Minutes of the Monetary Policy Board Meeting

August 2024

Bank of Korea

English version

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August 2024

Ⅰ. Outline

1. Date of meeting: Thursday, August 22, 2024

2. Place: Monetary Policy Board Meeting Room

3. Monetary Policy Board members present:
   Rhee, Chang Yong, Chairman (Governor)
   Shin, Sung Hwan
   Chang, Yongsung
   Ryoo, Sangdai (Senior Deputy Governor)
   Hwang, Kunil
   Kim, Jong Hwa
   Lee, Soo Hyung

4. Monetary Policy Board members absent: none

5. Participants:
   Kang, Sungjun, Auditor
   Lee, Jongryeol, Deputy Governor
   Kim, Woong, Deputy Governor
   Chae, Byung Deuk, Deputy Governor
   Kwon, Min Soo, Deputy Governor
   Park, Jongwoo, Deputy Governor
   Lee, Jae Won, Chief Economist
   Lee, Jiho, Director General, Research Department
   Chang, Cheong Soo, Director General, Financial Stability Department
   Choi, Chang Ho, Director General, Monetary Policy Department
   Choi, Yong Hoon, Director General, Financial Markets Department
   Yoon, Kyoungsoo, Director General, International Department
   Oh, Kum Hwa, Director General, Reserves Management Group
   Baek, Mooyeol, Director General, Office of Legal Affairs
   Lim, Kun Tae, Monetary Policy Board Secretariat
   Kim, Yong Sik, Press Officer
   Hur, Hyun, Head, MPB Administrative Support Team

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1) This English version is an excerpt of the Monetary Policy Board members' opinions on the Bank of Korea's Base Rate decision, taken from the minutes of the Monetary Policy Board Meeting.

Ⅱ. Discussions Concerning the Monetary Policy Decision

At the August 22, 2024, Monetary Policy Board meeting, each member expressed their opinion on the Bank of Korea’s Base Rate decision.

All members shared the view 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 expressed the view that it would be appropriate to hold the Base Rate at the 3.50% for the intermeeting period.

The member judged that, considering the persistently strong U.S. economy and the easing of sluggish growth in the euro area, the global economy would maintain its modest growth, although the pace of its recovery might be slower than initially expected.

The member stated that, recently, unexpected U.S. economic data had greatly shocked financial markets temporarily and raised concerns about an economic recession, but that the U.S. economy is generally unlikely to deviate from the expected soft landing path. Conflicting signals from U.S. employment indicators are being seen as the labor market gradually returns to its equilibrium level after exhibiting historic growth since the pandemic, rather than representing any downside risk to the U.S. economy.

The member forecast that, although the domestic economy recorded negative growth in the second quarter, affected by substantial corrections in domestic demand -- in particular, private consumption and investment, owing chiefly to base effects -- the economy would exhibit favorable growth in annual terms, with strong export growth acting as a key driver of economic growth. However, growth momentum is expected to weaken somewhat, as global trade is likely to improve slowly and as domestic demand will likely recover at a slower-than-expected pace due to complex and unpredictable geopolitical risks.

The member stated that consumer price inflation had rebounded temporarily in July driven by fluctuations in global oil prices and a reduction in the fuel tax cut rate. The member, however, projected that consumer price inflation would continue its downward trend and gradually approach the target level, influenced by reductions in supply-side inflation pressure.

Concerning financial markets, the member noted that restrictive financial conditions have continued to ease, while Treasury bond yields declined substantially, widening the inversion between the Base Rate and Treasury bond yields, driven by the spread of expectations of a rate cut by the U.S. Federal Reserve and by Treasury bond futures purchases by foreign investors. Herd behavior in the bond market seems to have resulted from excessive expectations concerning future U.S. and Korean monetary policies, and as such expectations can suddenly be reverted in the future, careful attention to market volatility is necessary.

The member was of the view that, as the disparity in economic growth between the U.S. and other major countries has been narrowing and as a rate cut by the U.S. Federal Reserve is now in sight, there is growing likelihood that factors supporting the strong dollar will gradually weaken. In this regard, although concerns remain in the foreign exchange market, upward rigidity of the won-dollar exchange rate is expected to strengthen gradually.

The member presented the view that, given these domestic and external economic conditions, and, specifically, housing price hikes in the Seoul metropolitan region and the consequent growth in household lending, it would be desirable to keep the Base Rate at its current level of 3.5%.

The member saw that, while exchange rate depreciation pressure has been weakening, the current Base Rate level, which has been unchanged now for an extended period, is showing inflation to have gradually converged on the target level, while it is also working restrictively on the real economy, such as consumption and investment. Accordingly, expectations and conditions for monetary policy easing have been gradually ripening. However, it should be accompanied by effective macroprudential policies to curb financial imbalances, such as rising housing prices and any growth in household lending.

Another member expressed the view that it would be appropriate to leave the Base Rate unchanged at this meeting and maintain it at 3.50%.

The member commented that, as the slowdown in consumer price inflation has become apparent across major economies, pivots in monetary policy stances are coming into full swing. In the U.S., uncertainties regarding the pace of economic slowdown remain, as the market responded sensitively to the unemployment rate, which was slightly higher than projected. However, the dominant view is that the U.S. Federal Reserve's pivot is now in sight.

As for the domestic economy, the member projected that even with strong exports led by semiconductors, due to the slow recovery in domestic demand the growth rate for the year will reach the level of its long-term average. With regard to employment, aggregate indicators are favorable, with the unemployment rate reaching a record low, while employment is weak in domestic demand sectors, including construction.

The member forecast that consumer price inflation, if it remains on the downward path, would decline to the lower 2% level at the year-end. Given stable inflation, the slow recovery of domestic demand, and high delinquency rates among some vulnerable sectors, it seems to be the right time for gradual monetary easing. Such expectations can be also seen in the sharp decline in market rates.

The member, however, expressed huge concerns about the rapid rise in real estate prices, particularly in the Seoul metropolitan region. While financial conditions are easing, rate cuts should not act as a catalyst to accelerate the rise in real estate prices. Real estate price hikes in some regions could not only intensify household debt growth and worsen wealth inequality but could also undermine the efficiency of resource allocation in the long-term.

The member pointed out that interest rates have non-discriminatory effects on the economy as a whole. Negative side effects of rate cuts can be eased when accompanied by macroprudential policies curbing real estate demand. In this regard, it is necessary to monitor whether future policies have tangible results.

With all these factors taken into consideration, the member believed that it would be appropriate to keep the Base Rate at the current level of 3.5% and determine future policy directions while keeping an eye on major countries' monetary policies, the process of resolving real estate proejct financing, and developments in the housing market and in household debt.

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

The member noted that the global economy is expected to continue its trend of modest growth. However, uncertainties over the pace of future growth increased with growing concerns about an economic recession in the U.S.

The member observed that inflation in major economies continued to slow across the board. As a result, most central banks in advanced economies began cutting rates or have signaled the possibility of doing so. Although geopolitical risks somewhat heightened in the Middle East, international oil prices generally stabilized at low levels due to the prediction of a softening in global oil demand.

With regard to international financial markets, the member noted that major price variables showed significant volatility as the risk-off sentiment strengthened considerably and then reversed in response to worries about an economic recession in the U.S. and policy rate hikes in Japan. Global stocks bounced back quickly after having plunged, and government bond yields in advanced economies fell considerably on heightened expectations of the U.S. Federal Reserve's rate cuts.

The member stated that domestic financial and foreign exchange markets witnessed high volatility affected by changes in the global risk-off sentiment. Stock prices rebounded after having fallen steeply and long-term government bond yields dropped below 3%. The won-dollar exchange rate decreased due to the weakening of the dollar.

Regarding the domestic economy, the member observed that exports were booming, whereas the recovery in consumption had been slower than anticipated due to the monsoon season being longer than in an average year and due to a delayed improvement in income conditions. Looking ahead, the domestic economy is projected to show modest growth, as exports continue to grow and as consumption gradually recovers due to improved real incomes. However, there are high uncertainties concerning the sustainability of the strong export growth.

As for inflation, the member judged that domestic inflation continued to cool. In July, consumer price inflation increased slightly owing to rises in international oil prices, but the core inflation rate remained low, at the lower 2% level, and short-term inflation expectations moved down as well. Going forward, inflation is anticipated to continue its slowing trend.

The member observed that household loans in the financial sector rose at a rapid pace, driven by the increase in apartment prices and transaction volume in Seoul and its surrounding areas. Given that the government recently announced real estate measures to cool the market, it would be necessary to examine the policy effects, while closely monitoring household debt and housing market conditions for the time being.

Meanwhile, the member stated that, although credit risk aversion had somewhat eased thanks to the government's real estate project financing soft landing measures, delinquency rates on loans from non-banks still remained at high levels.

In summary, the member expected inflation to converge toward the target level, with the domestic economy maintaining a moderate growth trend. However, concerns about the buildup of financial imbalances have increased due to rising housing prices and expanding household loan growth. Additionally, there is still caution in foreign exchange markets due to increased volatility in international financial markets.

Taking these circumstances into comprehensive consideration, the member took the view that the Base Rate should be maintained at the current level of 3.50% at this meeting. In addition, it is necessary to manage market expectations appropriately through communication to prevent risks to financial stability from escalating.

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

The member observed that, amid the recent modest global economic recovery, concerns about a recession in the U.S. were highlighted due to the weaker-than-expected jobs report. However, such fears had somewhat eased in line with the subsequent release of positive economic data. Given that the services industry, which accounts for a large share of the U.S. economy, remained robust, the likelihood of a sharp slowdown in U.S. economic growth was not high. Meanwhile, on the inflation front, as the disinflationary trend continued, the U.S. Federal Reserve's burden of pivoting waned significantly. In Japan, the Bank of Japan's rate hike triggered a significant repatriation of yen carry funds accummulated over an extended period, leading to a sharp strengthening of the yen and a significant increase in risky asset price volatility. Japan's monetary policy emerged as a major source of uncertainty in global financial markets. In China, amid ongoing weak domestic demand and a sluggish real estate sector, the pace of its economic recovery would likely depend on the extent of practical policy support from the Chinese government after the third plenum.

The member noted that the domestic economy continued to show divergence, with exports booming but with domestic demand remaining sluggish. However, domestic demand is expected to improve modestly following the third quarter of 2024, with private consumption projected to gradually pick up on the back of sustained real wage growth. In the labor market, while the unemployment rate declined slightly, the growth in the number of persons employed remained lower than expected. Meanwhile, since inflation continued to slow in line with the forecasted path, it was not seen to be a constraint on rate cuts at this moment.

The member observed that in global financial markets, government bond yields in major economies fell significantly in response to the dovish July FOMC meeting outcome and in response to concerns about a U.S. economic recession. Affected by this, government bond yields in the domestic financial market declined sharply as well, easing financial conditions. Moreover, overall liquidity remained quite favorable, with a continuous increase in the money supply (M2). However, delinquency rates have continued to rise driven by corporate loans from non-bank financial institutions, and risks are still lurking with regard to some construction firms and non-bank financial institutions involved in real estate project financing. Therefore, the member noted that caution was needed to ensure that financial market unrest does not materialize during the restructuring process of real estate project financing. Meanwhile, housing prices continued to gain strong growth momentum with a steady rise in housing prices in the Seoul metropolitan area, and home mortgage loans also rose significantly. In addition, if the U.S. Federal Reserve cuts interest rates going forward, domestic financial market conditions could ease through interest rate synchronization, further fuelling the rise in housing prices. This could increase the demand-side pressure on household debt, so it is time to pay close attention to the possibility of another large increase in household debt, the member noted.

Concerning the domestic foreign exchange market, the member stated that the won-dollar exchange rate fell, affected mainly by a decline in the U.S. Dollar Index (DXY). The foreign currency money market remained generally stable. Arbitrage incentives still remained low, although there was an increase due to a stronger risk aversion in line with the emergence of concerns over a U.S. economic recession, while foreign currency borrowing spreads and CDS premiums maintained low levels as well.

In consideration of the abovementioned economic and financial conditions at home and abroad, the member judged that it was appropriate to maintain the Base Rate at the current level of 3.50% at this meeting. Whereas the pivot risk associated with inflation had decreased greatly, and the need for a pivot increased due to lagging domestic demand, the likelihood of rate cuts translating into a rise in housing prices in the Seoul metropolitan area had risen significantly. It would be necessary to do the best to stabilize housing prices, as excessively high housing prices relative to income levels do not only undermine financial stability, but also decrease productivity in the economy by distorting resource allocation. In light of this, the member assessed that, at this point, it was proper to make sure that monetary policy would not further spur financial market instability, and noted that it would be desirable to determine rate cuts while examining the effects of real estate measures going forward, including macroprudential policies.

Another member expressed the view that it would be appropriate to leave the Base Rate unchanged at the current 3.50% at this meeting.

The member saw that the global economy has continued its moderate growth trend, but uncertainties regarding economic conditions in major countries, such as the U.S. and China, had somewhat increased. Regarding inflation in major countries, there had been progress in disinflation, with consumer price inflation rates generally continuing to slow. In international financial markets, risk aversion had intensified significantly due to concerns about an economic slowdown stemming from worsening U.S. employment indicators, as well as to a sudden strengthening of the Japanese yen due to the Bank of Japan’s interest rate hike. However, such risk averse sentiments have been largely reversed, with key price variables showing high volatility throughout this process.

The member stated that the domestic economy had resumed moderate growth in the second half of the year after contracting on a preliminary basis in the second quarter due to the base effect, but that the divergence between exports and domestic demand was continuing. While exports have continued to grow at a high rate due to the strong IT industry, the recovery in private consumption has been slower than expected due to the impact of abnormally high temperatures and heavy rainfall, with the consumption of goods remaining sluggish despite an improvement in real incomes. While construction investment remains sluggish due to the impact of sluggish construction starts and orders, facilities investment has turned positive as delayed investment in capital goods, such as semiconductor manufacturing equipment and aircraft, has resumed. On the employment front, the number of persons employed continues to grow and the unemployment rate remains low. Looking ahead, the domestic economy is expected to maintain growth above its potential level, driven by continued export growth and by a gradual recovery in consumption stemming from improvements in real incomes. However, the future growth path will likely be influenced by the recovery in consumption, the magnitude of the expansion of the IT sector, and economic conditions in major countries.

As for domestic inflation, the member noted that, while core inflation had continued to slow, the overall consumer price inflation rate temporarily increased in July due to higher petroleum product prices. Given the base effect of the sharp increase in oil and agricultural product prices last year and the downward stabilization of core inflation, inflation is expected to continue its slowing trend. The future path of inflation is likely to be influenced by international oil prices and exchange rate movements, agricultural product price trends, and whether public utility fees are adjusted. In the real estate market, the volume of housing transactions is increasing, particuarly for apartments in the Seoul metropolitan area, and housing price growth is also expanding.

The member took the view that, in the domestic financial market, the easing trend of financial conditions appears to have intensified, with market interest rates falling significantly and lending rates decreasing due to preemptively reflected expectations of a shift in monetary policies at home and abroad. Household loans have been increasing by about 5 trillion won per month, mainly driven by home mortgage loans, with a rise in housing transactions in the Seoul metropolitan area. Given the recent increase in housing transactions, it is likely that the growth in individual home mortgage loans, and in jeonse leasehold deposit loans in particular, will continue to expand for some time. However, risks related to real estate project financing remain latent, with delinquency rates on loans from non-banks staying high. In the foreign exchange market, the Korean won to U.S. dollar exchange rate dropped significantly due to the weakening of the U.S. dollar stemming from heightened expectations of a rate cut by the U.S. Federal Reserve, but concerns remain regarding the U.S. economic slowdown, the unwinding of the yen carry trade, and geopolitical risks.

Taking these points into overall consideration, the member saw it desirable to maintain the Base Rate at the current level of 3.5% at this meeting. Although inflation is expected to continue its slowing trend and gradually converge toward the target level, and as the recovery in domestic demand is slow, the possibility of financial imbalances growing due to rising housing prices, particularly in the Seoul metropolitan area and due to expanding growth in household loans is significant, and concerns in the foreign exchange market still persist. Against this backdrop, it is necessary to carefully assess the impact of any shift in monetary policy on financial stability. At this point, it is necessary to respond with an appropriate policy mix to prevent any prolonged expansion of risks in the housing market and in household debt.

Going forward, the member stated that it is necessary to closely monitor the inflation and growth trajectories in the conduct of monetary policy. When determining the timing and extent of any Base Rate cut, the direction of monetary policies in major countries, movements in financial and foreign exchange markets, and the financial stability situation, including the housing market and household debt, should be taken into consideration. At the same time, more vigilance when communicating is necessary to avoid any significant divergence between policy intentions and market expectations.

Another member presented the view that it would be appropriate to hold the Base Rate unchanged at the current 3.50% at this meeting.

The member noted that, regarding global economic conditions, as inflation gradually approaches the target level, more central banks in major countries are lowering their policy rates, and the possibility of a rate cut by the U.S. Federal Reserve has also increased. As central banks and markets in major countries gradually shift their focus from inflation to growth, market sensitivity to real economic indicators has heightened, as seen in the sharp fluctuations in stock prices in response to indicators like U.S. employment growth.

The member saw that the domestic economy has continued to grow, driven by stronger-than-expected export performance, particularly of IT products, but that the recovery in domestic demand remained sluggish. Although facilities investment has rebounded, the recovery in private consumption has been delayed as the positive momentum from strong exports has not extended to wages or employment growth, with the self-employed sector remaining weak, mainly due to structural challenges.

The member stated that the Korean won to U.S. dollar exchange rate has fallen from the upper 1,300 won range to the lower 1,300 won range lately. Although uncertainties remain high, including geopolitical risks and the outcome of the U.S. presidential election, the Korean won to U.S. dollar exchange rate is expected to continue its downward trend due to the U.S. Federal Reserve's rate cuts.

The member noted that underlying inflation indicators, including core inflation, have been stabilizing, approaching the 2% target level. While consumer prices have slightly increased, inflation expectations among the general public continue to decline. If no unexpected supply shocks occur, consumer price inflation is expected to narrow the gap with core inflation and converge toward the target level.

The member took the view that domestic financial conditions have eased further, with significant declines in both short- and long-term interest rates, in credit bond yields, and in lending rates. The growth in household loans, particularly home mortgage loans, expanded further in July and is at risk of increasing faster than GDP growth. Considering the relatively accommodative macroprudential policy stance, declining household lending rates, and the possibility of continued housing supply-demand imbalances in the Seoul metropolitan area, housing prices are likely to keep rising. Consequently, the rapid increase in household debt is expected to persist for some time.

The member argued that this trend could weaken household spending capacity due to the increasing debt repayment burden and threaten financial stability. It could also undermine economic dynamism by expanding the flow of funds into the real estate sector rather than into productive investments. Furthermore, it should be noted that high housing costs and asset prices relative to labor income can worsen wealth inequality, exacerbating structural problems in Korean society, such as the low birth rate and intergenerational or class conflicts.

Overall, the member presented the view that, considering that inflation is approaching the 2% target in a more stable manner after having surged since the pandemic, and that the external sector, including the exchange rate, is generally settling down, but that the recovery in domestic demand, such as private consumption, is slow, conditions are being created in which it would be possible to shift to a less restrictive monetary policy stance.

The member, however, emphasized that financial conditions had eased before a shift in monetary policy, and this, combined with vulnerabilities in the real estate market, was driving up housing prices and contributing to the growth in household debt. These developments have, in turn, increased the risk of negative impacts on financial stability, on medium- and long-term growth, and on the implementation of structural reforms. This suggests that it is necessary to operate the policy rate path on a higher trajectory than it would be if only inflation and growth forecasts were considered.

In this regard, the member expressed the view that it would be appropriate to keep the Base Rate at its current level of 3.5% at this meeting. Going forward, it is necessary to make monetary policy decisions carefully, by taking into account future economic and financial developments, the benefits and costs that Base Rate adjustments could have on domestic demand, inflation forecasts, financial stability, and the effects of the recently announced government housing and macroprudential policies.