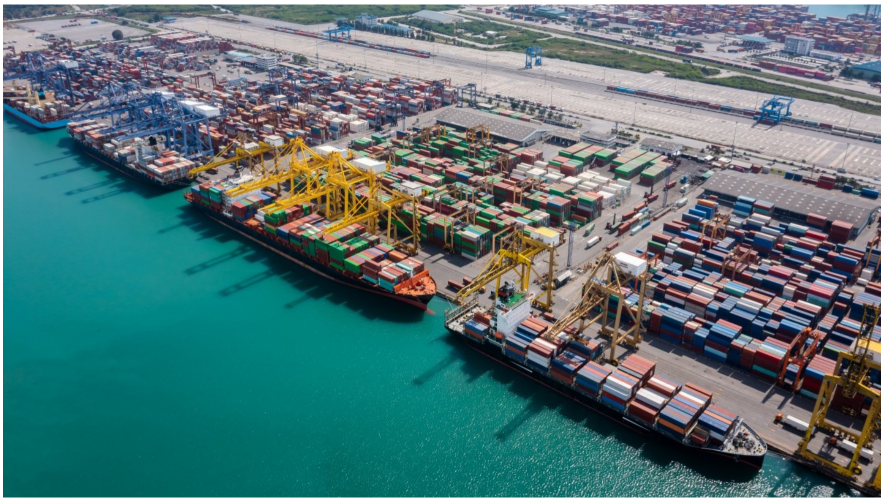
# South Korea: All-industry output contracted for the third consecutive month in July

Weaker-than-expected monthly activity data supports the Bank of Korea easing rates, but the timing remains uncertain



Source: shutterstock.com

-3.6%

Industrial Production

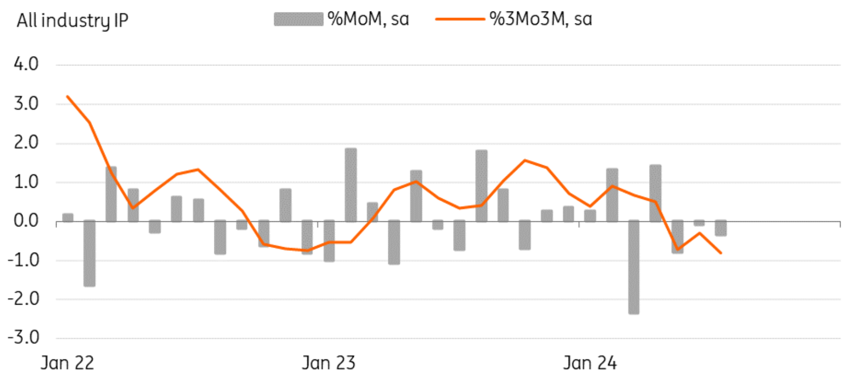
% MoM, sa

Lower than expected

## Industrial production fell but partly due to temporary reasons

Industrial production (IP) fell more than expected -3.6% MoM sa in July (vs revised 0.7% in June, -0.6% market consensus). The output for major manufacturing items such as semiconductors (-8.0%) and cars (-14.4%) dropped due to temporary factors, and we expect output to rebound in the coming months. The significant drop in car production was partly due to labour strikes and summer maintenance-related halts, while the decline in semiconductor output was probably due to inventory management rather than slowing demand. Still, we think overall production conditions deteriorated compared to the previous month as shipments fell -5.8% faster than production, and inventories increased by 2.6%. The weak IP growth in July is likely to weigh on GDP this quarter. We currently expect a 0.2% QoQ sa rebound but downside risks to that forecast grew based on today's outcome.

## All industry output declined for a third month



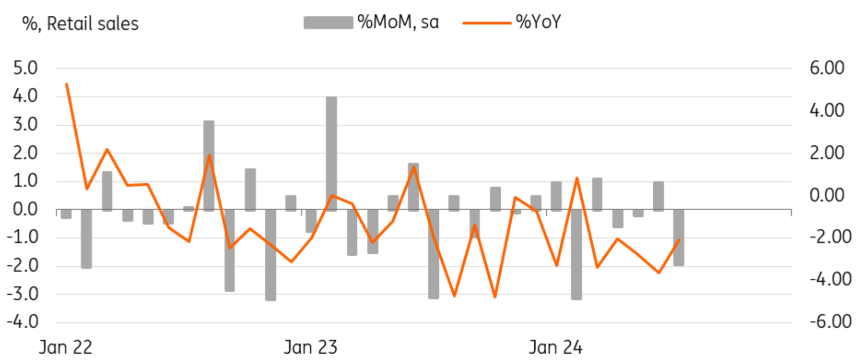

Source: CEIC

## Service sector is brighter

In contrast to industrial production, service sector output rose 0.7% MoM sa in July (vs 0.3% in June). Retail/wholesale (0.1%), transportation (3.1%), and communications (4.5%) rose while accommodation & eating out (-2.8%), and leisure services (-1.3%) continued to drop.

Retail sales fell significantly -1.9% MoM sa in July, more than wiping out the 1.0% rise in the previous month. On a three-month trend basis, retail sales have now contracted for five months (-0.23% in July) and we expect this contraction to deepen in the coming months, which will be a major drag on growth in the current quarter.

## Weak retail sales continued




Source: CEIC

## Equipment investment is a bright spot

Equipment investment jumped 10.1% MoM sa in July, boosted by a rise in aircraft investment (111.4%), which tends to be volatile from month to month. However, motor vehicle investment also rose solidly by 14.5%. Among today's data outcomes, equipment investment gains were the most notable. Combined with the solid increase in forward-looking machinery orders, we continue to expect facility investment to remain a key driver of growth for a couple more quarters.

Meanwhile, construction investment declined for the third month in a row and orders received fell too. Inventories of unsold units have not reduced meaningfully, suggesting construction will struggle for several quarters to come.

## What does this mean for the Bank of Korea?

Signs of weakening growth are becoming ever more apparent, and we expect consumer inflation to fall below 2% YoY in August. Macro conditions clearly support policy easing by the Bank of Korea (BoK). We still think October is the most likely timing for the first cut, but an October cut is not a done deal yet.

The recent surge in household debt and the rally in the KTB (bond) market may force the BoK to delay the timing of its policy shift by a few months. The government and banks are already tightening lending conditions and other macroprudential measures. So, we will see how this affects the mortgage and housing markets in the coming months. In addition, the recent announcement of next year's KTB issuance has pushed KTB yields slightly higher, but with expectations of a Fed rate cut growing, the BoK will also need to keep an eye on market interest rate movements.

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