appropriate and consistent macroeconomic policies, and ample buffers. The new government is in a good position to embark on a reform agenda that could support higher and more inclusive growth through investment in human capital across all country's regions.

Thailand's economy has slowed down, in part because of the impact of global trade tensions on Thai exports. Emerging market economies like

Thailand suffer the consequences of protracted disruption of international trade through its ramifications through global value chains. However, Thailand's GDP growth has remained below regional peers for most of the last decade and employment rates have steadily declined since 2012, which suggests that structural factors have also played a role in Thailand's sub-par growth performance. In fact, productivity growth has remained low in recent years, and high labor costs have eroded external competitiveness, leading Thai firms to increase investment in neighbor countries to take advantage of lower labor costs. The initiation of the Eastern Economic Corridor (EEC) project would be an opportunity to ramp up public investment and moderately loosen the fiscal stance to help reverse recent growth trends, especially since public debt is expected to stay well below the ceiling established in the Fiscal Responsibility Law over the medium term.

The new government has the opportunity to introduce a front-loaded fiscal impulse that would trigger higher and more inclusive growth. Higher public investment that may crowd in private sector participation would be a desirable initial strategy. However, staff acknowledges that there are many areas for improvement on public investment management, including simplifying procurement procedures and enhancing transparency in the land expropriation process. Moreover, although the new procurement law provides a good framework to avoid cost overruns and contain corruption risks, some operational aspects could still be improved. In light of this, some caution is warranted in designing the fiscal-impulse investment package, gradually implementing well-designed public investment projects with private sector buy-in as the public finance management framework improves.

Revenue mobilization requires the implementation of a medium-term revenue strategy that includes key revenue administration reforms. These should include revisions to the personal income tax code, and a new law to allow the access to all necessary bank information for a better tax administration. On the ongoing revenue-neutral changes in tax policy, could staff indicate if it would it be possible to include a higher VAT rate among the measures to be considered? We welcome the authorities' intention to introduce technical assistance recommendations to implement the medium-term revenue strategy. Looking forward, we encourage the authorities to consider a revision of the coverage of personal income, wealth, corporate income, and energy-related taxes to support the tax administration efforts.

Inflation continued declining up to August 2019, especially food and energy products. Low inflation, a large current account surplus, and decelerating credit growth suggest a negative output gap. Consistent with the inflation outlook, the central bank reduced its interest rate by 25 basis points last August but decided to keep the policy rate on hold in the most recent monetary policy committee meeting. We would be interested to hear staff's views on the latest central bank decision. We understand that technological factors and a low global inflation environment also contributed to headline inflation laying slightly below the lower bound of the inflation target range, as indicated by Ms. Mahasandana and Mr. Srisongkram in their statement. However, the persistence of a household debt overhang constrains borrowing, which in turn limits private consumption, which may justify further monetary easing down the road to bring inflation back to the central bank target, especially if downside risks materialize. In this regard, while we agree with the authorities that monetary policy decisions should continue being data dependent and focused on inflation expectations, we would encourage them to take a holistic view at the inflation outlook to inform their decisions.

Strong capital inflows triggered a significant appreciation of the baht, despite a decline in the external current account surplus. Consequently, the central bank stepped up its intervention in the foreign exchange market to contain exchange rate volatility and introduced a reduction in the limit of outstanding balance for non-resident baht accounts to curtail short-term speculative capital flows. Given that strong capital inflows have continued, it is not surprising that central bank forex intervention has been one-sided (purchases). Loose global financial conditions may continue to trigger massive capital inflows into Thailand and we share the authorities' concerns about the impact of rapid exchange rate movements on financial stability in small economies like Thailand, which are highly sensitive to capital flows. We note that the BOT has pursued a gradual and prudent liberalization of the capital account since 2007, relaxing major capital outflow regulations and introducing more flexibility to Thai companies to manage their foreign exchange risk exposures. For the medium term, we agree with staff that structural reforms to encourage investment accompanied by a policy mix supporting demand would lead to an orderly reduction of the current account surplus and gradual growth-driven currency appreciation. As global liquidity normalizes, the authorities should consider phasing out the new limits to non-resident baht accounts' balances.

Risks to financial stability remain low, but pockets of vulnerability should be addressed to better prepare the country for an eventual tightening of global financial conditions. Thailand's largest banks can withstand a shock comparable to the one experienced during the Asian crisis. The central bank has taken measures to contain risky borrowing, including by tightening the

LTV ratio for housing-related loans. However, as the FSSA highlights, the limited coverage of the macroprudential framework, which does not include a large share of non-bank institutions, remains a concern. Introducing a regulatory framework for financial cooperatives and specialized financial institutions comparable to the one in place for the banking system should remain a policy priority. In addition, we agree with staff that a multi-pronged approach is needed to address the private sector debt overhang that constrains private demand and productivity growth. Such an approach should introduce mechanisms to facilitate the deleveraging process and enhance the debt resolution framework.

Boosting labor productivity would be instrumental in raising potential growth. Investment in human capital across regions would help unlock growth potential and support inclusiveness. This would help reverse the moderation in real wage growth that resulted from low private sector employment growth in recent times. Labor market policies should aim at increasing labor force participation and attenuate the impact of aging on growth and poverty. In this regard, the pension system sustainability risks should be addressed while the authorities' plans to upgrade the system by expanding private sector coverage are implemented.

We look forward to the introduction of AML/CFT legislation to address deficiencies identified by the Asia Pacific Group in 2017. New legal provisions will allow for the expansion of coverage of the AML/CFT framework, improvements in the quality of suspicious transaction reports, and the identification of sources of wealth of politically exposed persons. These provisions would complement the progress achieved under the 2016 Collective Action Coalition Against Corruption, with participation of the private sector, and the 2018 Organic Act on anti-corruption.

With these remarks, we wish the authorities success in their policy endeavors.

Mr. Mozhin and Mr. Palei submitted the following statement:

We thank staff for a comprehensive Article IV report on Thailand as well as the FSSA. We also thank Ms. Mahasandana and Mr. Srisongkram for highlighting the remaining differences in views on several important policy issues. Overall, we welcome the ongoing consultations between the authorities and staff and support the continuing provision of technical assistance, including on possible improvements in the area of external sector statistics.

The Thai economy, like many others, has been affected by the ongoing crisis and continuing attacks on the WTO-centered rules-based international trade system. The slowdown in growth was largely driven by the decline in exports linked to the global production chains. We also note the continuing appreciation pressures on the baht, in part driven by the current account surplus and a surge in capital inflows. While it is difficult to disentangle the push and pull factors affecting capital flows to Thailand, we support the authorities' cautious approach to managing these flows. From this point of view, we welcome the introduction of macroprudential measures aimed at making the banking sector more resilient to the developments in the housing sector and households' debt. Given the shifts by the central banks in large advanced economies towards additional easing and the spillovers to international financial markets, ongoing accumulation of foreign exchange reserves by the central bank is also warranted. Similar to the Thai authorities, we continue to consider EBA estimates to offer only a rough range of possible equilibrium exchange rates, as it is the case for the vast majority of the IMF members.

Core and headline inflation rates remain below or close to the lower bound of the authorities' target. Last year staff argued for an additional reduction in the policy rate. While the authorities did reduce the policy rate somewhat, staff believe that an additional easing might be appropriate. We believe that staff offered compelling arguments in favor of such a course of actions, including the continuing fueling of trade conflicts and more uncertain outlook for global and regional growth. At the same time, we agree with the Thai authorities that monetary policy stance should be seen as part of a broader policy mix. The authorities intend to maintain accommodating fiscal policy this year, and the increase in infrastructure expenditures is already in the pipeline. On balance, we believe that the central bank should continue monitoring the evolving economic and financial environment and lean toward acting preemptively to ensure that inflation returns to the targeted range.

In the fiscal area, we note the authorities' continuing reforms to broaden the tax base and gradually increase tax revenues. The improvements in procurement procedures and, more broadly, in fiscal transparency will benefit the overall fiscal framework. We encourage the Thai authorities to focus on a more holistic approach to further strengthening governance and addressing the risks of corruption.

With these remarks, we wish the authorities success in facing challenges ahead.

Mr. Saraiva and Mr. Antunes submitted the following statement:

We thank staff for the comprehensive set of reports, including a detailed FSAP. We also thank Ms. Mahasandana and Mr. Srisongkram for the compelling and informative buff statement.

The cyclical slowdown amplified by global trade tensions has impacted Thailand's growth trajectory, but the outlook remains positive. GDP had been growing strongly until the first half of last year, progressively closing the output gap. External headwinds affected exports in 2019, bringing growth down to around 3 percent. Nevertheless, medium-term outlook continues to be positive, supported by investment levels around 25 percent of GDP. Taking into account that inflation is below the target, and given the existence of fiscal space, the ongoing monetary easing has been appropriate, and some fiscal impulse could be employed to boost domestic demand, in line with staff recommendation. Accordingly, we encourage the Thai government to remain vigilant in face of downside risks, in particular the escalation of global trade tensions, and take the adequate measures to sustain domestic demand should risks materialize.

The Bank of Thailand (BOT) recent decision to ease monetary policy was adequate, particularly considering subdued demand and persistently low inflation. The BOT is already using its tools to steer headline inflation back to the target range. We fully support the authorities' firm commitment to a data-dependent monetary policy, as well as the assessment that Emerging Markets may have a non-zero lower bound. We thank Ms. Mahasandana and Mr. Srisongkram for explaining the reasons that motivated recent FX interventions, and we are sensible to the fact that the sharp appreciation of the Thai baht may pose risks to macroeconomic stability. All things considered, flexible exchange rates should continue to provide a first line of defense against external shocks, and FX interventions should be limited to controlling disorderly market conditions. Could staff elaborate on alternatives to cope with the current challenges posed by capital inflow pressures on the Thai baht in light of the ongoing Integrated Policy Framework discussions?

Additional fiscal stimulus channeled to productivity enhancing investments may play a countercyclical role and increase potential growth over the medium term. With a public sector debt well below 45 percent of GDP, Thailand should explore existing fiscal space to implement strategic countercyclical policies with a view to smooth the downward phase of the economic cycle and boost potential output. Indeed, sluggish productivity growth and persisting regional and social inequalities are still major challenges that need to be addressed. We welcome the authorities' plans to upgrade infrastructure and modernize legal frameworks, aiming at integrating Thailand into high value-added GVCs and promoting the digital economy. We take note of staff's recommendation that any adjustments to the minimum wage should be underpinned by productivity growth, which may limit the policy options for improving income distribution and reducing regional inequalities. Does staff have additional suggestions to boost the competitiveness of the Thai economy, while reducing social and regional inequalities?

Thailand's financial sector is on a solid footing, but there is no room for complacency. The FSAP reveals no immediate vulnerabilities in the Thai financial sector. Major banks appear able to withstand severe shocks, and oversight is generally strong. Although staff insists that the operational independence of supervisory agencies can be strengthened, the authorities highlight that the current architecture is producing adequate results. We take note of the authorities' views that the presence of a representative of the Ministry of Finance in the composition of the Financial Institutions Policy Committee can bring benefits without compromising the operational independence of that agency. We agree that institutional arrangements should be assessed from a context-specific vantage point. Still, we encourage the authorities to carefully consider all FSAP recommendations, as well as to continue the close monitoring of the evolution of household debt, which remains at relatively high levels.

Going forward, strengthening democratic institutions and persisting on anti-corruption efforts will be key to consolidate Thailand's global position as a highly attractive emerging market. Permanent social accountability through solid democratic institutions is a fundamental feature of modern market economies. We encourage the Thai authorities to persist on their commitment to anti-corruption initiatives, and echo staff's view that the start of a new government provides an opportunity to push towards an ambitious policy agenda.

Mr. Inderbinen, Mr. Sigurgeirsson, Ms. Karjanlahti and Ms. Urbanowska submitted the following joint statement:

Thailand's economic fundamentals remain robust, with ample buffers to weather external headwinds. The economy has shown resilience, with comfortable levels of fiscal buffers and international reserves, as well as low unemployment. At the same time, we note the domestic and external imbalances associated with weak domestic demand, below-target inflation, and structural bottlenecks. We thank staff for their candid set of reports and Ms. Mahasandana and Mr. Srisongkram for their insightful buff statement. We offer the following specific comments for emphasis.

We concur with staff that risks to the outlook are tilted to the downside. External risks remain of particular significance. The cyclical global downturn and ongoing trade tensions are already weighing on Thailand's exports. In the near term, possible further trade actions could further disrupt global supply chains and depress investors' confidence. Moreover, a sharp rise in risk premia could cause higher debt service and refinancing costs. On the domestic front, further waning of domestic demand could translate into declining growth rates. Additionally, an increasing level of household debt acts as a drag on consumption. Against this background, the authorities' accommodative policy package and the continued implementation of structural reforms is welcome.

Thailand has a solid track record of fiscal discipline. We welcome the authorities' plans to increase spending on infrastructure, education, and digitalization of the economy, with the aim of lifting domestic demand and potential growth. However, we would encourage the authorities to balance these aims with preserving sufficient fiscal buffers in light of the notable downside risks. Furthermore, monitoring and implementation capacity of macro-critical projects should be strengthened to ensure efficiency of spending. In the medium- to long term, enhancing revenue mobilization will be necessary to finance the aging-related expenditure pressures and preserve fiscal sustainability.

The current monetary policy stance seems appropriate. We note staff's arguments in favor of further monetary easing. On the other hand, we see merit in the authorities' cautious approach toward further easing in view of financial stability concerns and limited monetary policy transmission. At the same time, we encourage the authorities to use macroprudential tools to address financial sector vulnerabilities. Also, we welcome the authorities' continued commitment to a flexible exchange rate regime and the progress in the capital account liberalization. Further deepening of capital markets and FX regulation reform will be important moving forward.

While the financial system is assessed to be resilient, we encourage efforts to further contain household indebtedness. Elevated household debt levels can act as a significant drag on consumption and growth. We commend the authorities on tightening macroprudential measures on household and commercial loans. Given the increasing share of non-bank borrowing, we support staff's advice on addressing the leakages of macroprudential measures and extending supervision, and we welcome the measures underway to this end. We note the differing views of staff and the authorities on the merits of establishing an FSC. Could staff elaborate on the statement in the buff that the current institutional set-up reflects country-specific experience in crisis management? More generally, we urge staff to refrain from providing off-the shelf advice on macroprudential institutional settings. This said, we agree on the need to strengthen the operational independence of supervisory agencies more broadly and address possible conflicts of interest.

The large unexplained residual in staff's assessment of Thailand's external position illustrates the need to further refine the EBA methodology. We welcome the focus on structural factors in Appendix IV. We note the authorities' expectation that the current account balance will narrow further over the medium term in the course of reform implementation. More generally, we underline that caution should be exercised when interpreting the EBA results to reflect country-specific factors.

We welcome the authorities commitment to structural reforms, which are key to boost domestic demand and support growth. A comprehensive package of macroeconomic, financial, and structural policies would boost competitiveness, create a healthy business climate, and contribute to the ongoing rebalancing process. We concur with staff that investment in human capital through expenditure on education and health, as well as equalizing opportunities is desirable. Moreover, addressing the large regional disparities and strengthening the social safety nets would be essential to enhance inclusiveness and increase potential growth. We also agree with staff that further efforts are needed to address governance and corruption vulnerabilities, and we welcome the measures detailed in the buff in this regard.

Mr. Sun and Ms. Lok submitted the following statement:

We thank staff for the insightful reports and Ms. Mahasandana and Mr. Srisongkram for the helpful buff statement. We take positive note of Thailand's sound policy framework and ample buffers that have contributed to the economy's resilience against external headwinds. Going forward, we encourage the authorities to maintain policy prudence and continue to tackle structural challenges to support sustainable and inclusive growth. We broadly agree with staff's appraisal and would like to offer the following comments for emphasis.

We take positive note of the authorities' expansionary fiscal stance, which will contribute to maintaining growth momentum. We appreciate the buff statement's update on the Cabinet's approval of the budget envelop for FY2020 and that fiscal spending and investment projects will be broadly on track. Going forward, to tackle longer term challenges including population aging while maintaining fiscal sustainability, we encourage the authorities to continue to exercise fiscal prudence and further improve revenue administration. We also see merit in broader tax policy reforms that can enhance the overall efficiency of the tax system and mobilize additional resources to bolster growth and resilience.

We welcome the Bank of Thailand's recent decision to cut the policy rate. Noting the authorities' view that further easing at this juncture may raise financial stability concerns, we believe that any further action should be proceeded carefully in a data-dependent manner, balancing among output, inflation, and financial stability objectives.

We support the authorities' continued commitment to exchange rate flexibility and recognize the role that foreign exchange intervention (FXI) has played in coping with disorderly market conditions. While we note the merits of greater transparency, we believe it is important for appropriate preconditions to be in place before FXI data can be published, so as to safeguard against unintended adverse effects on FX operations and market stability.

On capital flows, staff has recommended to phase out the reduction in the limit on nonresident baht accounts and replacing the measure with a comprehensive package of macroeconomic, financial, and structural policies. Calibrating an appropriate package of policies would take time, while volatile speculative capital flows can pose imminent threat to stability. We therefore see a reason for maintaining the measure to manage risks in the short run and encourage staff to continue to engage with the authorities in drawing up a policy package that can effectively address challenges associated with capital flows.

It is encouraging to note from the Financial System Stability Assessment that Thailand's financial vulnerabilities appear contained, and the banking sector is resilient to severe shocks. Building on the substantial upgrades to financial system oversight, the authorities should continue to strengthen and refine their regulatory, supervisory, and resolution frameworks. We also see merit in harmonizing the regulatory and supervisory framework for Specialized Financial Institutions (SFIs) and commercial banks. To this end, we welcome the authorities' ongoing efforts to enhance SFI regulations, crisis management and bank resolution, and the macroprudential toolkit. On staff's recommendation relating to institutional arrangement, we note from the buff statement that the current system was designed based on Thailand's experiences and circumstances, and wonder if there should be more recognition for the merits of the current arrangement, and whether there are any risks to shifting away from a system that seems to be working well so far. Staff's comments are welcome.

On the external sector, we take positive note that structural balancing efforts would continue to contribute to the narrowing of the CA gap. Considering the uncertainties and sizeable unexplained residual for Thailand, we continue to emphasize that care should be exercised when interpreting and communicating the results from the external balance assessment model.

With these remarks, we wish the authorities every success in their policy endeavors.

Mr. Merk and Mrs. Koh submitted the following statement:

We thank staff for its informative set of reports and Ms. Mahasandana and Mr. Srisongkram for their insightful buff statement.

As a small open economy, Thailand is particularly vulnerable to external pressures and volatile capital flows while being confronted with structural domestic challenges and an aging society. Against this background, prudent and judicious policies pursued by Thai authorities are bearing a large pay-off, particularly with regards to negative spillovers stemming from increased protectionism and geopolitical tensions. In addition, ambitious and well-targeted structural reforms are key to reduce private debt overhang and strengthen domestic demand, enhance labor productivity and support potential growth.

Moderate fiscal expansion should be well targeted at public investment projects with high multipliers that crowd in private investment and increase long-term productivity. We commend the authorities for their strong commitment and track record in safeguarding fiscal sustainability and encourage them to maintain their efforts. In light of the cyclical position, persistently low inflation and substantial public investment need, authorities could consider staff`s argument to use existing fiscal space for a relatively moderate fiscal expansion. However, keeping a close eye on the evolution of the public debt ratio in order to keep a comfortable distance to the 60 percent ceiling is warranted. We thereby echo staff’s call to implement past PIMA and capacity development recommendations that will enhance the effectiveness of infrastructure projects currently in the pipeline for the Eastern Economic Corridor (EEC).

In addition, we underscore the need to invest in human capital to enhance Thailand’s competitiveness and master challenges resulting from an increasingly digital economy. In our view, there seems to be space for reform and investment especially in primary and secondary education considering that Thailand lags competitors in educational attainment scores such as the PISA score by some margin.

Furthermore, we encourage the authorities to seek technical assistance on pension reform considering long-term unfunded liabilities, fragmentation of the system and weaknesses in degrees of coverage for some segments of the population. We see merit in the assertion that more liberal immigration policies might also play a role in addressing demographic challenges.

Monetary and exchange rate as well as macroprudential and related policies need to be conducted in a judicious and well-coordinated manner. We agree that further monetary easing could be beneficial in the context of low inflation and would help attenuate appreciation pressure. At the same time, we take note of the authorities’ concerns about attendant risks to financial stability. We fully agree that macroprudential policies should bear the main burden of ensuring financial stability and take positive note that the authorities have taken substantial measures to strengthen financial stability. We encourage authorities to continue with reforms that make the macroprudential policies (MPP) toolkit more effective. We look forward to discussing the staff’s ongoing work on the Integrated Policy Framework (IPF).

We fully agree with staff that exchange rate flexibility should be the first line of defense. We also take note that Thailand has prudent policy frameworks in place while facing uncertainties surrounding real exchange rate assessments. We are interested in staff`s view on strategies and instruments for small open economies facing situations of sharp and excessive appreciation pressures. In particular in the case at hand, are there arguments in favor of well-targeted capital flow management measures (CFMs) and possibly limited foreign exchange intervention, which are embedded in a well-communicated strategy of judicious macro-financial policies? Could staff please elaborate on its suggestion to “provide a robust and durable solution to attenuating volatile capital flows” and on a possible accompanying role to be played by the limited and temporary use of CFMs in this context?

With regard to high household debt, we encourage the authorities to implement both ex ante measures such as increased use of credit information systems and informal debt restructuring, as well as ex post measures such as bankruptcy repayment plans, and bankruptcy liquidation mechanisms as outlined by staff recommendations.

Last, we echo staff's call for addressing governance and corruption vulnerabilities, establishing a robust whistleblower protection framework and maintaining the ongoing efforts to address the AML/CFT deficiencies.

Mr. Kaya and Mr. Bayar submitted the following statement:

We thank staff for their comprehensive set of reports, and Ms. Mahasandana and Mr. Srisongkram for their insightful buff statement. Thailand has an impressive track record of sound macroeconomic policies which have underpinned the strong fundamentals and resilience of its economy. The strong buffers of the economy, epitomized by a very comfortable budget position as well as an external account which is firmly in surplus, provide the authorities with ample room to address structural challenges facing Thailand. However, we note that staff and the authorities differ rather substantially on the appropriate mix of policies, reflecting particularly the authorities' cautious approach which has delivered well so far. On that note, with some nuances, we agree with the thrust of the staff appraisal and would like to provide the following comments for emphasis.

A more accommodative fiscal stance could help buttress economic activity while at the same time help the transition to a more balanced growth model. We concur with staff that the most appropriate use of Thailand's fiscal room is through the scaling-up of productive investments, including in the Eastern Economic Corridor projects, while improving the efficiency and coverage of social assistance programs. We believe that the successful implementation of the macro-critical investment projects will go a long way in crowding in private investment and stimulating demand in the short run, while raising potential growth in the longer run. On staff's recommendation to increase the public capital outlays above the authorities' already ambitious investment plan, we wonder whether Thailand currently has sufficiently high-quality projects in the pipeline? We underscore the importance of complementing the accommodative policy steps with comprehensive fiscal structural reforms. In this regard, we welcome the authorities' ongoing efforts to reform the tax policy and administration, which should provide in the medium-term a durable basis to finance the development programs and social protection needs. We also support the emphasis on the sustainability of the pension system, which needs to adapt to the fast-changing demographic profile of the Thai society. It remains critical to improve the monitoring and reporting of the quasi-fiscal activities of state-owned enterprises to better manage contingent liabilities.

Monetary policy should continue to be guided by the price stability objective and remain data-dependent. In view of the subdued inflation outlook, the protracted weakness in demand conditions, and the renewed cycle of monetary expansion in advanced economies, we welcome the Bank of Thailand (BoT)'s decision to cut the policy rate by 25 bps in August. While we agree that macroprudential policies could be employed to address financial stability concerns, we believe that their role is complementary in nature and should be well-aligned with the direction of the macro policy mix. Therefore, going forward, we tend to associate ourselves with the authorities' more cautious view, and consider that further monetary easing should be gradual and strictly driven by data. We support the authorities' commitment to a flexible exchange rate regime, notwithstanding increasing appreciation pressures on baht. We concur with the authorities that the challenges stemming from the swings in global financial conditions require an integrated and comprehensive policy response on the side of the emerging market economies. We therefore remain skeptical about the efficacy of isolated policy measures, such as lowering the ceiling on the end-of-day outstanding balance of non-residents' baht accounts. We encourage the continued engagement between the authorities and staff on the appropriate policy mix vis-à-vis large and volatile capital flows. We support staff's recommendation to publish foreign exchange intervention data, and agree that further transparency in this regard would enhance the BoT's communication efforts and its commitment to the inflation target.

We welcome the FSAP's findings that the risks to the Thai financial system appear to be contained, although pockets of vulnerability remain. The Thai banking system is well-capitalized, highly profitable, and has a healthy asset structure. We take positive note of the results of the FSAP stress tests, and the sensitivity analysis on solvency and liquidity, which conclude that the domestic systemically important banks can withstand a very severe adverse shock akin to the Asian Crisis. Nonetheless, vulnerabilities could arise, particularly from the elevated household debt levels (i.e. 80 percent of the GDP). We therefore encourage the authorities to implement the recent FSAP recommendations with particular respect to the leakages in the BoT's macroprudential toolkit. On the architecture of the financial oversight, we concur with the authorities' view that the design should be best suited to country-specific circumstances. Specifically, we agree that the presence of a

Ministry of Finance representative on the Financial Institutions Policy Committee can help improve the inter-institutional coordination without undermining the operational independence of the monetary and supervisory authorities. We would be interested to learn if staff has heard different perspectives from the representatives of the supervisory agencies on this particular matter?

Finally, the political panorama in Thailand presents a window of opportunity to undertake a comprehensive reform agenda that should, inter alia, aim to enhance labor productivity, facilitate the shift toward digital economy, and improve inclusivity. The authorities' commendable commitment to fighting corruption should continue to register significant improvements to the overall business climate in Thailand.

Mr. Ronicle and Mr. Clark submitted the following statement:

We thank Staff for the clear set of papers, including the comprehensive Financial System Stability Assessment, and Ms. Mahasandana and Mr. Srisongkram for their comprehensive buff statement.

Whilst Thailand's policy framework and buffers continue to underpin resilience to emerging risks, the economy is likely to face continuing challenges both domestically and externally. Growth has decelerated, and the pronounced impact of the global economic slowdown, worsening trade tensions, and weak domestic credit growth is likely to weigh on short and medium term growth. We agree with staff that the start of a new government is an opportune time to tackle long-standing structural issues and address external imbalances.

We welcome the ongoing judicious management of the public finances and strong commitment to long-term financial stability, which should allow the authorities to use existing fiscal space to undertake productive infrastructure investment, and to expand the social assistance programs, focusing on broadening coverage for the most vulnerable. This will help spur domestic demand and foster more inclusive growth. Over the medium-term, the authorities should also focus efforts on greater revenue mobilization to address further development needs.

We agree that monetary easing may be appropriate given both domestic and global conditions; a monetary easing would help support domestic demand and external rebalancing in the short term. We welcome the authorities' commitment to pursuing a gradual and prudent liberalization of the capital account. We support staffs' recommendations that capital flow measures should be phased out if there are alternative macroeconomic, macroprudential or structural polices that could appropriately address underlying imbalance.

A concerted effort is needed to address underlying productivity challenges and boost medium-term growth prospects. This will also require a concerted investment in human capital and improving access to infrastructure and telecommunications in less developed regions. This should be underpinned by an overhaul of legal frameworks, which would allow the private sector to expand, and a strengthening of the anticorruption framework, with a focus on implementation.

We welcome the thrust of the FSAP 2019 recommendations, and we welcome the good progress on the previous FSAP recommendations, whilst also noting the reality of emerging risks and vulnerabilities. In this vein, we note the staff view that, while fintech does not present a financial stability risk at this time, an overall regulatory strategy should be articulated, given the use of digital financial services can rapidly change. On global regulatory principles, we particularly welcome the coverage of Basel core principles for effective banking supervision; the insurance core principles; the principles for financial market infrastructures; and the IOSCO objective and principles of securities regulation.

On the financial sector specifically, we welcome the progress made in creating a well-functioning macroprudential framework but note that further efforts are needed to clarify governance and accountability. Specifically, we welcome calls for the Financial Institutions Policy Committee (FIPC) to have a narrower membership; have a clear macroprudential mandate and to hold regular hearings with an appropriate legislative body. On crisis management and resolution, we support staffs' calls for improving the resolution decision-making process. We agree with staff that moving resolution decision-making from the FIPC to a body within the central bank will help ensure the central bank's operational independence, facilitate prompt decision making, and avoid dilution of institutional accountability.

We also note the expansion of non-bank financial institutions, although not identified as a concern in the FSAP, its rapid growth warrants close monitoring. With the expanding role of the government-owned SFIs and Thrift and Credit Cooperatives in providing credit to households, it will also be important to strengthen the regulatory and supervisory regime of these entities. We note that financial performance of these entities has been mixed and there are differences between the supervision and regulation of SFIs and TCCs and recommend greater alignment with those for commercial banks. The authorities should also continue to address AML/CFT deficiencies.

Mr. Tanaka, Mr. Chikada and Mr. Kuretani submitted the following statement:

We thank staff for the comprehensive reports and Ms. Mahasandana and Mr. Srisongkram for their informative statement. We commend the authorities for the robust policy framework which underpin the economy's resilience to external headwinds. In particular, we would like to underscore the Bank of Thailand's careful consideration and effort to preserve financial stability in light of the low interest environment and volatile capital flows. To further strengthen Thailand's resilience and improve its growth potential notwithstanding demographic challenges, we encourage the authorities to continue their efforts in domestic and external rebalancing and the structural reforms. We would like to offer the following points for emphasis.

Fiscal Policy

Thailand should use available fiscal space judiciously to spur domestic demand to counter external headwinds and also to address its high current account surplus. In this regard, we would appreciate staff's view on the efficacy and adequacy of fiscal stimulus package approved in August 2019.

Financial Sector Policy

We welcome the FSAP report concluded that financial vulnerabilities appear to be contained and that the banking sector is resilient to severe shocks. We take notes that the high household debt could further weigh upon private consumption and pose risks to growth. In addition, staff analysis that there are signs of weaknesses in some corporates and small-and medium enterprises (SMEs). In this regard, we concur with staff that data improvements, including on liquidity and SFIs, and the development of tools to assess concentration risk at an entity level would benefit risk analysis on financial vulnerabilities.

Monetary Policy, Exchange Rate Policy and Capital Flow

We concur with the authorities that due consideration is warranted for the further interest rate cuts in light of preserving financial stability. While staff recommends further monetary policy easing against the background of various factors including the recent escalation in U.S.-China trade tension, we share the authorities’ concern for further rate cuts based on financial stability angle as the Thai financial system has been in the low interest rate environment for long (similar to advanced economies and unlike other EM). In this regard, we appreciate if staff could elaborate on the difference of views regarding macroprudential policy between the authorities and staff. Also, we wonder the extent of efficacy of further rate cuts in stimulating the economy (given the low for long environment) and moreover it could slow the rebalancing of the economy and improving the current account imbalances. Staff’s views are welcome.

The authorities adopted the reduction in the limit on nonresident baht accounts (NRBS and NRBA) to help the economy navigate through the risk from volatile capital flows in the short run in July. However, views on the efficacy of the measure between staff and the authorities diverge completely. While the efficacy remains to be seen, it is also important to consider an exit strategy, that is when and how to unwind the measure and minimize backlash due to the unwinding. Staff’s views are welcome.

Structural Reforms

Against the background of Thai’s relatively low productivity growth and high wages in the region, Thai multinational firms have been increasing investment abroad, particularly in CLMV to take advantage of lower labor costs and access to global supply chains by combining their own developed infrastructure and industry clusters in Thailand. However, prolonged U.S.-China trade tensions could significantly change Asian supply chain and Thai’s role in the chain. We appreciate staff’s views on how the above factors could affect the CLMV strategies of Thai multinational firms.

While the profitability of small firms and their willingness to invest domestically have declined in the face of increasing global competition, the authorities endorsed a package of investment promoting measures, “Thailand plus”, in this September and aggressively commit to attract FDIs. However, increased domestic competition from foreign firms could put further stress on the domestic small firms and might have adverse effects. We appreciate staff’s comment regarding possible unintended consequence of “Thailand plus.”

We agree with staff, especially considering rapid aging of Thailand, that the pension system should be reformed to address old-age poverty risk, excessive precautionary savings, and pension system’s sustainability in longer-term. In addition, the demographic challenge from population aging would put strains on the healthcare (especially for the elderly). As such we would appreciate staff's further effort in analyzing the effects and implications of aging on fiscal sustainability and macroeconomy.

Ms. Levonian and Mr. Sylvester submitted the following statement:

We thank staff for the clear and balanced assessment of Thailand's economy and accompanying policy recommendations.

Thailand's economy continues to perform well on the back of a robust policy framework and ample buffers. However, the growth momentum is waning, and domestic and external headwinds are challenging the near-term growth prospects. Moreover, policies are needed to tackle longer-term challenges that are hampering a more robust, sustainable, and inclusive growth path. While we note some differences between staff and the authorities regarding the direction of policies going forward, we are encouraged by the authorities' commitment to sustain the growth momentum and to push ahead with structural reforms to ensure sustainable growth, as highlighted in the helpful buff of Ms. Mahasandana and Mr. Srisongkram. Against this backdrop, we offer the following comments.

We appreciate staff's analysis of Thailand's fiscal space and share their recommendation for its judicious use to support domestic demand, while ensuring fiscal sustainability. In this regard, we urge the authorities to focus fiscal policy on growth-friendly spending, including through investments in the Eastern Economic Corridor (EEC) initiative. We also urge the authorities to focus on domestic revenue mobilization to create further fiscal space for infrastructure and social spending and on reforms to further reinforce Thailand's rules-based fiscal framework, utilizing Fund's capacity development support.

Regarding monetary, exchange rate, and capital flow management policies, we note the huge divergence of views on the appropriate policies to support growth and external rebalancing. We would welcome staff's further elaboration on the disagreements, including whether any lessons could be drawn from the current work on the Integrated Policy Framework (IPF), which should take into consideration country specific circumstances.

We welcome the broadly positive findings of the FSAP, which confirms that Thailand's financial sector is sound and well supervised, although pockets of vulnerabilities remain, including risks associated with high household indebtedness. The authorities have made notable progress since the 2008 FSAP with the financial sector now well positioned to cope with most shocks. Also, the Bank of Thailand has improved its risk analysis and monitoring framework, which has led to a better identification of vulnerabilities. We note positively the authorities' general acceptance of many of the recommendations of the recent FSAP aimed at addressing these vulnerabilities and strengthening financial resilience. These include strengthening the macroprudential framework and policies, harmonizing the regulatory framework for commercial banks and Specialized Financial Institutions (SFIs), enhancing the crisis management framework, and further improving the AML/CFT regime with the support of Fund's technical assistance. However, we do not think staff has provided a convincing case for their recommendation to enhance accountability of supervisory agencies. We would encourage staff to focus their advice on what fits best for a particular country rather than on off-the-shelf "best practice," especially when recommending changes to a system that has served well. In light of the authorities' views regarding staff's recommendations on the current structure of financial oversight, could staff elaborate on their reasoning behind the suggested fixes to a system that appears to be working well?

A well-focused structural reform agenda will help address longer-term challenges, including a rapidly ageing population. As such, we encourage key reforms aimed at boosting long-term growth potential and supporting a more inclusive growth path. We agree with staff that such reforms should include advancing pension reform, boosting the efficiency of public investment and social safety nets, bolstering governance and anti-corruption frameworks, and increasing labor force participation.

Finally, staff's recommendation to address natural disasters and climate change risks seems inadequate. We note that one of the reasons for the weak domestic growth are weather shocks. Further, the risk of higher frequency and severity of natural disasters is assessed in the RAM as having potentially medium impact on growth. That said, staff's recommendations only include the strengthening of social safety nets of vulnerable populations to mitigate this risk. We would be interested in hearing staff's further comments on the authorities' plans to address natural disasters and climate change concerns.

Mr. Mojarrad and Mr. Badsi submitted the following statement:

We thank staff for the informative set of papers and Ms. Mahasandana and Mr. Srisongkram for their insightful buff statement. The Thai economy has been performing well despite heavy headwinds, thanks to its strong fundamentals, supported by a well-designed policy framework and abundant buffers. Going forward, against a background of low inflation and timid growth, the revival in domestic demand is key to a sustained and inclusive economic recovery. We commend the authorities for the strides made in improving the coverage and effectiveness of financial supervision and macroprudential policies. The risks to the outlook, which remain tilted to the downside, are mainly driven by the rising protectionism, intensification of geopolitical tensions and security risks, and sharply weakening global trade. We broadly concur with the thrust of the staff assessment and limit our comments to the following points.

We commend the authorities for their strong commitment to long term fiscal sustainability and encourage them to use their fiscal space judiciously to strengthen domestic demand and improve the effectiveness of social protection programs. Concomitantly, we are of the view that the proposed expansionary fiscal policy should go hand in hand with fiscal reforms while preserving the debt ceiling established in the fiscal responsibility law. In any event, we agree that the authorities should address the existing SOE reporting issues to guard against contingent liability risks and fiscal sustainability threats related to aging.

Based on the recent FSAP report, the banking system is sound and resilient to shocks although some pockets of vulnerability remain, including high household indebtedness and SME NPLs. We are pleased to note the shared views between the authorities and staff on the FSAP recommendations. While the current accommodative monetary policy stance seems appropriate, strong macroprudential tools are needed to preserve financial stability. We welcome the authorities' proactive response to risks associated with volatile short-term capital flows, as mentioned by Ms. Mahasandana and Mr. Srisongkram.

We commend the authorities for their commitment to exchange rate flexibility. We support their policy of gradual and prudent liberalization of the capital account and commend them for the steps taken to strengthen financial system stability, including through systemic risk analysis and monitoring.

In parallel with macro policy stimulus, targeted structural reforms are needed to unlock Thailand's full growth potential, and achieve sustained inclusive growth. In line with the staff recommendations, we call on the authorities to boost labor productivity; promote investment in human capital across regions; ease access to infrastructure and communication technology, particularly in the underdeveloped regions; and implement pension reform. We commend the authorities for their commitment to fight corruption and encourage them to step up efforts to address the remaining AML/CFT weaknesses.

We wish the authorities all the success.

Mr. Raghani, Mr. Nguema-Affane and Mr. Ondo Bile submitted the following statement:

We thank staff for the set of interesting reports and Ms. Mahasandana and Mr. Srisongkram for their informative buff statement.

Thailand's economy has remained somewhat resilient to adverse external developments, but policy mix should be geared toward supporting growth and addressing imbalances. Trade tensions and a sluggish global demand are taking a toll on Thailand's economy, as slowdown in exports is driving growth downward. Inflation remains persistently below the central bank target. The external position continues to be strong with higher international reserves. Looking forward, however, the Thai economy faces significant challenges including low productivity growth and elevated household debt. In addition, risks to the outlook are titled to the downside with notably protracted global trade disputes, slowdown in main trading partners and escalation of geopolitical tensions. Against this backdrop, we concur with staff that an economic stimulus through a greater use of policy space, coupled with structural reforms, is warranted to support economic activity and address bottlenecks to growth.

A fiscal stimulus is critical to support domestic demand over the medium-term while preserving long-term sustainability. We welcome the authorities' commitment to long-term fiscal sustainability and their agreement with staff's recommendations on increasing domestic revenue mobilization to meet expected increase in spending related to population aging and Public-Private Partnerships. The ongoing reforms of the pension system and social programs will also be critical to preserve longer term fiscal sustainability. In the meantime, the authorities should use their large fiscal space to increase public infrastructure, notably in the context of the Eastern Economic Corridor (EEC) projects. Nonetheless, further strengthening of public investment management will be needed to improve procurement process and cost control. Likewise, public financial management should be enhanced to increase the quality of spending and governance. In this regard, we encourage the Thai authorities to pursue the implementation of recent Fund TA recommendations in these areas.

Monetary policy stance is appropriately accommodative and should be maintained as needed to bring inflation closer to target. The recent monetary policy easing is appropriate given the protracted below-target inflation environment and the economic downturn unfolding in the country. The central bank's concerns about the potential impact of expanded easing on financial stability are understandable and we agree that further easing should be data-dependent. In addition, we tend to agree with the authorities on the need to carefully calibrate future policy stance, taking into account an accurate assessment of risks as well as the policy options as indicated in Ms. Mahasandana and Mr. Srisongkram's buff statement. As regard the exchange rate policy, we note the authorities' continued commitment to exchange rate flexibility. Speculative capital flows have been identified by the authorities as the cause for the rapid appreciation of the baht and the heightened exchange rate volatility. As a result, the authorities have resorted to foreign exchange interventions or tightening of existing capital financial management measure (CFM) to deter those flows. Staff's elaboration on the significance of speculative flows as source of financial stability risk in Thailand are welcome.

Addressing the remaining vulnerabilities in the financial sector will be essential to preserve its stability. We welcome the findings of the recent FSAP that financial stability risks in Thailand are contained and progress has been made in strengthening financial supervision and crisis management. We also find appropriate recent initiatives taken to tackle household indebtedness, including creation of a Debt Clinic, financial literacy programs, among others. Nonetheless, we encourage the authorities to implement the FSAP recommendations to address remaining financial vulnerabilities, notably with respect to consumer lending, and regulation and supervision on nonbank financial institutions. Further strengthening of the macro-prudential framework and policies would also help contain risks from search-for-yield behavior. In the same vein, work towards enhancing the AML/CFT framework should proceed, considering the findings of the evaluation of the Asia Pacific Group on Money Laundering as well as developments in the financial technology environment.

Enhancing labor productivity and resolving regional disparities will be critical to boost competitiveness, raise growth potential, and foster inclusiveness, consistent with the Thailand 4.0 strategy. Thailand is undergoing numerous structural changes, including weak wage dynamics and greater competition from foreign firms, which have led to a deterioration of the labor productivity and competitiveness of the economy. As Thailand seeks to move towards high value-added activities and a digital economy, there is a need for the authorities to press ahead with policies aimed at increasing labor productivity, including through investment in human capital, infrastructure and technology, while reducing social disparity. On governance, we welcome the strengthening of the anti-corruption framework with the adoption of the new anti-corruption law in 2018 and look forward to further progress in this area.

With these remarks, we wish the authorities every success in their future endeavors.

Ms. Mannathoko and Mr. Sitima-wina submitted the following statement:

We thank staff for an informative report and Ms. Mahasandana and Mr. Srisongkram for their insightful buff statement. We acknowledge that after several years of recovery, Thailand is now confronted with a cyclical slowdown as global trade tensions impact its exports, narrowing its current account surplus and curbing growth significantly. We commend the authorities for their robust policy framework and for adequate buffers that are able to contain the impacts from a deteriorating external environment. With growth in 2019 projected to decline sharply, we welcome measures taken to strengthen fiscal responsibility and improve financial stability; and in view of the available fiscal space, we support the expansionary fiscal stance recommended by staff. The rest of our comments are on monetary, exchange rate and financial sector policy proposals.

On monetary policy we note the recent accommodative measures taken by the authorities and believe that further decisions on easing should be guided by developments. We associate ourselves with the authorities' more cautious approach given the implications of the high level of household indebtedness and rising non-performing loans, for financial stability, and consider that further monetary easing should be gradual and strictly driven by data. Could staff elaborate on why they believe the transmission of recent policy measures is inadequate and needs further augmentation?

On exchange rate policy we note the authorities' commitment to a flexible exchange rate regime and support their view that this should, however, not translate into overburdening the exchange rate with the full adjustment envisaged. We note, in particular, that the authorities differ with staff on excessive exchange rate flexibility and agree with them that pursuing further appreciation despite the fact that the Thai currency has already appreciated significantly, driven by short-term (often speculative) capital inflows, is not advisable. We are concerned at the impact this has on export receipts - that are already in decline - and are more inclined to sympathize with the authorities’ desire to address the speculative flows directly. Could staff elaborate on their discussions with authorities on the appropriate response to large and volatile capital flows?

With respect to the FX market, we encourage staff to consider the level of financial market development in their recommendations on FX intervention data disclosure. We believe the best path when dealing with shallow markets, is a gradual and cautious approach to reforms; and we urge staff to support the authorities in this regard, to avoid unforeseen adverse outcomes. Could staff elaborate on work underway to develop Thai financial markets?

On the external sector assessment, concerns regarding the limitations of the EBA methodology are a recurring theme in Article IV discussions and we look forward to staff developing and using a revised methodology, as highlighted in the recent Risk Report. In this context, we share the authorities’ concern regarding the EBA assessment, given its well-known limitations and the fact that in this case, it fails to capture the implications of the large real currency appreciation in recent years, as well as other country specific circumstances.

On the financial sector assessment, we note that financial vulnerabilities appear to be contained and that the banking sector is resilient to severe shocks, and we commend the authorities on their strong regulatory regime. Regarding the issue of coordination between supervisory agencies, and the Ministry of Finance’s involvement; given that there is no objective evidence of lack of independence of the supervisory agencies, and current arrangements work well, we see merit in staff further consulting with the authorities to better understand the context for current arrangements, and jointly crafting any alternative framework that works well in practice.

With these few comments, we wish the authorities success in their endeavors.

The Acting Chair (Mr. Furusawa) made the following statement:

Thailand’s robust policy framework and buffers have underpinned its resilience to external headwinds. However, economic growth has slowed, and risks are tilted to the downside owing to the impact of the global economic slowdown, rising trade tensions, and weak domestic demand.

In their gray statements, Directors have emphasized the need for an expansionary policy mix to support domestic demand and structural reforms to address the macroeconomic imbalances and promote inclusive and sustainable growth. Directors have also noted the divergence of views between the authorities and staff on appropriate monetary policy, exchange rate policy, and capital flow management policies.

The staff representative from the Asia and Pacific Department (Mr. Leigh), in response to questions and comments from Executive Directors, made the following statement:[1]

I thank Ms. Mahasandana and the other Directors for their insightful commentaries on the report and the questions they have raised.

A number of Directors have raised questions related to the policy mix, the potential application of the Integrated Policy Framework (IPF) on Thailand, the elaboration on the case for capital flow easing, capital flow management issues, the assessment of fiscal space, and recent stimulus measures announced by the authorities. I would like to frame these issues in a bigger context.

As highlighted in the report, the Thailand authorities are facing multiple headwinds that are complicating macroeconomic management. One set of issues is the ongoing cyclical slowdown, which applies to a number of other countries, and weak global demand, as well as the capital flow volatility. The other set of challenges is more idiosyncratic, more country-specific. It is the longstanding macroeconomic imbalances, the low investment, high savings, and low productivity, and challenges associated with domestic demand driven in part by structural factors. The authorities are navigating these challenges as we speak.

These issues have also brought to the fore more prominently difficult policy tradeoffs for the authorities. One is inflation versus financial stability considerations, and the other related issue is the perennial debate in both academia and policymaking circles about the nexus between monetary policy and macroprudential measures. The third is whether to stimulate demand to address the external imbalances while at the same time preserving Thailand’s longstanding practice of judicious management of public finances.

[1] Prior to the Board meeting, SEC circulated the staff’s additional responses by email. For information, these are included in an annex to these minutes.

Those are the prominent policy tradeoffs that the authorities are facing. How do they see these policy tradeoffs? The authorities acknowledge that subdued inflation prevails, but they see limited risk of inflation expectations becoming de-anchored. Therefore, on balance, and in relative terms, financial stability issues loom large in their considerations, in their objective function, and more generally in their policy deliberations, although they take into account other factors as well.

On the staff side, given these multiple challenges, staff see the need for a comprehensive policy package that would address these multiple challenges aimed at boosting growth while promoting domestic and external rebalancing and enhancing inclusive growth. We have put together a policy package that focuses on taking advantage of the low interest rates, sluggish inflation, and weak domestic demand, to engineer a judicious fiscal expansion taking advantage of the existing fiscal space combined with fiscal reforms to mainly strengthen domestic demand.

Another pillar of the policy package is further monetary easing given the deterioration in both domestic and global economic conditions, while using macroprudential tools to preserve financial stability.

The third pillar is lifting potential growth through productivity enhancement measures and in a broad-based manner.

In terms of the policy mix, the policy assignments that staff has advocated in the consultation are in line with the Fund’s surveillance guidelines. Monetary policy ensures internal balance. Exchange rate l flexibility should address external balance. Macroprudential policies address the financial stability issues. Foreign exchange intervention is mainly geared toward avoiding disorderly conditions, and capital flow management measures (CFMs) are used sparingly and under very specific circumstances.

A few Directors have asked about the potential application of the ongoing work on the IPF for Thailand. The Fund’s current workstream on an IPF seeks to identify the best available policy mix that could help countries pursue growth and stability objectives, particularly in the face of rising spillovers and deepening macrofinancial and external linkages.

As this work is proceeding and progressing, it will be premature to speculate what this work might imply for a particular country such as Thailand. While the analytic work proceeds, our advice is guided by existing surveillance framework. We very much welcome the dialogue with the Thai authorities on these IPF issues, and I can also report that staff's ongoing work in these areas will be presented in the forthcoming joint Bank of Thailand-IMF high-level conference in Bangkok in early November.

Our hope is we can jointly leverage the ongoing work on the IPF and move the discussions forward in a manner that can address both the short-term challenges and the medium- to longer-term issues.

Turning to specific issues that have been raised on monetary and fiscal issues, a few Directors asked staff to elaborate on the rationale for the monetary easing. I would emphasize two main points here. One is the ongoing cyclical slowdown across all sectors of the economy, along with the weak global demand, global cyclical conditions, and the tepid existing fiscal support, a clear moderation of the financial cycle, and very subdued inflation dynamics. These are the factors that support our case for monetary easing. The authorities have raised financial stability concerns and in the past have argued that macroprudential policies may not always get through all the cracks, and thus address all the issues. In response, we have recommended, based on the work of the Financial Sector Assessment Program (FSAP) that the authorities address the current leakages in the macroprudential policy toolkit. This goes in two directions. One is to expand the set of macroprudential policy framework tools used in terms of the instrument space and the other dimension is to expand it to non-bank financial institutions that are not comprehensively covered. We believe that addressing these leakages will provide a stronger basis for macroprudential policies to contain systemic risk and provide monetary policy the necessary space to focus effectively on targeting inflation. Our understanding is that the authorities are open to considering some of these recommendations to address leakages.

The main difference on the monetary stance comes from our assessment of the risk to entrenched low inflation that can result from de-anchored long-term inflation expectations. The authorities see these risks as relatively limited, and they view the expectations as well anchored. In contrast, staff takes a more cautious approach. Our recommendation of strengthening the monetary policy transmission mechanism draws particular attention to effective communication that will help anchor long-term inflation expectations. Given persistently low inflation below or around the lower bound of the inflation target, staff sees the high risk of entrenched low inflation that will worsen the macroeconomic environment, increase real interest rates and the real debt burden.

Turning to fiscal issues, the assessment of the fiscal space and the recent measures that were announced by the authorities, staff's assessment is that there is some fiscal space. This assessment is based on the fact that with low interest rates, the Thailand government has comfortable market access to finance the budget deficit , and with low interest rates and the current cost of debt financing, public debt and growth financing path are well below vulnerability benchmarks, as well as the debt ceiling approved by the cabinet in the fiscal responsibility law. The proposed scaling up in investment is only temporary and would help sustain higher growth, thereby having limited impact on the debt in the long run.

On the recently announced fiscal stimulus package, our understanding is that the amount that has been announced is equivalent to about 1.2 percent of GDP in state bank loans and 0.6 percent in budgetary expenditure. At this point, it is difficult to tell how much of these resources constitute fresh stimulus, as the work on the FY2020 budget is still ongoing and is expected to be discussed in the National Assembly in January 2020.

The impact on aggregate demand will depend to a large extent on the proposal of fresh stimulus and how it is allocated and the associated multiplier effects. While the authorities in principle have embraced the concept of pushing the infrastructure push based on the Eastern Economic Corridor projects, the measures that have been announced recently focus mainly on current spending. Staff, on the other hand, focuses on the scaling up of public investment and thus on capital spending to address short-term needs, to add to domestic demand, the capital stock, and provide room to boost productivity and growth in the medium term.

On the social protection framework, the authorities have made remarkable progress in reducing poverty over the last three decades. The national poverty rate dropped from 67 percent in the mid-1980s to about 10 percent in 2015, while extreme poverty also declined sharply.

Our recommendation during the consultation leverages on the recent work that was done by the Fiscal Affairs Department (FAD) on strengthening the social protection framework in line with the ongoing emphasis in the Fund for strengthening capacity development and surveillance integration. The analysis that was done in that technical assistance (TA) report did not call for an increase in welfare spending. It basically focused on how to enhance the targeting of the welfare program. In other words, the focus was on efficiency considerations. Our understanding is that the authorities' current efforts to strengthen the welfare program go in this direction in terms of strengthening the targeting.

Finally, on issues related to the overall external position, staff is of the view that the strong external position should be interpreted as an opportunity to further understand what might be holding back investment in Thailand and what is inducing too much savings in the economy. This is why in this round of consultations, staff thought that it was necessary to do analytic work to gain a better understanding of the macro foundations of the macro imbalances. In that respect, we have looked at the factors affecting investment and the factors that potentially explain the high level of savings. One area is the private debt overhang that has been a drag on growth and investment, and firm-level data that we analyzed a few months ago also supports the fact that the high level of debt constrains both tangible and intangible investment.

With that backdrop, we thought that approaching the issues relating to the external position from a savings-investment balance perspective provides a deeper understanding of the factors contributing to the stronger external position. It is the staff's view that given the ongoing challenges on capital flow volatility, CFM issues needs to be looked at from this broader savings-investment balance and from the perspective of factors that are contributing to low investment and inducing higher savings investment in Thailand.

Mr. Alkhareif made the following statement:

When it comes to the Fund's advice to countries, our chair's longstanding position is that the Fund should focus on country-specific circumstances when delivering its advice, and in the case of Thailand, this is a very timely point. Ms. Levonian raised an important point that staff avoid using best practices to justify a one-size-fits-all approach, and we encourage staff to focus on providing tailored policy recommendations to countries, which will enhance the traction of policy recommendations.

Moving to the other policy areas, on the fiscal policy, we take positive note of today's remarks by the mission chief that the fiscal space is available, which can be used to enhance capital expenditure. We agree with Ms. Pollard and Ms. Crane on the need to utilize available fiscal space to support aggregate demand while ensuring fiscal sustainability. We encourage the authorities to continue their focus on improving public investment management, enhanced targeting of social assistance, reforming the pension reforms, and strengthening revenue administration. We also encourage the authorities to focus on improving fiscal transparency and procurement procedures, which will enhance the fiscal framework, as rightly mentioned by Mr. Mozhin.

With regard to the foreign exchange market, we note the authorities' commitment to the flexible exchange rate regime. At the same time, Ms. Mahasandana shared her authorities' concern that letting the exchange rate act as a shock absorber would risk disruption to the real economy. She also highlighted that the exchange rate can become a shock amplifier in an environment of excessive global liquidity. In this context, policy should avoid overburdening the exchange rate with the full adjustment in the real economy, as rightly highlighted by Ms. Mannathoko.

On the disclosure of foreign exchange intervention data, we agree with Mr. Sun and Ms. Mannathoko and others on the need to ensure that all preconditions should be in place before sharing foreign exchange intervention data. This is important to safeguard against an unintended adverse effect on the foreign exchange operations and market stability.

Finally, we welcome the authorities' commitment to structural reforms, which are key to boost domestic demand and support growth potential. We concur with staff that the investment in human capital through expenditure on education and health care, as well as ensuring access to opportunity for all, would be a priority. We also encourage the authorities to step up their efforts in advancing the Anti-Money Laundering and Combating the Financing of Terrorism (AML/CFT) framework, as rightly mentioned by Mr. Raghani. With these comments we wish the authorities continued success.

Mr. Tanaka made the following statement:

On fiscal policy, we commend Thailand's robust policy framework, which underpins the economy's resilience to external headwinds. At the same time, as the country continues to face domestic and external imbalances, we concur with the staff that the authorities should use available fiscal space judiciously to spur domestic demand to counter external headwinds and to address the high current account surplus.

On monetary policy, exchange rate policy, and capital flows, we could understand the authorities' view that due consideration is warranted for further interest rate cuts. In this regard, we could share the authorities' concern about a further rate cut from the perspective of financial stability, as Thailand's financial system has been in a low interest rate environment for a long time.

On the other hand, while the authorities adopted a reduction in the limit for the Non-Resident Baht Account for Securities (NRBS) and the Non-Resident Baht Account (NRBA), it is important to consider an exit strategy that will govern when and how to unwind the measure and minimize the backlash due to the unwinding.

Finally, on the structural reforms, considering the rapid aging of the population, we concur with the staff that the pension system should be reformed to address old-age poverty risk, excessive precautionary savings, and pension system sustainability in the longer-term. In this regard, we would appreciate staff's further effort in analyzing the effects and implications of aging on fiscal sustainability and the macroeconomy. We wish all the best for Thailand.

Mr. Villar made the following statement:

We broadly share the staff's assessment, but we also understand the concerns raised by the authorities about some of the recommendations, in the same line as Mr. Alkhareif's comments. Although we issued a gray statement, I would like to highlight a few messages.

We welcome the measures on fiscal stimulus and monetary easing that the authorities have been executing. However, we share the concerns expressed by the authorities regarding the impact on household debt and financial stability that could arise from further easing the monetary policy and from continued large capital inflows. We share staff's recommendations on addressing systemic risks and high household indebtedness through macroprudential tools such as tightening the loan-to-value (LTV) ratios. However, the authorities note that some of the vulnerabilities are beyond the Bank of Thailand's regulatory reach and that efforts to strengthen the macroprudential toolkit may take time, including the time required to harmonize the regulatory framework for banks and other institutions, as the staff recommends, and to guarantee the availability of comprehensive data about household debt to manage properly the LTV ratios. In this context, capital inflow regulations may play an important role, and we feel that the staff's insistence on continued liberalization of the capital account may not consistent with the Fund's Institutional View on capital flows.

We also concur with the authorities with regard to the financial oversight architecture. We do not see a strong enough argument from staff to exclude the Ministry of Finance in the specific case of Thailand. This is a case in which local authorities may have a better feeling of what works well for their economy.

Finally, we would like to congratulate Thailand's economic authorities for their achievements and wish them continued success.

Mr. Saraiva made the following statement:

I want to touch on two issues, and the first one is that we agree that staff made a good case, and the Thai authorities should consider exploring the use of existing fiscal space. Fiscal space always has to be used wisely. When you provide the countercyclical stimulus, you should also do it in a way that promotes productivity, enhances welfare, and addresses distributional issues as well. It seems to be clear that the output gap is closing, but on the other hand, we see indicators such as inflation and the current account that suggest there is still a gap to be filled. Moreover, the Thai economy, which is well integrated in global value chains, even with all the buffers and its resilience, is still sensitive to external shocks and to deterioration in global trade and global growth. We therefore suggest that the Thai authorities should consider the possibility of exploring the use of existing fiscal space and do it in a way that also promotes and enhances potential growth.

The second issue regards perhaps the most consequential debate that arose in this discussion. We see diverse views in the staff report, the buff statement, the gray statements, about the foreign exchange intervention and the external sector assessment. I want to echo what Mr. Alkhareif and Mr. Villar have said. This is a clear case in which the Fund has something to learn from the dialogue with the Thai authorities. The strength of the Fund's analysis and the persuasiveness of its policy advice is derived from strong, robust, well-grounded economics, but also from the richness of the vast experience of the membership. Surveillance should always be a two-way process in which the Fund also learns from the country experience. Ms. Mahasandana and colleagues were very compelling in explaining the reasons that motivated recent foreign exchange interventions in Thailand, pointing to the fact that the sharp appreciation of the Thai baht may pose risks to macroeconomic stability. We agree that flexible exchange rates should continue to provide the first line of defense against external shocks, but policymakers do not take decisions in a static textbook environment, so they are far better placed to understand the constraints that they are facing. We expect that the ongoing discussion surrounding the IPF will reflect this enhanced understanding and leave enough policy space for local authorities.

Ms. Mannathoko made the following statement:

We have already issued a gray statement in which we supported the emphasis on judicious fiscal expansion and structural reforms that are needed to safeguard long-term growth and to enhance the economy's capacity to manage the large fiscal impacts that will come in the future with an aging population. Given the magnitude of these upcoming demands from the aging population, as well as Thailand's sizeable vulnerability to external risks, we understand the authorities' need to resuscitate growth and build adequate buffers to be able to manage future fiscal demands and risks. With regard to aging, like Mr. Tanaka, we want to encourage more work on strengthening the pension system. As the old-age-dependency ratio raises, we wonder if more work on capital market development could help channel more savings toward boosting domestic investment and domestic demand.

We also wanted to associate ourselves with the comments from Mr. Alkhareif, especially on the importance of a country-specific focus and ensuring that during the liberalization process, preconditions are in place prior to taking measures, such as full transparency, because things get tricky during the process of liberalization.

I have a comment on the various points of difference between the authorities and staff. We note that staff also point out that policy choices always have tradeoffs, and the Board in the past has recommended often that staff try to present authorities with different policy options and their respective implications so that the authorities are better equipped to weigh the options put before them. We would encourage staff to consider taking this approach in their engagement with the Thai authorities.

On the topic of foreign exchange regulations, the reform program and the ongoing liberalization of the capital account, we do believe the authorities' cautious approach to managing this transition is understandable given the current instability in external markets and past ASEAN experience during the Asian financial crisis. Managing transitions can be tricky. It is important, for example, to try to foresee and manage market imperfections during liberalization. You want to avoid sudden, harsh, and disruptive events.

On monetary policy and the weak domestic demand, our understanding is that there are also some structural issues at play influencing inflation that may not be resolved by a more accommodative monetary stance, so we wanted to encourage staff to explore this further with the authorities. Other than that, we wish the authorities success going forward.

Mr. Rozan made the following statement:

First, the staff's report demonstrates that Thailand should implement a more expansionary policy mix, as others have said this morning. With slowing growth, low inflation, and high current account surplus, the economy is performing under its growth potential, and given the existing fiscal space and monetary policy room for maneuver, the case for an expansionary policy mix is strong. By being overly conservative, the policy mix is hampering both short-term and long-term growth potential at the cost of current and future Thai generations.

Second, as for other economies with a high current account surplus and with fiscal space, we are concerned by the argument that fiscal space cannot be used because of the future cost of aging. Excessive current account surpluses have negative spillovers across the world, and moreover, as recommended by staff, the costs of aging would be better addressed by a strategy that improves growth potential and limits future spending related to aging, and increases public revenues in the medium term.

Third, we reiterate our call for an evenhanded use of the External Balance Assessment (EBA) model. The assessment of the external position and exchange rate is a key mandate of the Fund, and it is important that this assessment remain informed by a multilaterally consistent model-based framework. In particular, we encourage staff to refrain from ad hoc adjustment when presenting the model results. Let me also mention that aging is already taken into account in the model, and it would not be coherent to make additional adjustments.

Fourth, we are generally very supportive of the financial sector assessment that has been made and the resulting recommendation, but I do have some sympathy for Mr. Villar's remarks on the supervisory arrangement and the possibility of the Finance Ministry having some involvement in the process regarding supervisory arrangements.

Mr. Morales made the following statement:

We reiterate our recommendation to the authorities for appropriate and consistent macroeconomic policies, and we agree with Ms. Mannathoko and Mr. Saraiva that the case made by the authorities regarding the need to limit speculative capital inflows is a strong one that should be taken into account by staff.

We want to emphasize the importance of moving to higher growth and higher inclusiveness. The staff report shows that public and private investment have been picking up in recent times; however, it is still puzzling that Thailand’s GDP and productivity growth has remained below that of regional peers for some time now. As we indicate in our gray statement, we hope the new government takes this as an opportunity to introduce a frontloaded fiscal impulse to accelerate growth and make it more inclusive. We want to also stress our message that higher public investment that may crowd in private sector participation would be a desirable initial strategy, with the caveat that steady efforts to strengthen the public financial management (PFM) framework should need to be redoubled to avoid mismanagement risks.

Staff estimates the value of infrastructure projects in Thailand at about US$50 billion, 10 percent of Thailand’s 2018 GDP. We believe that this shows that the prospects for an effective fiscal stimulus are quite positive and significant. In this regard, the recently announced fiscal stimulus package sought by the authorities seems in principle a good initial step in the right direction, although it is still unclear how much of the resources constitute fresh stimulus rather than the re-allocation of spending items. We also believe the staff’s case for a temporary scale-up of public investment would strengthen demand in the short-term and growth and productivity in the medium and long term and has great merit given existing fiscal space. With these remarks, we wish the authorities success in their policy endeavors.

Mr. Jost made the following statement:

We agree there should be a judicious use of public finances to spur investment and to raise potential output, in particular to invest in human capital and social protection. At the same time, when I look at the Risk Assessment Matrix on page 39, it lists around eight external risks, and five of them are classified as being highly likely. As others have pointed out, the Thai economy is very much integrated, and so these are external risks where the authorities have very little leeway to deal with them, except for having buffers in place. In that sense, while public finances should be used to improve potential output, I believe there is also a case to be made to do so in a sensitive manner. As Mr. Leigh pointed out, there is some room before the debt becomes vulnerable, so that is a threshold that we should look at more carefully. I do not think the authorities should always be on the road to the vulnerable level.

Ms. Pollard made the following statement:

Let me begin by thanking Ms. Mahasandana, not so much for the buff statement, which is excellent, but for presenting us with such a fascinating economy to study, which presents so many of the issues that economists and policymakers are grappling with, and so I find this to be a fascinating case. It must be an interesting country to work on, and I very much appreciate Mr. Leigh's answers to the technical questions and his comments this morning, and I think the divergence of views expressed here today just point out the interesting issues that we are all grappling with. As an economist, I find this fascinating, and I am interested in looking back 10, 15 years from now as to how this will all turn out.

With that, I want to focus on a few points. The first is on the domestic demand issue, and we would underscore the strong case that staff has made for the multipronged approach to address weak domestic demand, and the comments of Mr. Saraiva were excellent on the use of fiscal space.

We welcome staff's use of an alternative scenario to demonstrate the benefits of stepped-up fiscal stimulus and monetary easing, and we encourage the authorities to proceed with a frontloaded boost in public investment, accompanied by improvements in public investment management, and improved targeting of social assistance and training programs for low earners.

Turning to the issue of CFMs, the idea that was raised this morning about looking at the saving/investment balance perspective and capital flows in the external sector is really the right focus and an interesting way to think about looking at economies in the future, and the answers to questions 19-22 on CFMs in the written responses to technical questions were also incredibly helpful. We welcome that staff is engaging constructively with the authorities to provide advice on how to durably address capital flow volatility through a combination of macroeconomic, structural, and financial policies. While temporary and targeted CFMs can play a role in certain circumstances, we underscore staff's focus on the role of weak domestic demand and the need for a broader policy response rather than relying simply on the tightening of CFMs. This is another issue where we need to recognize that capital flow volatility is an issue for countries and then figure out the best way holistically to address that.

On the issue of foreign exchange intervention, staff's answers were very helpful, and although staff's advice in this area has not gained traction, their points are very well taken and would underscore in particular that the authorities' approach to foreign exchange intervention without an announcement is a communication choice in itself, increasing the chance of market participants misinterpreting the signal. I cannot help but to think about 20, 30 years ago, where we were having these conversations not around foreign exchange intervention but about monetary policy announcements in general and the issue of whether the central bank should announce its policy decisions and how this would destabilize markets, and that you needed to have preconditions. The experience of that has led us to believe that the idea of markets overreacting was not as much as we had feared. I also think the experience of other emerging markets who have gone to announce foreign exchange intervention is very helpful and think that studies of those could be helpful for countries like Thailand.

Finally, I just want to echo Mr. Rozan's comments on the EBA.

Mr. Inderbinen made the following statement:

We note the resilience of Thailand's economy but also the downside risks against the background of weak domestic demand and increased external stability. Against this background, we welcome the authorities' plans to increase spending, but we encourage them to balance this with the need to preserve fiscal buffers under the current circumstances. Similarly, we see much merit in the Bank of Thailand's cautious monetary policy stance given the prevailing financial stability risks.

We note staff's assessment of Thailand's external position, and we appreciate the detailed account of structural factors in the write-up in the appendix. We also note the large unexplained residual, and we reiterate as a general point that caution is required when linking unexplained current account gaps to policy distortions. In general terms, we believe that more emphasis needs to be placed on exchange rate models rather than relying primarily on current account assessments.

Finally, as we note in our common gray statement, Thailand's case does underline the need to further refine the EBA methodology, including to better capture the link between demographics and the external position. We thank staff for the Financial Sector Stability Assessment (FSSA), and we are encouraged by the broad agreement of the authorities on the recommendations, including on strengthening oversight of the special financial institutions and the need to define the regulatory regime for the credit cooperatives, both of which have gained importance in the financial system. But like Mr. De Lannoy and his colleagues, Mr. Villar and Mr. Ray and others, we did note the differences between staff and the authorities on the institutional setup for macroprudential oversight, and we thank staff for the written answer that they provided to our question on this.

We fully agree that safeguarding the independence of the supervisory authorities is essential, but we remain to be convinced of the merits of recommending changes to the current arrangement for financial stability oversight in the case of Thailand.

Staff essentially present a blueprint derived from what they perceive as international best practice on this, but this may not necessarily work as well in practice compared to the abstract. We note from the buff statement that the current setup has proven to be effective in past crisis situations, which is the true litmus test of institutional setup.

We would also note that the assessment of the Basel Principle II on independence and accountability of the supervisors does, “not observe any objective evidence of lack of independence of the Bank of Thailand,” so it is a relatively sound assessment in this regard, although we do not have the grading. We would believe the underlying issue is likely the public ownership of some of the non-bank institutions, and the staff’s focus on this in the policy recommendations is not essential to making the institutional setup even nicer than it is at the moment.

Mr. Ray made the following statement:

I would like to begin by thanking staff for an excellent set of comments this morning, including this emphasis on the saving/investment balance, which is the right way to think about these things.

We issued a gray statement. I just wanted to pick up on a few issues that raise broader matters for us to think about, and I would start by echoing what Mr. Inderbinen has just said about the FSSA. I thought he set it out very well. This is an issue that has come up in Financial Sector Assessment Programs (FSAPs) as well. These exercises are extremely resource-intensive, both for the Fund but also for the authorities, and it strikes me that applying some rather simple, one-size-fits-all methodologies is not very helpful. If we are going to devote a lot of our resources and authorities’ resources around things like the institutional arrangements for regulators, then we need to make them useful, and we should also focus on the outcome rather than the input.

My second observation is that Mr. Leigh really put his finger on the issue with Thailand when he said that financial stability considerations loom large in the authorities' objective function. That is not a surprise given the history, and it has been the case now for more than 20 years. The authorities are making policy choices which involve some costs as well as some benefits, and it would be helpful to help the authorities think their way through those decisions in a way that we would generally agree would be less costly for Thailand's policy framework and mix.

On fiscal space, this chair has raised concerns before about trying to fine-tune this too much. My personal experience is that once you tell policymakers to spend more, it is hard to tell them to stop spending more. Therefore, when it comes to this idea that you raise spending in a very short term and then you wind it back again, do not assume it will be wound back because that is just not the way policymakers think. That said, there are many no regrets things that staff are recommending around investing in human capital but also in physical infrastructure investment. In that regard, what matters is the institutional arrangements to achieve efficient spending, and staff might think about that in the future.

Lastly, on pension reform, this is a politically very challenging area, and this is actually about choices, and this is an issue where governments are making choices for future generations, not themselves. These are reforms that have very long-term payoffs. It might be helpful if staff thought about how to draw on other countries' experience when providing advice to authorities in this area and to set out the framework for how you think about lifting the pension age now, lifting saving now—which is effectively forcing a tax—or whether it is about future taxes. Those things are difficult for any authorities to think through, and it would be helpful to frame it a bit like that.

Mr. Sigurgeirsson made the following statement:

First, as Mr. Ray and others here have expressed, we sympathize with the pressures that small open economies sometimes face in an environment of large volatile capital flows. This is eerily familiar to me. As Mr. Ray indicated, financial crises do cast a long shadow and influence policymaking for many years. We take the divide between the authorities and staff on the appropriate policy mix as a case in point for the need to deepen the Fund's advice on the appropriate response to pressures arising from the accommodative environment. It showcases the importance of having a more integrated policy framework, which hopefully can provide more countries specific advice. Overall, we are encouraged by the authorities' commitment to a flexible exchange rate and gradual opening of the capital account. I would also like to highlight the importance of implementing the structural and prudential policies as advised by staff to address imbalances and vulnerabilities. On a point raised by Ms. Pollard, I fully agree that enhanced transparency in monetary policy decisions over the years has proven very useful for policy transmission, and the same should apply for foreign exchange interventions.

Secondly, on crisis management, as Mr. Ronicle mentioned in his gray statement, we see merit in simplifying the decision-making process for crisis resolution, both on approving resolution frameworks and emergency liquidity assistance provision. From my personal experience, I have learned that complex decision-making processes constrained our abilities to respond swiftly and effectively, and I guess there is some merit in what is said about problems associated with too many cooks in the kitchen.

Finally, since this chair has been often mentioning capacity development in the recent past, we are very encouraged and pleased to hear of the integration of capacity development work into the Article IV analysis and policy advice. Thank you, Chair.

Mr. Kaya made the following statement:

We issued a gray statement and therefore I want to limit my remarks to three points.

First, as a general note, Thailand has one of the most stable economies in the emerging market sphere with very strong fundamentals. The growth is resilient. Inflation is low, which we believe could be gradually steered toward the authorities' target. The fiscal position is comfortable, and external account is firmly in surplus. The recent FSAP also confirmed that the financial sector is broadly sound, and risks appear to be contained. Overall, this is a very healthy picture, and we would like to commend the authorities for their prudent policies.

Second, on the monetary policy, we believe that future decisions on the policy rate should be guided by the price stability objective and be driven by incoming data. Nonetheless, we agree that Thailand as an emerging market economy has a non-zero lower bound, and thus the room for further policy rate cuts is fairly limited. We also see the complexities against which the authorities have to design their policies, stemming particularly from the renewed cycle of monetary easing in the major central banks. Such rapid shifts in the external environment pose significant policy challenges for the emerging market economies, and the appropriate response requires a mix of internally consistent policies comprising different tools and levels. Like the Thai authorities, we have high expectations from the IPF.

Finally, we are pleased to note the FSAP's findings that the risks to the Thai financial system appear to be contained. Nonetheless, like in other countries, challenges exist, and the authorities should continue to improve their macroprudential toolkit, including to address possible risks related to high household debt.

On the architecture of the financial oversight, we believe the authorities have set up a well-functioning architecture which appropriately fosters interagency coordination and is able to effectively manage risks. This structure reflects Thailand's own experience and peculiarities, and therefore, we respect the authorities' position on this issue. In the absence of strong objective evidence, we believe staff should refrain from putting in place strong policy recommendations especially in favor of amending an already well-functioning framework. With these remarks, we wish the authorities all the success in their endeavors.

Ms. McKiernan made the following statement:

First, on the FSSA, I would like to echo the point made by many other Directors, including Mr. Alkhareif, Mr. Villar, and Mr. Rozan, Mr. Inderbinen, Mr. Ray, and Mr. Kaya. We also felt that the response to our question regarding the institutional setup of the supervisory agencies and macroprudential oversight did not fully answer the question as to why a change was necessary. The existing system was acknowledged as well-functioning, and so we would have appreciated further information on that.

Second, we did feel that the response by staff to our disaster risk-related question was very helpful. This chair is always aiming to ensure that staff adequately consider and address these risks and propose strategies to mitigate them when they are macrocritical.

Lastly, we echo Mr. Sigurgeirsson's remark in welcoming the helpful integration of capacity development into this report.

Mr. Sun made the following statement:

First, I agree with Mr. Alkhareif on his point on country-specific advice. This is not easy to do, but it is very important for effective policy advice.

Second, like Mr. Ray, Mr. Sigurgeirsson, and others, we feel that emerging markets and developing countries, especially small states, small open economies like Thailand, are often facing daunting challenges arising from global financial conditions and capital flows. We believe the Fund's ongoing work on the IPF has the potential to assist the authorities in tackling those challenges, and we look forward to further progress by staff.

Third, to boost productivity and promote sustainable and inclusive growth in the long run, the Thai economy would benefit from further structural reforms as well as investment in human capital and infrastructure development. This requires a comprehensive set of fiscal and structural policies, as many Directors emphasized, to ensure that resources are spent efficiently to generate the most growth impact.

Finally, on foreign exchange data publication, we encourage greater transparency, but in order to do that effectively, the way it is done matters. We therefore encourage the authorities to enhance financial markets' width and depth to further develop financial infrastructure. During this process, we also encourage staff to closely work with the authorities to put in place those preconditions. With these remarks, we wish the authorities continued success.

Ms. Abdelati made the following statement:

I would like to join others in thanking staff for the Article IV report, the FSSA report, the written responses, and the verbal remarks at the beginning of today's meeting. It has been quite a rich discussion, as Ms. Pollard mentioned, and I have enjoyed listening to the views around the table.

Many commented on the divergence of views on a number of issues, and this seems to call into question the definitiveness of staff's views. Ms. Mannathoko in particular asked about looking at tradeoffs and providing options or alternative views and not just one view. In light of the discussion today, I just wonder if there is scope to modify the first sentence in the Main Themes in Grays, which always says grays broadly agreed with the thrust of the staff appraisal and should say something like grays mostly agreed with the thrust of the staff appraisal.

The staff representative from the Monetary and Capital Markets Department (Mr. Lopez Mejia), in response to further questions and comments from Executive Directors, made the following additional statement:

> I would like to elaborate on the staff's view regarding the institutional setup for financial sector oversight that is recommended in the FSSA. We agree with the authorities, and we agree with some of the Directors who said that there is no one-size-fits-all approach to institutional arrangements, and it is key to take into account Thailand's history and other characteristics. We also agree that so far the arrangements have worked well, and there is no effective evidence of lack of supervisory independence. The question is, why do we recommend changing something that has been working well? We do feel that despite all these strengths, the presence of the Ministry of Finance could pose a potential risk to the independence of the different regulatory agencies if political circumstances were to change in the future, mainly because the Ministry of Finance is the owner of the Specialized Financial Institutions (SFIs) and several large public banks. By being present at the deliberations, the Ministry of Finance could influence the position of other members in the boards, and also could hamper its ability to perform the ex-post assessment it is supposed to be doing of the regulators. It would compromise the ability of the Ministry of Finance in the sense that by having been part of the decisions, then it would be difficult for the Ministry of Finance to criticize such decisions afterwards. We do believe it is important for the Ministry of Finance to be present in discussions related to financial sector policy, and that is why we are proposing to have an umbrella committee where the Ministry of Finance would be a member along with the other regulators. This umbrella committee would have mechanisms that would preserve the independence of the regulators.
>
> At the same time, we are suggesting that this umbrella committee could have more regulators, thereby enhancing the already strong coordination mechanisms that exist. In particular, it is important to include the deposit insurance agency and also the Ministry of Agriculture and Cooperatives, as cooperatives play an important role in lending to households.
>
> Our argument is aimed at ensuring that what has been working well continues to work well if, under other circumstances the Ministry of Finance starts interfering with the operational independence of regulatory agencies, which has not been the case so far.

Ms. Mahasandana made the following concluding statement:

On behalf of the Thai authorities, we would like to thank Mr. Leigh and Mr. Lopez and their respective Article IV and FSAP teams for the close engagement and candid discussions with our Thai authorities. We thank Directors for the understanding of our situation and offering us insightful comments, which we will certainly convey to our authorities.

The Thai economy has been affected by ongoing trade tensions, and we expect to see some slowdown this year, mainly from export contractions. Risks to the growth remain tilted to the downside from external factors. As for inflation outlook, headline inflation is likely to average below the lower bound of the target this year but would inch up toward the target in 2020.

Structural factors also contributed to more persistent low inflation than in the past. The authorities share the view that an accommodative policy mix is warranted at this juncture. Fiscal policy remains expansionary in this fiscal year. Disbursement is expected to be on track for the most part. The government is committed to boost government investment and make good progress in the various infrastructure projects. However, these large-scale projects tend to have a complicated implementation process, and so there might not be much room for frontloading.

The monetary policy stance is already accommodative. The central bank has recently cut the policy rate to 1.5 percent in August and kept it at the level in the monetary policy committee meeting last week. The authorities welcome the FSAP assessment that the Thai financial system remains sound and that financial stability risks are contained while there are still pockets of risk, mainly from household debt overhang.

The authorities are strongly committed to various reforms to address structural bottlenecks and improve productivity for more sustainable and inclusive growth in the long run. They have put in significant efforts to expedite the implementation of Eastern Economic Corridor projects, while promoting the digital economy and pension reform to address demographic challenges, among many others.

I also want to touch on five areas where our authorities see things differently from staff and where Directors' views vary around the table. First, on monetary policy, staff's longstanding argument for a rate cut is well noted. Meanwhile, we must reiterate that the monetary policy committee takes a cautious approach in its policy formulations. Thailand is an environment of prolonged low interest rates, and policy rate has been near record low for the past four years. Given that there remain pockets of risk that could threaten financial stability, the future policy calibrations will be data-dependent and must carefully consider the policy tradeoffs.

In the meantime, the authorities have made concerted efforts to tackle household debt overhang. Aside from strengthened oversight of the non-bank and SFI, tightened macroprudential measures, launching a financial literacy campaign and debt training, there are also some additional recent ex ante measures, namely the introduction of responsible lending directive, ongoing efforts on standardizing the debt service ratio calculation to ensure good underwriting standards, and the newly released sustainable banking guidelines from the Thai Banking Association, which includes a guideline to curb predatory lending to vulnerable groups.

Second, on the exchange rate and capital flows, the Bank of Thailand is committed to exchange rate flexibility. We reiterate that our foreign exchange intervention is not intended to disrupt, but to facilitate orderly market adjustment. This is all evident by the significant appreciation of the baht in the past three years despite our operations. Adjusting the policy rate in response to exchange rate and capital flow volatility has limits and has great financial stability consequence. While we understand the Fund's Institutional View, the authorities are of the view that dealing with the challenges Thailand faces on many fronts requires an integrated approach and a mix of policy tools to achieve a more favorable outcome for the economy. In this regard, we appreciate that a number of Directors recognize and understand the challenges we face. At the same time, the authorities also launched many initiatives to further develop financial markets so that the economy can better absorb the impact of capital flow volatility. These include further liberalization of capital account transactions and streamlined regulation related to foreign exchange and hedging transactions, developing hedging instruments and educating small- and medium-sized enterprises about how to hedge foreign exchange risks, coordinating with some regional central banks to promote the use of local currency for settlement of cross-border transactions. That said, these actions take time to bear fruit. Until then, it is necessary to help the economy cope with short-term volatile capital flows, and this is why some capital flow measures will tighten.

We also welcome the comments made by some Directors to continue working closely with staff on policy alternatives and that our country case may provide input for the IPF exercise. The authorities also welcome the opportunity to discuss policy options with the staff in the future.

Third, on the publication of foreign exchange intervention data, while we recognize the potential merit of transparency, we are worried about the unintended consequences on the effectiveness of our foreign exchange operations, especially given relative shallow financial markets. Our current practice of disclosing weekly reserves data within two weeks flat should provide sufficient information on our foreign exchange operations to the markets.

Fourth, on the FSAP recommendations, our authorities reaffirm that the Ministry of Finance representative on the Financial Institution Policy Committee does not compromise the operational independence of the committee and brings more merit to the table. That said, the authorities are discussing the possibility of setting up an overarching financial stability body to enhance potential stability oversight.

Finally, on the external balance assessments, the authorities recognize the need to pursue structural policy to address Thailand’s external imbalances. This is in line with our view that the burden of adjustment should not be borne only by the exchange rates. That said, provided that the current account gap from the EBA plays a key role in identifying country external imbalance and policy recommendations, we encourage staff to continue to work on refining the analytical framework given the model’s limitations and large unexplained residuals for some countries’ assessments, including Thailand.

I would like to end my remarks by saying that while we are trying to build a stronger roof for our house, we also experience thunderstorms, maybe hurricane sometimes. That is why we need some shelter so that we can make it through and pursue our goal of having a stronger house in the future.

The Acting Chair (Mr. Furusawa) noted that Thailand is an Article VIII member, and no decision was proposed.

The following summing up was issued:

Executive Directors broadly agreed with the thrust of the staff appraisal. They noted that Thailand’s robust policy framework and ample buffers, created through the authorities’ judicious management of public finances, continue to underpin its resilience to shocks. Directors also welcomed the progress in improving the coverage and effectiveness of financial supervision and macroprudential policies which has enhanced financial stability. They noted, however, that external and domestic headwinds are challenging near term growth prospects, and that risks are tilted to the downside stemming from the impact of the global economic slowdown, ongoing trade tensions, and weak domestic demand. In this regard, Directors encouraged an expansionary policy mix to support domestic demand, and structural reforms to promote inclusive and sustainable growth.

Directors encouraged the authorities to undertake an investment-led expansion through the judicious use of existing fiscal space, while preserving sufficient buffers and ensuring fiscal sustainability. Strong implementation of macro-critical public infrastructure projects currently in the pipeline would crowd in private investment and stimulate domestic demand in the short run, while helping lift up potential growth in the long run. Directors emphasized the importance of better targeting social assistance to protect vulnerable households while minimizing distortions. They welcomed the authorities' intention to strengthen revenue mobilization over the medium to long run, as part of a broader strategy to prepare for aging-related expenditure pressures.

Directors welcomed the Bank of Thailand's August decision to cut the policy rate. Going forward, a number of Directors saw scope for further monetary easing to help steer inflation back to target. Many other Directors considered the current monetary stance to be sufficiently accommodative, and noted that monetary policy should be calibrated based on assessment of financial stability risks. Complementary use of macroprudential policy would also address financial stability concerns.

Many Directors considered that Thailand's external position remains substantially stronger than warranted by medium-term fundamentals and desirable policies. A number of other Directors called for a more cautious interpretation of the external balance assessment citing Thailand-specific issues as contributing factors.

Directors emphasized the importance of exchange rate flexibility, with foreign exchange intervention limited to avoiding disorderly market conditions. While a number of Directors recognized that recent tightening of existing capital flow management measures (CFMs) plays an important role in mitigating short-term volatility, a number of other Directors considered that these measures should be phased out and replaced with appropriate macroeconomic, financial and structural policies.

Directors agreed that financial stability risks appear contained although household indebtedness is relatively high and there are pockets of vulnerability in the corporate sector. In line with the FSAP recommendations, they encouraged the authorities to strengthen the crisis management and resolution framework, close leakages in the macroprudential toolkit, and establish an overarching body to help enhance coordination among supervisors. Many Directors noted that the recommendations on institutional arrangements of supervisory agencies should be tailored to a country-specific context. To enhance oversight of the non-bank sector, Directors recommended strengthening the supervision and regulation of Specialized Financial Institutions and Credit Cooperatives.

Directors emphasized that the start of the new government is a timely opportunity to forge ahead with a concerted reform agenda. Targeted policies to enhance labor productivity across the regions can boost competitiveness, raise potential growth, and enhance its inclusiveness. A key priority is to address population aging through pension reform and investment in human capital that will help unlock growth potential, including through education, health, and equalizing opportunities. Directors took note of the authorities' ongoing efforts to strengthen anti-corruption institutions and called for improving the operational aspects of the procurement law and addressing AML/CFT deficiencies.

It is expected that the next Article IV consultation with Thailand will be held on the standard 12-month cycle.

APPROVAL: May 29, 2020

JIANHAI LIN
Secretary

Annex

The staff circulated the following written answers, in response to technical and factual questions from Executive Directors, prior to the Executive Board meeting:

Outlook

1. ***Investment has not been consistently the highest among the four peers, and was among the two lowest during 2014-2017, which also coincides with a higher current account balance since 2014. One reason mentioned is that of outward investment to Asian countries, to take advantage of lower labor costs. We also see considerable outward investment to Europe and the Americas during the same period, which presumably is not related to lower wages. We would appreciate staff views on whether this is related to building of global value chains during that period.***

- Thailand's outward direct investment reaches countries outside Asia and exports to advanced economies have also grown rapidly during 2011-2017. Staff acknowledge different factors that may have contributed to the underlying changes in outward investment and trade dynamics, including through development of global and regional value chains and factor prices underpinned by cost of labor and investment.

- In particular, outward investment to Europe and the United States during this period reflects continued integration in global value chains, particularly backwards integration, to support intermediate imports in the automotive, chemical, and electronics sectors.

Fiscal Policy

2. ***Could staff comment the recent budgetary measures announced by the authorities and mentioned in the buff statement, elaborating on its economic impact and whether it answers staff call for further fiscal easing?***

- The recently announced fiscal stimulus package amounts to 1.2 percent of GDP in state bank loans and 0.6 percent of GDP in budgetary expenditure. It is difficult to tell, at this point, how much of these resources constitute fresh stimulus rather than a reallocation of state bank assets and government budgetary spending. The FY 2020 Budget is expected to be discussed in the National Assembly in January 2020.

- The impact on aggregate demand will depend, to a large extent, on the proportion of fresh stimulus, how it is allocated and the related multiplier effects.

- Staff recommends a temporary scaleup of public investment that would strengthen demand in the short term, and growth and productivity in the medium and long term. The fiscal package announced by the authorities seems to have a large component of current spending. This would contribute to strengthening aggregate demand, but would not necessarily have the same beneficial impact on potential growth and productivity.

3. *We would appreciate staff's view on the efficacy and adequacy of fiscal stimulus package approved in August 2019.*

- Please see answer to Question 2.

4. *Could staff elaborate further on their judgement that there is "some" fiscal space in Thailand?*

- In line with the fiscal space framework, staff's judgment—that there is some fiscal space—takes into account:

  - financing availability: Thailand sovereign interest rates are low with comfortable access to financing by the government;
  - behavior of debt burden indicators under baseline and stress scenarios: debt/GDP and financing needs remain well below EM thresholds under the baseline and reasonable stress scenarios;
  - Fiscal adjustment needed, including over the long term, is within realistic range.

- Judgment is that there is some space for temporary public investment scaleup in the near term. Over the medium term, revenue mobilization would help finance the long-term fiscal costs from aging.

5. *On staff's recommendation to increase the public capital outlays above the authorities' already ambitious investment plan, we wonder whether Thailand currently has sufficiently high-quality projects in the pipeline?*

- Thailand has a large set of infrastructure projects (amounting to about US$ 50 bn or about 10 percent of 2018 GDP) in the pipeline, which would be more than enough to achieve the recommended investment scaleup.

- We recognize that the implementation and execution of large infrastructure projects is a challenge, and believe that recommendations from PIMA's past TA would help improve implementation capacity and quality. These recommendations include increasing market access and strengthening regulation, bringing all capital spending on the budget, improving capacity for project appraisal, and strengthening risk monitoring including for PPPs.

6. ***While we encourage staff to further reflect on this trade off in future Article IV, we would be interested to have staff elaboration on the best strategy to deal with the fiscal cost of ageing?***

- TA on pension reform is being planned for this fiscal year. This mission would be best placed to produce a strategy to strengthen the current pension system and social safety nets for the aging population.
- The current pension system faces several challenges that need to be addressed, including: (i) fragmentation and very large differences in benefits between civil servants' regimes and that for private sector workers; (ii) sustainability given the retirement age 55 and low contribution rate for Old-Age Benefit under the Social Security Fund; (iii) low coverage, with 60 percent of the working-age population not covered by a formal pension; and (iv) low replacement rates for the formal private sector.
- As noted in Appendix VIII, the fiscal cost of pensions and health care will increase significantly over the next 15 years, by about 2.3 percent of GDP, even under current coverage, and significantly more if coverage of the informal worker is increased with public funding.
- The team's recommended strategy is for a temporary scaleup in infrastructure investment to boost demand and productivity, followed by mobilization of fiscal revenues over the medium term once domestic demand strengthens to adequately address the fiscal cost of aging. Broader coverage of personal income, wealth, corporate income, and energy-related taxes, as well as higher VAT rate would help finance these costs.

7. ***We would appreciate staff's comment on the adequacy of the social assistance program implemented over the last two years amounting to about 0.5 percent of GDP, and what share of the most vulnerable household are covered by some form of social assistance.***

- The social assistance program is reaching over 11 million recipients that qualified for a welfare card, through which they receive cash transfers and subsidies. In addition, training is provided to improve work opportunities.
- Although the number of recipients is large, a TA mission in 2018 noted that the qualification process should be improved to make sure that the resources actually reach the vulnerable population. This is currently hard to assess with the information provided by applicants to the authorities. In addition, consolidating the different programs scattered across agencies would help improve the distribution of benefits across the target population.

- In order to improve the program's targeting, the authorities are planning a new round of welfare card distribution, by which all applicants (including current recipients) would need to apply, this time providing better and verifiable information to the authorities.

8. ***On the ongoing revenue-neutral changes in tax policy, could staff indicate if it would it be possible to include a higher VAT rate among the measures to be considered?***

- Staff recommends increasing the VAT rate only in the medium term, once domestic demand has strengthened. This would avoid offsetting part of the impact from the infrastructure push on aggregate demand.

Monetary Policy & External Sector

9. ***We note that staff and authorities do not agree on the need to strengthen monetary policy transmission (p.13). We would appreciate staff's comments on the sources for this difference in view.***

- The difference in view mainly comes from the assessment of risks to entrenched low inflation that can result from de-anchored long-term inflation expectation. The authorities see that such a risk is relatively limited as inflation expectation is well anchored (paragraph 23, Staff Report). In contrast, staff takes a more cautious approach. Our recommendation of strengthening monetary policy transmission draws particular attention to effective communication that would help anchor long-term inflation expectation. Given persistently low inflation below or at around the lower bound of the inflation target, staff sees high risk of entrenched low inflation that would worsen the macroeconomic environment, increasing real interest rates and the real debt burden, and posing risks to corporate, household, and financial sector balance sheets (Appendix II: Risk Assessment Matrix).

10. ***Could staff elaborate on why they believe the transmission of recent policy measures is inadequate and needs further augmentation?***

- Given the recent domestic and external developments and their outlook, staff see the need of a multi-pronged approach to address weak domestic demand. Given the delay in the FY 2020 Budget and consequent weaker support for domestic demand, together with the moderation of the financial cycle, staff sees further room for monetary policy to support growth in domestic demand. While staff agrees with the authorities on a data-dependent approach for monetary policy, such an approach needs to take account of both incoming data as well as the economic outlook, which looks precarious, and thus staff sees merit in further monetary easing. This would help curtail risks of low inflation becoming entrenched and would support domestic demand and external rebalancing in the short term (paragraph 21, Staff Report)

11. ***In this regard, we appreciate if staff could elaborate on the difference of views regarding macroprudential policy between the authorities and staff. Also, we wonder the extent of efficacy of further rate cuts in stimulating the economy (given the low for long environment) and moreover it could slow the rebalancing of the economy and improving the current account imbalances. Staff's views are welcome.***

- Staff recommendation is a policy mix of continued application of macroprudential policies in tandem with monetary easing that would help preserve financial stability (paragraph 22, Staff Report). Staff also stresses the need to strengthen the macroprudential policy (MPP) framework, including through closing the leakages in the BOT's macroprudential policy toolkit. Thailand's MPP coverage of Specialized Financial Institutions, cooperatives, and other non-bank financial institutions is limited, potentially affecting the potency of the MPP toolkit. The authorities agree on the need to further strengthen the macroprudential toolkits, though such efforts may take time.
- Strengthening the MPP framework would allow the authorities to continue to contain systemic risks and provide monetary policy the necessary space to effectively target inflation.
- See also answer to questions #9 and #10 on why staff recommend further monetary easing.

12. ***We would be interested to hear staff's views on the latest central bank decision***.

- Thailand's Monetary Policy Committee met on September 25 and decided to hold the policy rate at 1.50 percent. The press release points to the current monetary policy stance as sufficiently accommodative, contributing to the continuation of economic growth and should support the rise of headline inflation toward target. The decision to keep the policy rate was also underpinned by need to safeguard financial stability.
- Staff recognizes the authorities' data dependent approach and as explained in question 10 above, sees a need for further monetary policy easing.

13. ***We concur with the suggestion to encourage authorities to publish FXI data, but we believe that the authorities should do it gradually and with a lag, in a way that does not hamper the effectiveness of FX interventions. Could staff elaborate on the recommended frequency and granularity of the FXI data to be published?***

- Publication of timely, accurate, and comprehensive FX intervention data could enhance the transparency, credibility and communication of the policy reaction function of monetary authorities (particularly for inflation targeters such as Thailand) by reinforcing the view that intervention is being used for its stated purpose (i.e., to address disorderly market conditions).

- The exact parameters (frequency, lag, granularity) of publication will vary with country circumstances. Practice among EMs that publish FXI data varies, with daily, same day publication (Brazil, Colombia, Peru, Russia) to monthly (India, Mexico, with 1-2 month lag).
- In general, data on FXI should be reported at the highest possible a high enough frequency and reporting lag as short as possible without becoming overly onerous.
- Market sensitivity is another consideration in the publication of FXI data. For Thailand, however, the large daily FX market turnover probably provides limited opportunities for speculation. In situations of poor market liquidity and depth, when intervention is often used to address disorderly market conditions, announcements could take the form of high-level objectives that are too general to be of use to speculators. This is generally preferable to the alternative of no announcement, as this is also a communication choice given that market participants can observe the intervention but are more likely to misinterpret the signal.

14. ***Speculative capital flows have been identified by the authorities as the cause for the rapid appreciation of the baht and the heightened exchange rate volatility. As a result, the authorities have resorted to foreign exchange interventions or tightening of existing capital financial management measure (CFM) to deter those flows. Staff's elaboration on the significance of speculative flows as source of financial stability risk in Thailand are welcome.***

- Speculative flows could have an impact on domestic financial system through various channels, including exchange rate and asset prices, but the associated risks appear to be contained. In particular; (i) external debt account for less than 15 percent of corporate debt (and some is denominated in local currency), and most of corporate foreign currency exposures are hedged either naturally or financially; (ii) banks' foreign currency exposures are limited, and (iii) the authorities have taken steps to contain risks from inflows to the real estate market (including from non-residents) by introducing tighter LTV limits.

15. ***As a small open economy with the experience of currency crisis, Thailand could provide an interesting case study for the ongoing work on the "Integrated Policy Framework". In that regard, the assessment on the recently introduced adjustment to the ceiling on non-residents Baht accounts would need to be made in such a holistic approach and considering the macroeconomic effects of the policy change. Staff's view would be welcome.***

16. ***Could staff elaborate on alternatives to cope with the current challenges posed by capital inflow pressures on the Thai baht in light of the ongoing Integrated Policy Framework discussions?***

17. ***Regarding monetary, exchange rate, and capital flow management policies, we note the huge divergence of views on the appropriate policies to support growth and external rebalancing. We would welcome staff's further elaboration on the disagreements, including whether any lessons could be drawn from the current work on the Integrated Policy Framework (IPF), which should take into consideration country specific circumstances.***

Answers on IPF related questions 15, 16, and 17:

- Staff followed prevailing IMF surveillance guidance which comprises the following policy assignments: monetary policy ensures internal balance; exchange rate flexibility ensures external balance; macroprudential measures (MPMs) ensure financial stability; FXI is used mainly to avoid disorderly market conditions; and capital flow management measures (CFMs) are only used under specific circumstances. The IMF's current work stream on an integrated policy framework (IPF) seeks to identify the best available policy mix that could help countries pursue growth and stability objective, particularly in the face of rising spillovers and deepening macro-financial and external linkages. It would be very premature to speculate what this work might imply for a particular country. While the analytical work proceeds, our advice is guided by the existing frameworks. We very much welcome the dialogue with the Thai authorities on these issues.

18. ***In particular in the case at hand, are there arguments in favor of well-targeted capital flow management measures (CFMs) and possibly limited foreign exchange intervention, which are embedded in a well-communicated strategy of judicious macro-financial policies?***

- The authorities argue that capital inflows into EMs are well supported by low interest rates, excess liquidity driven by the easy monetary policy in major economies. Staff advocates for a comprehensive approach that is consistent with the Fund's IV as described in question 18. Further monetary easing would also have the added benefit of attenuating excessive appreciation pressures and potentially dampening speculative portfolio inflows into Thailand. This comprehensive approach could be complemented by ongoing efforts to liberalize capital outflows in an appropriately paced and sequenced manners. (Please also see answers for questions 19-22)

19. ***Capital inflows regulations may play an important role in the transition period and help mitigating exchange rate appreciation that may not be warranted by economic***

fundamentals. Can Staff elaborate on the sequencing and mix of recommended policies, and if the integrated policy framework may apply considering authorities' views?

20. ***We are concerned at the impact this has on export receipts - that are already in decline - and are more inclined to sympathize with the authorities' desire to address the speculative flows directly. Could staff elaborate on their discussions with authorities on the appropriate response to large and volatile capital flows?***

21. ***Could staff please elaborate on its suggestion to "provide a robust and durable solution to attenuating volatile capital flows" and on a possible accompanying role to be played by the limited and temporary use of CFMs in this context?***

22. ***While the efficacy remains to be seen, it is also important to consider an exit strategy, that is when and how to unwind the measure and minimize backlash due to the unwinding. Staff's views are welcome.***

Answer to Questions 19, 20, 21, and 22:

- The discussion with the authorities focused on the objectives of the CFM, whether the CFM is appropriate, policy alternatives to the CFM, the effectiveness of the measure, and recommendations on the CFM.
- The objective of the first measure, as officially stated, is to discourage short-term speculative flows and limit appreciation pressures on the currency. Staff recognizes the authorities' concerns around the impact of recent baht appreciation on exports receipts, and the challenge that prolonged loose monetary conditions place on small open economies more generally.
- In line with the IV, well-targeted capital flows measures may be appropriate to the (i) extent that the room for adjusting macroeconomic policies is limited; (ii) appropriate policies require time to take effect; (iii) the inflow surge contributes to systemic financial risk; and/or (iv) there is heightened uncertainty about the underlying economic stance due to the surge. Under current conditions in Thailand, it is not clear that any of these conditions hold.
- Staff is of the view that the underlying capital inflow surges can be addressed by more robust and durable solutions than the CFM measure, whose efficacy is unclear. While this measure could create distortions and increase operational cost and operational risk for investing in the baht, it would likely not have a material impact on net capital flows beyond the immediate horizon.
- Staff's view is that capital flow management should be addressed primarily through macroeconomic, structural and financial policies. In the context of loosening of global financial conditions, a flexible exchange rate should serve as a key shock absorber in response to volatile capital flows, while targeted macroprudential policies can address possible financial stability risks, including the unhedged FX exposure for

SME. This would complement the authorities' ongoing efforts to liberalize capital outflows in an appropriately paced and sequenced manners.

- Capital inflow surges ultimately reflect perceptions of Thailand as a safe haven in the region, due to its considerable stock of international reserves and large and persistent current account surpluses. However, the CA surplus reflects a savings-investment imbalance, notably weak domestic demand, due largely to structural reasons. In staff's view, a growth-driven rebalancing over the medium term, where a pickup in domestic demand is supported by macroeconomic (investment led fiscal stimulus and monetary easing), financial, and structural policies, should narrow the current account surplus, and ameliorate volatile capital flows that do not reflect fundamentals.
- Looking ahead, staff recommends the measure be phased out as supportive macroeconomic and structural policies are implemented. Appropriate implementation of macro and structural policies should reduce the current account surplus and minimize any untoward effects of unwinding the measure. Further, staff recommends that the reduction in the limit be phased out, not the removal of the limit altogether, which should also limit any untoward effects.

23. ***We would welcome staff's clarification to the three points raised by the authorities, namely that more could be done to account for Thailand specific factors in the assessment model, such as population aging, and that it does not reflect the large real appreciation realized over the past few years.***

- Staff carefully reviewed the case for country specific adjustors not accounted for in the revised EBA model, including in the light of evenhandedness, given the EBA is a multilateral exercise. Staff maintained the case for adjustors for two Thailand specific factors, one data related (terms of trade measurement) and one accounting for temporally low domestic demand (political uncertainty, which has declined relative to preceding years).
- Demographics was a key refinement to the 2018 revision of the EBA, as additional demographic variables to account for the speed of aging, and longevity risks. The addition of these variables increases the estimate current account norm for Thailand. Staff notes in the EBA writeup (page 56) that the large informal sector and low pension coverage derive in informal and uncertain social safety nets. The interaction of a rapidly aging population with an informal and uncertain social safety, could lead to larger precautionary savings in Thailand than accounted for by the model. Indeed, given the difficulties in measuring informality and uncertainty, it is challenging to numerically account for this in a regression. Over time, as social safety nets are enhanced, the contribution of this factor should decline.
- The EBA methodology links externals sector indicators to a rich set of macroeconomic fundamentals and policies identified in the literature. Idiosyncratic factors not captured by the models and that can be reasonably identified and estimated are introduced as adjustors. In Thailand's case, adjustors amount to

1.5 percent of GDP for 2018. Exchange rate developments may or may not mimic contemporaneous movements in the current account, depending the source of the shock

24. ***Could staff explain why the demographic variables in the model and the proxy variable for social spending do not capture Thailand specific factors?***

- While the EBA model incorporates a rich set of indicators to capture demographic and structural features, including the extent of social safety nets (through the use of a health spending proxy), some policy distortions may not be fully identified or quantified in the model. Specific knowledge of the economy informs staff's assessment of the policies needed to address external gaps. In this regard, staff is of the view that Thailand's weak social safety nets (not fully captured in the proxy) remain an important driver of precautionary saving and the excess current account surplus. The assessment does not include adjustors for demographic variables or social spending.

25. ***Could staff elaborate on the decomposition of the current account surplus by institutional sectors (government, households and firms)?***

- While staff does not have data on the current account surplus by institutions, the Flow of Funds data from the National Accounts provides the net real savings ratio as a share of GDP by institution, which can provide insight on the savings-investment balance by institution (see Table 1)
- For the latest available data as of 2016, we observe that households have had a long standing positive savings balance, corporations (financial and non-financial) have increasingly positive savings balances, with while the government sector has had a negative savings balance.

Table 1: Thailand: Net real savings ratio, as a share of GDP

	2012	2013	2014	2015	2016	Average 2012-2016
Household	8.41	7.78	9.64	10.88	10.74	9.49
Non-financial corporation	-9.26	-11.01	-1.78	4.12	11.31	-1.33
Government	-3.21	-2.69	-5.26	-5.12	-6.55	-4.57
Financial institutions	3.34	3.97	4.98	6.18	7.92	5.28
Rest of the World	0.72	1.95	-7.57	-16.05	-23.42	-8.88
Total	0.00	0.00	0.00	0.00	0.00	0.00

Source: Flow of Funds, National Economic and Social Development Board

Financial Sector

26. ***Further staff comments regarding the current governance structure and recommendations to transform it will be welcomed.***

- We agree that there is no one-size-fits all on institutional arrangements and that it is key to take into account a country's context when designing these arrangements. We also acknowledge that the existing arrangements have so far helped ensure effective oversight and that there is no objective evidence of lack of supervisory independence.
- At the same time, staff's view is that the Ministry of Finance (MoF) has a conflict of interest as owner of Specialized Financial Institutions and several large commercial banks, thus posing a risk to the operational independence of the supervisor. Moreover, cross-directorships could dilute accountability and delay decision making. For this reason, staff recommends reducing the involvement of the MoF in prudential issues and creating an overarching body with a "comply or explain mechanism".
- This overarching body would help reduce the inaction bias of regulators and maintain their operational independence. It would also help strengthen accountability and its broader membership would enhance the already strong coordination and cooperation among agencies, a key lesson of the 1997 financial crisis.

27. ***Could staff elaborate on the statement in the buff that the current institutional set-up reflects country-specific experience in crisis management?***

- Please refer to our response to Question #26.

28. ***On staff's recommendation relating to institutional arrangement, we note from the buff statement that the current system was designed based on Thailand's experiences and circumstances, and wonder if there should be more recognition for the merits of the current arrangement, and whether there are any risks to shifting away from a system that seems to be working well so far. Staff's comments are welcome.***

- Please refer to our response to Question #26.

29. ***We would be interested to learn if staff has heard different perspectives from the representatives of the supervisory agencies on this particular matter?***

- Please refer to our response to Question #26.

30. ***In light of the authorities' views regarding staff's recommendations on the current structure of financial oversight, could staff elaborate on their reasoning behind the suggested fixes to a system that appears to be working well?***

- Please refer to our response to Question #26.

31. ***Could staff elaborate on work underway to develop Thai financial markets?***

- Thailand's securities market is fairly well developed, with active participation of retail, institutional, and foreign investors. The authorities have indicated the implementation of several measures aimed at developing further the capital markets: (i) establishing an independent organization, the Capital Market Development Fund (CMDF), to promote the development of capital markets, human resources and infrastructure for the Stock Exchange of Thailand (SET) and R&D; (ii) granting the Securities and Exchange Commission (SEC) the final authority to approve a securities company to operate in the SET and to allow the trading of foreign securities in the SET, (iii) empowering the SEC to prescribe securities companies the amount of required capital on a discretionary basis so that it can authorize less capitalized FinTech and Regulatory Sandbox initiatives; and (iv) issuing guidelines for equity crowdfunding by the SEC as well as continuing offering a set of sandboxes to encourage innovation.

32. ***Besides their cautious approach regarding using the policy rate to stimulate growth, how did the authorities react to the analysis and recommendations of Appendix VII, and which parts are likely to be pursued in the near term?***

- The authorities agreed with the recommendation a multipronged approach to address high household debt. They have undertaken several initiatives that reflect this multipronged strategy, and will continue to strengthen them in the near term, including tightening lending standards for consumer and auto loans, enhancing financial literacy, and promoting the resolution of debts via the Debt Clinic (including debts from both banks and nonbanks).
- Staff's work will also be presented in a forthcoming joint Bank of Thailand-IMF conference in early November in Bangkok.

Structural reforms

33. ***Does staff have additional suggestions to boost the competitiveness of the Thai economy, while reducing social and regional inequalities?***

- Staff stress that Thailand would need to further improve economic environment that would unlock potential to economic growth in the long term. This would require public investment in both physical and human capital that encourage private sector investment. Coherent development policies that aims to attract FDI as well as identifying and addressing bottlenecks to investment are paramount to boosting competitiveness and lending to long-term economic growth.

34. ***Prolonged U.S.-China trade tensions could significantly change Asian supply chain and Thai's role in the chain. We appreciate staff's views on how the above factors could affect the CLMV strategies of Thai multinational firms.***

- Strong economic prospects in the CLMV region have driven increased investment by Thai multinational firms in the region (particularly in energy, food and agriculture processing, and services). With greater uncertainty from prolonged US-China trade tensions, and were supply chains to shift to CLMV (early evidence suggests increased investment diversion to these countries), it is likely Thai firms will explore further opportunities in the region.

35. ***However, increased domestic competition from foreign firms could put further stress on the domestic small firms and might have adverse effects. We appreciate staff's comment regarding possible unintended consequence of "Thailand plus."***

- The authorities most recently implemented a stimulus package called "Thailand Plus" to attract FDI. Staff sees that increase in FDI will likely create jobs and help spur economic growth. With the ongoing project through the Eastern Economic Corridor (ECC), "Thailand Plus" will likely contribute to economic growth outside the Bangkok area. Given high mobility of labor in Thailand, employment opportunities will encourage workers to migrate from other regions to the areas where investment take place. It is important for the authorities to continue their effort to address inclusive growth by reducing regional disparities.

36. ***We would be interested in hearing staff's further comments on the authorities' plans to address natural disasters and climate change concerns.***

- The Office of Natural Resources and Environmental Policy and Planning, responsible for climate change policy, has put forward several initiatives, including:
  - Producing and publishing the Climate Change Master Plan to achieve sustainable low carbon growth and climate change resilience by 2050.
  - Submitting to the UN Framework Convention on Climate Change its intention to reduce greenhouse gas emission by 20 percent from the projected level by 2030.
  - Drafting legislation that will provide legal basis for further climate change action.

- The BOT is currently looking at other countries' experiences and best practices for integrating climate-related risks into financial stability monitoring.