

Bank of Korea delivered a 25bp hike in the absence of a governor

Bank of Korea rose its policy rate to 1.5% for the fourth time since the pandemic started, in order to contain intensifying inflationary pressure. As inflation is expected to climb further, the central bank will continue to stay on the hike cycle till the end of this year



Bank of Korea's
governor-nominee
Rhee Chang-yong

1.50%

 Bank of Korea policy rate

As expected

Bank of Korea is expected to raise rates by 50bps this year

In line with our expectations, the Monetary Policy Committee (MPC) has unanimously decided to raise its policy rate by 0.25%. As the market consensus was split sharply with almost 50:50 odds, the unanimous decision has left the market curious about the next hike. We do not expect an immediate rate increase in May – Bank of Korea (BoK) will take a breather, monitor the impact of rate hikes, and carefully study the future paths of growth and inflation. The MPC statement clearly expressed that today's decision was made based on heavier concerns about the inflation outlook,

thus further policy adjustments are needed, while the downside risk to growth is somewhat limited.

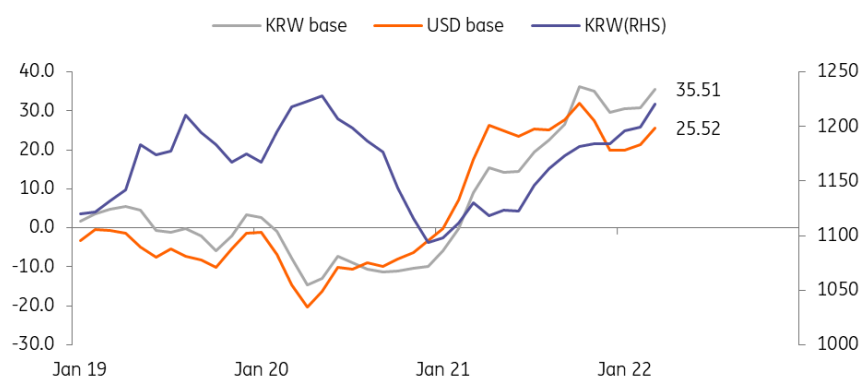
Bank of Korea will be cautious about future rate hikes

The negative impact of the Ukraine war and supply chain disruptions will feed through into data by July and August. As pipeline prices and global energy prices suggest, inflation will accelerate further into the second quarter of the year. On growth, export is expected to decelerate but be partially offset by improved domestic demand supported by expansionary fiscal policy and the reopening of the economy. We believe this will justify two more rate hikes in the second half of this year. However, once inflation begins to slow down in the third quarter of 2022, then BoK's focus will shift to financial stability and growth. Also, BoK will be keen to watch whether rate hikes moderate household leverage, including mortgages. At this point, we believe that BoK will put a brake on the rate hike at 2% as we estimate it is an approximate borderline between normalisation and tightening.

Pipeline prices hint that an inflation peak is not coming anytime soon

Import prices (Korean won base) soared 35.5% year-on-year in March (vs 29.4% in February), with a weak won adding more upside pressures. Raw materials prices went up the most, driven by a 90.4% gain in energy, while capital and consumer goods prices rose moderately by 6.3% and 7.2% respectively. Meanwhile, export prices also gained firmly by 22.8% in March (vs 20.5% in February). The weak won may be favourable for price competitiveness for Korean exporters and better earnings, but the faster growth of import prices than exports is likely to carry the risk of high inflation and trade deficit in the near term.

Import prices rose sharply mainly due to higher energy prices and a weak Korean won



Source: CEIC

What to watch from the next MPC meeting

With governor-nominee Rhee Chang-yong's parliamentary hearing scheduled for 19 April, we will closely listen to his views on the Korean economy and inflation at the hearing. If things go smoothly, the next MPC meeting will be chaired by Rhee as the new governor. There will also be another member change in the MPC, as Lim Jiwon ends her term in early May. As mentioned

earlier, we expect no change for the next meeting, but it is worth watching how the BoK assesses its future outlook of growth and inflation as it will release a revised macro outlook report. At today's press conference, acting chairman Joo Sang-yong commented that GDP is expected to revise down to around 2.8% while CPI will revise up to near 4%.

Author

Min Joo Kang

Senior Economist, South Korea and Japan

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 <http://www.ing.com>.