

THAILAND ELECTIONS

Summary

Thailand will hold its general elections on 3 July 2011. At present, Prime Minister Abhisit Vejjajiva's Democrat Party leads the government in a coalition of seven parties, although they have fewer seats than the largest party Puea Thai, linked to fugitive ex-Prime Minister Thaksin Shinawatra.

We see three possible broad outcomes:

- 1) Puea Thai wins enough seats to form a government
- 2) Democrats win less seats than Puea Thai but form government with coalition parties
- 3) Democrats win enough seats to form a government

We are short term cautious in Thailand ahead of the elections, as we view the election results too close to call. While we like valuations of Thai banking and property sectors on a fundamental basis, political risks may weigh on performance in the short term. We believe that the second scenario outlined above (Democrats form the government with coalition parties) is the most likely, followed closely by the first scenario (Puea Thai forms the government) and the lowest probability tied to an outright win by the Democrats. With that, we view the risk-rewards not attractive enough for the market to outperform. The market has underperformed recently as political risks re-emerge, and is likely to trade sideways until there is more clarity on the election outcome.

If the Democrats form the government without major post-election disputes by the Red shirts, we would see weakness in the market as opportunity to buy stocks with good medium term earnings visibility from improved political climate such as banks and consumer. However, we will be more cautious should the Puea Thai lead the government as lingering political uncertainty could weigh on performance of the market and the valuation discount to the region could widen.

Thailand Elections

Thailand will hold its general elections on 3 July 2011. At present, Prime Minister Abhisit Vejjajiva's Democrat Party leads the government in a coalition of seven parties, although they have fewer seats than the largest party Puea Thai, linked to fugitive ex-Prime Minister Thaksin Shinawatra. Having come into power with the backing of the military after Thaksin and his party were ousted in a series of interventions from late 2006, the Democrats' mandate to rule has been the bone of contention between Thaksin supporters 'Red shirts' and the government, culminating in clashes between protesters and the military with the last major riot ending in violence last April – May.

At this point, polls are mixed and the results too close to call whether the incumbent Democrat party will continue to form the government or will there be a shift of power to Thaksin's Puea Thai party. Based on public opinion surveys, opposition Puea Thai party appears to be gaining popularity, led by Thaksin's sister Yingluck Shinawatra. Another factor adding to the uncertainty is the allegiance of other smaller parties.

We see three possible broad outcomes:

1) Puea Thai wins enough seats to form a government

In recent surveys, the likelihood has risen that Puea Thai may win enough seats to form the government either by itself (by winning majority of the seats) or with coalition parties. The market may take this negatively due to heightened medium term political risks. There are fears that a Puea Thai-led government will be unstable due to potentially unfavorable reactions from the military, as Puea Thai's priority seems to be demanding a pardon for Thaksin.

2) Democrats win less seats than Puea Thai but form government with coalition parties

If the Puea Thai emerges as the largest party but is unable to form the government, then the second largest party (likely the Democrats) will have the chance to form the government with other parties. In the short term, there could be some uncertainty while the parties negotiate with smaller parties, and possibility that the 'Red shirts' riots again, questioning the election results.

We view this outcome as medium term positive as continuity in government is good for consumer and business confidence. This should see some medium term political stability as the elections would give Democrats some form of mandate even if it has less seats than the Puea Thai.

3) Democrats win enough seats to form a government

An outright win by the Democrats would be positive for the market as political stability would return with Red shirts having little cause to dispute the mandate of the government.

Outlook and Strategy

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While we do not see major economic policy differences between the two main parties, we expect politics to be an important factor in driving economic growth and market performance. Political instability may lead to de-rating of the market relative to the region, as consumer and business sentiment turn sour on fears of further protests and possible military intervention. After the last military coup in 2006, Thailand's economic growth was lower than other Southeast Asian economies and the market traded at a deep valuation discount to the region.

Over the last twelve months, the Thai market's discount to the region has narrowed as the perception of the political situation improved and the economy delivered strong GDP growth, riding on the back of recovery of global trade. Current valuations are no longer as attractive on a relative basis and the Thai economy is also facing global headwinds of a soft patch and rising inflation in the coming quarter.

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