

Republic of Korea

Yield Movements

Local currency (LCY) government bond yields in the Republic of Korea fell for all tenors between 1 March and 8 May, resulting in the entire yield curve shifting downward (**Figure 1**). Yields for short-term tenors fell 3 basis points (bps) on average, while yields for maturities of between 2 years and 50 years declined an average of 12 bps. The largest decline in yields was noted for the 20-year and 30-year maturities, which fell 15 bps each. The spread for the 2-year and 10-year tenors slipped to 15 bps on 8 May from 16 bps on 1 March.

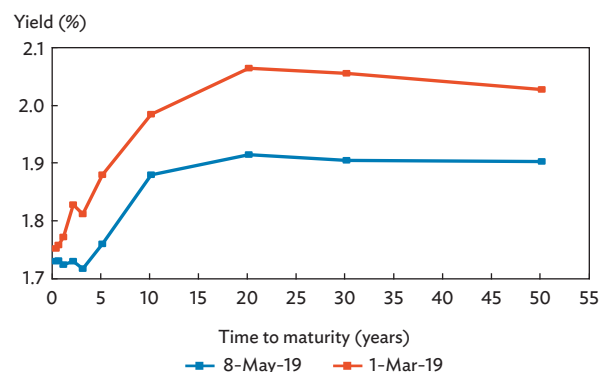
The downward trend in yields during the review period was due to market expectations that the Bank of Korea might cut its key rate this year as export growth weakens, inflation remains subdued, and uncertainties over global trade disputes persist. Recent domestic and global developments contributed to the overall decline in yields. Aside from trade tensions between the United States (US) and the People's Republic of China, Brexit also poses uncertainties, which could lead to increased international financial market volatility and a further slowdown in the global economy. The pace of domestic economic growth also moderated during the review period as consumption slowed, investments adjusted, and export growth weakened.

On 18 April, the Monetary Policy Board of the Bank of Korea decided to maintain the base rate at 1.75%, where it has been since the last adjustment in November 2018. The board noted that risks have increased and it therefore will ensure that economic growth continues and inflation remains stable.

The Republic of Korea's real gross domestic product (GDP) grew 1.7% year-on-year (y-o-y) in the first quarter (Q1) of 2019, down from 3.1% y-o-y growth in the fourth quarter (Q4) of 2018. Growth was weighed down by the decline in gross capital formation, a slowdown in final consumption expenditure, and a slump in exports. The economy shrank 0.4% on a seasonally adjusted quarter-on-quarter (q-o-q) in Q1 2019 following the previous quarter's 1.0% q-o-q expansion.

Consumer price inflation in the Republic of Korea was subdued in Q1 2019 with a quarterly average of

Figure 1: The Republic of Korea's Benchmark Yield Curve—Local Currency Government Bonds



Source: Based on data from Bloomberg LP.

0.6% y-o-y, down from the 1.8% y-o-y in Q4 2018. In April, inflation slightly picked up to 0.6% y-o-y from 0.4% y-o-y in March, while prices for services and oil products remained stable.

Size and Composition

The Republic of Korea's LCY bond market grew 1.8% q-o-q in Q1 2019 with outstanding bonds amounting to KRW2,278.7 trillion (USD2.0 trillion) at the end of March on account of increases in the stocks of central government bonds and corporate bonds (**Table 1**).

Government bonds. The Republic of Korea's LCY government bond market grew 1.9% q-o-q in Q1 2019 to reach KRW930.9 trillion at the end of March. The stocks of central government bonds and National Housing Bonds expanded during the review period, while the outstanding amount of Monetary Stabilization Bonds issued by the Bank of Korea slightly contracted 0.3% q-o-q in Q1 2019.

The government issued a higher volume of Korea Treasury Bonds during the review period to fund its fiscal spending. The government frontloaded its spending plan in the first half of the year to help boost economic growth and create jobs. The stock of central government bonds posted growth of 3.0% q-o-q in Q1 2019.

In Q1 2019, issuances of government bonds registered hefty growth of 20.7% q-o-q, amounting to KRW80.3 trillion, mainly through large issuances from the Treasury and other government agencies. Issuances from the Bank of Korea slightly increased 0.1% q-o-q in Q1 2019.

Corporate bonds. The outstanding amount of LCY corporate bonds increased 1.8% q-o-q to reach KRW1,347.8 trillion at the end of March. **Table 2** lists the top 30 LCY corporate bond issuers in the Republic of Korea with aggregate bonds outstanding of KRW1,104.2 trillion, comprising 67.4% of total LCY corporate bonds at the end of March. Financial institutions such as banks and investment and securities firms continued to dominate the top 30 list in the Republic of Korea. Mirae Asset Daewoo Company, the brokerage arm of Mirae Asset Financial Group, was the largest issuer at the end of March with outstanding bonds of KRW132.0 trillion.

Issuances of corporate bonds declined 22.6% q-o-q in Q1 2019 due to a drop in private corporate issuances. **Table 3** presents notable corporate bond issuances in Q1 2019. Financial firms such as Shinhan Bank, KEB Hana Bank, Woori Bank, and Hyundai Capital Services were the top issuers during the quarter.

Investor Profile

Insurance companies and pension funds were still the top holders of LCY government bonds with a share of

36.0% at the end of December 2018 (**Figure 2**). Next was the general government with a share of 19.2%, which was slightly lower than its 19.9% share in December 2017. Next were banks whose shareholdings increased to 16.8% of the total local government bonds at the end of December 2018 from 16.0% a year earlier.

For the LCY corporate bond market, insurance companies and pension funds remained the largest investor group in December 2018, maintaining their share at around 40% (**Figure 3**). The share of other nonbank financial institutions declined to 33.3% from 34.8% a year earlier. Meanwhile, the general government increased its share to 13.7% from 13.2% during the review period.

Net foreign investment inflows into the Republic of Korea's LCY bond market dropped in the first 2 months of 2019 following net inflows in most of 2018 (**Figure 4**). January saw net foreign investment outflows amounting to KRW3,739 billion, which eased in February to KRW2,719 billion before rebounding in March when net foreign investment inflows surged to KRW1,468 billion. In April, net foreign bond inflows slowed to KRW526 billion.

Ratings Update

In May, RAM Ratings reaffirmed the Republic of Korea's rating at gAA3(pi) and seaAAA(pi) on the global and ASEAN scales, respectively, with a stable rating for both. In making its decision, RAM Ratings took note of the Republic of Korea's economic resilience, sturdy external balance sheet, and prudent fiscal management.

Table 1: Size and Composition of the Local Currency Bond Market in the Republic of Korea

	Outstanding Amount (billion)						Growth Rate (%)			
	Q1 2018		Q4 2018		Q1 2019		Q1 2018		Q1 2019	
	KRW	USD	KRW	USD	KRW	USD	q-o-q	y-o-y	q-o-q	y-o-y
Total	2,186,590	2,056	2,237,400	2,014	2,278,665	2,007	1.2	4.4	1.8	4.2
Government	915,155	860	913,966	823	930,886	820	3.0	4.9	1.9	1.7
Central Government Bonds	568,774	535	567,044	510	584,006	514	4.0	6.7	3.0	2.7
Central Bank Bonds	174,790	164	171,640	154	171,150	151	2.3	(0.04)	(0.3)	(2.1)
Others	171,591	161	175,282	158	175,730	155	0.5	4.6	0.3	2.4
Corporate	1,271,435	1,195	1,323,434	1,191	1,347,779	1,187	(0.1)	4.0	1.8	6.0

() = negative, KRW = Korean won, LCY = local currency, q-o-q = quarter-on-quarter, Q1 = first quarter, Q4 = fourth quarter, USD = United States dollar, y-o-y = year-on-year.

Notes:

1. "Others" comprise Korea Development Bank Bonds, National Housing Bonds, and Seoul Metro Bonds.

2. Calculated using data from national sources.

3. Bloomberg LP end-of-period LCY-USD rates are used.

4. Growth rates are calculated from local currency (LCY) base and do not include currency effects.

5. Corporate bonds include equity-linked securities and derivatives-linked securities.

Sources: The Bank of Korea and EDAILY BondWeb.

Table 2: Top 30 Issuers of Local Currency Corporate Bonds in the Republic of Korea

	Issuers	Outstanding Amount		State-Owned	Listed on		Type of Industry
		LCY Bonds (KRW billion)	LCY Bonds (USD billion)		KOSPI	KOSDAQ	
1.	Mirae Asset Daewoo	131,965.8	116.3	No	Yes	No	Securities
2.	Korea Housing Finance Corporation	118,054.9	104.0	Yes	No	No	Housing Finance
3.	Korea Investment and Securities	112,888.0	99.4	No	No	No	Securities
4.	NH Investment & Securities	94,254.4	83.0	Yes	Yes	No	Securities
5.	KB Securities	80,250.0	70.7	No	No	No	Securities
6.	Hana Financial Investment	62,249.0	54.8	No	No	No	Securities
7.	Samsung Securities	52,085.2	45.9	No	Yes	No	Securities
8.	Industrial Bank of Korea	51,670.1	45.5	Yes	Yes	No	Banking
9.	Korea Land & Housing Corporation	30,857.4	27.2	Yes	No	No	Real Estate
10.	Shinyoung Securities	29,910.0	26.3	No	Yes	No	Securities
11.	Shinhan Bank	29,571.5	26.1	No	No	No	Banking
12.	Korea Electric Power Corporation	27,090.0	23.9	Yes	Yes	No	Electricity, Energy, and Power
13.	Korea Expressway	21,820.0	19.2	Yes	No	No	Transport Infrastructure
14.	Kookmin Bank	21,288.7	18.8	No	No	No	Banking
15.	Woori Bank	19,610.0	17.3	Yes	Yes	No	Banking
16.	KEB Hana Bank	19,250.0	17.0	No	No	No	Banking
17.	Korea Rail Network Authority	18,960.0	16.7	Yes	No	No	Transport Infrastructure
18.	Hanwha Investment and Security	18,570.6	16.4	No	No	No	Securities
19.	Daishin Securities	17,866.4	15.7	No	Yes	No	Securities
20.	Korea Deposit Insurance Corporation	15,630.0	13.8	Yes	No	No	Insurance
21.	The Export-Import Bank of Korea	15,375.0	13.5	Yes	No	No	Banking
22.	Shinhan Card	14,220.0	12.5	No	No	No	Banking
23.	Nonghyup	13,710.0	12.1	Yes	No	No	Banking
24.	Hyundai Capital Services	13,606.0	12.0	No	No	No	Consumer Finance
25.	Small & Medium Business Corporation	13,203.1	11.6	Yes	No	No	SME Development
26.	Korea Gas Corporation	12,738.6	11.2	Yes	Yes	No	Gas Utility
27.	Meritz Securities	12,715.5	11.2	No	Yes	No	Securities
28.	KB Kookmin Bank Card	12,190.0	10.7	No	No	No	Consumer Finance
29.	Standard Chartered Bank Korea	11,610.0	10.2	No	No	No	Banking
30.	Korea Student Aid Foundation	11,020.0	9.7	Yes	No	No	Student Loan
Total Top 30 LCY Corporate Issuers		1,104,230.3	972.7				
Total LCY Corporate Bonds		1,637,371.3	1,442.4				
Top 30 as % of Total LCY Corporate Bonds		67.4%	67.4%				

KOSDAQ = Korean Securities Dealers Automated Quotations, KOSPI = Korea Composite Stock Price Index, KRW = Korean won, LCY = local currency, SME = small and medium-sized enterprise, USD = United States dollar.

Notes:

1. Data as of 31 March 2019.

2. State-owned firms are defined as those in which the government has more than a 50% ownership stake.

3. Corporate bonds include equity-linked securities and derivatives-linked securities.

Sources: AsianBondsOnline calculations based on Bloomberg LP and EDAILY BondWeb data.

Table 3: Notable Local Currency Corporate Bond Issuance in the First Quarter of 2019

Corporate Issuers	Coupon Rate (%)	Issued Amount (KRW billion)
Shihan Bank		
2-year bond	1.93	300
3-year bond	1.99	300
20-year bond	2.56	50
KEB Hana Bank		
1.5-year bond	1.95	100
2-year bond	1.96	100
3-year bond	1.96	100
Woori Bank		
1-year bond	1.93	200
2-year bond	1.95	200
10-year bond	2.68	200
Hyundai Capital Services		
5-year bond	2.45	10
7-year bond	2.52	35

KRW = Korean won.

Source: Based on data from Bloomberg LP.

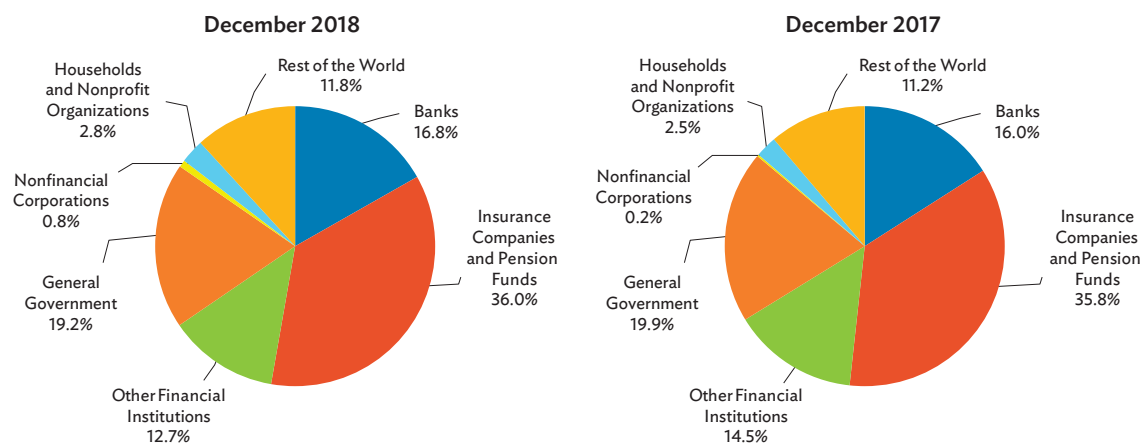
RAM Ratings expects firmer growth in the Republic of Korea during the rest of 2019 given the recovery in the semiconductor industry. Although exports weakened in Q1 2019, the current account stayed in positive territory and foreign reserves remained adequate. In March, the government announced a supplementary budget of KRW6.7 trillion, or 0.3% of GDP, to counter near-term headwinds.

Due to the economy's growth resilience and the government's expansionary fiscal stance, RAM Ratings views the Republic of Korea as credit positive. However, if weakening GDP growth persists and/or fiscal prudence significantly diminishes, it could exert pressure on the ratings.

Policy and Regulatory Developments

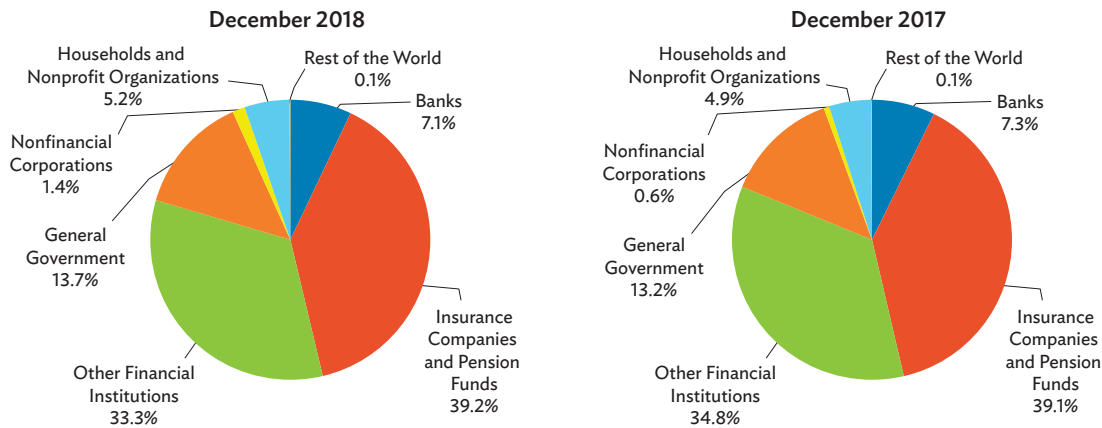
Financial Services Commission Releases Financial Policy Road Map for 2019

The Republic of Korea's Financial Services Commission (FSC) announced in March its 2019 financial policy aimed at promoting financial innovation, ensuring trust in finance, and securing financial stability. Financial innovation will be accelerated as the newly enacted laws for online banking and financial regulatory sandbox will take effect this year. The government will provide financial support to small and medium-sized enterprises and start-ups to boost economic vitality. The government will continue its policy efforts to curb household debt, keeping its growth between 5% and 6%, and will preemptively manage corporate debt risk with an enhanced evaluation system. The FSC will enact a comprehensive bill for better consumer information and protection. To ensure fairness and transparency in order to protect investors and shareholders, the FSC will remain vigilant against potential risks through the close monitoring of financial markets and active policy responses.

Figure 2: Local Currency Government Bonds Investor Profile


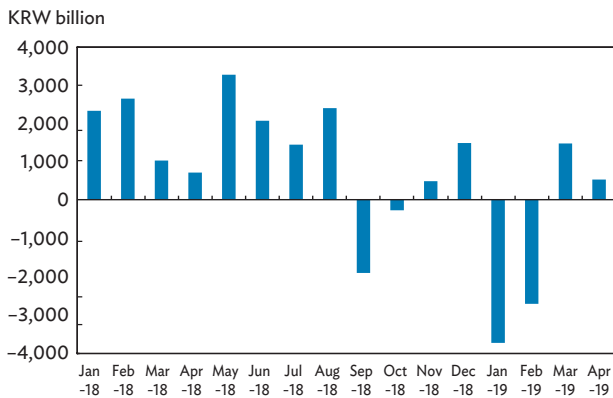
Sources: AsianBondsOnline and the Bank of Korea.

Figure 3: Local Currency Corporate Bonds Investor Profile



Sources: AsianBondsOnline and the Bank of Korea.

Figure 4: Net Foreign Investment in Local Currency Bonds in the Republic of Korea



KRW = Korean won.
Source: Financial Supervisory Service.

Republic of Korea to Cut Stock Transaction Tax

The Government of the Republic of Korea will cut taxes on stock transactions effective 3 June to support the secondary market for venture firms and promote venture capital. The trading tax for stocks listed on the Korea Composite Stock Price Index and Korea Securities Dealers Automated Quotation markets will be reduced by 0.05 percentage points each, for unlisted stocks by 0.05 percentage points, and for Korean New Exchange stocks by 0.2 percentage points to promote venture capital. A special tax for rural development of 0.15%, levied on Korea Composite Stock Price Index transactions, will remain unchanged.

Starting 1 January 2020, the government will change capital gains taxes on stock transactions to allow the transfer of losses between domestic and foreign stock transactions. Taxes will also only be imposed on net gains that are earned throughout the year.