

Minutes of the Monetary Policy Committee Meeting

August 8, 2013

The Bank of Korea

Minutes of the Monetary Policy Committee Meeting¹⁾

(August 2013)

I . Outline

1. Date of meeting : Thursday, August 8, 2013
2. Place : Monetary Policy Committee Meeting Room
3. Monetary Policy Committee members present:
Kim, Choongsoo, Chairman (Bank of Korea Governor)
Lim, Seungtae
Park, Won Shik (Senior Deputy Governor)
Ha, Seong Keun
Chung, Hae-Bang
Chung, Soon Won
Moon, Woosik
4. Monetary Policy Committee members absent : none
5. Participants :
Song, JaeJung, Auditor
Kim, Jun Il, Deputy Governor
Kang, Juno, Deputy Governor
Kang, Tae Soo, Deputy Governor
Hur, Jae Sung, Deputy Governor
Suh, Young Kyung, Deputy Governor
Choo, Heung Sik, Director of Reserve Management Group
Choi, Woon Gyu, Director of Economic Research Institute
Shin, Woon, Director General of Research Department
Seong, Byung Hee, Director of Macprudential Analysis Department
Kim, Min-Ho, Director General of Monetary Policy & Markets Department
Ryoo, Sangdai, Director General of International Department
Jeon, Seung-Cheol, Director General of Monetary Policy Committee Secretariat
Kim, Tae Suk, Director General of Press Office
Kim, Nam Young, Director of Financial Markets Division
Moon, Han Geun, Head of MPC Administrative Support Team

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

II. Summary of Discussions on the Current Economic Situation²⁾

After briefings by staff on 'Current Economic Developments in Korea', 'FX and International Finance' and the 'Financial Markets', the discussions of the Monetary Policy Committee (MPC) members covered the following areas:

Concerning **the global economy**, the members' assessment was that, the moderate economic recovery in the US had been sustained but the sluggishness of economic activities in the euro area had continued, while economic growth in emerging market countries such as China had slowed somewhat. Many members expected **the global economy** to sustain its modest recovery **going forward**, due mainly to improvements in the US economy, but judged that factors such as the uncertainties surrounding the monetary policy stances and fiscal consolidations in major countries including the US, and the possibilities of slower economic growth in China would remain as downside risks to growth.

Many members mentioned that, in **the international financial markets**, with global interest rates showing stable trends due to the easing of concerns about early QE tapering by the US Federal Reserve, stock prices had risen sharply.

Concerning the **domestic economy**, members assessed domestic demand such as for consumption and investment to be increasing, helped by the Base Rate cut and the stimulus measures taken by the government, with exports also showing buoyancy centering around those to the US and China.

As for **the future outlook**, many members anticipated that the negative output gap would narrow steadily, as the domestic economy sustained its

2) The contents of 'Current Economic Developments in Korea' and the 'Financial Markets' are posted in English on the Bank of Korea website.

modest recovery due mainly to the gradual improvements in external conditions and to continuation of the government policy effects.

With regard to the **domestic financial markets**, members pointed out that, after having declined under the influence of the movements of major country government bond yields, long-term market interest rates had risen with the improvements in economic indicators, causing the spread between long- and short-term rates to widen. They went on to note that stock prices had fallen again, after having risen due mainly to increases in global stock prices and to foreign capital inflows, while the Korean won had appreciated slightly.

Many members mentioned that, although **consumer price inflation** had risen compared to the previous month, with the reversals to increase in the prices of agricultural and livestock products and petroleum products, it still maintained a low level of around 1%. Many members forecast that, although inflation would be higher than its current level, due mainly to imbalances in supply and demand for agricultural products resulting from the bad weather conditions and to a base effect from its low rate of increase in the second half of 2012, it would show a stable trend for the time being as the output gap remained negative.

III. Discussions Concerning Monetary Policy Decision (Summary)

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

Members shared the opinion that it would be desirable to hold the Base Rate at its current level for the intermeeting period, as with prices stabilized the domestic economy was forecast to sustain its trend of recovery, albeit moderate, due mainly to the gradual recovery of the global economy.

One member expressed the opinion that, given the ongoing concerns about QE tapering by the US Federal Reserve and the occurrences of foreign capital outflows from some emerging market countries, it would be desirable to review the effectiveness of the measures for mitigating capital flow volatility carried out to that point.

Another member commented that, with the recent expansion in size of the domestic bond market and the growing influence of foreign investors, the possibility was rising of shocks to the Korean economy caused by changes in long-term market interest rates owing to external shocks related for example to the question of US exit strategy implementation, and that effective policy measures in response should therefore be sought.

Another member pointed out that, while bearing in mind the phenomenon of microeconomic shocks affecting the macroeconomy as shocks to certain industries transformed into shocks to macroeconomic variables through the interconnected structure of the economy, it was necessary for macroprudential policy to be conducted in harmony with monetary and credit policy to ensure that financial sector procyclicality did not expand through the linkages between input and output.

In addition, one member noted that the volume of foreign investment

in the domestic bond market had recently soared to a level more than 13 percent higher than at the beginning of the year, and asserted the need for devising preemptive measures to stabilize the inflows of short-term speculative funds so as to minimize the harmful consequences of excessive in- and outflows of investment funds of foreigners.

Finally, another member expressed the view that it was necessary for the Bank of Korea, as the central bank, to analyze the path through which household debt could return to an appropriate level that would not pose a burden to the macroeconomy and the financial system, and contribute thereby to improving the effectiveness of the measures being carried out by the government to achieve a soft-landing of the household debt problem.

IV. Results of Deliberation of Monetary Policy Directions

Reflecting the outcome of these discussions, the following Monetary Policy Decision statement was prepared and then unanimously approved by the members:

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Monetary Policy Decision

- ☐ The Monetary Policy Committee of the Bank of Korea decided today to leave the Base Rate unchanged at 2.50% for the intermeeting period.
- ☐ Based on currently available information, the Committee considers the moderate economic recovery in the US to have been sustained but the sluggishness of economic activities in the euro area to have continued, while economic growth in emerging market countries such as China has slowed somewhat. The Committee forecasts that the global economy will sustain its modest recovery going forward, helped primarily by improvements in the US economy, but judges that the possibilities of changes in global financial market conditions related to the exit strategy of the US Federal Reserve, and of a slowdown in Chinese economic growth, and the uncertainties surrounding the implementations of fiscal consolidation in major countries, remain as downside risks to growth.
- ☐ In Korea, the Committee appraises economic growth to be continuing, albeit moderately, mainly led by exports. On the employment front, the increase in the number of persons employed has accelerated, centering around the 50-and-above age group and the service sector. The Committee expects that the domestic economy will maintain a negative output gap for a considerable time going forward, although it forecasts that the gap will gradually narrow.
- ☐ Consumer price inflation rose to 1.4% in July, from 1.0% the previous month, as the prices of agricultural and livestock products

as well as petroleum products turned upward, and core inflation excluding the prices of agricultural and petroleum products increased slightly to 1.5%, from 1.4% in June. The Committee forecasts that inflation will show a stable trend for the time being as the output gap remains negative, although it will rise above its present level due mainly to imbalances in agricultural product supply and demand caused by bad weather and to a base effect from its low rate of increase in the second half of last year. As for housing prices, those in Seoul and its surrounding areas sustained their downtrend, while those in the rest of the country continued their uptrend.

- ☐ The domestic financial markets have generally stabilized with the easing of concerns about an earlier-than-expected tapering off of US quantitative easing. Long-term market interest rates have risen modestly, primarily on improved global economic indicators, after having declined in concert with those of major economies. Stock prices, after having risen due to a shift to net inflows of foreigners' stock investment funds, have fallen back somewhat recently and the Korean won has appreciated.
- ☐ Looking ahead, while closely monitoring the trends and the influences of changes in external risk factors, and the effects of the Base Rate cut and of the government's economic policies including the supplementary budget, the Committee will conduct monetary policy so as to keep consumer price inflation within the inflation target range over a medium-term horizon while ensuring that the growth potential is not eroded due to the continuation of slow growth.