

## Thailand Macro Flash

### Protracted Crisis Sustains a 'Live' Portfolio Bond Exit Risk Given Non-Resident Holdings of US\$20.8bn

■ **NACC 'discount'** — The National Anti-Corruption Commission (NACC) is filing legal charges against PM Yingluck because she condoned alleged corruption in the rice pledging scheme, as was signaled earlier in previous reports. This could create conditions for a 'judicial coup' if PM Yingluck is found guilty by the Court before a formal government/Parliament is in place. Similar to a previous political incident years back, chances are the Court may have to 'appoint' a caretaker government if PM Yingluck is declared guilty and removed from office. Post-Feb elections, government remains in a caretaker status with by-elections for other districts without 'representation' planned in Apr, needed to complete the necessary quorum in Parliament. This plays well into opposition leader Suthep's demand for PM Yingluck to step down and another caretaker government appointed to institute reforms before elections. In the meantime, police security forces are reclaiming 'protest' sites that escalate potential for violence between the police and opposition groups.

■ **THB risk resulting from non-residents unwinding portfolio bond exposure** — While legal drama unfolding may usher the NACC discount on the local currency assets, non-residents' (NR) unwinding portfolio bond exposure on the back of a prolonged crisis, would constitute a larger direct risk to THB. As of Jan 2014, NR holdings of outstanding local government bonds stood at US\$20.8bn (Bt685bn) of which US\$17.3bn are government bonds. Current NR bond exposure has fallen from the record high of US\$28.7bn-US\$29.7bn in Mar-Apr that probably put pressure on BoT's official reserves (while its forward book was kept intact) at a time when current account funding risk intensified. As a share to local government debt, NR exposure accounted for 10.1% in Jan down from 12.7% share in Mar. In our recent note, BoT's forward book has narrowed by less than US\$1bn (swap contracts not rolled over) since start of 2014 to beef up reserves and for 'intervention' to ease THB weakness to within 33 (see *Thai Macro Flash*, 2/14).

■ **Not just a liquidity adjustment** — Should we worry when NR bond investors unwind their exposure in response to the protracted crisis? Not to worry, since BoT's official reserves stood at US\$167.6bn while its forward book is down to US\$22bn during the week of 7 Feb. Both the official and 'shadow' reserves can easily address portfolio exit risk of offshore bond investors. However, in true BoT fashion, we don't sense its intervention to ease THB vulnerability from bond portfolio exit risk would primarily take the form of selling USD only. We suspect BoT would accommodate a weaker THB since portfolio bond exit this time around could last until political risk has diminished materially. When stability beckons likely coincident with THB prospects and in a sense, exchange gains, firm up, would portfolio flows find it more appealing to rebuild long positions. With extended political uncertainty, we continue to argue that THB upside to 33.50 cannot be ignored particularly when a portfolio bond exit overhang remains an issue.

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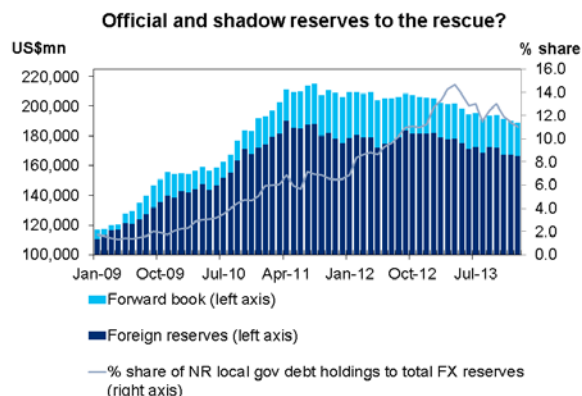
## Protracted crisis sustains a 'live' portfolio bond exit risk given non-resident holdings of US\$20.8bn

Figure 1. Still a THB risk if US\$20bn worth of portfolio bond investments are unwound due to the protracted crisis



Source: CEIC, Citi Research

Figure 2. Non-resident holdings of local government debt account for roughly 11% of total FX reserves (official and forward book)



Source: CEIC, Citi Research

## Appendix A-1

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