Minutes of the Monetary Policy Board Meeting

October 2023

Bank of Korea

English version

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October 2023

Ⅰ. Outline

1. Date of meeting: Thursday, October 19, 2023

2. Place: Monetary Policy Board Meeting Room

3. Monetary Policy Board members present:
   Rhee, Chang Yong, Chairman (Governor)
   Cho, Yoon-Je
   Suh, Young Kyung
   Shin, Sung Hwan
   Park, Chunsup
   Chang, Yongsung
   Ryoo, Sangdai (Senior Deputy Governor)

4. Monetary Policy Board members absent: none

5. Participants:
   Kang, Sungjun, Auditor
   Min, Jwa Hong, Deputy Governor
   Lee, Sang Hyeong, Deputy Governor
   Lee, Jongryeol, Deputy Governor
   Kim, Woong, Deputy Governor
   Chae, Byung Deuk, Deputy Governor
   Lee, Jae Won, Director General, Economic Research Institute
   Choi, Chang Ho, Director General, Research Department
   Kim, Inkoo, Director General, Financial Stability Department
   Hong, Kyung Sik, Director General, Monetary Policy Department
   Park, Jongwoo, Director General, Financial Markets Department
   Oh, Kum Hwa, Director General, International Department
   Kwon, Min Soo, Director General, Reserve Management Group
   Min, Jun Gyu, Director General, Office of Legal Affairs
   Choi, Yong Hoon, Director General, Monetary Policy Board Secretariat
   Kim, Yong Sik, Press Officer
   Hur, Hyun, Head, MPB Administrative Support Team

1) This English version is an excerpt of each Policy Board member's opinion on the Bank of Korea's Base Rate decision, taken from the Minutes of the Monetary Policy Board Meeting.

Ⅱ. Discussions Concerning Monetary Policy Decision

At the October 19 Monetary Policy Board meeting, each member expressed their opinion on the Bank of Korea’s Base Rate decision.

All members shared the opinion that, in overall consideration of the domestic and international financial and economic environments, it would be desirable to leave the Base Rate unchanged at the current 3.50% level for the intermeeting period.

One member noted that it would be appropriate to maintain the Base Rate at the current level of 3.50% for this meeting.

Concerning the global economy, the member noted that the U.S. economy had maintained growth based on favorable employment and consumption and that the euro economic recovery had been subdued owing to sluggish indicators related to production and consumption amid persistent high inflation and high interest rates. The member commented that in China, while economic indicators had been improving somewhat, boosted by the government’s stimulus measures, the economic recovery was expected to be modest due to a slump in its real estate market and the continued downward trend of its exports. The member added that the Japanese economy showed faster-than-expected growth, driven by the rise in automobile exports and the arrival of foreign tourists, more than offsetting sluggish domestic demand. Regarding the Korean economy, the member assessed that its slowdown had been easing in-line with a gradual recovery in exports, and those of semiconductors in particular, and added that uncertainties exist surrounding the future growth path involving the recovery pace of the semiconductor industry, the extent of the Chinese economic recovery, and the direction of the Israel-Hamas conflict.

Looking at external conditions, the member viewed that exports, having shown a downward trend since October last year, had continued to recover gradually and that the decrease in exports had been decelerating accordingly, and went on to forecast that exports would shift to a year-on-year increase in October. The member noted that the trade account had recorded a surplus for four months in a row since June, led by an increase in exports of automobiles and vessels and a decline in energy imports. The member also stated that the current account switched to a surplus in May, recording a surplus of 10.98 billion dollars until August, but that the recently heightened uncertainties surrounding international oil prices would likely affect the scale of any future current account surplus. The member commented that the index of all industry production grew by 2.2% in August, led by the semiconductor industry, while private consumption growth had been slowing, influenced by sluggish commodity consumption. The member noted that consumer price inflation in September recorded 3.7%, up from a month earlier, driven by a rise in agricultural product and food prices, and added that core inflation excluding food and energy remained unchanged from the previous month's 3.3%. The member assessed that uncertainties remained along the future inflation path regarding international oil price and exchange rate trends related to the Israel-Hamas conflict and to domestic and overseas economic developments. The member assessed that the employment situation is robust in that the employment and unemployment rates are reaching a record high and a record low, respetively, and that the number of persons employed in September increased by 309,000 year-on-year, driven by a rise in the number of persons employed in the construction sector for the first time in 10 months. The member however pointed out that those aged 60 or older, who are responsible for the majority of the growth seen in employment figures, and a decline in the number of persons employed in the manufacturing industry were both challenges to the labor market. The member also mentioned that the number of young people employed had been falling for 11 months in a row, affected by a shrinking population.

The member commented that market interest rates and the exchange rate had risen greatly and that volatility had expanded in financial markets due to strengthened expectations of prolonged tightening monetary policy stances in major countries and to a strong U.S. dollar. The member noted that the Israel-Hamas conflict was affecting financial markets with some time lag, and could deliver a big shock depending on its future developments. The member stated that the increase in household loans had declined greatly in September affected by temporary factors, but demanded that household loans be managed so that an increase in household loans and a subsequent rise in household debt do not undermine financial stability, as household loans had continued to increase for six consecutive months since April, and as the size of those loans could possibly be larger in October than in September. The member also stressed the need to deleverage corporate debt in order to reduce the corporate debt-to-GDP ratio, which stood higher than it was during the Asian Financial Crisis. The member assessed that, as for the real estate market, uncertainties regarding the future direction of the housing market had heightened considering downside factors such as stronger lending regulations and a rise in lending rates, as well as an upward trend of housing sale transactions in-line with strengthened expectations of a rise in housing prices this year.

Looking at conditions surrounding the Base Rate decision, the member commented that inflation was forecast to be above the target level for a considerable time, and that the increase in household debt had not moderated, with risks in vulnerable sectors, such as real estate project financing, not being resolved. The member added that the trend of higher interest rates had been persisting for a considerable time due to a prolongation of tightening monetary policy stances in major countries, and that uncertainties surrounding the Israel-Hamas conflict were elevated. Therefore, the member expressed the view that it would be desirable to leave the Base Rate unchanged at the current 3.50% for this meeting, to maintain a tightening policy stance and to make any decision at the next meeting regarding whether the Base Rate needs to be raised further, all while monitoring developments of the Israel-Hamas conflict, global oil price and core inflation trends, the Korean won to U.S. dollar exchange rate, household debt trends, the extent of any recovery in the real economy, including the real estate market, and monetary policies in the U.S. and other major countries.

Another member judged that it was appropriate to leave the Base Rate unchanged at the current 3.50% for the intermeeting period.

The member noted that despite the generally solid growth of the global economy, growth trends differed across countries and that growth would slow gradually going forward. The member observed that the combination of short-term factors, such as the prospect of prolonged tightening monetary policy stances in major countries and continued high interest rates, and structural factors, such as the decline in international investment and in supply chain efficiency resulting from geopolitical conflict, excessive debt, demographic shifts, and climate change, may cause economic players to be pessimistic about the future outlook, suppressing private consumption and investment for some time. The member noted that inflation in major economies was likely to slow gradually going forward, although uncertainties remained high given the movements in international oil prices amid the Israel-Hamas conflict.

The member noted that the domestic economy showed a modest recovery, as the export slump had eased, despite a slow consumption recovery. The member stated that private consumption had recovered moderately, as the modest recovery in services consumption driven by improved weather conditions, long holidays, and the increase in foreign tourist arrivals, had been offset by sluggish goods consumption. The member added that facilities investment remained in a slump, while sluggish construction investment had alleviated modestly due to the resumption of construction, which had been delayed due to unfavorable weather conditions. The member observed that exports had improved, led mainly by semiconductor exports, and that labor market conditions had remained generally solid with a low unemployment rate, despite the moderately slowing growth in the number of persons employed. The member mentioned that the outlook for the property market remained unclear, given that the transaction volume had decreased somewhat despite the continuing rise in housing prices mainly in the Seoul metropolitan area. The member noted that consumer price inflation was likely to stand above the August forecast affected by the rise in international oil prices and the unfavorable weather conditions, and that core inflation and inflation expectations had remained subdued for the past three months. The member expected that prices would be affected by movements in international oil prices and in exchange rates, and by economic conditions at home and abroad, and that the pace of increase would slow gradually, although upside risks seemed larger at present.

In terms of financial and foreign exchange markets, the member observed that volatility had increased, driven by the outlook for a tighter-for-longer monetary policy in major countries. The member noted that long-term treasury bond yields had inreased, affected by the rise in treasury yields in major countries, while short-term interest rates had risen driven by banks' increased issuance of short-term bonds. The member also noted that the Korean won to the U.S. dollar exchange rate had risen considerably, due to expectations for a prolonged tightening stance at the U.S. Fed and to the strong dollar. The member stated that the growth in household debt had slowed in September compared to the previous month due to seasonal reasons, while the sharp growth in housing-related loans had continued, and corporate borrowing had significantly increased driven by demand for funds and by more aggressive lending operations at banks, in addition to some seasonal factors.

The member assessed that both drivers for a further Base Rate hike and for a freeze were present under the current domestic and global circumstances.

In the member’s view, the steady growth in household and corporate borrowing indicated that monetary and credit policies had not been as tightening as intended. The member cited the stagnant slowing of core inflation and public inflation expectations over the past three months, the exchange rate movement affected by the U.S. policy rate outlook, and the larger-than-expected upside pressures on inflation as drivers for a further Base Rate hike, which called for an additional pre-emptive rate hike to achieve a speedy return to the inflation target. In contrast, the member mentioned that certain other factors -- including the sluggish growth rate, the unclear recovery in domestic and overseas demand, the prospect of slowing inflation with gradually stabilizing international oil prices and exchange rates, rising delinquency rates among non-bank financial institutions, and the potential financial market risk -- would indicate a rate freeze, and that a monitoring of future developments would be more appropriate.

In overall consideration of the fact that the considerable rise in short- and long-term market interest rates had practically brought a stronger tightening effect on financial markets, that financial supervisory authorities had become more alert about the household debt growth, and that uncertainties had grown over global economic environments due to the escalated tension in the Middle East, the member deemed it appropriate to keep the Base Rate at the current level and to further monitor domestic and global economic developments and monetary policy changes in major countries before considering any need for an additional rate hike.

Meanwhile, another member presented the view that it would be desirable to keep the Base Rate at its current level of 3.50%.

The member mentioned changes in the domestic and international economic environments after the previous MPB meeting. First, looking at the global economy, the member assessed that, while the growth trend had differentiated across major economies and as inflation had continued to moderate in its underlying trend, uncertainty had increased overall due to a prolongation of tightening monetary policy stances in advanced countries and heightened geopolitical risks. The member noted that, despite expectations of high interest rates for longer, the U.S. economy maintained strong growth, exceeding its potential level, boosted by a decreased sensitivity of the economy to interest rates in-line with reduced private debt and a higher share of fixed rate loans since the Global Financial Crisis, and by expanded private investment in new growth industries. The member commented that the euro area, meanwhile, had been showing a modest economic recovery, owing to the sluggishness of manufacturing exports and domestic demand, offsetting a recovery in tourism demand. The member added that the Chinese economy had been in a structural decline, particularly in the real estate sector.

The member judged that there was a mix of upside and downside risks to domestic economic growth. The member assessed that exports had been showing a faster-than-expected recovery, driven by growth in semiconductor exports and a slower decline in exports to China since September. The member forecast that exports would sustain their robust growth next year, mainly in the semiconductor sector. The member also anticipated that facilities investment and fiscal expenditures would make a greater contribution to growth compared to this year, boosted by growth in semiconductor investment demand and a rise in tax revenue. The member expected that private consumption, on the other hand, would see its growth momentum weaken compared to the past average due to the combined effects of increased household debt repayment burdens and weakening propensity for consumption following an aging population, which would more than offset any improvements in real purchasing power in-line with slower inflation.

Concerning inflation, meanwhile, the member assessed that upside risks outweighed downside risks. The member added that this was because supply-side inflationary pressures had recently increased to a greater extent than expected due to rising oil prices and to the exchange rate, and, if the situation in the Middle East worsens, there was a significant risk of a further rise in oil prices and a further strengthening of the U.S. dollar simultaneously. The member argued that the fact that demand-side pressures were weak might limit businesses from passing on cost increases, but, if multiple supply shocks accumulate in a situation of persistently high inflation expectations, it would become challenging to rule out the possibility of inflation risk escalating once more and the timing of inflation converging on the target level being delayed.

Looking at financial markets, the member mentioned that long-term market interest rates and the won-dollar exchange rate had risen significantly, affected by expectations of an extension of the U.S. Federal Reserve's tightening monetary policy stance, but that markets had not become as unstable as in the previous year thanks to enhanced supply and demand conditions in the bond and FX swap markets, and to improved capacities of the private and government sectors to cope with the situation. The member, however, assessed that, despite accumulated Base Rate hikes, household and corporate lending had maintained strong growth, mainly in real estate mortgage loans, and added that its negative side effects had been building up, such as worsening financial imbalances and a consequent risk of financial system instability, a weakening demand capacity, and an inefficient allocation of resources.

The member argued that, considering heightened upside risks to inflation and the buildup of financial imbalances amid increased economic uncertainties at home and abroad, it would be appropriate to keep the Base Rate unchanged at this meeting, while the possibility of further rate increases should be left open. The member also stated that it would be necessary to employ various policy instruments, such as monetary policy, macroprudential policy, and structural reform policy in a coordinated and consistent manner in order to ease conflicts among multiple policy goals, including growth, inflation, and financial stability.

Another member noted that it would be appropriate to maintain the Base Rate at the current level of 3.50% for this meeting.

The member noted that the global economy showed more favorable growth than expected, particularly in the U.S. However, the member assessed that downside risks had increased due to the impact of the ongoing tightening monetary policies in major economies, the increased geopolitical risks resulting from the Israel-Hamas conflict, and the possibility of a slowdown in the Chinese economy. The member saw that, in the U.S., the economy exhibited strong growth thanks to robust consumption and employment conditions, and that inflation was falling slowly, prompting a longer duration of the Federal Reserve's tightening policy stance than initially expected. The member judged that consumer price inflation was highly likely to fall slowly going forward, as employment still remained robust, and as service sector inflation was declining slowly. The member stated that, in the case of China, the government stimulus policy measures had temporarily alleviated the economic downturn, but uncertainties persisted regarding the sustainability of the recovery due to downside factors, such as deepening sluggishness in the real estate market and a continued export slowdown stemming from sluggish overseas demand. The member noted that, in the euro area, economic growth remained weak, particularly due to a struggling manufacturing sector, and that the prolonged tightening policy stance as a response to persistently high inflation would likely have a negative impact on the real economy in the future.

In assessing the domestic economy, the member saw that there were growing uncertainties in policy conditions due to the expansion of downside risks to growth and in upside risks to inflation stemming from heightened geopolitical risks. The member stated that there was an increased possibility that the growth forecasts for this year and the next would fall slightly short of the August forecasts, primarily due to weaker-than-expected private consumption. The member noted that, on the labor market, the pace of growth in the number of persons newly employed and the rate of growth in regular workers' fixed wages had been slowing moderately, and that the number of persons newly employed continued to increase, particularly among the elderly and among women. The member presented the view that, along the future growth trajectory, downside factors would appear to be predominant, including the potential for further increases in international oil prices due to heightened geopolitical risks, a weakening recovery in private consumption, and a possible weakening of external demand resulting from prolonged tightening stances in major economies. However, the member saw that there would also be the possibility of an upward adjustment in the forecast path depending on the pace of recovery in the global IT industry. The member thus found the situation highly uncertain.

The member noted that consumer price inflation exceeded expectations in September, impacted by rises in agricultural product prices and by international oil prices, and upside risks had increased due to a possible further increase in international oil prices following future developments in the Israel-Hamas conflict. The member expected core inflation to continue a gradual slowing trend going forward, but uncertainty remained regarding the pace of slowing due, for instance, to secondary spillover effects resulting from accumulated cost pressures and the possibility of hikes in public utility charges.

The member observed that an increase in long-term U.S. interest rates had pushed up domestic long-term rates, which leads to further tightening financial conditions. Nonetheless, the member pointed out that corporate borrowing had grown sharply, so that the growth trend should be monitored closely going forward. Noting the continued growth in household borrowing, the member stated that for more effective control, authorities should take a qualitative approach, focusing on the risk of household debt instead of on the total debt amount, and that a comprehensive risk management system to assess and control household debt risk was needed. On domestic foreign exchange markets, the member remarked that the Korean won to U.S. dollar exchange rate had fluctuated at around its annual peak. The member judged that the fluctuation was driven primarily by changes in expectations of the U.S. Federal Reserve’s monetary policy and of movements in the U.S. dollar index, rather than by domestic factors, and therefore did not warrant a monetary policy response. However the member added that caution was still needed so that any increase in volatility due to intensifying geopolitical risk would not lead to any financial market unrest.

The member presented the view that, in overall consideration of the above-mentioned domestic and global economic and financial conditions, it would be desirable to maintain the Base Rate at the current level of 3.50% for the intermeeting period, and then determine whether any additional tightening or easing would be necessary in the future, based on the monitoring of domestic and global financial market developments, and trends in growth and inflation.

Another member also presented the view that it would be desirable to keep the Base Rate at its current level of 3.50% for this meeting.

The member stated that the global economy was displaying varying growth trends from country to country and that it was gradually slowing. The member commented that, despite the intensive policy tightening so far, the U.S. was maintaining stronger-than-expected growth, bolstered by favorable employment conditions and solid consumption. However, the member saw that, in a situation in which it would be unavoidable to expand government bond issuance to address the accumulated fiscal deficits, robust economic indicators and persistent inflation concerns were increasing the possibility of the Federal Reserve's “higher for longer” stance. The member noted that China was exhibiting a weaker-than-expected recovery trend despite its government stimulus measures.

Meanwhile, the member argued that with the global goods trade still in a slump, the outbreak of a Middle East conflict had further heightened external uncertainties. The member saw that the impact of the armed conflict in the Middle East remained limited for now, but that it would be very difficult to gauge future developments and potential ramifications for the global economy. The member expressed the opinion that the conflict could lead to repercussions, such as increases in international oil prices, an exchange rate depreciation, or supply chain disruptions, thus constraining growth and inflation, and increasing instability in international financial markets through heightened risk aversion. The member thus saw the need to pay close attention to relevant developments there in the future.

The member stated that the domestic economy exhibited growth in-line with expectations thanks to a recovery in semiconductor exports, despite weak improvements in private consumption and in facilities investment. However, the member pointed out that consumer price inflation had risen significantly, reaching the mid- to upper 3% range of late, surpassing initial projections, driven by sharp increases in oil and agricultural product prices. The member saw that core inflation had remained at 3.3% for the third consecutive month, indicating a slower pace of disinflation compared to the past. The member added that the uncertainty regarding the timing of any price target convergence had increased, influenced by the situation in the Middle East. The member presented the view that, fortunately, the labor market maintained a strong recovery trend despite these conditions.

The member saw that, in the financial sector, the volatility of price variables (interest rates and exchange rates) had expanded somewhat, reflecting expectations of prolonged monetary tightening. The member stated that household debt in the financial sector saw a decrease in its growth due to temporary factors, such as write-offs and sales of loans at the end of the quarter, but that housing-related loans still maintained high growth, in the range of 6 trillion won per month. The member argued that, given the relatively lax regulations on real estate, comparatively low mortgage rates, and the possibility that the general public was perceiving housing prices as being at a low point, household debt growth could expand again. Therefore, the member pointed out that deleveraging efforts should be sustained by strengthening the management of household debt by the government while maintaining a high-interest rate policy.

The member presented the view that the domestic and international conditions facing our economy were challenging. The member noted that an additional interest rate hike could not be ruled out, in the midst of the expected prolonged period of high interest rates in major economies. The member saw that the real economy had seen an increase in downside risks to growth and in upside risks to prices, and that heightened geopolitical tensions had increased concern in financial markets. The member presented the opinion that, given the significantly increased uncertainty in the current situation, it would be appropriate to maintain the Base Rate at the current level of 3.5% and to prepare for the potential impact of future domestic and international developments and to prepare policy changes for the domestic economy.

Another member expressed that it would be appropriate to keep the Base Rate at the current level of 3.50% for this meeting.

The member stated that global economic growth had been slowing overall, albeit differentiated from country to country, and that this trend of a growth slowdown was forecast to continue, affected by a prolongation of tightening monetary policy stances in major countries. The member added that inflation in major advanced countries had continued to moderate in its underlying trend, mainly on core inflation, but that it still remained above the target level, and that uncertainties regarding the price trend had risen due, for example, to greater volatility in international oil prices stemming from the Israel-Hamas conflict. The member noted that in global financial markets, long-term government bond yields in major advanced countries had risen greatly, especially U.S. Treasury bond yields, and that the U.S. dollar had strengthened considerably amid expanded volatility in major price variables.

The member pointed out that domestic economic growth had continued improving at a modest pace as the sluggishness in exports had eased while the recovery in private consumption had slowed somewhat. The member forecasted that the domestic economy would continue to improve going forward. However, the member added that uncertainties surrounding the future growth path were judged to be high, influenced by the timing of any recovery in the semiconductor industry, geopolitical risks, and the impacts of prolonged tightening monetary policy in major countries.

The member stated that the moderating trend in inflation had slowed. The member noted that consumer price inflation had risen to the mid- to upper 3% levels in August and September driven by the increase in the prices of global oil and agricultural products, while core inflation had remained unchanged since July. The member forecasted that the slowing trend in inflation would resume going forward, but that close attention should be paid to its timing and pace as the timing of inflation converging on the target level was more likely to be delayed than previously expected. The member commented that there were elevated uncertainties along the future inflation path regarding geopolitical risks, global oil price movements, exchange rate trends, and economic conditions at home and abroad.

The member stated that in financial markets, interest rates had risen sharply, particularly in long-term bonds, and that interest rate volatility had heightened, affected by higher volatility in global financial markets and by the rise in long-term government bond yields in major advanced countries. The member noted that housing-related loans had continued to increase, although the overall increase in household loans had slowed in September. The member judged that liquidity risk in the non-banking sector was seemingly subsiding, but emphasized the need to be attentive to relevant credit risks, considering rising loan deliquency rates, the slump in regional real estate markets, and elevated interest rate levels. The member commented that in FX markets, the Korean won to U.S. dollar exchange rate had remained high with its volatility expanded. The member stressed the need to closely monitor FX market trends, as the market would be greatly affected by a strong U.S. dollar and by geopolitical risks.

In summary, the member stated that although inflation was forecast to resume its moderating trend, it would be necessary to closely examine what impacts changes in external conditions and Base Rate hikes so far would have on the overall economy, as uncertainties surrounding policy conditions at home and abroad had heightened due to, for example, the Israel-Hamas conflict.

The member expressed the view that it would be desirable to keep the Base Rate at the current 3.50% for this meeting. The member emphasized that the possibility of maintaining a tightening policy stance for longer than originally expected had increased, considering recent upside risks in inflation. The member stated that an additional rate hike would be needed if the possibility of an inflation slowdown being delayed more than previously forecast increased significantly due to the realization of upside risks in inflation.