

## Bank of Korea delivers another 25bp hike with hawkish tilt

The Bank of Korea (BoK) raised its policy rate to 3.50% from 3.25%. The big question now is whether this will be the end of the current hike cycle. We expect the BoK to top out at 3.50% but the central bank seems to want to leave the door open for further hikes as inflation remains high



**3.50%** 7-day repo rate

As expected

### The BoK board is divided on rate hikes

Today's rate hike decision was not unanimous as expected, with two members disagreeing about today's 25bp hike call. At the press conference, Governor Rhee Chang-Yong said that board members have different opinions on the terminal rate level over the next three-month

horizon. Three members see the terminal rate at 3.5% and the other three think that 3.75% should not be ruled out.

Although we thought the BoK would pause this time considering the recent slowdown in inflation and growing concerns over growth, resuming rate hikes in February, the BoK seems to have focused more on the high inflation figure rather than the fact it is on a downward trend, as the uncertainty over inflation is still large.

The BoK also announced today that the short-term market stabilisation measures will be extended for another three months until the end of April. The short-term financial market has been stabilising since last November, but the risks surrounding PF financing and credit markets are still significant. This extension will therefore support improving market liquidity.

## **It ain't over till it's over**

Listening to Governor Rhee, it is clear he was trying not to give a definite answer to the market about whether this will be the end of the current hike cycle or not. But in his remarks about inflation, growth and the housing market, we understood that the BoK is primarily focused on stabilising inflation. Thus, if inflation does not go down faster than expected, there will continue to be the possibility of further rate hikes.

As for the economic outlook, the current inflation path is in line with the current BoK's forecast (3.4% year-on-year), while growth is expected to fall short of the current forecast of 1.7% YoY. Rhee added that the economy may have contracted in the fourth quarter mainly due to sluggish exports and domestic demand, but GDP in the first quarter is expected to rebound on the back of fiscal spending, better-than-expected growth in the US and EU, and the possibility of a rapid recovery in China based on the latest preliminary data.

It seems to us that the BoK believes the economy is heading for (a mild) recovery after bottoming out last quarter. The first half of this year will be tough, but it is still too early to tell whether the economy will fall into recession. Regarding the recent housing market adjustment, Rhee drew a line that monetary policy should not target a specific sector of the economy, and that the recent easing measures would not likely reverse the housing market situation.

## **We still think the BoK has ended its tightening cycle**

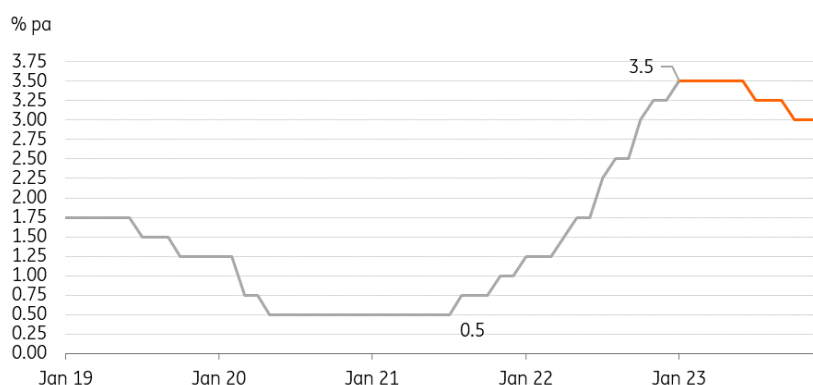
We believe that inflation is going to slow down faster in the coming months. Global commodity prices continued to fall over the last quarter and the strengthening Korean won will likely lighten the burden on domestic pass-through inflation. Today's import price index levelled down from 14.0% in November to 9.1% in December. We expect CPI to decelerate to the 4% level in the first quarter despite the recent hikes in utilities and gasoline prices.

As for growth, weak growth in the fourth quarter could provide a technical rebound in the first quarter. However, as interest rates have remained in restrictive territory for more than three months, the negative impact of the interest rate hike on the economy is expected to increase. Credit market conditions have been stabilising mainly due to supportive policy and has helped companies raise operating funds, but it is not expected to encourage companies to invest in Capex given the high level of interest rates. As for consumption, a temporary rebound can be seen in December as weather-related consumption should rebound and impact of the tragic Itaewon crowd crush should fade. But, the debt service burden on households will likely weigh on

consumption, and labour market conditions also seem to be weakening. We have to closely monitor how China's Covid-19 situation evolves, but in our view, the positive impact is expected to materialise in the second half of the year.

Thus, apart from the hawkish comments from the BoK, we think that the central bank will take a pause for a while on rate hikes. We maintain our rate cut call in the second half of this year.

## BoK is expected to stand pat for a while



Source: BoK, ING estimates

### Author

**Min Joo Kang**

Senior Economist, South Korea and Japan

[min.joo.kang@asia.ing.com](mailto: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>.