

Korea: consumer sentiment worsens while inflation expectations soar

The chances of a 50bp hike at the July MPC meeting have increased as inflation expectations rise to nearly 4%, while weak consumer sentiment indicates a slowdown in household spending and adds downside risk to the 3Q GDP forecast



Source: Shutterstock

3.9% Inflation expectations

The BoK's consumer confidence index fell sharply to 96.4 in June (vs 102.6 in May), falling below the long-term average of 100 for the first time since Feb 2021

All six sub-components for the consumer sentiment index (CSI) were down, with indices for both

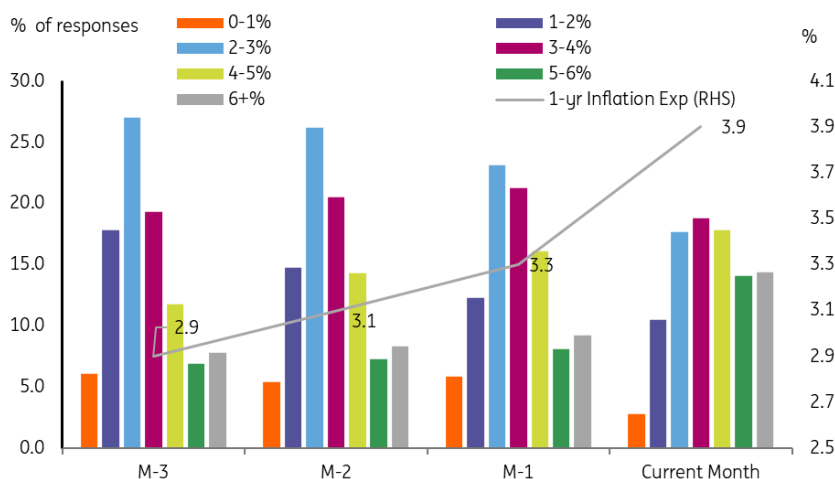
the current assessment and expectations on the domestic economic situation falling significantly (-14pt and -15pt respectively). Spending plans remained above the neutral level, but fell by 2pt, the first decline in four months. Expectations for travel, eating out, and recreation were weak especially ahead of the summer vacation season, and probably reflect higher fuel and service prices. The pent-up reopening boost in 3Q may end up being smaller than expected.

We expected the CSI to slip this month, but not to this extent. The decline in confidence now puts downside risk to our GDP forecasts (0.7% q/q sa in 3Q22). The KOSPI has tumbled by more than 9%MTD while the KRW has broken through the 1300 level. Also, mortgage/lending rates have risen further. All these factors are probably hurting consumer sentiment.

Today's highlight should be inflation expectations, which rose to 3.9% in June (vs 3.3% in May)

Inflation expectations reached 3.9% in June (vs 3.3% in May), which could be a bigger concern for the Bank of Korea (BoK) than the decline in consumer confidence. The BoK has already expressed concern about self-fulfilling inflation increases, in which expected inflation rises first then actual inflation rises accordingly. Additionally, the rate of increase of inflation expectations is quite fast. A 0.6pt increase in a single month is the biggest rise in recent history.

Inflation expectations rose sharply in June



Source: CEIC

The probability of realizing the "big step" scenario of the BoK is increasing, but...

We think that today's CSI outcomes send a conflicting message to the BoK. Rising inflation expectations increase the likelihood that the Bank of Korea will hike by 50bp in July. But at the same time, the sharp decline in consumer sentiment will add to concern over an economic slowdown. A sharp rise in interest rates could exacerbate falling sentiment as well as actual future spending. The Korean economy is in a recovery phase, but it is heavily dependent on economic reopening and fiscal stimulus. As domestic demand is the main driver of growth, rapid rate hikes would curb the recovery in consumption. This could keep the BoK on its current path of raising

rates in 25bp increments in July. We will check if the June CPI inflation rate exceeds 6% before committing to any forecast changes on our base case BoK call.

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>.