Minutes of the Monetary Policy Board Meeting

July 2024

Bank of Korea

English version

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Ⅰ. Outline

1. Date of meeting: Thursday, July 11, 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, Jiho, Director General, Research Department
   Chang, Cheong Soo, Director General, Financial Stability Department
   Choi, Chang Ho, Director General, Monetary Policy Department
   Yoon, Kyoungsoo, Director General, International Department
   Oh, Kum Hwa, Director General, Reserves Management Group
   Baek, Mooyeol, 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

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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 July 11, 2024, 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 hold the Base Rate unchanged at the current 3.5% for the intermeeting period.

The member commented that the global economy was expected to maintain modest growth as initially projected, while economic trends would continue to vary in major countries. Inflation continues to moderate in its underlying trend across all major countries, but the expected point at which inflation converges on the target level differs among countries.

Regarding the domestic economy, the member saw that the economy was exhibiting different trends across sectors, with exports remaining strong while domestic demand was more sluggish than expected. Private consumption showed strong growth in the first quarter, driven by one-off factors, before correcting in the second quarter. Construction investment remains lackluster due to the sluggishness of construction commencements and orders received, while facilities investment also suffers from delayed investment by some corporations. Going forward, economic growth is expected to remain consistent with the pace projected in May (2.5%), as exports are likely to maintain favorable growth, led by a buoyant IT industry, and consumption is also likely to recover gradually, affected by improvements in real income conditions and corporate performance. Affected by sluggish domestic demand, employment is forecast to show slower-than-expected growth, particularly in the contact-intensive services sector.

With regard to the real estate market, the volume of housing transactions has been increasing, led by those of Seoul apartments, and housing prices have exhibited faster growth in the Seoul metropolitan region, while remaining on the decline in provincial areas. Concerning domestic inflation, consumer price inflation as a whole has been slowing, as core inflation continues to slow and as agricultural product price growth has recently decelerated significantly. Considering the base effect from last year's surge in oil and agricultural product prices and the downward stabilization of core inflation, inflation will likely continue to slow going forward.

Regarding international financial markets, the member noted that major price variables fluctuated substantially, influenced largely by changing expectations of the U.S. Federal Reserve's monetary policy and political uncertainties in the U.S. and Europe. In domestic financial markets, financial conditions continue to ease, as seen in the declines in market and lending rates driven by the preemptive reflection of expectations for a shift in domestic and international monetary policy stances. Growth in household lending, and home mortgage lending in particular, has been accelerating. The won-dollar exchange rate has risen, affected by the strengthening dollar and the weakening yen, and the foreign capital market remains stable. However, there are persistent uncertainties related to project financing restructuring, which is one risk factor in domestic financial markets, and exchange rate risks persist due to changing expectations of a shift in the U.S. Fed's monetary policy, in addition to recent high exchange rate levels. In this regard, a close monitoring of relevant developments is required.

In overall consideration of the above-mentioned economic and financial conditions, the member believed that it was desirable to keep the Base Rate at the current 3.5% at this meeting. Although there has been further progress in disinflation since the previous meeting, there remain uncertainties caused by geopolitical risks and weather conditions. Persistent expectations of high inflation necessitate a wait-and-see approach to determine whether inflation will converge on the target level, and it is necessary to consider financial stability aspects, such as increasing FX volatility, a substantial uptrend in household lending, and higher housing prices in the Seoul metropolitan area.

In future monetary policy operations, the member stated that decisions about adjusting the monetary policy stance should be made after closely monitoring inflation and growth paths, examining financial stability risks, including monetary policy changes in major countries, upward pressure on exchange rates, and household debt, and should be made in consideration of monetary and macro-prudential policy coordination.

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

The member commented that inflation is slowing in major countries and that some central banks are changing their policy stance accordingly. In the U.S., the unemployment rate has risen, implying a slight sluggishness in the labor market. However, it is uncertain when the U.S. is going to pivot, with some voices arguing that more confidence regarding disinflation is needed.

Regarding the domestic economy, the member expected GDP growth to be around 2.5% in 2024, in line with previous projections, due to sluggish domestic demand with high prices and high interest rates, although exports, including semiconductors, were strong. While aggregate labor market indicators, such as employment and unemployment rates, show favorable trends, the number of persons employed may increase at a slower pace due to the weak construction sector.

The member noted that consumer price inflation and core inflation in June stood at 2.4% and 2.2%, respectively, converging on the target level of 2%. The stabilization of prices, which is the primary objective of monetary policy, is encouraging and this is thanks to the prolonged policy of high interest rates. If the downward trend in inflation continues, a rate cut could be considered, especially given the weak domestic economy.

However, the member mentioned that two conditions have to be met first if there is to be a rate cut. First, there must be a stabilization of the foreign exchange market. Most of the currencies are weak because of the strong dollar. However, it is a red flag that the Korean won to U.S. dollar rate is stuck in the upper 1,300 won range, even when the current account is in surplus. Second, there must be economic restructuring and housing price stabilization. A possible rate cut should not undermine efforts to restructure the economy or trigger a rise in housing prices in some regions. It is also worrying that the increase in household debt is accelerating slightly, with most of it concentrated in home mortgages.

The member saw that it is very disappointing that more aggressive deleveraging could not have been made while interest rates were high. Going forward, this may hinder Korea’s economic growth and limit the flexibility of monetary policy operations.

The member assessed that, for now, the Base Rate should be maintained at the current level of 3.50%, while closely monitoring major countries' management of their monetary policies, the process of project financing restructuring in the real estate market, and developments in financial and foreign exchange markets.

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

The member saw that the global economy has continued to grow at a moderate pace. Overall growth in the U.S. is favorable, although there are signs of a slowdown in consumption, and the eurozone economy is recovering, led by consumption, amid political instability. China is showing signs of a recovery with domestic stimulus measures and improved exports, although there is weakness in the real estate market. While some central banks' policy rates have started to move into less restrictive levels, expectations as to when and how many rate cuts the U.S. Fed will make have been highly volatile following the release of key U.S. economic data, leading to increased volatility in global financial markets.

The member assessed that, although the domestic economy underwent a significant adjustment following the rebound in domestic demand in the first quarter, recovery has continued thanks to robust export growth. In terms of employment, additional monitoring is needed as the increase in the number of persons employed has recently slowed. Consumption adjusted in the second quarter after the strong increase in the first quarter, but recovery is expected to continue in the second half of the year. Meanwhile, construction investment is expected to decline due to the effects of the contraction in housing starts to date. Facilities investment is also expected to grow at a slower pace due to revised investment plans at IT companies.

With regard to the domestic foreign exchange market, the member noted that the won-dollar exchange rate remained high, slightly below the 1,400 won level. Going forward, attention should be paid to the possibility that the exchange rate may become highly volatile due to political conditions in major countries, the weakening Japanese yen and Chinese yuan, and due to the continued reversal of the Korea-U.S. interest rate differential.

As for inflation, the member stated that consumer price inflation declined to the mid-2% range and that inflation expectations among the general public fell to the 3% range. As inflation slows in accordance with the forecast path, there are growing expectations that inflation will converge on its target level in the second half of next year. However, inflation expectations remain higher than the target level and adjustments in public utility charges are becoming more likely. Additionally, inflation may have become more sensitive to the exchange rate than before. In this regard, continued attention should be paid to future upside risks to inflation.

The member commented that domestic financial conditions have eased substantially, affected by widespread expectations of rate cuts at home and abroad. Corporate financing and the supply-demand conditions for corporate and other credit bonds have been favorable, while money growth has remained in the upper 5% range. Risks related to project financing have been under control overall, as seen in the falling interest rates on PF-ABCPs.

However, the member observed that household lending exhibited faster-than-expected growth, boosted by falling home mortgage rates, and the supply of government-sponsored finance, and that apartment sale prices and leasehold deposits have continued to rise, particularly in the Seoul metropolitan area. Looking back at patterns of the past, this trend can lead to overheating of the entire housing market.

The member argued that particular attention should be paid to rising housing prices, as they could cause household debt to increase and housing expenses to rise, consequently limiting household consumption and aggravating inflationary presssure. More specifically, there is a higher likelihood of housing sale prices becoming more sensitive to lending rates, as household liquidity holdings have increased and recent housing transactions have been mostly driven by non-speculative demand. In this regard, inflows of liquidity into the housing market need to be closely monitored, considering progress in macro-prudential policy implementations, such as future management of policy loans and the introduction of stress DSRs.

In summary, the member saw that, while inflation was slowing toward its target level, upside risks still required attention, and that, given current conditions, including exchange rate increases, household debt growth, and rising housing prices, any monetary easing would bring about higher risks than before.

In light of this, it will be appropriate to keep the Base Rate unchanged at 3.5% at this time and to leave it at the current level for the time being.

The member pointed out that future monetary policy decisions should be made in comprehensive consideration of both the benefits and risks of any Base Rate adjustment concerning the overall economy and financial conditions, including growth and inflation, household debt and housing prices, and debt servicing burdens. This should include developments in external conditions and consequent FX market changes, such as those in exchange rates, any progress made in macro-prudential policy implementations, and the degree of convergence of inflation toward its target level over the medium-term horizon.

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

The member commented that global and domestic economic conditions have followed a similar trend since the last meeting. Although the U.S. economy, which has led the global economy, is now slowing slightly, the global economy is expected to continue to expand moderately, supported by the recovery in the euro area and in emerging countries.

The member observed that while the easing of the global contractionary stance and improving trade conditions are putting upward pressure on the economy, the persistence of high interest rates, never-ending regional conflicts, the strong dollar, which has recently become even more apparent, and political uncertainties, with elections in the U.S. and in other key countries, are all putting downward pressure on the economy.

The member expects the Korean economy to grow at a slower pace in the second quarter due to weak domestic demand, particularly in retail sales, facilities investment, and construction investment, although exports were strong. However, the economy is expected to recover starting in the second half of this year. As we see that consumption and investment demand in major countries are spilling over into the manufacturing sector, supported by robust employment, a recovery in domestic demand would be crucial in order to follow the momentum of the global economic expansion.

Though uncertainties still remain on the supply side, the member judged that prices are stabilizing, or at least the prices that are affected by monetary policy operations are on a downward trend toward the target level.

The member stated that while the dollar remains strong and monetary policies are beginning to differentiate across countries, exposure to external risks has increased due to the restructuring of the foreign exchange market, making it necessary to monitor exchange rate volatility.

The member saw that Korea’s financial and foreign capital markets have been stable overall. However, as housing prices in the Seoul metropolitan region are rising, leading to a significant increase in household lending, it is important to monitor economic sentiment in the real estate market and to manage household lending.

In overall consideration of the domestic and international economic environments, the member judged that there is not much need to adjust the current Base Rate and that it is therefore appropriate to leave it unchanged at 3.5%.

The member noted that, as countries are differentiating their monetary policies according to their own economic contitions, Korea is also at a crucial moment when it needs to review the benefits and costs of a policy pivot on the real and financial sectors and the trade-offs in policy effects across sectors, and to find the right combination of monetary and macroprudential policies to minimize costs.

Another member presented the view that it would be appropriate to maintain the Base Rate at the current level of 3.50% for the intermeeting period.

The member commented that the global economy had been on a modest recovery lately, with a strong U.S. economy spilling over into other economies, including Europe, Japan, and China. The U.S. economy has made some progress on disinflation, with the Consumer Price Index (CPI) and Personal Consumption Expenditures (PCE) inflation declining slightly in May. However, the pace of disinflation is expected to remain moderate as the labor market remains strong, despite the gradual normalization of the labor market, with the June unemployment rate slightly higher than expectations. The euro area is improving slightly, led by exports, and the Chinese economy is showing signs of a recovery, but the real estate sector there remains sluggish. The Japanese economy has shown signs of a modest recovery, but it is somewhat unclear whether this will continue.

The member pointed out that in the domestic economy exports were performing better than expected, influenced by the global economic recovery, whereas domestic demand, including private consumption, facilities investment, and construction investment, remained weaker than anticipated. The contrasting effects of external and internal demand are offsetting each other, leading to overall economic growth that does not significantly deviate from previous forecasts. In the labor market, the increase in the number of persons employed remained at a low level during May and June. Meanwhile, inflation continued to show a clear slowdown, largely in line with the forecast path, driven by falling agricultural product prices. In addition, based on the three-month moving average of month-on-month inflation, there has been significant progress in slowing consumer and core inflation, suggesting that the conditions necessary for a rate cut are largely met from an inflation perspective.

The member saw that in international financial markets political uncertainties in Europe and in the U.S., as well as changing expectations regarding the U.S. Federal Reserve's rate cuts, had led to significant fluctuations and increased volatility in major countries' long-term government bond yields. This has also caused fluctuations in the U.S. Dollar Index (DXY). Meanwhile, the yen has continued to weaken significantly, which appears to be due to the prevailing expectation that Japan's policy rate and neutral rate will remain low for an extended period, given the condition of the Japanese economy. The Korean won to U.S. dollar exchange rate has risen due to increased political uncertainty in major countries and the significant weakening of the yen, but the possibility of a rapid change in the won/dollar exchange rate is considered limited, as global dollar liquidity remains abundant and as the dollar remains strong.

The member pointed out that, in domestic financial markets, overall liquidity remained very favorable as short-term interest rates remained at low levels and as monetary (M2) growth slightly increased. In addition, the degree of tightening in financial conditions eased as long-term government bond yields declined significantly compared to those in major advanced economies, due to strengthening expectations of a pivot from a contractionary monetary policy stance at home and abroad, as well as to large net purchases of government bond futures by foreign investors. Meanwhile, the recent increase in housing transactions has led to a significant increase in home mortgage lending, and housing prices have been rising steeply, particularly in Seoul and in the greater Seoul metropolitan area. Given the historically high correlation between housing prices and household debt levels, it is necessary to be cautious about the possibility of another substantial increase in household debt if the upward trend in housing prices continues. Meanwhile, the delinquency rate on corporate loans, especially among non-bank financial institutions, continues to rise. In the case of real estate project financing, risks remain, particularly for some construction companies and non-bank financial institutions with significant real estate project financing exposure. As the net issuance of public corporation bonds is expected to increase in the second half of the year, it is necessary to ensure financial market stability to prevent financial market turbulence from materializing during the restructuring process of real estate project financing.

The member presented the opinion that, taking into consideration these domestic and international economic and financial conditions, it is deemed appropriate to maintain the Base Rate at the current level of 3.50% at this time. While pivot risk on the inflation side has significantly decreased, pivot risk on the financial stability side stemming from the expansion of housing price growth has increased. It will be necessary to closely monitor future developments in inflation and housing prices to determine the timing of a rate cut and it will be essential to coordinate closely with macroprudential policies to ensure that a rate cut does not amplify financial market instability.

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 commented that the global economy maintained modest growth, boosted by a recovery in the global manufacturing sector. The economic upturn is expected to continue, but its pace will depend on the timing and pace of monetary policy shifts in major economies, alongside developments concerning geopolitical risks and political uncertainties.

The member stated that inflation in major countries varied from country to country, but it was continuing to slow, with the pace generally becoming more moderate. However, after a temporary decline due to the announcement of smaller voluntary production cuts by OPEC+, international oil prices have risen again due to renewed military tensions in the Middle East and prospects of increased crude oil demand.

The member saw that, in international financial markets, major price variables fluctuated repeatedly, influenced by changes in expectations of the U.S. Federal Reserve's monetary policy and by a preference for safe assets resulting from political instability in Europe.

The member noted that, concerning the domestic economy, while exports continued to show high growth, particularly in IT products, including semiconductors, domestic demand remained sluggish. Moving forward, the domestic economy is expected to show a moderate growth trend as robust export momentum continues and as sluggishness in domestic demand gradually eases due to slowing inflation and improving household real income conditions.

The member saw that domestic inflation continued its slowing trend. In June, consumer price inflation eased to 2.4%, driven by a substantial deceleration in agricultural product price increases, while core inflation remained in the low 2% range. Although this disinflation trend is expected to continue going forward, it is important to remain vigilant about the developments and impacts of major upside risk factors, such as international oil prices, exchange rates, and agricultural product prices.

The member commented that, in domestic financial markets, government bond yields declined due to expectations of a shift in domestic and international monetary policy stances, while the Korean won to U.S. dollar exchange rate rose owing to increased political uncertainty in Europe, interest rate cuts in some advanced economies, and a weaker yen.

The member stated that household loans in the financial sector were continuing to grow at a somewhat high rate, mainly driven by home mortgage loans. This appears to be because the expansion of government sponsored finance and the decline in bank mortgage lending rates have improved buying sentiment, which has led to an upward shift in apartment prices in the Seoul metropolitan area and to increased transaction volumes. Considering this situation, it is essential to pay close attention to the possibility of a resumption of a buildup in financial imbalances for the time being.

Meanwhile, the member noted that the delinquency rate on corporate loans continued to rise, particularly in the non-banking sector. It is essential to closely monitor business conditions and financial risks in the construction and real estate industries, as well as the potential increase in risks within the non-banking sector during the restructuring process of real estate project financing.

In summary, the member saw that inflation was expected to continue to decelerate and the domestic economy was expected to continue to show moderate growth. However, there is a heightened need for caution regarding the potential increase in volatility in foreign exchange markets, and the accumulation of financial imbalances, including rising housing prices and household debt.

Taking these factors into overall consideration, the member was of the view that it would be appropriate to hold the Base Rate unchanged at the current level of 3.50% at this meeting. At the same time, it should be necessary to continue to effectively manage market expectations through appropriate communication to prevent excessive expectations of a shift in the policy stance that could escalate risks regarding foreign exchange markets and financial stability.