

Inclusive Growth and the Conduct of Monetary Policy in Thailand

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Lecture 25

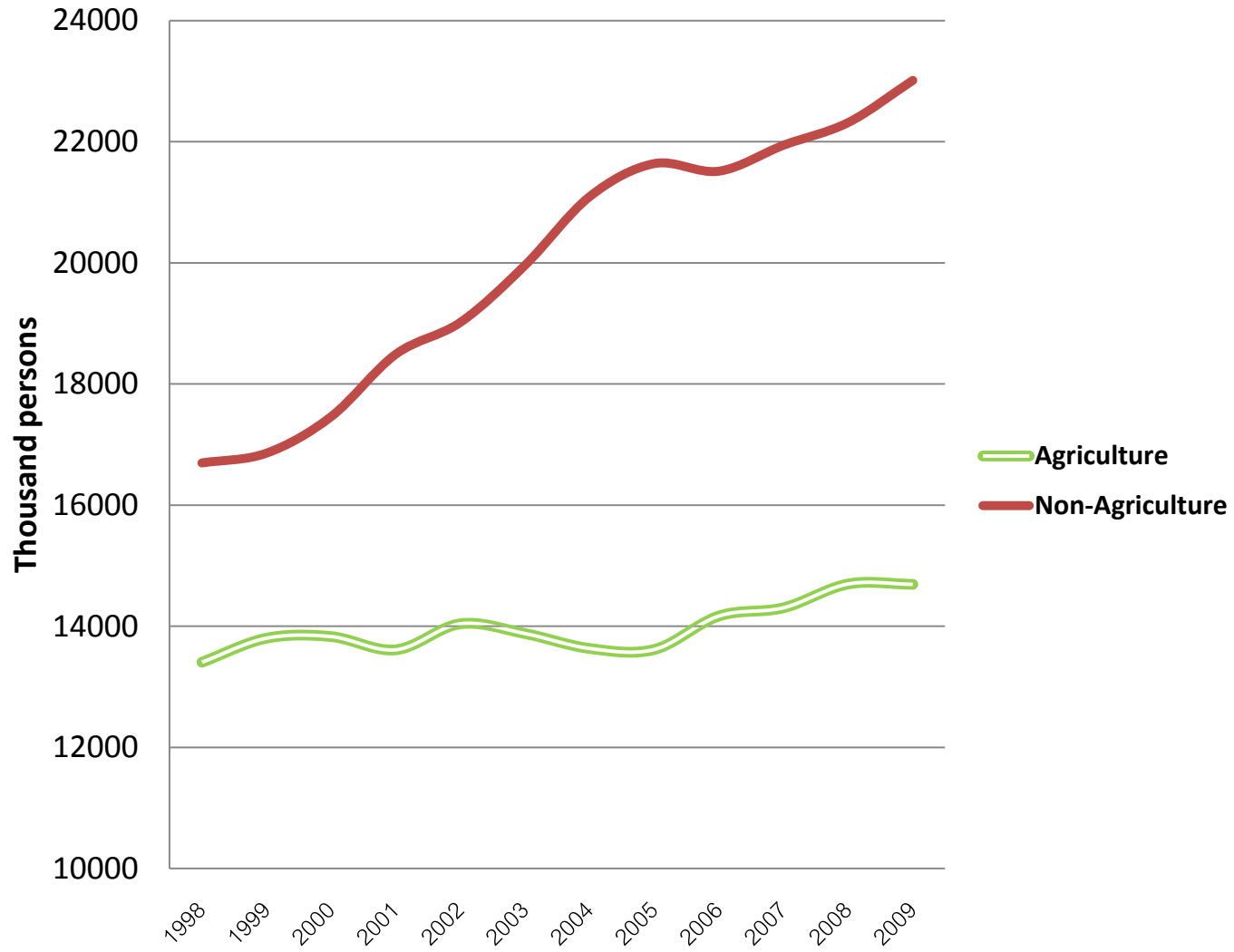
Main Themes

- Objectives of monetary policy
- Inclusive Growth
- Characteristics of the Thai labor market
- Monetary policy impact
- A VAR Model
- Macroeconomic policy alignment

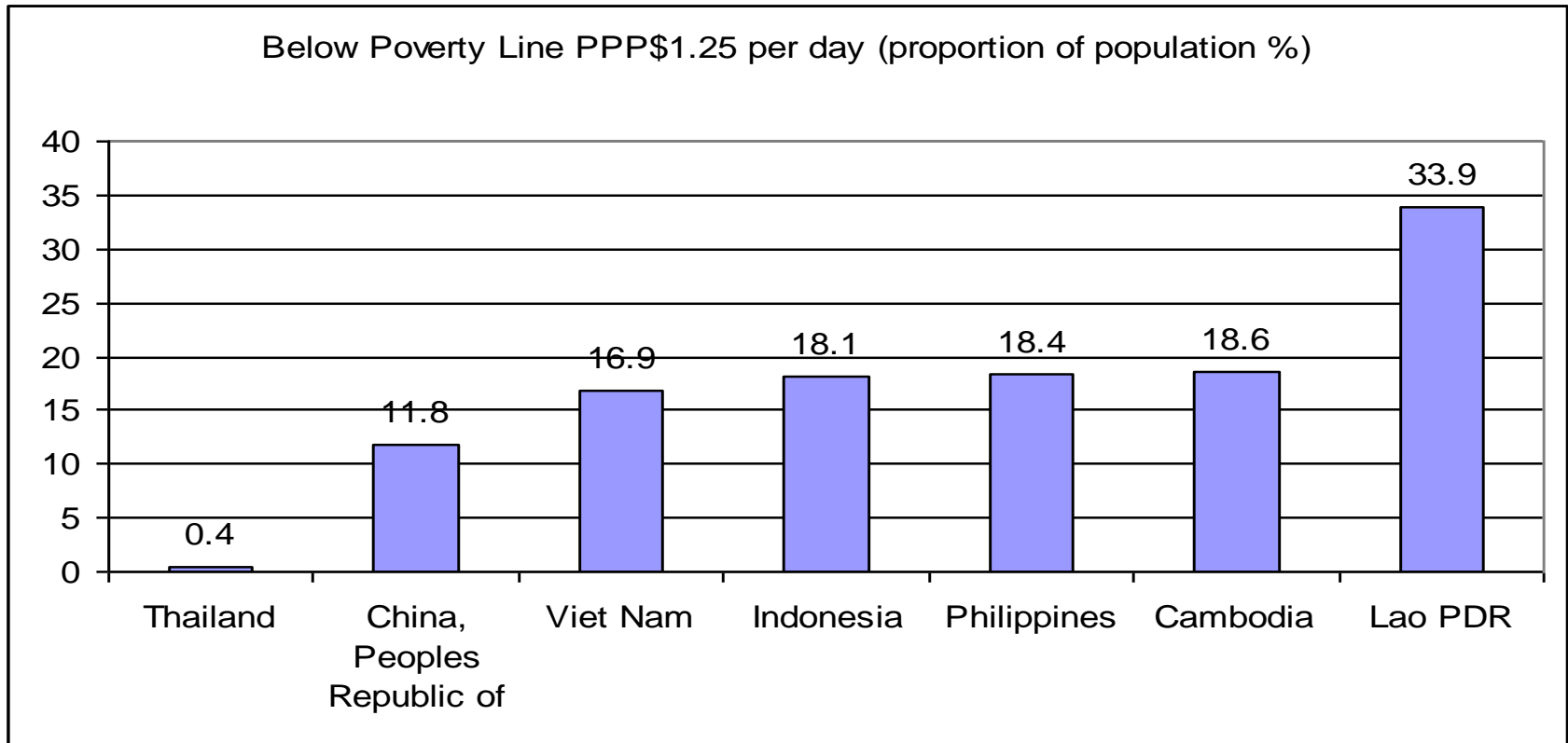
Inclusive Growth

- Economic growth must generate employment, reduce poverty, and mitigate inequality.
- Virtuous cycle of growth can reduce poverty through increasing employment with rising productivity.
- Growth may not impact the poor due to segmented labor markets and labor immobility.

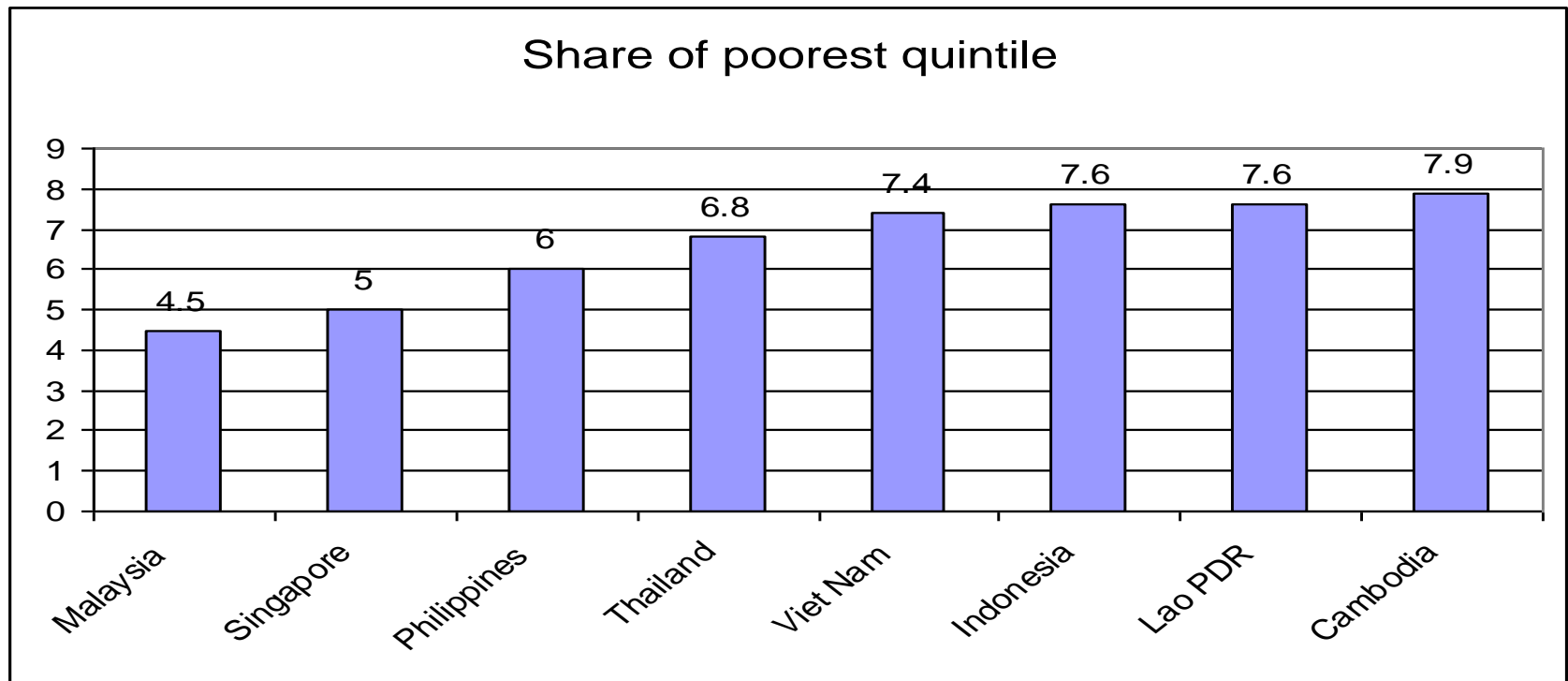
Thailand's employment-generating sectors



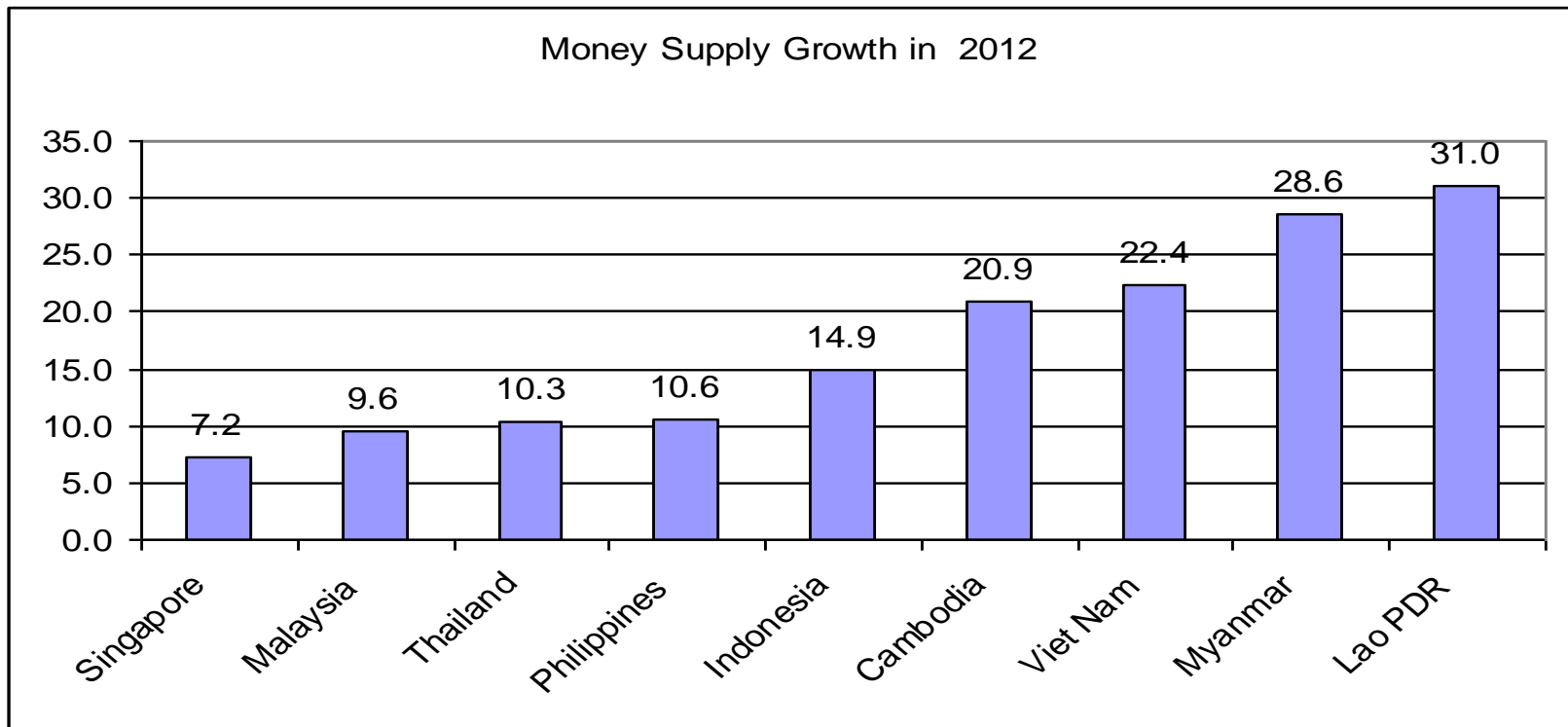
Inclusive vs. non-inclusive growth



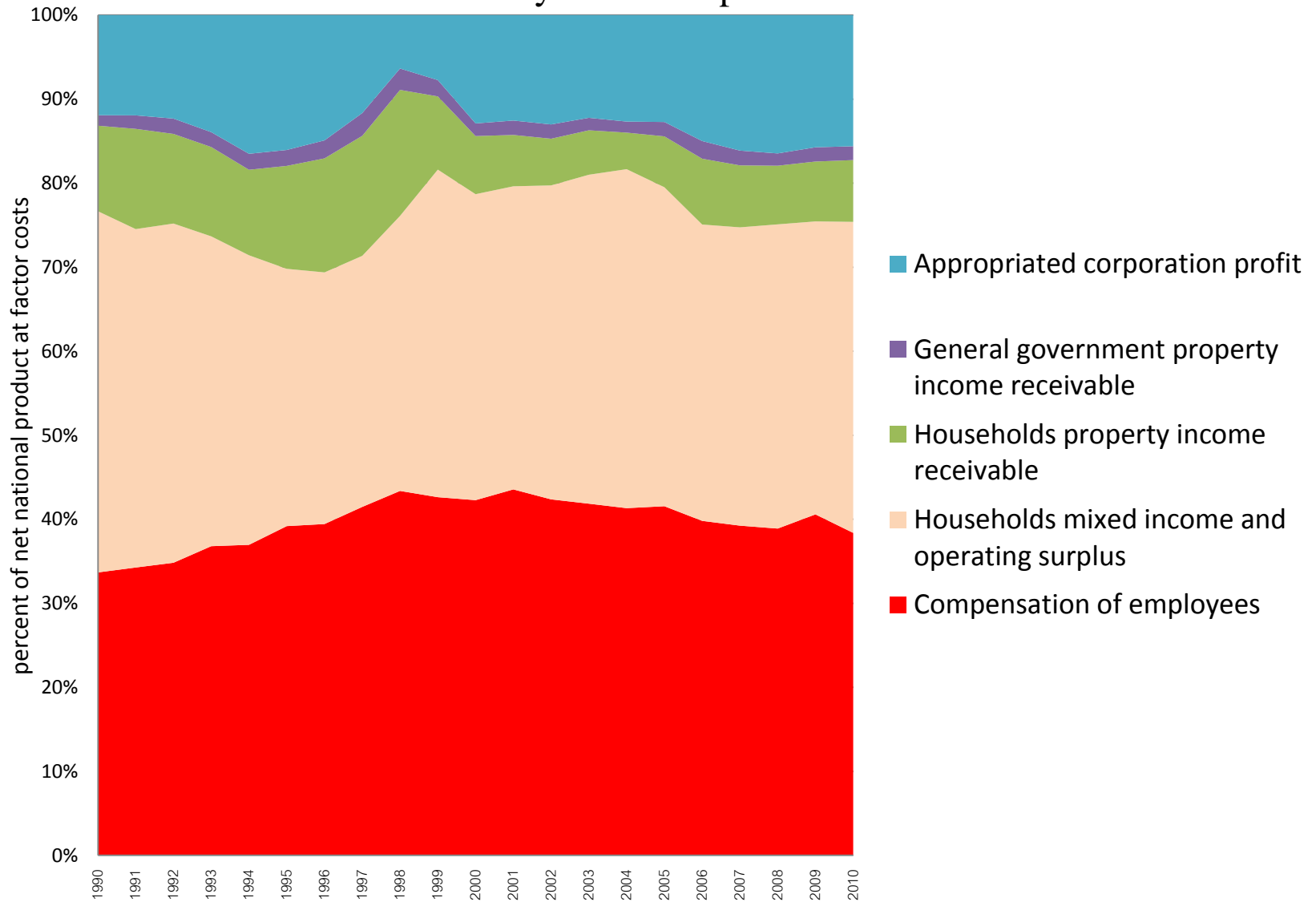
Inequality remains in high growth economies



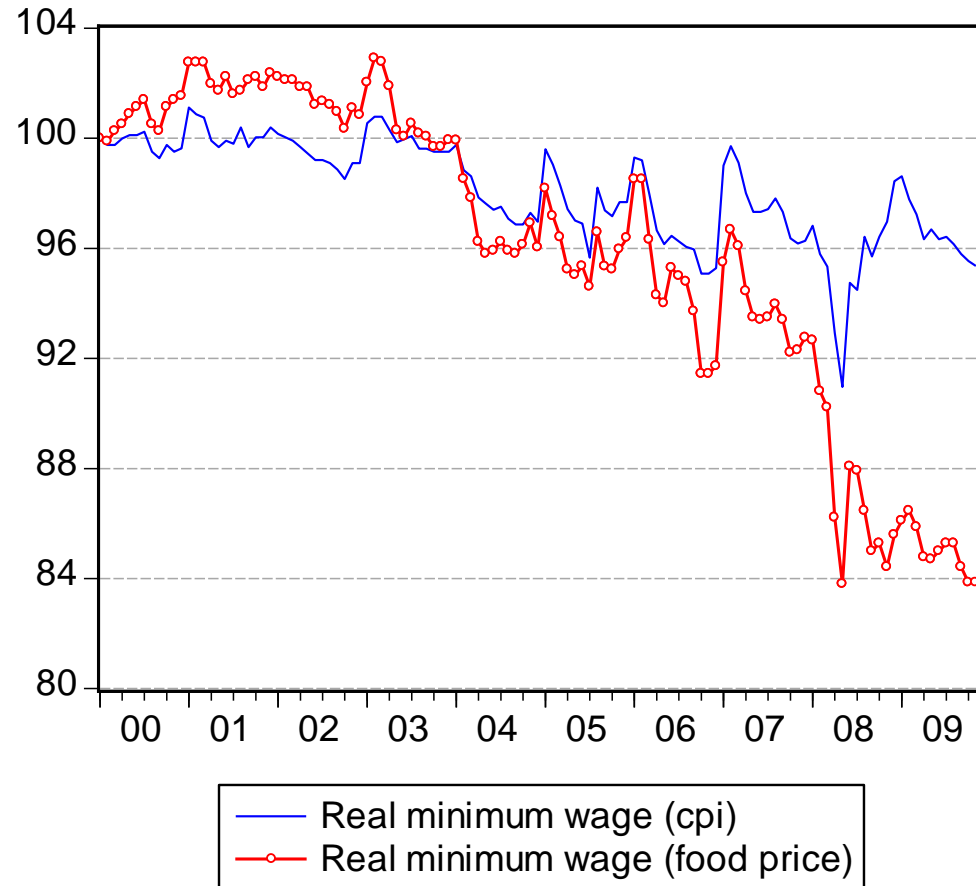
How does monetary growth impact poverty?



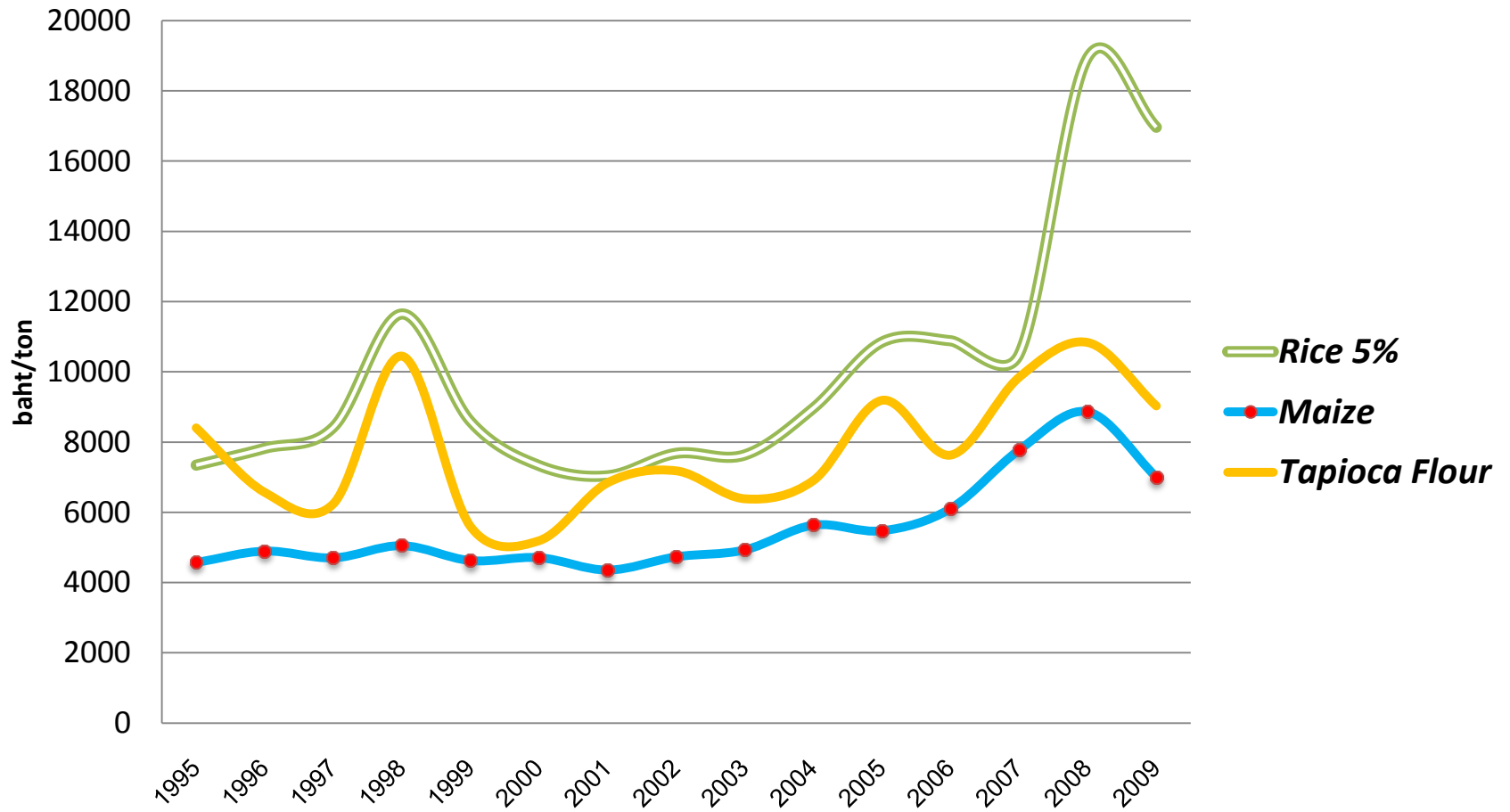
Distribution of income by factors of production



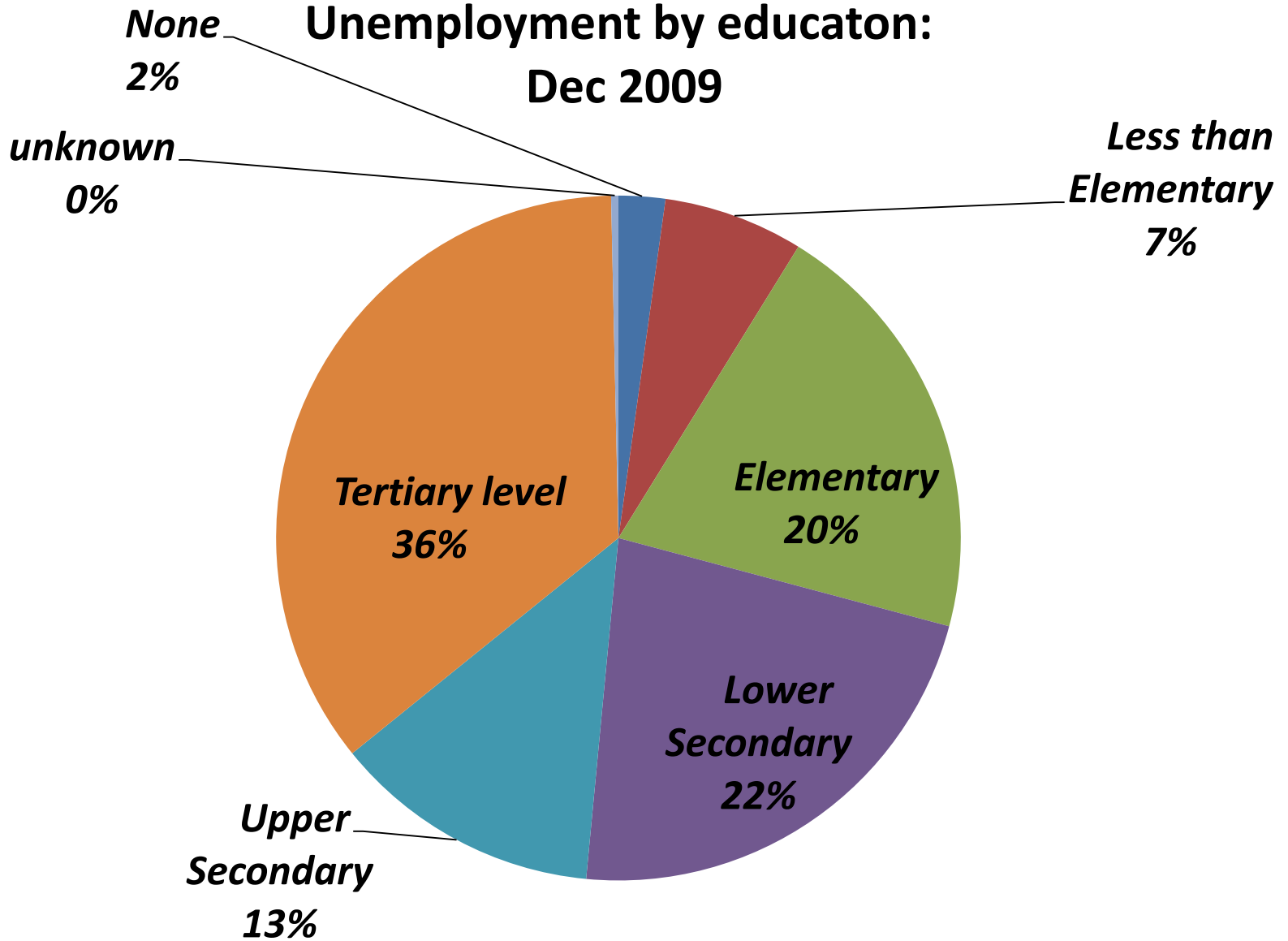
Declining real wage rates: social unrest and subsequent populist policy



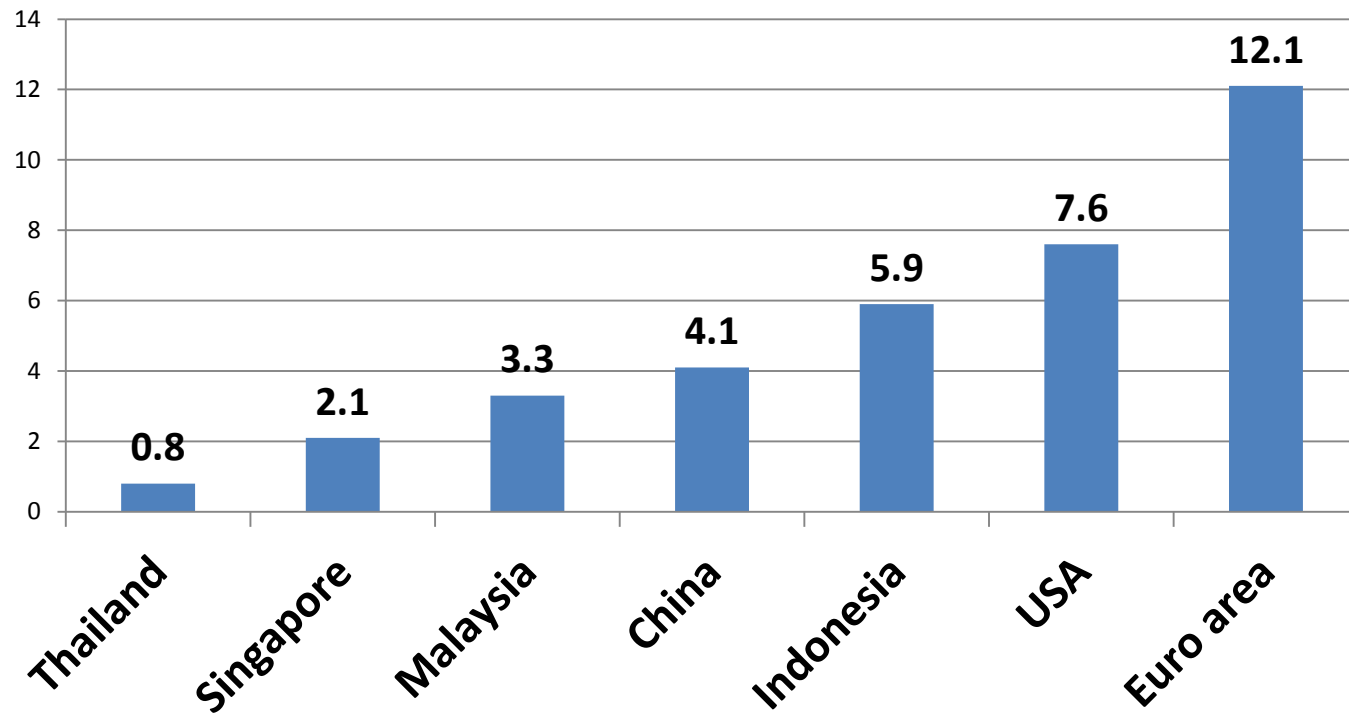
Global food price crisis in 2008



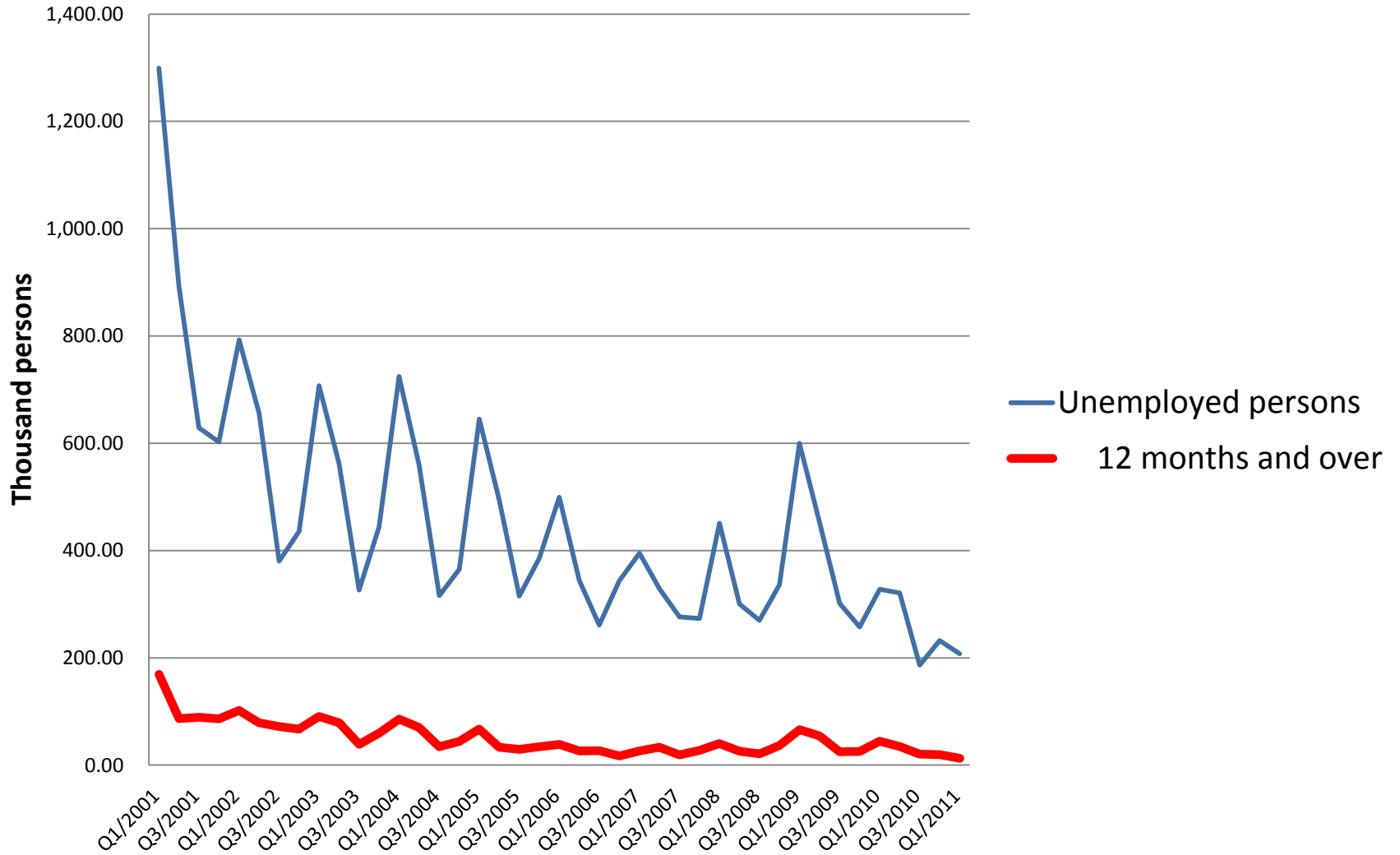
Unemployment by education: Dec 2009



Unemployment Rate: 2013

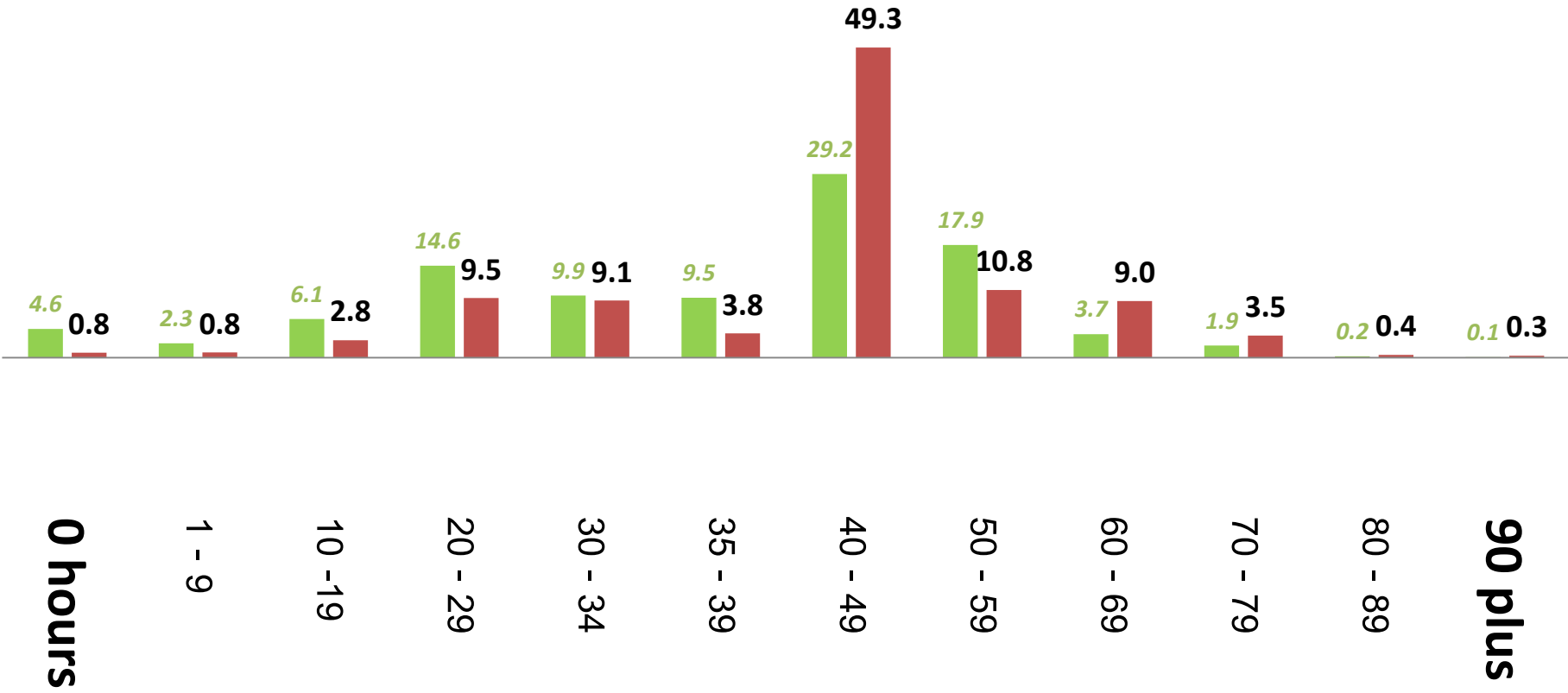


Unemployment duration



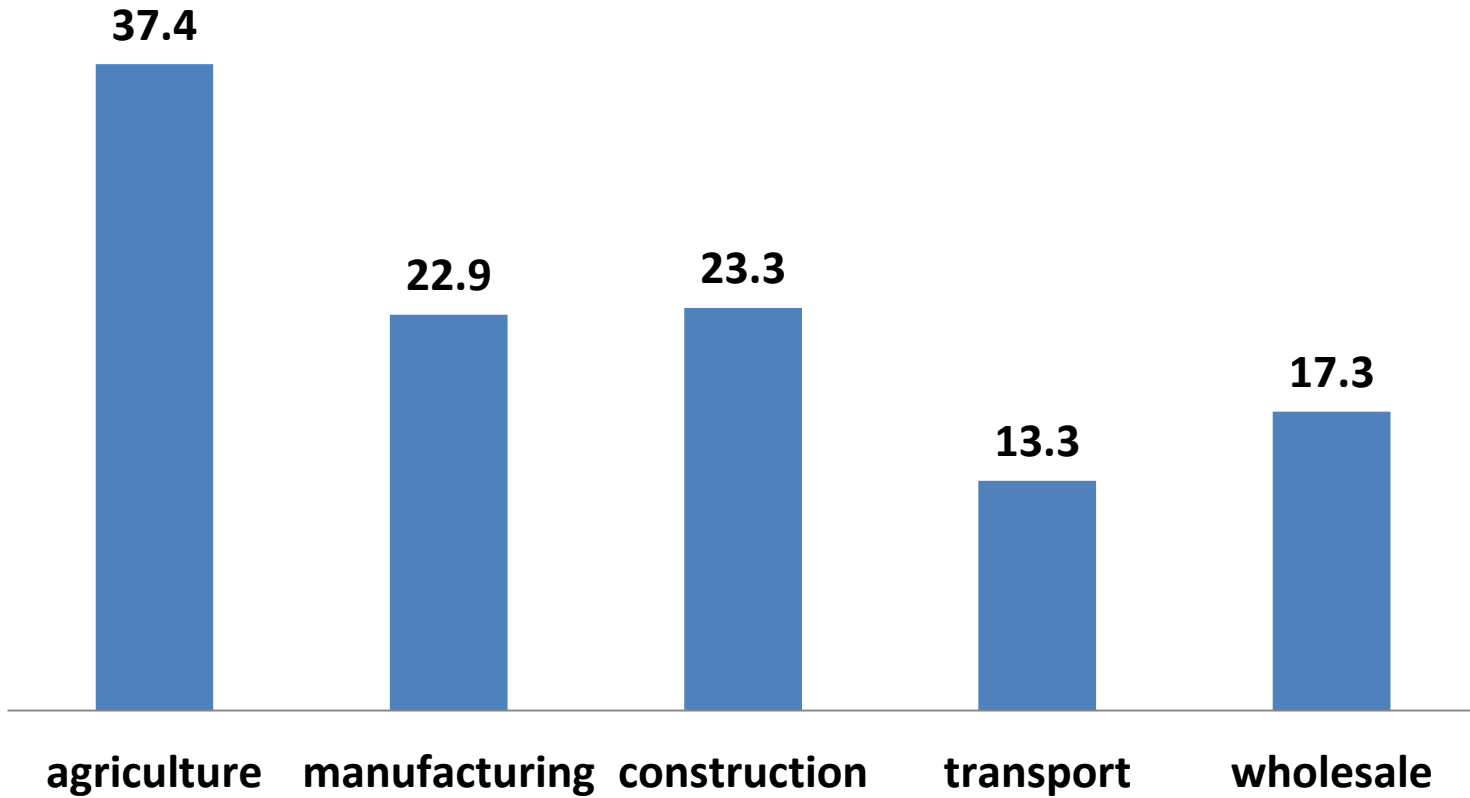
Employed person by hours per week (2011, percent)

■ agriculture ■ manufacturing



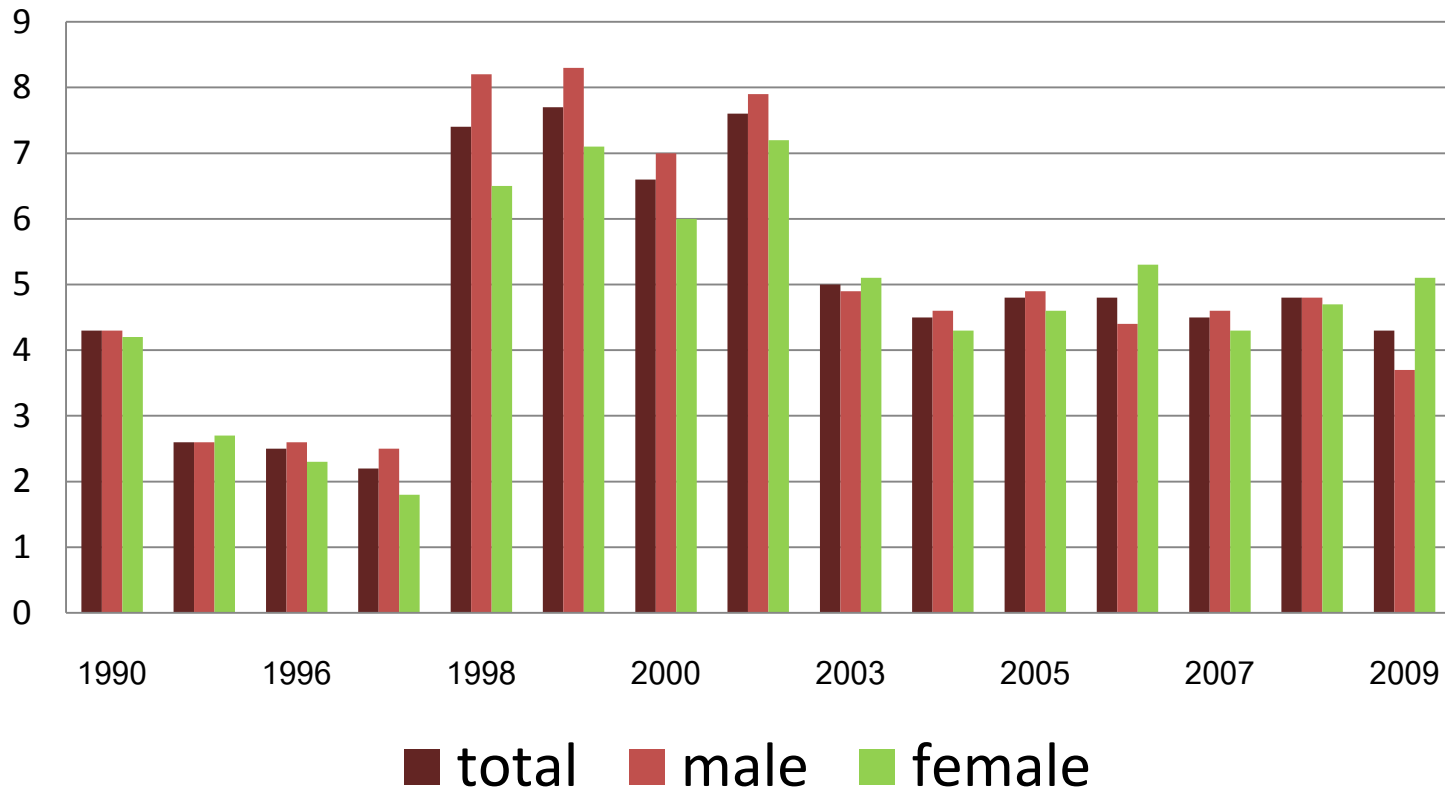
Underemployment

percentage of those who worked *fewer* than 34 hours a week
in 2011

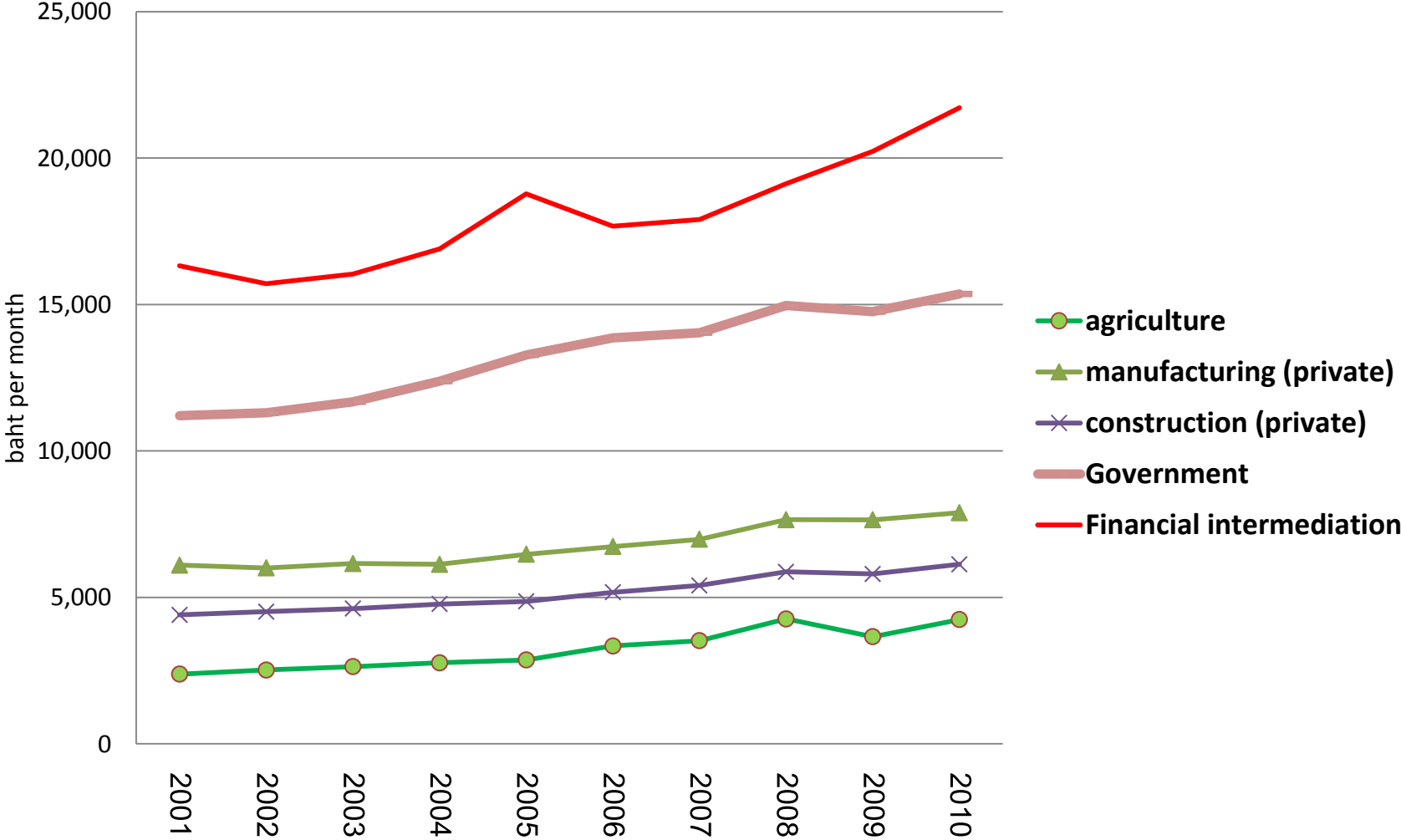


Growth is good for the young

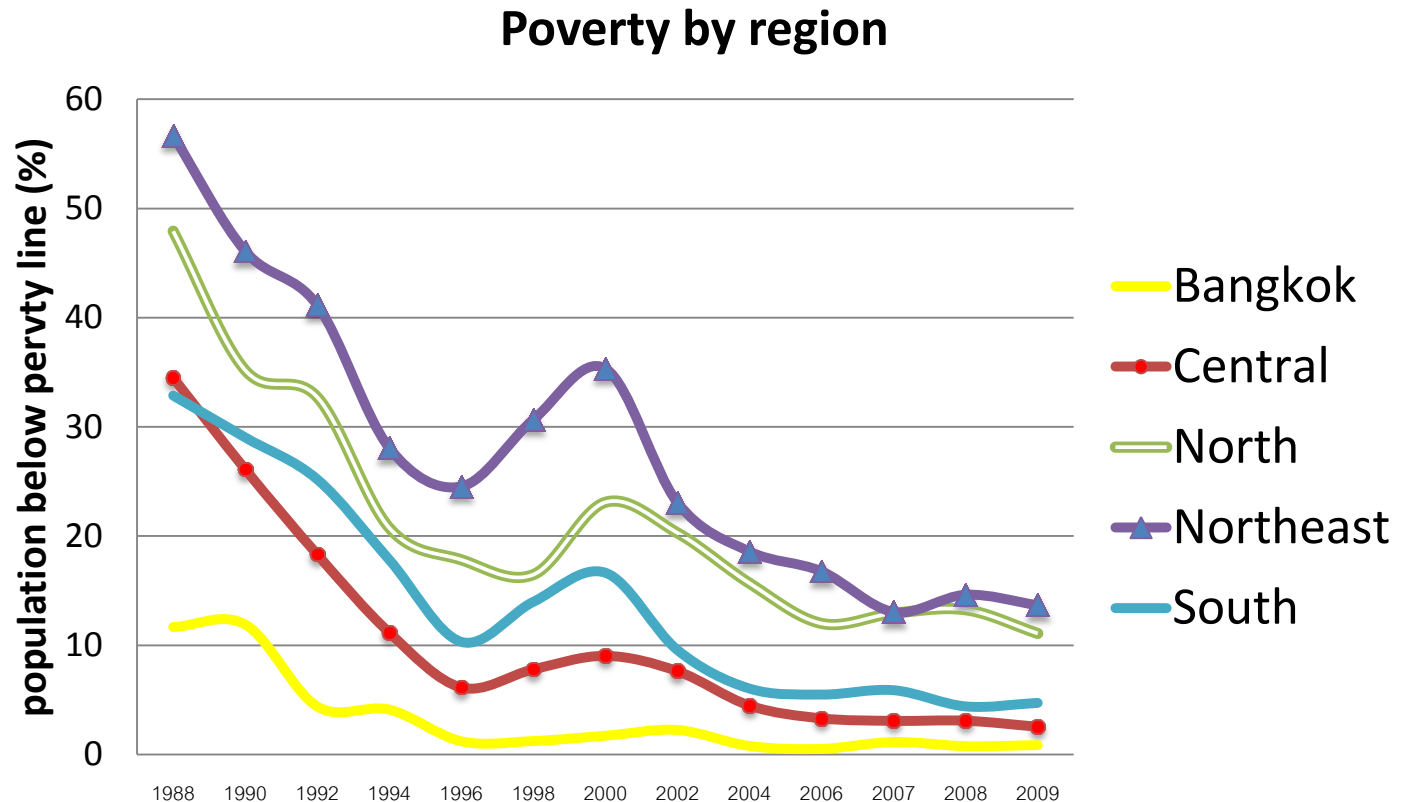
Youth unemployment rate



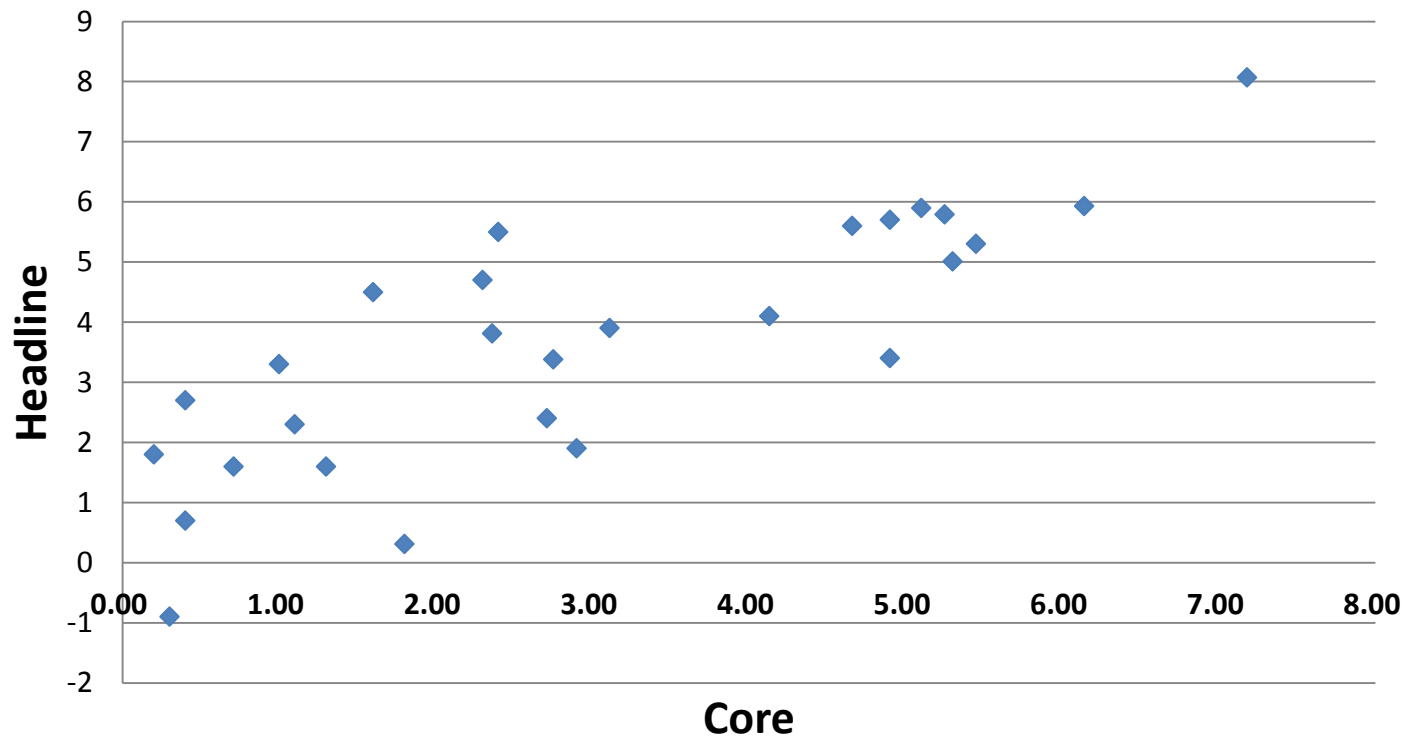
Limited upward mobility from low to high productivity



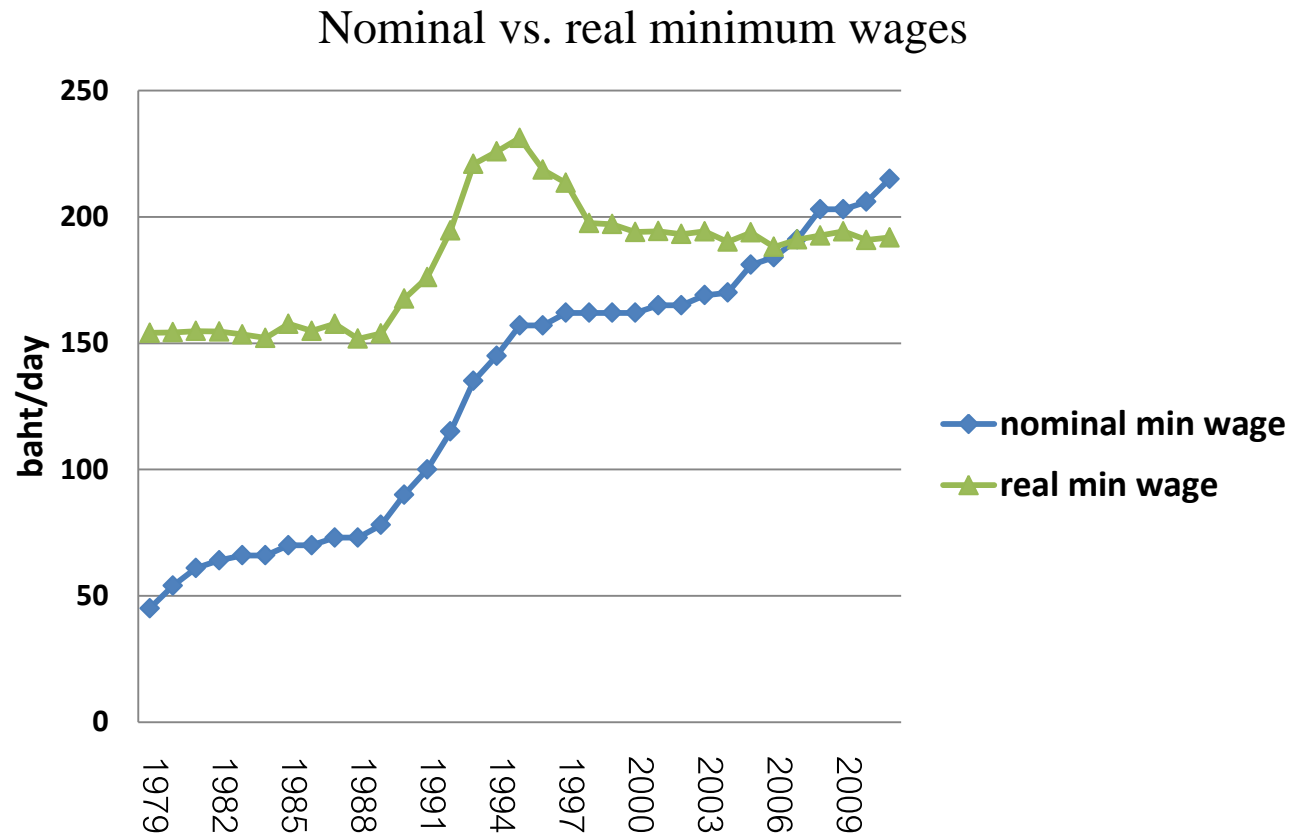
Jobs must be generated where the poor are located



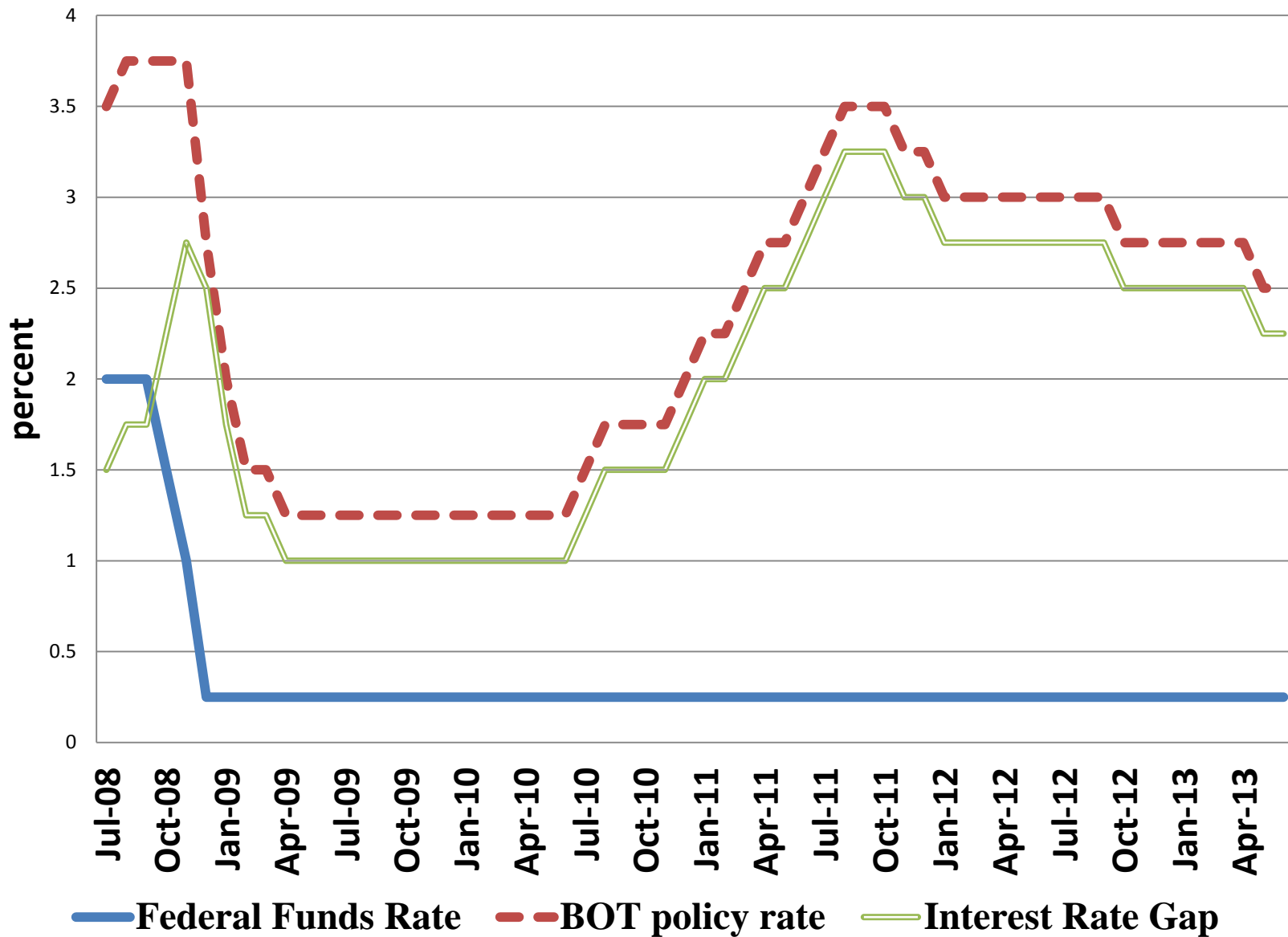
Monetary Strategy: Targeting Core Inflation 1986-2012



Minimum wage rate in 2013: 300 baht (USD10)



Key Policy Rates: Independent monetary policy



Empirical evidence

- A Vector Autoregressive model is constructed to examine the impact of monetary policy on output growth and inflation.
- The model employs monthly data from 2001 to 2011.
- All data are obtained from statistical data base of the Bank of Thailand.

Empirical evidence

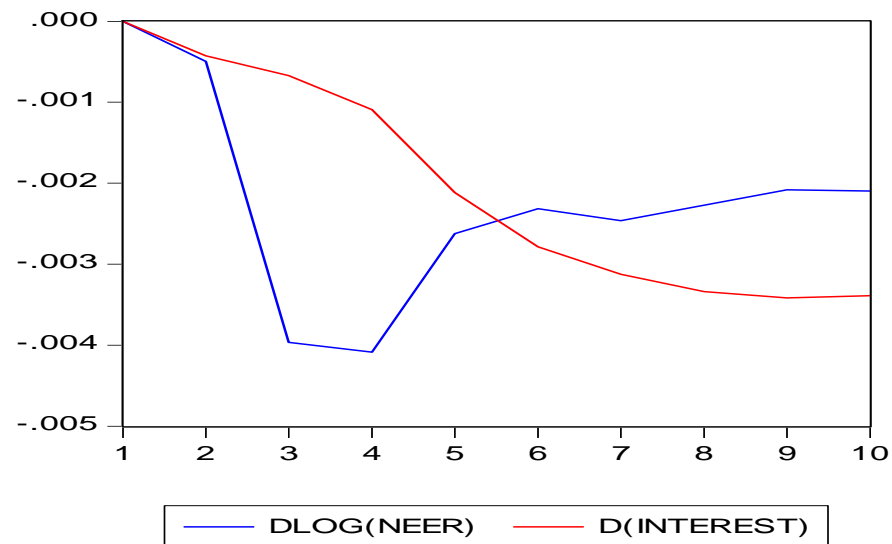
- There are five variables in the model: output (represented by manufacturing production index), the price level (consumer price index), employment (millions of employed workers), key policy rate of the Bank of Thailand, and the nominal effective exchange rate (NEER).
- The last two variables are policy instruments, while the first three variables are ultimate objectives of monetary policy.

Impact on *employment*

Exchange rate appreciation

Tight monetary policy

Accumulated Response of DLOG(EMPLOYMENT) to Cholesky
One S.D. Innovations

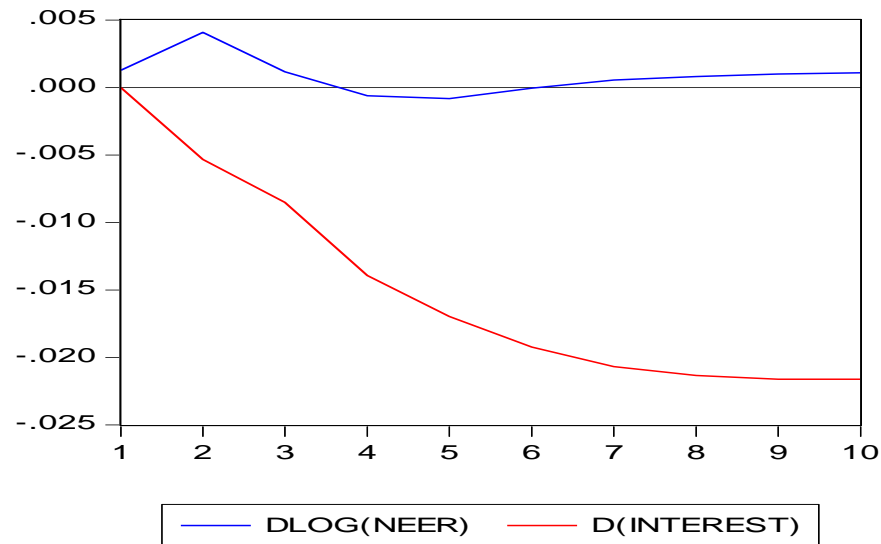


Impact on *output growth*

Exchange rate appreciation

Tight monetary policy

Accumulated Response of DLOG(OUTPUT) to Cholesky
One S.D. Innovations

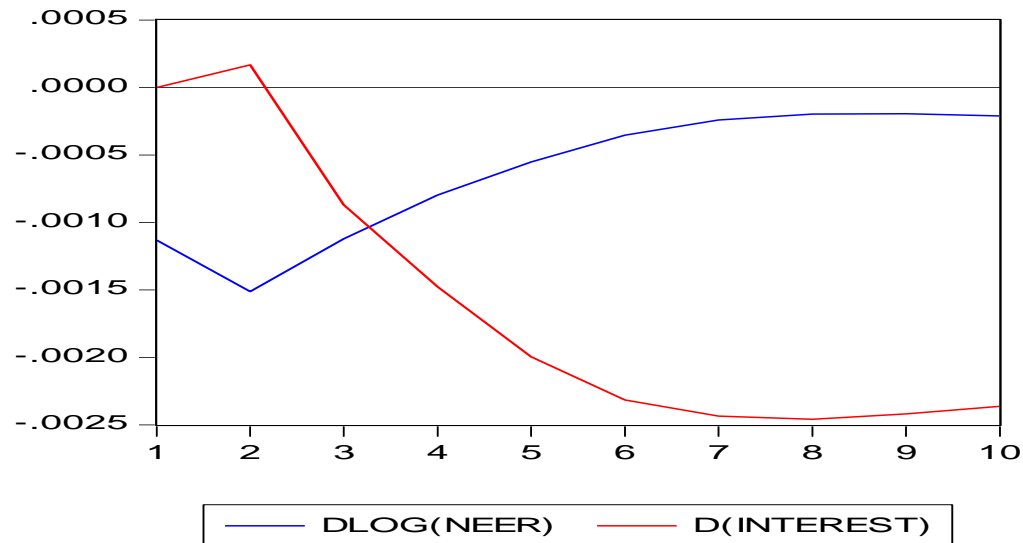


Impact on *inflation*

Exchange rate appreciation

Tight monetary policy

Accumulated Response of DLOG(PRICE) to Cholesky
One S.D. Innovations



Concluding remarks

- Monetary policy can be employed to minimize deviation from long-term growth path.
- Price stability can be maintained through using consistent macro policy mix.

Monetary policy

- Empirical evidence suggests that an increase in the key policy rate can effectively slow down output growth and dampen employment.
- Monetary policy can exert its impact on the labor market through changing output growth; thereby affecting the demand for labor.
- There is an impact on the labor market of changes in monetary policy stance.

Monetary policy

- The impact of changes in the key policy rate on employment is ***stronger*** than changes in the nominal effective exchange rate,
- Because consumption and investment are interest-sensitive components of aggregate demand, which respond to changes in the cost of borrowing.

Exchange rate policy

- Changes in the exchange rate indirectly affects productivity improvement enabling importation of high productivity capital goods
- The cost of imported capital goods must be reflected by the realistic exchange rate.
- An appreciation of the nominal effective exchange rate exert a deflationary impact on employment, but not significantly on output.

Exchange rate policy

- Exchange rate appreciation can lessen the inflationary pressure from supply shocks.
- If the exchange rate is allowed to become more realistic, and capital account becomes more liberalized, the benefits of external liberalization can accrue to labor in the form of productivity improvement in both agricultural and service sectors.

Capital account management

- Restrictions of foreign direct investment in protected sectors have resulted in substantial disparities of capital-labor ratios between the agriculture and industrial sectors.
- Productivity growth in the agricultural sector lags behind those in the manufacturing and services sector; thereby widening income gaps of people in urban and rural areas.

- Monetary policy is effective in stabilizing the economy, but it should be employed in line with fiscal policy stance.
- Some novel goals of inclusive and quality growth **require** other policy mix to bring about the benefits of growth to the vulnerable.

- Monetary policy should not be employed for micro objectives that might lead to distortion of resource allocation.
- If growth with stability can be achieved, the Central Bank can obtain a broader goal of poverty reduction.