

South Korea: Weak IP report suggests a bleak outlook for 1Q23 GDP

Forward-looking data suggest the economy will contract in the current quarter. The Bank of Korea will pause its tightening policy from February.



Source: Shutterstock

-2.9% Industrial Production
% MoM, sa

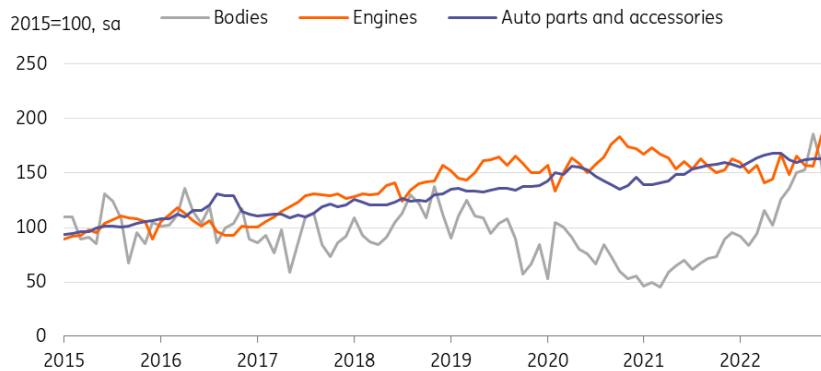
Lower than expected

Production activity declined while retail sales rebounded temporarily in December

Industrial production dropped more than expected -2.9% MoM sa (vs 0.6% November, -0.2% market consensus) in December. Semiconductor (4.9%) and basic material (3.1%) products rose, but motor vehicles (-9.5%), and electronic components (-13.1%) fell even more. The

inventory/shipment ratio edged down to 126 in December from 127.4 in November, but it remained at an elevated level, which is not favourable to the inventory cycle this quarter. Also, we believe there is a supply mismatch in some industries. For example, in the case of automobiles, inventories for engines and auto parts continued to grow, while those for auto bodies declined significantly.

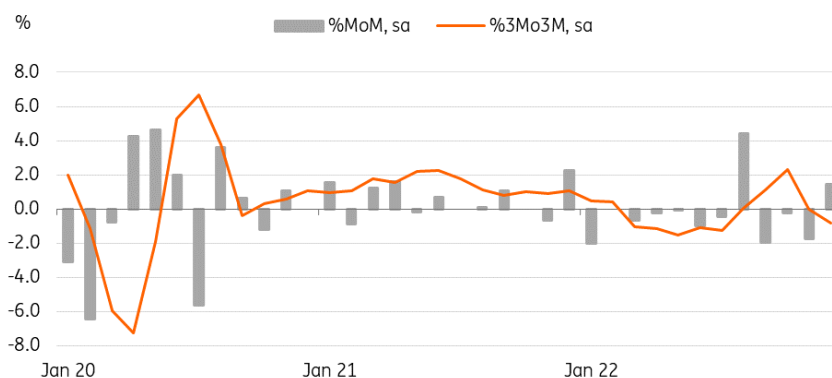
Supply mismatch in auto sector



Source: CEIC

Meanwhile, retail sales rebounded 1.4% in December, boosted by several one-off factors. Firstly, weather-related product sales rose as severe weather conditions continued. Secondly, there were larger-than-usual year-end sales promotions. And lastly, there was a technical payback from the early November crowd-crush accident. We believe that household purchasing power continues to weaken thanks to higher utility fees and a rising debt service burden. As a result, we expect retail sales to decline again in January.

Retail sales rebounded temporarily in December



Source: CEIC

Forward-looking data point to weak growth in the current quarter

Forward-looking data is more important to gauge this quarter's growth. The cyclical leading index fell 0.5 points, recording six consecutive monthly declines. Both machinery and construction orders

fell by -23.0% and -3.0%, respectively. Both are highly volatile in monthly comparisons, but in 3-month sequential terms, data show both intensifying their contractions in December. Today's data support our view that 1Q23 GDP will also contract (-0.2%QoQ sa), following the contraction in the fourth quarter of last year (-0.4%).

China's reopening is unlikely to have much positive impact on Korea's economy in the first half of the year

Forward-looking data suggest that Korea's growth momentum will soften further in the current quarter. At face value, China's reopening should be good news. But careful consideration of how this might affect Korea's exports and services suggests caution is warranted. Both Japan and the Netherlands have decided not to provide chip-manufacturing equipment to China. Korean semiconductor companies have production lines in China, which cannot install top-notch equipment from the second half of the year, and this should adversely affect exports.

As for services, it may take a bit longer for Korea to benefit from increased numbers of Chinese tourists entering the country as Korea now requires additional COVID-19 tests for Chinese tourists. These measures will eventually be lifted. But the initial reopening boost will be less than expected.

BoK watch

We maintain our view that the Bank of Korea will pause its rate hikes from February. We believe that the current quarter of growth is unlikely to improve, while inflation will slowly fall further over the next few months. We see no clear signs of improvement in exports while domestic economic activity continues to slow. Consumer price inflation in January will remain around the current level of 5.0% YoY (Market consensus 5.1%, ING forecast 4.9%) mainly due to hikes in gasoline and power prices, but the trend has clearly passed its peak. The Bank of Korea will monitor the cumulative impact of the earlier rate hikes from now on. If we are right about weak growth this quarter, coupled with weakening labour markets, tightening financial conditions, and slowing inflation, the Bank of Korea will probably consider a rate cut in the second half.

Author

Min Joo Kang

Senior Economist, South Korea and Japan

min.joo.kang@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.