

The Thai Baht and Gold¹

October 2, 2020

“All that is gold does not glitter, not all those who wander are lost; the old that is strong does not wither, deep roots are not reached by the frost.”

~ J.R.R. Tolkien

The Lord of the Rings: The Fellowship of the Ring

- Background:** Prior to 1939, Thailand was known by the exonym, *Siam*, said to be from the ancient *Pali* language word, *suvanṇabhūmi*, which means “Golden Land.”² The relationship between gold prices and the Thai baht appears to justify this moniker even in present times. Since 2018, more than 20 percent of the Thai baht’s daily volatility may be explained by changes in gold prices (Figure 1)—the strongest relationship among regional exchange rates (Figure 2). During this period, gold represented 3.5 percent of Thailand’s total international trade. Thailand’s share of gold exports has increased this year, to 7.2 percent of total exports, a consequence of both rising gold exports and shrinking non-gold exports.
- Unique Thai culture:** Gold is important to Thai culture, and is highly esteemed as an investment asset and a store of value. Next to cash, Thais perceive gold as a highly liquid asset that can be easily sold (Jaraskunlant and Kijboonchoo, 2016). Gold also plays an important role in religious ceremonies, and is a popular gift for newborns and weddings. It is typically kept not only in the form of jewelry and ornaments, but also in coins and bars. After India and China, Thailand is Asia’s third-largest gold market, with an estimated 7,000 gold shops and goldsmiths across the country, ranging from family-run stores to large chains (Singapore Bullion Market Association, 2020).
- Gold prices and the Thai baht:** Historically, gold prices have affected not only the Thai baht’s volatility but have added appreciation pressure to the currency. The strong correlation between the two means that the Thai baht tends to appreciate in periods when gold prices rise (Figure 3).³ The exception occurred in March this year, when high volatility in global markets led to a sell-off in emerging market assets, contributing to the divergence

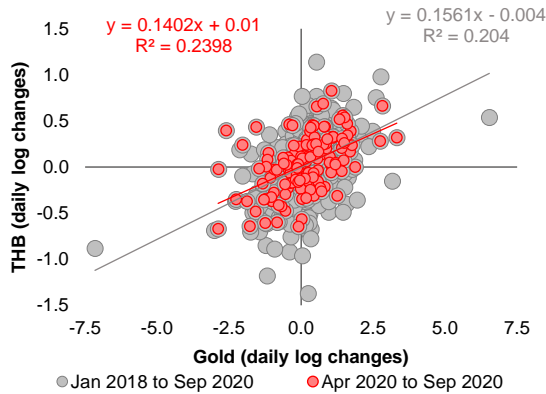
¹ Prepared by Prashant Pande (Financial Surveillance) and Ruperto Majuca (Thailand desk economist); reviewed by Li Lian Ong (Financial and Regional Surveillance) and Jae Young Lee (Thailand mission chief); authorized by Hoe Ee Khor (Chief Economist). The authors would like to thank Diana del Rosario for useful comments. The views expressed in this note are the authors’ and do not necessarily represent those of the AMRO or AMRO management.

² <https://www.bullionstar.com/gold-university/thailand-gold-market>.

³ The correlation coefficient for daily data from January 2018 is 0.42.

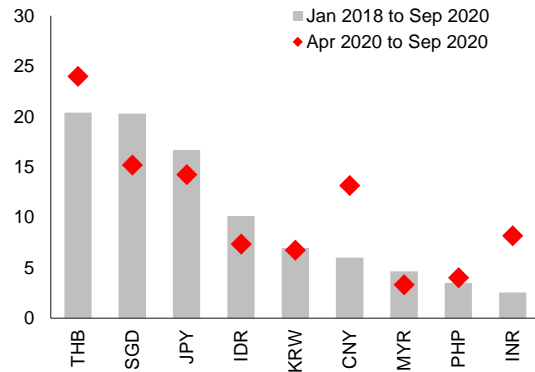
between the Thai baht and gold prices. The relationship has resumed since April—following the subsidence in market volatility—in conjunction with the sharp increase in Thailand's net gold exports as gold prices (Figure 4).

Figure 1. Thailand: Daily Changes in Gold Price and the Baht
(In percent relative to the US Dollar)



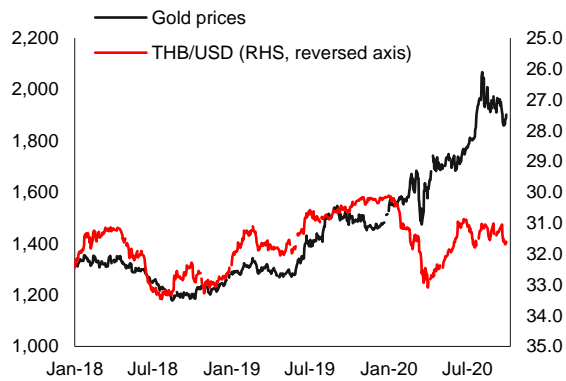
Sources: Bloomberg Finance L.P.; and AMRO staff calculations.

Figure 2. ASEAN+3: Daily Volatility in Exchange Rates Explained by Gold Prices
(Percent)



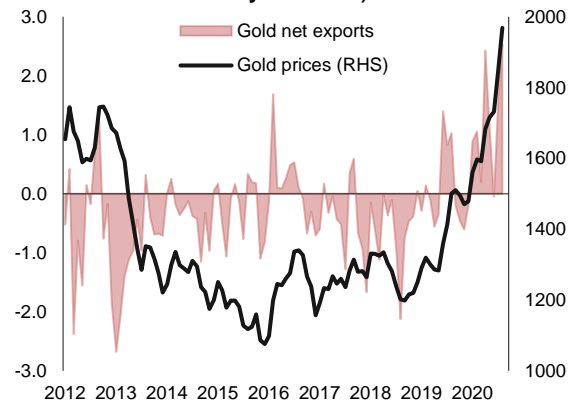
Sources: Bloomberg Finance L.P.; and AMRO staff calculations.

Figure 3. Gold Prices and Thai Baht Levels
(US dollar per troy ounce; Thai baht per US dollar)



Sources: Bank of Thailand; CEIC; London Bullion Market Association.

Figure 4. Gold Prices and Thailand's Net Gold Exports
(Billions of US dollars; US dollars per troy ounce)

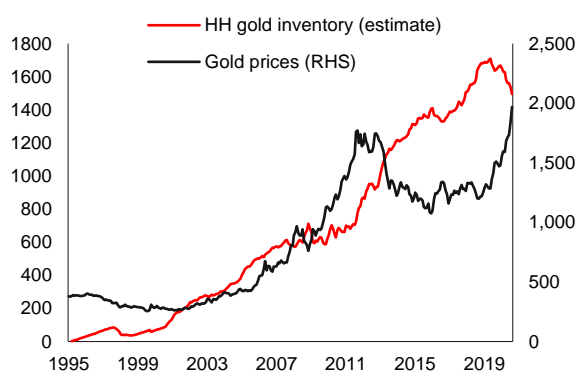


Sources: CEIC; Ministry of Commerce; The World Bank; and AMRO staff calculations.

4. The role of households: Many Thai households hold gold as personal reserves, for decades or even generations. They typically invest in physical gold and sell during economic downturns, or when gold prices rise (Saokaew, 2020; Chudasri, 2020). As the price of gold skyrocketed from early-2019—amid the uncertainty caused by the US-China trade conflict, followed by the COVID-19 pandemic—Thai households took the opportunity to divest their holdings, usually at local shops, which then sold them in the international market. While no official data is available as to the outstanding gold inventory among Thai households following the recent surge in selling, Thailand's accumulated trade deficit in gold serves as a useful proxy (Figure 5): Indications are that Thai households may have more gold to unload going forward, and thus gold prices may remain relevant for Thai baht.

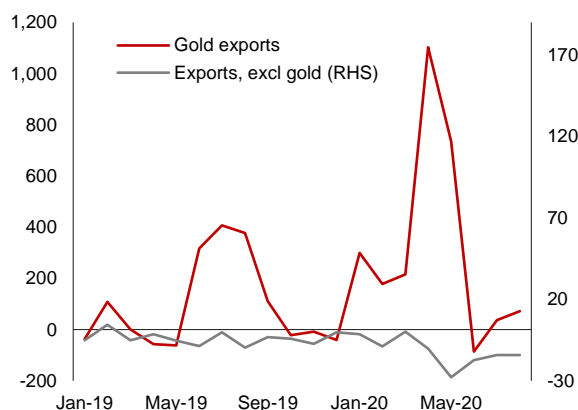
5. **Export patterns:** Despite not being a major gold producer, Thailand is the ninth-largest gold exporter in the world (as of 2019). Gold exports increased even as the country's overall exports fell during the COVID-19 pandemic, as a result of Thais selling their personal gold holdings. Thailand's gold exports surged in April, to 13.2 percent of its overall exports, diverging from the performance of its total exports excluding gold (Figure 6), and contributing to the currency's strength when sellers converted their US dollar proceeds back to Thai baht.

Figure 5. Gold Prices and Thailand's Estimated Gold Inventory
(kilograms; US dollars per troy ounce)



Sources: CEIC; Thailand Ministry of Commerce; The World Bank; and AMRO staff calculations.
Note: The household gold inventory is defined as net imports in kilograms derived from monthly net imports in US dollars divided by gold prices.

Figure 6. Thailand: Gold Exports and Total Exports Excluding Gold
(Percent year-over-year)



Sources: CEIC; Thailand Ministry of Commerce; and AMRO staff calculations.

6. **Gold futures:** The Thailand Futures Exchange (TFEX) is another channel through which gold is traded in Thailand. Over the past couple of years, trading volumes in gold futures on the TFEX have picked up when gold prices have risen (Figure 7). The net open interest in gold has also declined, pointing to the liquidation of long positions (that is, the selling of gold) as prices increased—further evidence that rising gold prices are stimulating exports of the valuable metal.

7. **A pro-active central bank:** The Bank of Thailand (BOT) has been on the front foot in trying to de-link gold trading and the Thai baht, to remove any unnecessary “noise” from the currency's volatility. Following the surge in gold prices and the country's corresponding increase in gold exports in Q3 2019, the BOT relaxed regulations on gold trade currency settlement in November 2019. From November 8, 2019, Thai residents are permitted to use foreign currencies in gold trading by opening foreign currency deposit (FCD) accounts with onshore banks.⁴ In the wake of the recent spike in gold prices and corresponding rise in Thailand's gold exports, the BOT conducted discussions with market participants to assess whether additional measures, such as shifting the price quotation for gold transactions to US dollars, would facilitate a move away from trading in Thai baht.

8. **Underlying macro-financial factors:** Ultimately, the main factor behind the Thai baht's strength is attributable to its strong overall balance of payments (BoP). While gold

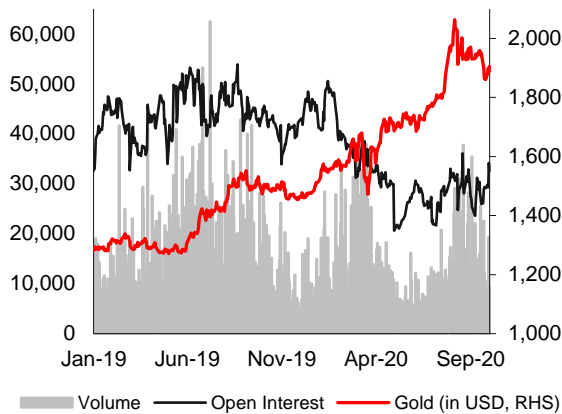
⁴ Prior to the relaxation in the regulation, gold trading could only be conducted using the Thai baht. The new regulation allows gold traders to retain the foreign currency acquired from selling gold in FCD accounts, which they can then utilize for future purchases, instead of having to convert immediately to Thai baht (Bank of Thailand, 2019). This flexibility allowed traders to keep their funds in foreign currency longer, hence reducing any impact on the Thai baht.

prices affect the Thai baht's volatility and strength, current and financial account dynamics are more important determinants (Figure 8). They include:

- a faster decline in Thailand's imports relative to exports (Figure 9), as both consumption and investment significantly contracted during the COVID-19 crisis, in addition to reduced imports of intermediate inputs used in the production of exported goods; and
- the repatriation of Thais' overseas investments (direct, portfolio, currency and deposits) (Figure 10), as households and corporates brought assets home to supplement lost income and, at the same time, reflecting risk aversion and lack of investment opportunities abroad.

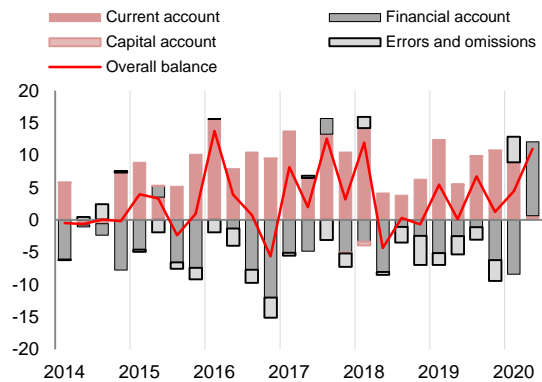
Figure 7. Thailand: Gold Trading Volume and Open Interest on the TFX

(Number of contracts; US dollar per troy ounce)



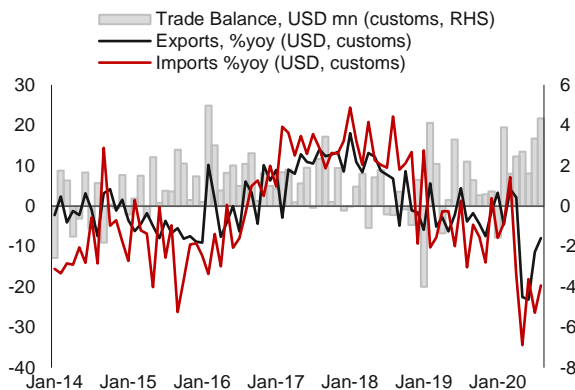
Sources: Thailand Futures Exchange; and AMRO staff calculations. Note: Trading volume and open interest are for GF10 (THB10 gold futures) and equivalent amount of GF (THB50 gold futures) contracts. Gold volatility is the three month implied volatility of gold prices.

Figure 8. Thailand: Balance of Payments (Billions of US dollars)



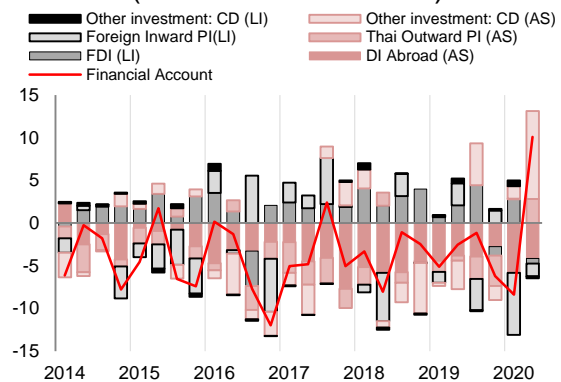
Sources: Bank of Thailand; CEIC; and AMRO staff calculations.

Figure 9. Thailand: Trade Balance (Percent year-over-year; billions of US dollars)



Sources: CEIC; Thailand Ministry of Commerce; and AMRO staff calculations.

Figure 10. Thailand: Financial Account (Billions of US dollars)



Sources: Bank of Thailand; CEIC; and AMRO staff calculations. Note: AS = Assets, LI = Liability, PI = Portfolio Investment, FDI = Foreign Direct Investment, DI = Direct Investment, CD = Currency and deposits.

9. **Conclusion:** In summary, gold prices have, to some extent, contributed to the volatility and recent strength of the Thai baht. The measures introduced by the BOT relating to gold trading currency settlement may help de-link the Thai baht from developments in gold markets. However, given the more important BoP factors supporting the Thai baht's strength, it may be more effective to also increase domestic public infrastructure investment and further liberalize capital flows.

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