Minutes of the Monetary Policy Board Meeting

April 2021

Bank of Korea

(English version)

Minutes of the Monetary Policy Board Meeting[1)]

(April 2021)

Ⅰ. Outline

1. Date of meeting: Thursday, April 15, 2021

2. Place: Monetary Policy Board Meeting Room

3. Monetary Policy Board members present:
   Lee, Juyeol, Chairman (Bank of Korea Governor)
   Koh, Seung Beom
   Lim, Jiwon
   Cho, Yoon-Je
   Suh, Young Kyung
   Joo, Sangyong
   Lee, Seungheon (Senior Deputy Governor)

4. Monetary Policy Board members absent: none

5. Participants:
   Jang, Ho Hyun, Auditor
   Ryoo, Sangdai, Deputy Governor
   Park, Jong Seok, Deputy Governor
   Lee, Hwan Seok, Deputy Governor
   Bae, Joonsuk, Deputy Governor
   Yang, Seok Jun, Director General of Reserve Management Group
   Kim, Woong, Director General of Research Department
   Min, Jwa Hong, Director General of Financial Stability Department
   Lee, Sang Hyeong, Director General of Monetary Policy Department
   Kim, Inkoo, Director General of Financial Markets Department
   Kim, Hyun Kee, Director General of International Department
   Shin, Woon, Director of BOK Economic Research Institute
   Park, Young Chool, Press Officer
   Chae, Byung Deuk, Director General of Monetary Policy Board Secretariat
   Sung, Kwang Jin, Head of MPB Team

1) This English version (summary) of the minutes of the Monetary Policy Board Meeting was produced at a working level, and is not an official document.

Ⅱ. Summary of Discussions on the Current Economic Situation

After briefings by staff on *Recent Economic Developments*,[2] *FX and International Finance Trends*, and *Financial Market Trends*, the discussions of the Monetary Policy Board (MPB) members covered the following areas:

All members expected the domestic economy to run above the path previously projected and show a trend of expanded recovery. Looking at specific sectors, members expected exports and facilities investment to maintain their trends of improvement and the sluggishness in private consumption to ease gradually. However, members assessed that uncertainties related to COVID-19 remained high and expected the pace of economic recovery to be heavily dependent on the vaccine rollout schedule and the consequent trend of recovery in face-to-face industries.

Members noted that sluggishness in employment conditions was easing gradually, with the year-on-year change in the number of persons employed turning positive in March. Members, however, pointed out that a closer look at the details of employment showed that the degree of improvement in overall employment conditions remained insufficient. Members saw that the upward trend of inflation had accelerated due to supply factors and could accelerate further in the short term. In this regard, some members gave attention to the pickup in the inflation expectations of the general public to the lower-2% level and presented the opinion that a close eye should be kept on the future inflation trend. Other members' assessment was that, despite the increase in the price level felt by the general public, present conditions did not give rise to concerns about inflation, in contrast with the situation in the US.

Members, meanwhile, judged that with accommodative financial conditions having been ongoing, financial stability risks had grown, as seen in a sustained increase in leverage in the private sector including household lending. Accordingly, some members called for increased vigilance with respect to financial stability conditions going forward.

Members also noted that household and corporate lending rates had been moving in somewhat different directions of late, requiring continuous monitoring and analysis in terms of the transmission of accommodative monetary policy. Members also emphasized the need to closely analyze major pending issues, such as the possibility of intensified

2) An English version of *Recent Economic Developments* is posted on the Bank of Korea website.

US-China disputes, medium- to long-term Treasury bond supply and demand conditions, and financial conditions in the corporate sector.

Ⅲ. Discussions Concerning Monetary Policy Decision (Summary)

The main details of the MPB members' discussions concerning a change in the Bank of Korea Base Rate were as follows:

All members shared the view that, in overall consideration of the domestic and international financial and economic environments, it would be desirable to keep the Base Rate at the current level of 0.50%.

One member presented the view that it would be desirable to keep the Base Rate at the current level of 0.50%.

The member assessed that the domestic economic recovery had been expanding of late, with the private consumption slump easing and the solid recoveries in exports and facilities investment continuing, led by the IT sector. The member saw that, going forward, the domestic economy would recover faster than the February projection, thanks to expanded growth in exports and investment, and gradual improvement in private consumption. The member, however, judged that uncertainties surrounding the pace of economic recovery in line with COVID-19 developments and vaccine supply remained high. The member pointed out that it was difficult to forecast the timing of normalization of domestic economic activity, due to disruptions in the global supply of vaccines and recent increases in new confirmed cases at home and abroad. Meanwhile, the member noted that labor market conditions were partially improving, with the number of persons employed shifting to an increase in March, but had not reached pre-pandemic levels.

The member noted that consumer price inflation had risen to the mid-1% level in March, influenced for instance by international oil prices and prices of agricultural, livestock and marine products. The member expected consumer price inflation to fluctuate at around the 2% level for some time, as upward pressures on the supply side would continue. The member also commented that the inflation expectations of the general public had risen to the lower-2% level, and presented the opinion that a close watch should be kept on the future movements of inflation expectations and their impacts on the actual price trend.

Concerning the financial market, the member assessed that preference for risk assets was continuing in line with improvements in domestic and overseas economic indicators. The member noted that market interest rates, and long-term ones in particular, had remained on a continuous rise overall, and stock prices had rebounded on improved investment sentiment after mid-March. The member added that the Korean won to US dollar exchange rate had risen significantly and then had fallen back, influenced by global movements of the US dollar. The member assessed recent financial market movements to reflect growing expectations for economic recovery. The member judged that overall financial conditions were maintaining an accommodative level that supported real economic recovery, as rises in short-term market interest rates and lending rates had been limited, although long-term interest rates continued to increase. The member, however, pointed out that such accommodative conditions and ongoing preferences for risk assets had been working to increase the risk of financial imbalances, through for instance the buildup of household debt and a continual rise in asset prices. The member also presented the view that it should be noted that the international financial market was showing much greater sensitivity to inflation and to changes in the US Federal Reserve's monetary policy stance.

Taking all this into consideration, the member presented the opinion that the accommodative stance should be maintained for some time, in consideration of the still-high uncertainties related to COVID-19 developments, although the domestic economic recovery had been expanding of late. The member went on to argue that, in this process, a close watch should be kept on changes in financial stability risks. The member thus judged that it would be appropriate to hold the Base Rate at the current level.

Another member presented the view that it would be appropriate to keep the Base Rate unchanged from its current level of 0.50%.

Looking at global economic developments since the February MPB meeting, the member assessed that the global economy was showing a trend of recovery, led by the US and China, but the pace of recovery differed from country to country, depending on the progress of COVID-19 vaccination. The member saw that, on the domestic economic front, major improvements in exports and facilities investment had been sustained and were likely to continue going forward, despite destabilizing factors such as possible intensification of US-China disputes. The member assessed that sluggishness in private consumption was easing gradually, and projected that a full-scale recovery would be heavily dependent on pandemic developments and vaccine distribution going forward. The member pointed out that, in the labor market, the number of persons employed had shifted to an increase, thanks for instance to a base effect, but employment felt by the general public was in a situation that could not be easily improved, due to sluggishness in services in the private sector. The member called for close monitoring to see whether trends of improvement in employment would continue or not, considering the greater difficulties for small businesses since the outbreak of the pandemic and changes in production and consumption patterns including the spread of work from home and increased online shopping. Meanwhile, on the inflation side, the member noted that consumer price inflation was likely to reach the 2% level in the second quarter, due mainly to rises in agricultural, livestock, and marine product prices and international oil prices, but would not reach the inflation target of 2% on an annual basis.

The member's evaluation was that, while the IMF and other major organizations had made upward revisions to their growth outlooks for the domestic economy, upward risks to growth and inflation had increased since the February projection. The member, however, judged that monetary policy should remain accommodative, as uncertainties related to the resurgence of the pandemic and vaccine supply were sustained, and consumer price inflation was likely to run below the target on an annual basis.

Meanwhile, the member commented that, although the international financial market had been stable overall, attention should be paid to the possibility of increased financial unrest in emerging market economies in line with rises in long-term market interest rates in the US. The member noted that long-term interest rates had risen in the domestic financial market as well, and assessed that this trend was in a way a natural consequence of expectations for recovery in economic activity and prices, just as had been seen in the US. The member estimated financial conditions to be considerably accommodative, and also emphasized the need to consider the point that the rises in financing rates for households and corporations were lower than the rises in long-term market interest rates. Meanwhile, the member assessed concerns about financial imbalances to have increased, with household lending in the financial sector in the first quarter increasing sharply, despite the government's strong regulations. Accordingly, the member stated that there was a growing need to consider financial stability issues at the monetary policy level.

Taking all this into comprehensive consideration, the member argued that it would be desirable to keep the Base Rate at its current level of 0.50% and continue monitoring real economic developments, the coronavirus vaccine rollout situation, and household debt and asset market trends.

One member presented the view that it would be appropriate to keep the Base Rate unchanged from the current level.

The member assessed that exports and investment were showing faster-than-expected recovery on noticeable improvements in economic conditions in major countries, influenced for instance by rapid vaccinations. The member, however, added that recovery in private consumption had been limited due to the continued spread of the pandemic and uncertainties related to vaccines. The member pointed out that, despite a shift to an increase in the number of persons employed in March, the details of employment conditions remained weak, as the contribution of growth in temporary workers was high, for instance. Looking at inflation, the member saw that consumer price inflation excluding administered prices had risen to the 2% level in March, but core inflation was likely to run at the lower- to mid-1% level for some time, even when the decline stemming from administered prices was accounted for. Taking all these into consideration, the member presented the opinion that the Base Rate should be kept at its current level to support the domestic economic recovery, since private consumption, employment, and prices remained sluggish, despite significant improvement in external conditions.

The member, however, raised concerns about the buildup of financial stability risks, as household lending was sustaining high growth of around 10 trillion won a month due to increased lending in the non-banking sector, and lending to small- and medium-sized enterprises also continued to rise sharply. The member stated that such loans appeared to be sound, with their delinquency rates remaining low, but pointed out that the actual credit risks were estimated to be higher in consideration of the growing debt burden stemming from the sluggishness in economic activity and employment, and the weakening financial strength of small- and medium enterprises. The member thus expressed the view that the relevant risk factors should be continually monitored, and macroprudential policy encompassing the non-banking sector should be implemented without delay. The member added that special attention should be paid to the recent increase in the interest repayment burden of households and corporations as financing rates rose due to higher market interest rates and the greater share of lending in the non-banking sector.

The member assessed that, with respect to expectations of economic conditions for conducting monetary policy going forward, the upside risks were greater than the downside risks: exports and investment continued to show improvement, bolstered by improved external conditions, and domestic demand and employment were continually recovering, albeit moderately. However, the member stated that it was too early to discuss monetary policy normalization, given the still-high uncertainties related to domestic COVID-19 developments and vaccination, and continued difficulties in damaged sectors. The member, however, added that, since the economy was becoming more vulnerable to rising interest rates in the future due to the buildup of private debt, it was important for economic agents to pay attention to and prepare for such a situation.

Meanwhile, another member presented the view that it would be appropriate to keep the Base Rate unchanged from the current level.

The member assessed that the global economy was showing a stronger-than-expected recovery, boosted by massive fiscal stimulus in major countries and the expansion of vaccinations. The member added that the domestic economy was also exhibiting a stronger recovery, as export growth was accelerating and facilities investment continued to recover, bolstered by the global economic recovery and the buoyant semiconductor industry, and as the sluggishness of consumption and employment was easing. Concerning inflation, the member mentioned that consumer price inflation would reach around 2% in the second quarter, driven by a base-period effect on top of the widening scale of increase in petroleum and agricultural product prices, and inflation expectations among the general public were growing slightly of late. Financial market conditions, meanwhile, had remained accommodative for a considerable period of time, with household lending sustaining substantial growth, and the domestic FX market continued its stable trend.

The member projected that the domestic economy would sustain a recovery, boosted by exports and investment, and that the growth rate for this year would be above the February forecast. The member, however, assessed that uncertainty surrounding the future recovery path remained high, as the worsening resurgence of COVID-19 and uncertainties related to vaccine distribution could have a considerable impact on consumption and employment.

Taking these overall conditions into consideration, the member assessed that it would be desirable to keep the Base Rate at its current level. The member expressed the view that, while maintaining the current accommodative monetary policy stance to support a full-fledged recovery, careful attention should continue to be paid to the accumulation of factors likely to undermine financial stability in the future due to the sustained monetary easing. The member added that it would be necessary to consider conducting monetary policy with a greater focus on financial stability once the spread of COVID-19 eases and the domestic economy shows a marked recovery.

One member presented the view that it would be desirable to hold the Base Rate at its current level.

The member assessed that the domestic economy was exhibiting robust growth boosted by exports and facilities investment, and expected that production and exports of not just the IT industry but also non-IT industries would contribute noticeably to growth this year. The member’s evaluation was that although the spread of COVID-19 was not easing and vaccinations were proceeding more slowly than expected, the consumer sentiment index had improved significantly and various consumption indicators were actually emerging rapidly from their sluggishness at the end of last year and at the beginning of this year. The member added that labor market conditions overall had started to show a recovery.

The member noted that the 10-year Korean Treasury bond yield had recently shown a larger extent of increase, in strong synchronization with US long-term rates, raising concerns that there might be inflationary pressures in the domestic economy. The member, however, took the view that domestic long-term rate fluctuations are analyzed as being affected more by US long-term rates and Korean Treasury bond supply and demand conditions than by inflation, and that in this regard it would be excessive to interpret the uptrend in long-term interest rates as signaling inflationary pressures at a similar level to those of the US. The member mentioned that both the Bank of Korea and the IMF had forecast consumer price inflation to remain in the low- to mid-1% range and the GDP deflator growth rate to be even lower this year. The member argued that the domestic economy was undoubtedly sustaining its recovery, but since the recovery was still at the early stages and employment, wages and inflation were moving slowly, it was still too early to talk about normalizing monetary policy out of concerns about inflation.

The member's evaluation was that, although the Base Rate had declined to an unprecedentedly low level due to the accommodative monetary policy over the past year, real interest rates had not fallen as much as nominal ones had when the low inflation trend was counted in, and it was also difficult to say that current rate was lower than the neutral one although there is some uncertainty in estimating the neutral rate. The member noted that, since inflation had fallen substantially below the Bank of Korea's target level, taking monetary policy in a more firmly accommodative direction would help speed up economic recovery. The member, however, expressed the view that, since this could lead to an excessive prolongation of the gap between the real economy and real estate prices, it would be necessary to focus on stabilizing funding rates for the government and enterprises, rather than to make additional rate cuts. More specifically, the member emphasized that it would be necessary to maintain and expand support measures for SMEs, such as the bank intermediated lending support facility, until the economy shows an even stronger recovery, while purchasing an appropriate amount of Korean Treasury bonds to control upward pressures on long-term interest rates.

Another member presented the view that it would be appropriate to keep the Base Rate unchanged from the current level.

First, looking at the global economy, the member assessed that the economic recovery was back on track, driven by expanded vaccine distribution and major countries' implementation of stimulus packages. More specifically, the member forecast that the quarter-on-quarter growth rate of the global economy would rebound again in the second quarter, as corporate investment in major countries and goods exports by Asian countries continued to grow robustly and major survey results improved greatly. The member, however, judged that uncertainty surrounding the medium- and long-term recovery path remained high, since it was still unclear how the spread of COVID-19 would play out and the gap in economic activity between countries had widened significantly.

The member assessed the domestic economy as maintaining more favorable growth than originally forecast, with manufacturing production and exports increasing sharply. The member added that the gap in economic activity between industries and sectors had been easing somewhat. The member, however, mentioned that demand in face-to-face industries remained extremely sluggish, and the business climate for related industries was unlikely to improve any time soon considering the pace of the recent spread of COVID-19 and the status of vaccine distribution in Korea. The member argued that it would be necessary to pay attention to the possibility that prolonged sluggishness in face-to-face industries would worsen employment conditions for vulnerable groups, preventing the economy from entering a full-fledged recovery phase and consequently having a negative impact on growth potential.

In terms of inflation, although consumer price inflation had accelerated month-on-month in March, the member projected that this trend would not continue after the second half of this year, considering the recent trends of international oil and grain prices and the influence of base-period effects. The member, however, presented the view that, since price rises caused by supply-side factors had continued longer than usual and inflation expectations at home and abroad were likely to increase somewhat while economic activities were getting back to normal, the possibility could not be ruled out of upward pressures on underlying inflation increasing to a greater extent than expected.

The member's evaluation was that financial conditions had become even more accommodative in the meantime. The member pointed out that a sharp rise in long-term market interest rates had only limited impacts on short-term benchmarks and lending rates in the banking sector and that prices of risk assets continued to rise. The member, however, pointed out that leverage in the private sector continued to increase, with household lending sustaining strong growth led by accommodative financial conditions, and went on to argue that attention should be paid to the possibility that this could heighten medium- and long-term financial vulnerability and negatively affect the efficiency of resource allocation.

Taking all these into consideration, the member argued that it would be desirable to keep the Base Rate at its current level of 0.50% to help the domestic economy become established in a broader recovery phase. The member, however, emphasized that, amid the continued accommodative financial conditions, expectations of domestic and overseas economic recovery and inflation had been growing, which could act to expand leverage in the private sector and increase the risk of the accumulation of financial imbalances, and added that heightened vigilance would be needed in this regard.

Ⅳ. Results of Deliberation on Monetary Policy Directions

Incorporating the outcome of the above discussions, the following Monetary Policy Decision statement was compiled. All MPB members supported the decision unanimously.

Monetary Policy Decision

□ The Monetary Policy Board of the Bank of Korea decided today to leave the Base Rate unchanged at 0.50% for the intermeeting period.

□ Currently available information suggests that the recovery of the global economy has remained slow due to the ongoing influence of the movement restrictions following the resurgence of COVID-19. In global financial markets, stock prices and government bond yields in major countries have increased, mainly driven by the expectations for economic recovery following the expansion of vaccinations and the prospect of a further fiscal stimulus package by the new US administration. Looking ahead, the Board sees global economic growth and global financial markets as likely to be affected largely by the severity of the resurgence of COVID-19 and the status of vaccine distribution, as well as by national policy responses and their effects.

□ The Korean economy has continued to recover modestly. Although private consumption has remained weak as social distancing has been prolonged, exports have sustained their buoyancy led by the IT sector and facilities investment has continued to recover. Labor market conditions have remained weak, as the number of persons employed declined sharply compared to the corresponding period last year. Going forward, the economy is likely to continue its recovery, led by exports and investment. However, uncertainties surrounding the pace of recovery are judged to remain elevated. GDP growth this year is projected to be around 3.0%, generally consistent with the November forecast.

□ Consumer price inflation has remained at the mid-0% level as the surging prices of agricultural, livestock, and fisheries products were offset by factors such as the decreasing prices of public services. Core inflation (excluding changes in food and energy prices from the CPI) has also remained at the mid-0% level. The inflation expectations of the general public have risen to 2%. It is forecast that consumer price inflation will run at the low- to mid-1% level this year, exceeding the November forecast of 1.0%, largely reflecting the increase in global oil prices and gradual improvement in economic activity. Core inflation is forecast to run at around 1%.

☐ In domestic financial markets, long-term market interest rates and the Korean won to US dollar exchange rate have risen, mainly driven by global financial market movements. Stock prices have fluctuated considerably, affected by both expectations for economic recovery and caution about the recent rally. Household loan growth has accelerated, and housing prices have continued to increase rapidly in all parts of the country.

☐ The Board will continue to conduct monetary policy in order to support the economy and stabilize consumer price inflation at the target level over a medium-term horizon, while paying attention to financial stability. As the recovery in the Korean economy is expected to be modest and inflationary pressures on the demand side are forecast to remain weak, the Board will maintain its accommodative monetary policy stance. In this process the Board will thoroughly assess developments related to COVID-19 as well as the effects of the policy measures taken in response to the pandemic, while paying attention to changes in financial stability conditions such as fund flows to asset markets and household debt growth.