

## Korea Data Brief: What you might have missed over the year-end holiday

Data clearly suggested the upturn of the semiconductor cycle to be Korea's main growth driver. But domestic growth deteriorated further due to tight credit conditions and risky real estate sector, weighing on overall growth. With inflation cooling to the 2% level, the Bank of Korea will have to consider the stability of the financial markets as well



Financial district in Seoul, South Korea

Thanks to solid global demand for semiconductors, manufacturing activity and exports should be the driving force behind growth after the fourth quarter of 2023, but we believe that the semiconductor boom won't be enough to drive overall growth. Services and investment are expected to contract as tight credit conditions will weigh more heavily on private consumption and investment entering 2024. The Korean domestic economy is likely to face strong headwinds as prolonged issues of construction and project financing will emerge in earnest, negatively impacting the growth throughout the first half of 2024.

Inflation cooled down more than expected in December and should reach the 2% range in the first quarter of 2024 with the help of government policies and falling commodity prices. But, after that, inflation will likely settle at the 2% level for a considerable time as accumulated inflation pressures,

such as delayed utilities and public service price hikes will be passed on to consumer prices. However, demand-driven price pressures will be set to die down with tight monetary conditions and sub-potential levels of growth.

With inflation anchored at the 2% level and the domestic economy suffering from tight credit conditions, the Bank of Korea (BoK) may begin its rate cuts from the second quarter at the earliest and deliver a total of 50bp in 2024.

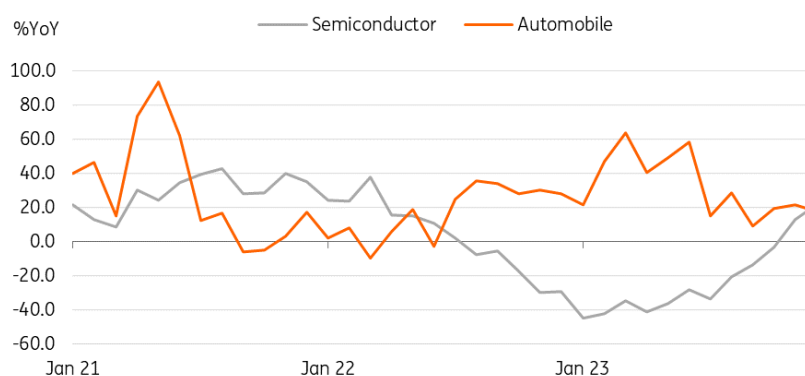
**5.1%** Exports  
%YoY

Higher than expected

## Exports gained for the third consecutive month thanks to solid semiconductor and vehicle shipments

Exports growth slowed to 5.1% year-on-year in December (vs 7.7% in November, 3.7% market consensus) due to unfavourable calendar effects. Eight out of 15 major export items increased with the most notable rise in semiconductors (21.8%) and vehicles (17.9%). The recovery in semiconductors is expected to continue to be led by new mobile model launches and increased investment in AI servers while vehicle exports have remained solid so far but are expected to lose some steam in the coming months. By export destination, exports to the US (20.8%), ASEAN (1.7%) gained while exports to China (-2.9%) and the EU (-20.0%) dropped. Imports declined -10.8% YoY in December (vs -11.6% in November, -11.1% market consensus) with falling global commodity prices. But consumer goods imports also dropped quite sharply (-10.0%), suggesting domestic demand weakened further. Combined with AI technology-driven semiconductor recovery and falling commodity prices, terms of trade will likely improve and the net export contribution to GDP should remain positive in the fourth quarter of 2023.

## Semiconductors and vehicles are the main drivers for export growth



Source: Government sources

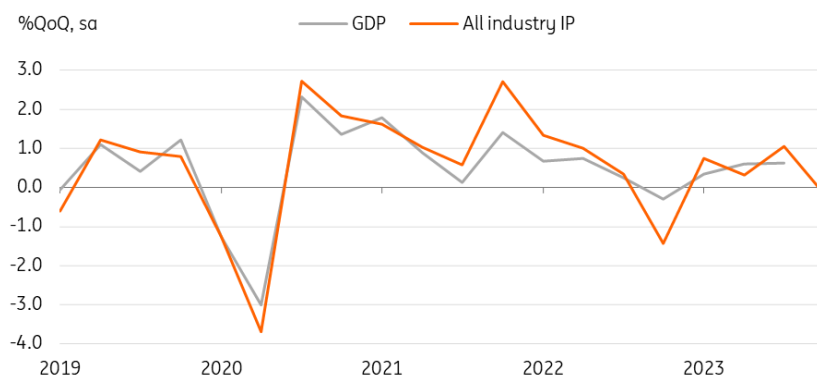
**3.3%** Industrial production  
% MoM sa

Higher than expected

## Manufacturing production rose stronger than expected, but all other industry activity contracted in November

All industry production edged up 0.5% month-on-month seasonally adjusted in November (vs -1.8% in October), narrowly driven by solid semiconductor output. Manufacturing IP gained a stronger than expected 3.3% (vs -3.8% in October, 1.4% market consensus) but did not fully offset the previous month's decline, and the gain was narrowly concentrated in semiconductors (12.8%) and related machinery while other major industries such as vehicles (-3.3%), electrical equipment (-1.5%), and basic metals (-5.7%) were down. Excluding manufacturing, other activities – services (-0.1%), construction (-4.1%), and public administration (-0.9%) all declined. Service activities fell for the second month as leisure-related services declined the most with accommodations (-2.0%), eating out (-0.3%) and recreation (-3.1%) down.

## Monthly IP suggested a quite sharp slowdown of GDP in 4Q23



Source: Government sources

## Retail sales rebounded but mainly due to government support

Retail sales rose 1.0% MoM sa in November (vs -0.8% in October) led by significant rises in vehicle sales (10.2%) and household appliances (5.1%), as both were supported by the government's tax benefits and shopping aid programme. Thus, we believe this month's rebound should be temporary and expect a negative technical payback in coming months.

## Investment should be the main risk factor for near-term growth, especially project financing-related issues

Both facility (-2.6%) and construction (-4.1%) outputs slid in November. Machinery orders gained for a second month thanks to the revival of the semiconductor cycle, but other orders remained soft. Construction orders continued to decline and thus the ongoing restructuring of project

financing and poor housing market will be the main risk factors for the economy.

## A major construction company applied for a debt restructuring programme

Over the Christmas holiday, Taeyoung E&C, one of Korea's largest builders (16th largest in terms of construction capacity), applied for a debt-restructuring programme due to a liquidity shortage, affected by large-scale project financing loans. The company owns quite valuable assets and subsidiaries, and thus the workout process will be processed smoothly in our opinion, with its direct negative impact on financial markets being quite limited. But, the real concern is that the industry itself has been suffering quite a long time from tight liquidity conditions amid a sluggish real estate market. The government and industry have supported several restructuring programmes since early last year but there will be more credit crunches, especially among small- and medium-sized local builders with high exposure to project financing loans, probably not covered by workout programmes. We believe that investor sentiment will be quite dampened for a while and non-IG credits will likely be hampered the most. As tight mortgage rules will be applied from early 2024 and higher borrowing costs to persist, we believe the slump in the property market will not only drag down investment but also consumption.

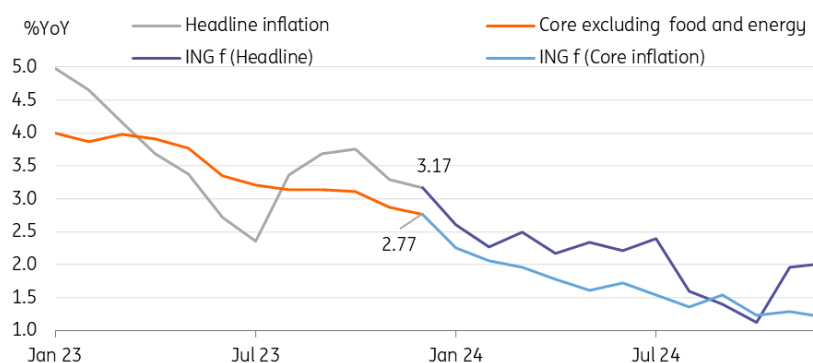
**3.2%** Consumer inflation  
%YoY  
Lower than expected

## Inflation slowed faster than expected in December mainly due to falling commodity prices

Consumer prices decelerated to 3.2% YoY in December (vs 3.3% in November and market consensus) mainly due to the sharp decline in petroleum prices (-4.5% MoM nsa) and rental prices (-0.1%). However, other major prices such as fresh food (2.1%), manufactured food (0.1%), and private services (0.3%) went up.

Going forward, the high base last year will bring down headline inflation quite sharply from early 2024. Also, we believe that government efforts to curb prices will continue to stabilise prices in the near future. The government decided to extend its fuel tax cut programme until February 2024 and reduce the liquor tax, while utility prices will likely be hiked in the second quarter. Most government programmes will probably come to an end in the second quarter. Then we expect utility and public service prices to rebound, and thus consumer prices will settle in the 2% range for a while. We see demand-side pressures softening due to tight monetary conditions and a sluggish domestic economy, and thus the Bank of Korea's policy will turn its direction in the second quarter at the earliest.

## Inflation will likely cool down quite sharply due to base effects and government support in 1Q24



Source: Government sources

## Survey results were stronger than expected but it did not change our cloudy near-term outlook

Consumer sentiment rebounded surprisingly in December, offsetting some of the previous four-month decline. The consumer sentiment composite index rose for the first time in five months to 99.5 in December (vs 97.2 in November). Future expected interest rate cuts by the Fed and the BoK and resilient labour conditions may have resulted in the biggest improvement in consumer confidence in the economic situation. We believe that a recovery in exports and equity markets also could be reasons for this month's unexpected turnaround, but we are not sure if the upbeat mood is temporary or sustainable from now on, as expectations on housing prices, which is the biggest risk factor for near-term growth and the most sensitive variable to sway consumer sentiment, have plunged for three months. Meanwhile, inflation expectations for the next 12 months dropped to 3.2%, the lowest since May 2022, and thus it could be a sign of relief for the Bank of Korea.

Despite the ongoing restructuring of the construction and project financing, the improvement in the business sentiment is believed to be largely due to the recovery of the semiconductor cycle. Local surveys conducted by the Federation of Korean Industry (95.2 in December vs 91.2 in November) and the Bank of Korea (72 in January vs 72 in December for manufacturing, 73 in January vs 71 in December for non-manufacturing) improved.

However, since the domestic construction industry is having trouble and credit conditions are expected to become tighter, we are cautious about giving a positive assessment of near-term future economic growth.

## Bank of Korea watch: Restrictive to Neutral but not to Accommodative

The Bank of Korea will be required to encompass not only price stability but also financial market stability and seek to induce an orderly soft landing of the domestic economy. We believe that the Bank of Korea's policy priority will shift from curbing inflation to stabilising the financial market in the first half of 2024 as tight credit conditions will begin to hit the economy. There have been some signs of it from the construction industry, surrounding bad project financing loans. But, the BoK's

cuts will inevitably be quite gradual. The ongoing efforts to slow down the excessive growth of private debt should be continued and the Fed's policy rate will remain higher than the BoK's throughout this year, which will hinder the BoK's aggressive rate cuts. Thus, we believe that the BoK will keep its policy rate at the neutral level and not enter into accommodative territory in 2024.

## Author

### Min Joo Kang

Senior Economist, South Korea and Japan

[min.joo.kang@asia.ing.com](mailto:min.joo.kang@asia.ing.com)

## Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies)*. The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit [www.ing.com](http://www.ing.com).