

Potentially better growth into 2017... but?

Thursday, April 13, 2017

Highlights

- **The Bank of Korea kept its 7-day repo rate unchanged at 1.25%**, in line with our expectations, after cutting 25bps back in June 2016. In its policy statement, the central bank cited that overall economic growth should print slightly higher than its initial 2.5% projection made back in January given the improvement seen in exports and investment growth. Elsewhere, inflation may “fluctuate at the 2% level”, up from previous projection of 1.8%.
- **Still, growth drags may persist given uncertainties from both domestic and external environments.** Chiefly, there are concerns over labour conditions and overall domestic consumption growth. Specifically, the decline in the number of persons employed in the manufacturing sector persists, while growing household debt may continue to deteriorate household’s purchasing power. Worryingly, BOK’s data showed that debt owned by high-risk household, defined as income and asset seen as insufficient to repay debt, rose to KRW62.0 trillion in 2016, up from KRW46.4 trillion in the previous year. In the global space, uncertainties over US economic policies, pace of policy normalization, possible rise in trade protectionism behavior and political uncertainties in the euro area should be closely watched by both policy-makers and market-watchers alike.
- **We view that BOK will likely keep rates unchanged throughout 2017.** At the top of our concerns are the record household debt to nominal GDP at 91% (vs OECD average of 70%) and risk of capital outflows given the possibility of further rate hikes by the US Federal Reserve into the year. Elsewhere, geopolitical tensions between the US and North Korea may limit investor appetite into the region as well, especially if issues intensify further. In view of these uncertainties, we maintain our GDP growth outlook at 2.5% while keeping our inflation outlook at 2.0% in 2017.

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