

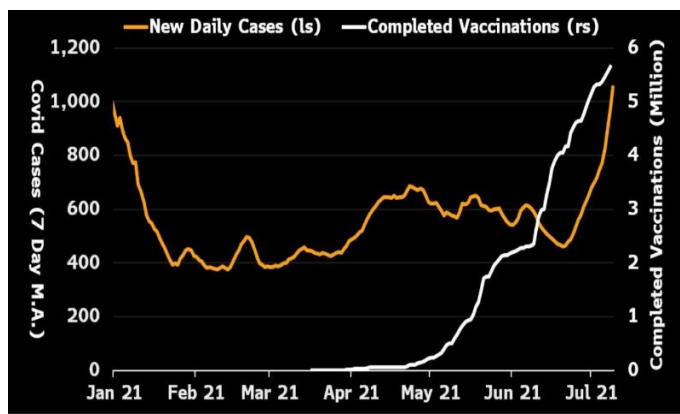
## MNI BoK Review – July 2021

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### MNI POV: Hawkish Dissent Surprises

The BoK kept rates on hold as widely expected, but did not adopt the dovish tone that most thought would be forthcoming. In the press conference Governor Lee noted that the decision was not unanimous, Dr. Koh Seungbeom voted for a hike. Dr. Koh has previously worked for the Financial Services Commission (FSC) and as such places an emphasis on risks to financial stability. Lee noted that many of the members were cognisant of potential financial imbalances, and also said that one or two hikes wouldn't be enough to address a financial imbalance.

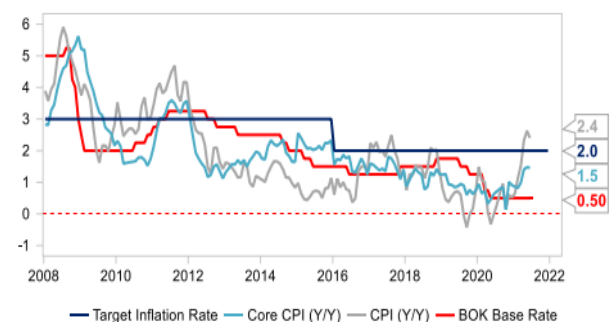


While the statement from the BoK and subsequent press conference did acknowledge downside risks from the latest surge in coronavirus cases MPC members were surprisingly upbeat. Lee noted that he is still confident that GDP projections of 4% from May are accurate, citing the vaccine rollout and noting the strength of the global economic recovery. He also said exports, investment and further fiscal stimulus will help to offset the drag from the fourth wave of coronavirus. **(Fig.1 Cases v Vaccinations, Source: Bloomberg)**

As well as maintaining growth forecasts the MPC noted upside risks to inflation, specifically mentioning building pressure in demand side inflation. Lee acknowledged that CPI could run above target in the near term, which suggests the BoK are likely to upgrade inflation forecasts in August and, along with financial stability risks, is another supporting factor for policy normalisation.

**(Fig.2 BoK Rate, CPI, Inflation Target, Source: Macrobond/UOB)**

Source: Macrobond, UOB Global Economics & Markets Research



The Governor indicated that August could be a live meeting, saying that next meeting would be the time to discuss adjusting policy, he also added that one or two hikes should be interpreted as normalising policy, as opposed to outright tightening.

## MNI STATE OF PLAY: BOK Holds Rates, Weighs Pandemic, Inflation

The Bank of Korea on Thursday warned of uncertainty over the outlook for the economy on the latest increase in coronavirus cases as it kept monetary policy unchanged, maintaining its base rate at a historical low of 0.5%.

"In this process the Board will judge whether it is appropriate to adjust the degree of accommodation while thoroughly assessing developments related to COVID-19, changes in the pace of growth and inflation, and the risk of a buildup of financial imbalances," the BOK said.

The decision had been widely expected as seen in MNI's story published Wednesday. The next policy meeting is scheduled on Aug. 26, after the release of GDP for the second quarter on July 27.

"The Board will continue to conduct monetary policy in order to sustain the recovery of economic growth and stabilize consumer price inflation at the target level over a medium-term horizon, while paying attention to financial stability," a statement issued by the BOK said.

Bank officials are concerned about high housing prices and prolonged easy policy, but they are now weighing those elements against the potential impact of the spread of coronavirus on economic activity.

It also said, "The Board will maintain an accommodative stance of monetary policy as there remain uncertainties posed by the virus, although the Korean economy is expected to continue its recovery and inflation to remain at a high level for some time."

But the BOK warned, "Household loan growth has remained high, showing a record level on a first-half basis, and housing prices have continued to increase rapidly in all parts of the country."

BOK Governor Lee Juyeol has flagged future rate hikes, saying that the bank should normalize its monetary policy in an appropriate timing if the economy continues recovery. He also said that the bank stands ready to scale down its easy policy amid accelerating inflation rate and growing financial imbalances.

As for the outlook for economy, the BOK said, "exports and investment will sustain their buoyancy, while private consumption is forecast to temporarily weaken affected by the coronavirus resurgence but then return to the path of recovery supported by the execution of a supplementary budget. GDP growth this year is projected to be around 4%, consistent with the forecast in May."

The government imposed its strictest social distancing rules in Seoul for two weeks from Monday and daily cases hit a new record high of 1,615 on Wednesday.

## Monetary Policy Statement

The Monetary Policy Board of the Bank of Korea decided today to leave the Base Rate unchanged at 0.50% for the intermeeting period.

Currently available information suggests that the recovery of the global economy has strengthened, supported by accelerated vaccinations and the relaxation of restrictions on economic activity in major countries. In global financial markets, stock prices have continued to rise, reflecting the economic recovery. The US dollar has strengthened, while long-term government bond yields have declined considerably due mainly to the spread of COVID-19 variants. Looking ahead, the Board sees global economic growth and global financial markets as likely to be affected largely by the severity of the resurgence of COVID-19 and the status of vaccine distribution, as well as by national policy responses and their effects.

The Korean economy has continued its sound recovery. Exports and facilities investment have sustained their buoyancy and private consumption has shown improvement. Labor market conditions have continued to improve, with the year-on-year increase in the number of persons employed remaining high. Going forward, exports and investment will sustain their buoyancy, while private consumption is forecast to temporarily weaken affected by the coronavirus resurgence but then return to the path of recovery supported by the execution of a supplementary budget. GDP growth this year is projected to be around 4%, consistent with the forecast in May.

Consumer price inflation has remained high at the mid-2% level due to the rising prices of petroleum products and agricultural, livestock, and fisheries products as well as the accelerating increase in service prices. Core inflation (excluding changes in food and energy prices from the CPI) has run at the lower-1% level. The inflation expectations of the general public have risen slightly to the lower-to mid-2% range. Looking ahead, it is forecast that consumer price inflation will continue to run in the lower- to mid-2% range for some time, exceeding the path projected in May. Core inflation is forecast to increase gradually to the mid-1% range.

In domestic financial markets, stock prices and the Korean won to US dollar exchange rate have risen, mainly driven by global financial market movements. The 3-year Korean Treasury bond yield has risen considerably, while the 10-year yield has fallen. Household loan growth has remained high, showing a record level on a first-half basis, and housing prices have continued to increase rapidly in all parts of the country.

The Board will continue to conduct monetary policy in order to sustain the recovery of economic growth and stabilize consumer price inflation at the target level over a medium-term horizon, while paying attention to financial stability. The Board will maintain an accommodative stance of monetary policy as there remain uncertainties posed by the virus, although the Korean economy is expected to continue its recovery and inflation to remain at a high level for some time. In this process the Board will judge whether it is appropriate to adjust the degree of accommodation while thoroughly assessing developments related to COVID-19, changes in the pace of growth and inflation, and the risk of a buildup of financial imbalances.

## Sell-Side Reviews

**ING:** At their policy meeting today, the Bank of Korea left the policy 7-day repo rate unchanged at 0.5%. But one of the board members dissented, preferring an immediate rate increase. We see this as the BoK laying down a clear marker of their intended direction, though with only one dissenter, this keeps their options open in terms of the timing. Two dissenters would have signalled a more imminent policy change. We are currently favouring the October policy meeting as the likely date of the first hike. The key text in the statement, which was released along with the decision is *"The Board will maintain an accommodative stance of monetary policy as there remain uncertainties posed by the virus, although the Korean economy is expected to continue its recovery and inflation to remain at a high level for some time. In this process the Board will judge whether it is appropriate to adjust the degree of accommodation while thoroughly assessing developments related to COVID-19, changes in the pace of growth and inflation, and the risk of a buildup of financial imbalances"*.

**Barclays:** As widely expected, the Bank of Korea (BoK) maintained its 7- day repo rate at a record low of 0.50% today. However, one monetary policy board (MPB) voted for a 25bp rate hike. This is against our view of a unanimous hold. BoK Governor Lee Ju-yeol said the dissenter was Koh Seung Beom, who spent most of his career in the Financial Services Commission (FSC) and has tended to place greater emphasis on financial stability risks. The meeting minutes will be released on 3 August, which will be key for market to assess the probability of an August hike, in our view.

**HSBC:** While the Bank of Korea (BoK) kept the policy rate unchanged at 0.50 as widely expected, the decision was not unanimous as Dr. Koh Seungbeom voted for a hike. This was in line with market expectations, but HSBC had forecast a unanimous decision. The dissent was despite the record number of COVID-19 cases and social distancing measures raised to the maximum level in the Seoul Metropolitan Area where half of Korea's population reside. Hinting at near-term action, Governor Lee said that most of the policy board are still focused on financial imbalances and added that, if the fourth wave turns out to be temporary, he believes there should not be any further delay (in normalization). Moreover, since April 2014 when Mr. Lee became the governor, the BoK has hiked twice. The first in November 2017 was just one meeting after a dissenter and the second one in November 2018 was three meetings after a dissenter. We now forecast the BoK to hike the base rate by 25bp to 0.75% at the next meeting on 26 August.

**JP Morgan:** As widely expected, the Bank of Korea maintained the base rate in the July meeting. Yet, the overall communication from the official MPC statement and the governor's press conference was hawkish, and there was a hike dissent vote from MPC member Koh. We had expected a close call for one dissent vote in the July meeting in our MPC preview, but from MPC member Cho, based on our reading of the May meeting minutes. While we wait for more clarity in each member's stance from the July minutes release due in early August, one hike dissent vote in July suggests initiation of the hike cycle in the upcoming two meetings (either in August or October).

**Goldman Sachs:** Bottom line: The Bank of Korea kept its policy rate on hold at 0.5%, as widely expected. One MPC member cast a dissenting vote calling for a 25bp rate hike, and the forward-looking section of the MPC statement opened the door for a rate hike as early as August. The BOK governor reiterated during the press conference that current macro conditions would warrant the start of gradual monetary policy normalization sooner rather than later, with the recent coronavirus resurgence effectively the only critical factor that counters a hike argument. Today's hawkish MPC meeting, together with the release of a detailed vaccine supply plan (35 million from now through end-August), meaningfully raises the odds of an earlier liftoff. While this is a close call, we bring forward the liftoff timing in our normalization roadmap, to August from October previously, followed by the second rate hike in November (vs. February 2022 previously).

**UOB:** In line with consensus and our expectation, the Bank of Korea (BoK) kept its benchmark base rate unchanged at a record-low of 0.50% today. One board member voted for a 25 bps rate hike as opposed to the previous meeting in May where the decision to keep the rate unchanged was unanimous. Governor Lee Ju-yeol was also steadfast in his guidance for rate normalisation to start this year despite the resurgence in domestic COVID-19 infections as he signaled a potential hike as early as August. This means that BoK's guidance leading up to the 26 August meeting will be crucial as is the domestic COVID-19 situation. We believe this is still contingent on the containment of the domestic infection rate before it becomes a larger drag on the economy.