Minutes of the Monetary Policy Board Meeting

January 2024

Bank of Korea

English version

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Ⅰ. Outline

1. Date of meeting: Thursday, January 11, 2024

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
   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 January 11 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 presented the view that it would be appropriate to keep the Base Rate at its current level of 3.50% for the intermeeting period.

This member noted that, affected by ongoing high interest rate policies, global inflation had entered a subdued phase and that inflation in most countries had been substantially down from its peak. The member projected that the global economy would slow somewhat with monetary tightening having repercussions in the real sector. The member however anticipated that global trade, which had been unusually sluggish last year, would recover gradually, having positive impacts on Korea's exports.

Regarding the domestic economy, the member noted that growth was exhibiting a gradual recovery trend, boosted by favorable semiconductor and automobile exports, while domestic demand, such as private consumption and investment, had continued to show a weak recovery. The member assessed the labor market as being robust, with the unemployment rate hitting a record low of 2.3% in the third quarter of 2023. The member stated that the strong employment indicators were a result of growing economic participation by women and by the elderly, and went on to argue that a recovery in employment among young people would be needed to enhance long-term productivity and to expand growth potential.

With respect to inflation, the member commented that consumer price inflation had continued to decline to 3.1% in the third quarter last year, and that it then rebounded somewhat to 3.4% in the fourth quarter. The member noted that the rebound had been attributable to supply shocks, including the fading away of base-period effects and the rise in oil and agricultural product prices, and projected that the gradual decline would continue unless there were additional supply shocks. The member also forecast that core inflation excluding food and energy would continue to moderate, to reach the lower 2% level at the end of the year. Going forward, however, the member expected that it might take a considerable period of time for inflation to converge on the target level due to favorable labor market conditions and persistent inflation.

Concerning the financial sector, the member noted that difficulties in vulnerable sectors caused by persistently high interest rates were gradually becoming apparent, as seen in the escalating delinquency rates on loans to small businesses and on those related to real estate project financing. More specifically, the member pointed out that potential risks in financial markets had increased following Taeyoung E&C's application for a debt workout plan, but that markets remained stable so far without concern spreading across the entire market. The member argued that it would be necessary to closely monitor future issues related to real estate project financing so as to prevent them from developing into systemic risks.

The member believed that recent inflation developments have shown the tangible results of the high interest rate policy that the Bank has been maintaining to bring inflation down. However, the member also pointed out that it needed to maintain the tightening stance until it is confident that inflation is safely returning to the target. The member added that there had been past cases where long painstaking efforts turned out to have been in vain when inflation failed to become anchored. The member also stated that high interest rates help to strengthen the foundation for stable growth by reducing private debt and by securing future consumption and investment resources. The member mentioned that although recessions are painful, they also have a cleansing effect that allows the resolution of less competitive sectors so that resources can be used in a more productive manner. The member expressed the view that it was appropriate to keep the Base Rate at the current 3.5%, and to deal with the negative side effects of high rates with micro-level measures, such as ad hoc liquidity provisions, if necessary, while monitoring changes in domestic and overseas financial and economic developments.

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 stated that the global economy saw a gradual slowdown in growth as the effects of monetary tightening continued, but that growth was expected to improve modestly after the second half of the year. The member noted that inflation in the major advanced economies continued an underlying trend of deceleration but still remained elevated, and was expected to take some time to stabilize at target levels.

The member projected that the domestic economy would likely continue to improve modestly, with a weaker consumption recovery, but with ongoing strong exports. The member saw that employment remained favorable overall, although growth in the number of persons employed was gradually slowing. The member noted that the real estate market had seen a slowdown in transaction volumes and a downward shift in house prices in both the Seoul metropolitan area and in provincial areas, but that uncertainty remained high depending on the future policy direction. As for domestic inflation, the member noted that consumer price inflation declined due mainly to lower petroleum product prices and smaller increases in other industrial product prices, and core inflation continued to decelerate. Going forward, the member expected domestic inflation to continue its underlying slowdown, but at a moderate pace due to the spillover effects of accumulated cost pressures.

The member pointed out that financial and foreign exchange markets had seen a significant reduction in risk aversion sentiment since the December FOMC meeting. The member stated that government bond yields fell sharply due mainly to the sharp decline in U.S. Treasury bond yields, and short-term market interest rates also declined significantly. As for household loans, the member commented that other loans had declined, but housing-related loans had sustained strong growth, and delinquency rates on corporate loans had continued to rise led by loans to SMEs, but were still low compared to the long-term average delinquency rate in the past. The member presented the opinion that risks related to real estate project financing had emerged of late, but the impact on the financial system as a whole would likely be limited. However, the member saw a need to closely monitor future relevant developments.

The member expressed the view that, in consideration of the overall domestic and international economic conditions, it would be appropriate to keep the Base Rate unchanged at 3.5% at this meeting. The member stated that, while inflation was expected to continue in its underlying slowdown, it was still significantly above the target level and uncertainty surrounding the future inflation path persisted. In addition, the member saw that, while inflation expectations had moderated somewhat of late, it was expected to take some time to anchor at the target level.

The member pointed out that, in light of these considerations, it would be necessary to keep the Base Rate unchanged at 3.5% at this Monetary Policy Board meeting and to maintain a tight monetary policy stance for a sufficient period of time until the Board was confident that inflation would stabilize at the target level. The member presented the opinion that, going forward, it would be necessary to make monetary policy decisions by closely examining the inflation path with a focus placed on anchoring inflation at the target level, while taking into account domestic and international economic conditions, changes in monetary policies of major countries, and risks to economy and financial stability.

Another member suggested that it would be appropriate to leave the Base Rate unchanged at the current level of 3.50%.

The member observed that global financial market conditions had eased considerably with the U.S. long-term Treasury yield decreasing on heightened expectations of an earlier-than-anticipated pivot by the U.S. Federal Reserve. The member predicted that the global economy would continue its slow growth for some time due to tightening monetary policies, and that it would be affected by the pace of monetary policy shifts in major countries starting in the second half of this year. In the U.S., the member noted that the consumption slowdown had continued moderately, and that economic growth had slowed at a lower-than-expected pace. The member added that, while its inflation had slowed, core inflation had shown slower progress than anticipated. As for China, the member noted that domestic demand there has been sluggish, driven by the continuing real estate market slump, despite an accommodative fiscal policy. The member commented on the euro area, saying that its slump would continue for some time, weighed down by high inflation and high interest rates.

The member assessed that, on the domestic economic front, the effects of monetary policy tightening were being transmitted to the real economy, as the recovery in private consumption was weaker than expected, construction investment remained sluggish, and as the increase in the number of persons employed continued to decline moderately, although exports were recovering. Going forward, the member expected economic growth to continue to improve moderately in the real sector, led by exports, and private consumption to recover to a level consistent with the potential growth rate this year. However, the member also saw that uncertainty surrounding the forecast path for private consumpion had increased since the pandemic outbreak, and, by their nature, facilities and construction investment and exports were subject to large forecast errors along their paths. The member thus stated that the outlook for future growth paths was more uncertain than in the past.

The member stated that inflation had continued to slow moderately, consistent with the projected path, and that this trend was expected to continue this year, as well. However, the member pointed out that current consumer and core inflation were still well above the inflation target of 2%, and that the gap between them and the projected levels at the end of last year were quite large. The member saw potential upside risks to inflation coming from uncertainties in the pace of administered price increases in the future, from energy and agricultural and marine product prices, from the impact of the government's early fiscal spending in the first half of this year, from the speed of price transmission of accumulated supply shocks, and from geopolitical risks.

The member noted that, in financial markets, tight financial conditions had eased somewhat, with domestic long-term government bond yields falling sharply as a result of the decline in U.S. Treasury bond yields due mainly to strengthening expectations of an early shift in the U.S. Federal Reserve's policy stance. However, given that real estate prices had turned downward, growth in household debt had shrunk considerably, and that delinquency rates among households and corporations were increasing, the member judged that domestic financial conditions still remained tight. In addition, the member commented that, while the foreign exchange and financial markets had remained stable following the announcement of a debt workout application by a construction company, financial instability remained a potential risk, with widespread concern over the possibility of real estate project financing failures. The member considered it appropriate to respond with microeconomic policy measures targeted on the sectors triggering financial instability in the event that financial instability in certain sectors were to materialize in the future. The member saw that the domestic foreign exchange market had been generally stable and that foreign currency financing conditions had also been favorable.

Taking into consideration these domestic and overseas economic conditions, the member saw a need to keep the Base Rate unchanged at the current level of 3.50% this time and to monitor progress in the real economy and inflation relative to the projected paths for some time, while checking that both consumer and core inflation declined sufficiently in-line with their forecast paths.

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

The member noted that global economic growth had slowed, driven by the continuing tightening monetary policy stances in major countries and the weakened demand for services, and that this trend would continue into the first half of this year. The member also observed that international oil prices had fluctuated within a limited range, and that downward pressure would be dominant as supply and demand conditions improved. The member projected that it would take considerable time before inflation in major economies returns to the target, as the pace of slowdown will likely be modest despite a significant fall from its peak.

With regard to global financial markets, the member observed that government bond yields had declined in major countries driven by heightened expectations of policy rate cuts, that the U.S. dollar had weakened, and that global equity prices had risen. The member noted, however, that entering this year, the expectations for policy rate cuts had somewhat weakened in major countries, partially reversing developments in those indicators.

Concerning the domestic economy, the member projected that the recovery momentum for consumption would weaken, while exports and facilities investment would continue to improve moderately, led by the recovery in the global semiconductor business. The member expected this year’s growth to be in-line with the November forecast.

The member expected inflation to continue slowing this year. The member added that consumer price inflation is likely to approach the target level at year-end or early next year, and that core inflation seems to be gradually falling, considering the demand pressures.

However, the member viewed that some evidence warrants caution against jumping to a conclusion that inflation had entered a period of stability in spite of the moderating indicators. The member pointed out that inflation had not been fully down, and economic agents' sensitivity to prices still remained high, requiring caution against any remaining momentum for price change. The member concluded that a prudent approach, taking into account various indicators, was required, rather than putting too much meaning onto certain indicators.

The member noted that in domestic financial markets short- and long-term interest rates declined and exchange rates fluctuated within a limited range mainly on developments of global financial market.. In terms of household lending by financial institutions, the member expected that factors like strengthened government control of loans, housing prices that had shifted to declines, and a decrease in the number of housing transactions to come into play. However, the member added that any impact of the recent sharp fall in home mortgage loan rates should also be monitored closely. Despite the rise in delinquency rates at non-bank financial institutions, and credit events among some companies with larger exposure to real estate project financing (PF), the member believed that the risk is unlikely to spill over onto the overall financial system. However, the member argued that, given elevated wariness in the market regarding real estate PF loans, authorities should strengthen their monitoring and stand ready to face any market unrest.

In summary, the member assessed that, despite the continuing modest improvement in the economy and inflation seemingly stabilizing, one should remain mindful of any lingering uncertainties concerning the disinflation outlook, and keep monitoring markets for financial stability. In overall consideration of the above-mentioned circumstances, the member believed that it was desirable to keep the Base Rate at the current level of 3.50% for the intermeeting period, and to maintain the tightening stance while closely monitoring developments of inflation and key indicators of the monetary policy transmission channel, until uncertainties surrounding the inflation outlook are fully resolved.

Another member argued that it would be appropritate to leave the Base Rate unchanged at the current 3.50% for the intermeeting period.

The member stated that major economies had maintained price stability since the second half of last year and witnessed their growth and employment situations approach equilibrium levels. The member saw that the rapid expansion of the U.S. economy had slowed somewhat, but that it remained on track for a soft landing, sustaining favorable growth without massive job losses, with inflation decreasing. The member mentioned that, in the euro area, the manufacturing sector had been lackluster due to rising costs and a slowdown in China’s economic growth, and the services sector had exhibited a slower recovery, but inflation had fallen rapidly to the mid-2% range led by energy and food prices. The member projected that, in China, the real estate slump and geopolitical fragmentation had been working as a factor contributing to a strucutural slowdown in growth, but the pace of the slowdown would be modest, affected by economic stimulus measures.

The member also forecast that the growth rate of the domestic economy would be in the lower 2% range, slightly surpassing the potential growth rate, and that inflation would gradually converge on 2%. The member stated that, according to an analysis by the Research Department, this projection was made based largely on favorable external conditions, such as a recovery in global trade driven by goods and IT demand, as well as falling international oil prices, despite a global economic slowdown this year. The member assessed that the growth exhibited qualitative improvements, as well, with an increased contribution from the private sector, especially in facilities investment, a reduced dependency on government spending and construction investment, and progress made on diversifying export destinations.

The member however pointed out several factors continuously putting downward pressure on growth, such as a structural slowdown in private consumption affected by sluggish real income, increased debt-servicing burdens, and the population aging. The member also noted that weakening export and investment momentum due to global fragmentation and to increased offshore production, and weak employment growth among the prime working-age population in the labor market, were both factors putting downward pressure on growth.

Concerning financial markets, the member saw that market interest rates fell and stock prices rose as investor sentiment had improved, based on expectations of the easing of monetary tightening in major countries. The member however went on to state that potential destabilizing factors remained, such as rising delinquency rates on loans from non-banks, and heightening risks related to project financing following Taeyoung E&C’s application for a debt workout plan. As for FX markets, the member noted that, despite improvements in the current account, the won-dollar exchange rate, linked to the strengthening of the U.S. dollar, had been fluctuating at around the lower 1,300 won level. In terms of household debt, the member assessed that housing-related loans had continued to increase while the decline in loans from non-bank financial institutions and unsecured loans had accelerated, and they went on to argue that it would be necessary to closely monitor future trends here.

Summarizing all these economic and financial conditions, the member forecast that, while the economy would grow at a faster pace, there would be a further deepening divergence between the export and consumption sectors, and inflation would continue to moderate in its underlying trend. The member added that, in this regard, a need for further monetary tightening appeared to have decreased. The member however judged that, since consmer price inflation was expected to remain above its target for more than a year and since supply-side upward pressures remained, it would be necessary to maintain the current tightening stance for a considerable period of time. The member also argued that, in implementing a monetary policy pivot, priority should be placed on ensuring that inflationary pressures have slowed and that inflation expectations are stable. The member went on to state that consideration should also be given to domestic demand and private debt.