

## Republic of Korea

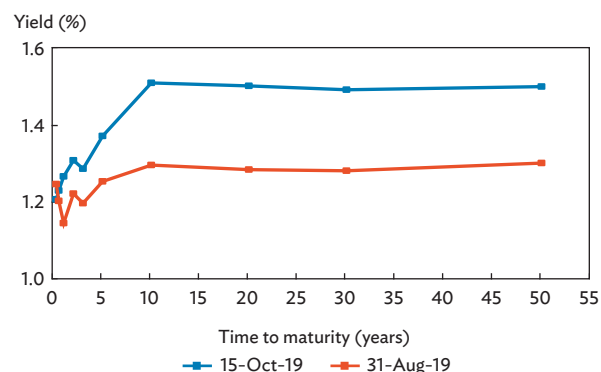
### Yield Movements

Between 31 August and 15 October, local currency (LCY) government bond yields in the Republic of Korea rose for all tenors except 3-month paper, which fell 4 basis points (bps). The rise in yields was more pronounced at the longer end of the curve, with the yields of 10-year to 50-year securities up 21 bps on average. The yield for the 6-month tenor rose 3 bps, while yields for bonds with tenors of between 1 year and 5 years increased at an average of 10 bps. The yield spread between the 2-year and 10-year tenors rose to 20 bps from 8 bps.

Yields rose during the review period as domestic bond yields tracked United States (US) Treasury yield movements, which gained in both early September and early October on positive news about trade talks between the People's Republic of China (PRC) and the US. Market participants took profits as the expected rate cut by the Bank of Korea on 16 October had already been priced in and on expectations of a pause in monetary easing for the year. The rise in yields was also driven by (i) expectations of increased bond issuance during the remainder of the year to fund the recently approved supplementary budget, and (ii) a higher bond issuance target next year to fund the 2020 budget passed by the government. The government submitted a KRW513.5 trillion budget for 2020, a 9.3% annual increase in spending, to help boost the economy as growth continues to slow.

At its monetary policy meeting on 16 October, the Bank of Korea decided to cut the base rate by another 25 bps to 1.25%, which followed a 25 bps rate cut in July. The Bank of Korea noted the slowdown in global economic growth due to the decline in global trade. It also highlighted the increased volatility in global financial markets, largely driven by the continued PRC-US trade dispute. On the domestic front, growth continued to slow due to weak consumption growth, exports, and facilities investments, leading to expectations by the Bank of Korea for growth to be below the projections announced in July. In September, consumer price inflation was negative; it is expected to remain near zero in the near-term and settle below the July projections.

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



Source: Based on data from Bloomberg LP.

The Republic of Korea's real gross domestic product growth eased to 0.4% quarter-on-quarter (q-o-q) in the third quarter (Q3) of 2019 from 1.0% q-o-q in the second quarter (Q2), based on advance estimates by the Bank of Korea. The lower growth was driven by the contraction in gross fixed capital formation, which declined 2.3% q-o-q in Q3 2019, following marginal 0.6% q-o-q growth in the previous quarter. In addition, final consumption expenditure growth eased as both private and government expenditure posted slower annual increases in Q3 2019. Meanwhile, export growth rose to 4.1% q-o-q from 2.0% q-o-q in the same period. On a year-on-year (y-o-y) basis, the Republic of Korea's economy grew 2.0% in Q3 2019, the same pace recorded in Q2 2019. Consumer price inflation eased from 0.6% y-o-y in July to zero in August, before posting a negative rate of -0.4% in September.

The Korean won had been one of the worst-performing currencies in the region year-to-date, depreciating 6.0% as of 15 October. However, the won experienced a reprieve in early September on positive developments in PRC-US trade talks. The currency remains volatile, and its appreciation is expected to be limited given the continued slowdown in domestic economic growth and fears of further deflation. The Korean won appreciated 2.2% between 31 August and 15 October.

## Size and Composition

The Republic of Korea's LCY bond market posted growth of 2.0% q-o-q to reach KRW2,378.2 trillion (USD1,987.9 billion) at the end of September (Table 1). The growth was primarily driven by the 2.3% q-o-q rise in corporate bonds in Q3 2019, while the government bond segment rose at a slower pace of 1.6% q-o-q.

**Government bonds.** The Republic of Korea's LCY government bonds outstanding increased 1.6% q-o-q to reach KRW961.4 trillion at the end of September, largely driven by the 2.3% q-o-q rise in the stock of central government bonds to KRW613.5 trillion. The outstanding amount of Monetary Stabilization Bonds issued by the central bank rose 0.8% q-o-q to KRW172.9 trillion. Meanwhile, bonds issued by government-related entities declined 0.2% q-o-q to KRW175.0 trillion.

Based on estimates, issuance of government bonds in Q3 2019 was almost at par with the previous quarter at KRW81.1 trillion. Issuance of central bank bonds in Q3 2019 reached KRW36.5 billion and was also at par with issuance in the previous quarter.

**Corporate bonds.** The size of the Republic of Korea's LCY corporate bond market rose 2.3% q-o-q in Q3 2019 to reach KRW1.4 trillion at the end of September on new issuance that remained relatively high. Table 2 lists the top 30 LCY corporate bond issuers at the end

of September, with aggregate bonds outstanding of KRW875.7 trillion, which comprised 61.8% of the total LCY corporate bond market. Financial companies such as banks and securities and investment firms continued to comprise a majority of the 30 largest corporate bond issuers. Korea Housing Finance Corporation remained the largest issuer with outstanding bonds valued at KRW119 trillion.

Issuance of corporate bonds fell 10.0% q-o-q in Q3 2019 to KRW120.8 trillion, but still exceeded first quarter bond issuance. There was a surge in issuance in Q2 2019 as companies took advantage of declining interest rates. This trend continued into July before slightly easing in August and September as yields rose. The continued slowdown and pessimistic outlook for economic growth also contributed to the relatively lower issuance volume in Q3 2019 as companies borrowed less. Table 3 lists the notable corporate bond issuances in Q3 2019. Major banks in the Republic of Korea such as NongHyup Bank, Kookmin Bank, and Woori Bank continued to be among the top issuers of bonds during the quarter.

## Investor Profile

Insurance companies and pension funds comprised the largest investor group in the LCY government bond market in the Republic of Korea's, with a holdings share of 34.4% at the end of June, which was almost at par with

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

	Outstanding Amount (billion)						Growth Rate (%)			
	Q3 2018		Q2 2019		Q3 2019		Q3 2018		Q3 2019	
	KRW	USD	KRW	USD	KRW	USD	q-o-q	y-o-y	q-o-q	y-o-y
<b>Total</b>	<b>2,223,799</b>	<b>2,005</b>	<b>2,331,705</b>	<b>2,019</b>	<b>2,378,232</b>	<b>1,988</b>	<b>0.1</b>	<b>3.6</b>	<b>2.0</b>	<b>6.9</b>
Government	928,209	837	946,417	820	961,420	804	(1.0)	5.4	1.6	3.6
Central Government Bonds	579,104	522	599,552	519	613,509	513	(1.8)	5.4	2.3	5.9
Central Bank Bonds	174,600	157	171,580	149	172,930	145	(0.02)	5.1	0.8	(1.0)
Others	174,505	157	175,285	152	174,981	146	0.7	5.7	(0.2)	0.3
Corporate	1,295,590	1,168	1,385,288	1,200	1,416,812	1,184	0.9	2.4	2.3	9.4

( ) = negative, KRW = Korean won, q-o-q = quarter-on-quarter, Q2 = second quarter, Q3 = first quarter, USD = United States dollar, y-o-y = year-on-year.

Notes:

- Q3 2019 government data are as of August 2019.
- Calculated using data from national sources.
- Bloomberg LP end-of-period local currency-USD rates are used.
- Growth rates are calculated from local currency base and do not include currency effects.
- "Others" comprise Korea Development Bank Bonds, National Housing Bonds, and Seoul Metro Bonds.
- 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.	Korea Housing Finance Corporation	119,019	99.5	Yes	No	No	Housing Finance
2.	Mirae Asset Daewoo Co.	76,760	64.2	No	Yes	No	Securities
3.	Korea Investment and Securities	65,311	54.6	No	No	No	Securities
4.	Industrial Bank of Korea	56,670	47.4	Yes	Yes	No	Banking
5.	KB Securities	52,357	43.8	No	No	No	Securities
6.	NH Investment & Securities	49,477	41.4	Yes	Yes	No	Securities
7.	Hana Financial Investment	46,857	39.2	No	No	No	Securities
8.	Samsung Securities	32,554	27.2	No	Yes	No	Securities
9.	Shinhan Bank	31,172	26.1	No	No	No	Banking
10.	Korea Land & Housing Corporation	28,905	24.2	Yes	No	No	Real Estate
11.	Korea Electric Power Corporation	26,440	22.1	Yes	Yes	No	Electricity, Energy, and Power
12.	Korea Expressway	22,050	18.4	Yes	No	No	Transport Infrastructure
13.	Woori Bank	21,050	17.6	Yes	Yes	No	Banking
14.	KEB Hana Bank	19,870	16.6	No	No	No	Banking
15.	Shinyoung Securities	19,527	16.3	No	Yes	No	Securities
16.	Korea Rail Network Authority	18,480	15.4	Yes	No	No	Transport Infrastructure
17.	Kookmin Bank	17,694	14.8	No	No	No	Banking
18.	The Export–Import Bank of Korea	15,905	13.3	Yes	No	No	Banking
19.	Hyundai Capital Services	15,206	12.7	No	No	No	Consumer Finance
20.	Shinhan Card	14,455	12.1	No	No	No	Credit Card
21.	Korea Deposit Insurance Corporation	14,330	12.0	Yes	No	No	Insurance
22.	NongHyup Bank	14,300	12.0	Yes	No	No	Banking
23.	Korea SMEs and Startups Agency	13,573	11.3	Yes	No	No	SME Development
24.	Hanwha Investment and Securities	13,429	11.2	No	No	No	Securities
25.	KB Kookmin Bank Card	13,000	10.9	No	No	No	Consumer Finance
26.	Standard Chartered Bank Korea	11,910	10.0	No	No	No	Banking
27.	Korea Gas Corporation	11,799	9.9	Yes	Yes	No	Gas Utility
28.	Nonghyup	11,600	9.7	Yes	No	No	Banking
29.	Meritz Securities Co.	11,029	9.2	No	Yes	No	Securities
30.	Korea Student Aid Foundation	11,000	9.2	Yes	No	No	Student Loan
<b>Total Top 30 LCY Corporate Issuers</b>		<b>875,731</b>	<b>732</b>				
<b>Total LCY Corporate Bonds</b>		<b>1,416,812</b>	<b>1,184</b>				
<b>Top 30 as % of Total LCY Corporate Bonds</b>		<b>61.8%</b>	<b>61.8%</b>				

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 30 September 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 Third Quarter of 2019**

Corporate Issuers	Coupon Rate (%)	Issued Amount (KRW billion)
NongHyup Bank		
1.5-year bond	1.52	667
2-year bond	1.56	508
2-year bond	1.60	427
3-year bond	1.57	255
5-year bond	1.50	339
Woori Bank		
1.5-year bond	1.54	334
1.5-year bond	1.41	304
2-year bond	1.42	296
LG Uplus Corp.		
3-year bond	1.81	437
Hanwha Life Insurance		
30-year bond	3.69	428
Kookmin Bank		
5-year bond	1.50	339
Shinhan Bank		
2-year bond	1.31	305
GS Engineering & Construction		
3-year bond	2.00	255

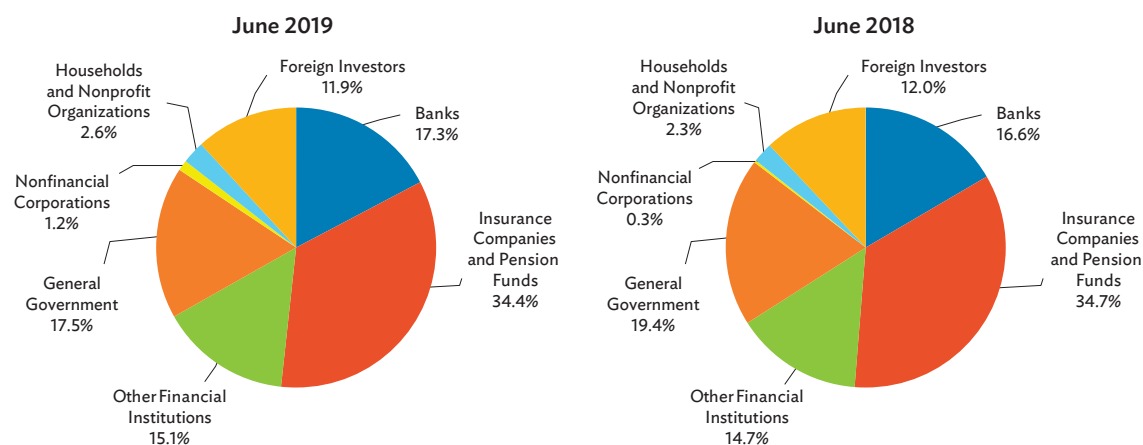
KRW = Korean won.

Source: Based on data from Bloomberg LP.

June 2018 (**Figure 2**). The general government remained the second-largest holder of government bonds at the end of June, even though its share fell to 17.5% from 19.4% in June 2018. Banks accounted for a 17.3% share at the end of the review period, up from 16.6% in June 2018. The share of other financial institutions was slightly up to 15.1% from 14.7%, while the share of foreign investor holdings was marginally changed at 11.9% versus 12.0%.

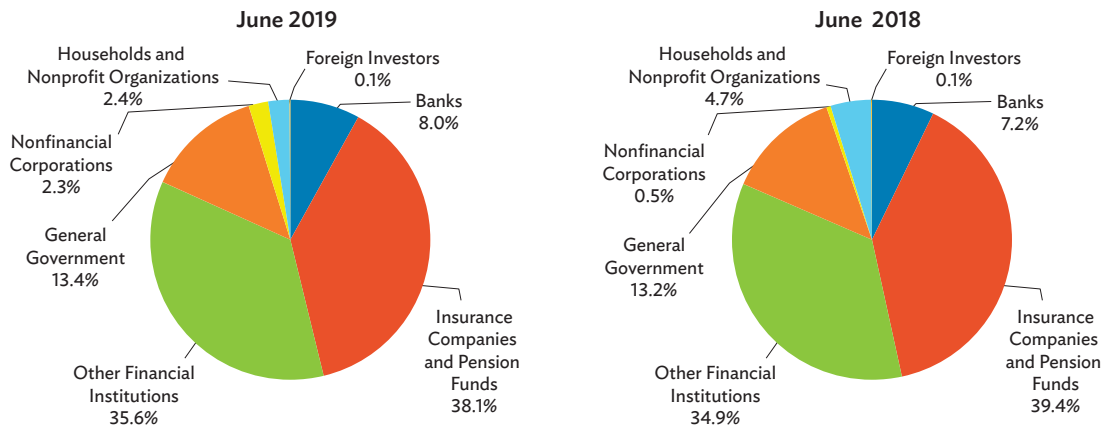
Insurance companies and pension funds, and other financial institutions remained the two largest holders of the Republic of Korea's LCY corporate bonds (**Table 3**). The share of insurance companies and pension funds fell to 38.1% at the end of June from 39.4% in June 2018, while the share of other financial institutions inched up to 35.6% from 34.9%. The share of the general government was mostly unchanged at 13.4%, while that of banks was up slightly to 8.0% from 7.2%. The share of foreign investors remained negligible at 0.1%.

The Republic of Korea's LCY bond market registered net outflows of KRW421 billion in July following a rate cut by the Bank of Korea as well as a large volume of maturities (**Table 4**). The direction of foreign fund flows reversed in August on net inflows of KRW1,741.0 billion. Net inflows of KRW1,416.0 billion were recorded in September. The reversal can be attributed to the strengthening of the Korean won and the reinvestment by a large foreign institutional fund of its holdings of domestic bonds.

**Figure 2: Local Currency Government Bonds Investor Profile**


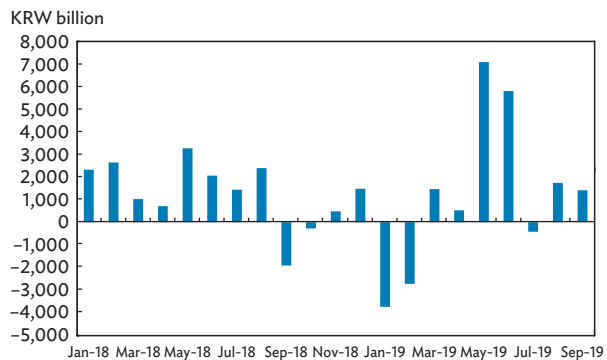
Sources: AsianBondsOnline and the Bank of Korea.

**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.

## Policy, Institutional, and Regulatory Developments

### The Republic of Korea’s Government Proposes KRW513.5 Trillion Budget for 2020

On 29 August, the Government of the Republic of Korea submitted its 2020 budget totaling KRW513.5 trillion for approval. The planned budget entails a 9.3% increase in government spending over 2019 levels and is focused on helping boost the economy and promoting innovation. The main policies of the 2020 budget include increased spending for research and development; support for exports, investment, and consumption; strengthened social safety nets; improved quality of life; and strengthened national defense and diplomacy. The government projects revenues to be KRW482 trillion, a marginal 1.2% annual increase, due to continued weakness in the semiconductor industry and fiscal decentralization. Correspondingly, the target fiscal budget deficit as a share of gross domestic product will rise to 3.6% in 2020 from 1.9% in 2019.