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Article

Korea central bank begins the tightening cycle

We forecast the next move to be a 25bp BoK policy rate hike in 2Q18 and expect the KRW to remain among outperforming Asian currencies in 2018

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1.5%

 The BoK policy rate

As expected

No surprises from the BoK today

Consistent with the consensus majority, the Bank of Korea Monetary Policy Committee decided to raise the policy rate by 25bp to 1.50% today, the first hike since 2011. The markets are priced for today's move, so the impact is expected to be muted. Surprisingly enough though, the Korean won (KRW) weakened by about 1% against the US dollar and government bonds gained. A strong rally in Korean risk assets and selloff in safe-haven treasury bonds since September coincided with a lull in North Korea's missile programme. Yesterday's missile launch failed to unsettle both markets and BoK policymakers.

A gradual policy normalisation

Is it one and done?

The MPC decision wasn't unanimous as there was a dissenter vote for no change in the policy rate. In his press conference Governor Lee pointed to near-potential growth and near-target inflation as factors warranting a policy adjustment to prevent risk of excessive accommodation. However, he also pointed to a continued accommodative stance, with an eye on financial stability to support growth. He was confident of the ongoing surge in semiconductor exports supporting growth in the period ahead. In essence, the governor's remarks imply a gradual normalisation of the policy. We forecast the next move to be a 25bp rate hike in 2Q18.

3.4% ING forecast of 4Q18 growth

GDP growth might have peaked

More October activity data released this morning pointed to slower GDP growth in the final quarter of 2017. As expected, surprisingly strong growth in industrial production and services activity in September was retraced in October, both contracting on a year-on-year basis. November export data due tomorrow will inform more about performance in the rest of the year. Our forecast of a modest slowdown in GDP growth to 3.4% in the current quarter, from 3.6% in the last, is on track. The consensus forecast is 3.3%.

KRW to remain Asia's top performer in 2018

Despite the unexpected market reaction today, the rally in the KRW and selloff in government bonds underway since September have room to run further. We expect the KRW to remain among the top performing Asian currencies in 2018. We have revised our USD/KRW forecast to 1,080 for end-2017 and to 1,000 for end-2018, from 1,110 and 1,050 respectively (spot 1,087).

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