

Republic of Korea

Yield Movements

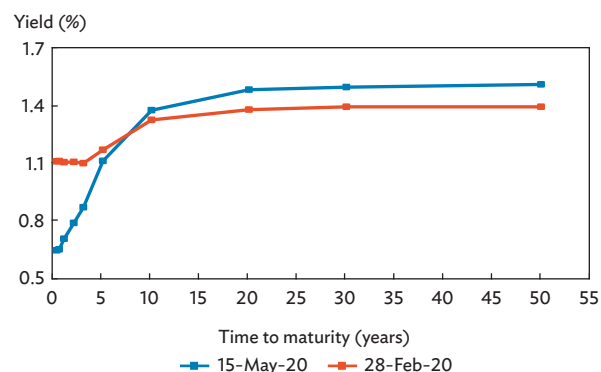
Between 28 February and 15 May, the Republic of Korea's local currency (LCY) government bond yield curve steepened as yields at the short-end fell, while yields at the long-end rose (**Figure 1**). The yields for 3-month and 6-month paper fell 47 basis points (bps) and 46 bps, respectively. The yield for 1-year paper fell 40 bps. Yields for medium-term tenors of 2 years and 3 years fell 27 bps on average; the 5-year tenor fell the least, dipping 6 bps. The yields for tenors ranging from 10 years to 50 years rose 9 bps on average. The spread between the 2-year and 10-year yields rose to 59 bps from 22 bps during the review period.

Yields at the short-end of the curve fell following the rate cut by the Bank of Korea in its emergency Monetary Policy Board meeting on 16 March, a day after the United States (US) Federal Reserve lowered its target range for the federal fund rate by 100 basis points to 0%–0.25%. The Bank of Korea decided to lower its base rate by 50 basis points to 0.75% to stabilize the financial market and in response to the impending economic impact of the coronavirus disease (COVID-19) pandemic. In its Monetary Policy Board meeting on 9 April, the central bank decided to leave its base rate unchanged.

The Bank of Korea has also announced and implemented several measures since March to provide additional liquidity in the market, which contributed to the fall in yields at the short-end of the curve. These included, among others, a (i) weekly reverse repurchase auction for a period of 3 months, available for financial institutions; (ii) broadening of the securities eligible for its open market operations; and (iii) new lending facility for companies with a ceiling of KRW10 trillion and a term of 3 months.

Despite various stabilization measures and strong foreign demand, yields continued to rise at the long-end of the curve, fueled by bond supply concerns as the government passed two supplementary budgets to support various sectors affected by the pandemic. As of 15 May, the National Assembly had approved a total of KRW23.9 trillion in supplementary budget funds to be partly financed via issuance of government bonds. A third supplementary budget is expected to be

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



Source: Based on data from Bloomberg LP.

submitted in June. However, market expectations that the Bank of Korea will purchase government bonds to address oversupply concerns have tempered the rise in yields, particularly in early May.

The Republic of Korea's real gross domestic product contracted 1.3% quarter-on-quarter (q-o-q) in the first quarter (Q1) of 2020, a reversal from the 1.3% q-o-q growth in the fourth quarter (Q4) of 2019, based on preliminary estimates by the Bank of Korea. This reflected the economic impact of COVID-19 as the country went on lockdown. Private consumer spending declined 6.5% q-o-q in Q1 2020 after an increase of 0.7% q-o-q in the previous quarter. Exports also fell 1.4% q-o-q from marginal growth of 0.6% q-o-q in Q4 2019. The q-o-q growth in government spending and fixed capital formation also slowed in Q1 2020. On an annual basis, the Republic of Korea's economic growth slowed to 1.4% year-on-year (y-o-y) from 2.3% y-o-y in the previous quarter. Consumer price inflation also decelerated in April to 0.1% y-o-y from an average of 1.2% y-o-y in Q1 2020, amid a slowdown in spending and production, and a drop in oil prices.

The Republic of Korea registered massive net foreign inflows in the months of March and April, providing downward support to bond yields. Foreign demand increased on the economy being considered a safe haven relative to its peers; a high interest rate differential with

other bond markets in the region, as well as US Treasuries; the implementation of policies to stabilize financial market volatility and address the economic impact of the pandemic; and a relatively stable Korean won.

The Korean won depreciated versus the US dollar during the review period, particularly in March, due to financial market volatility and foreign selling, with the foreign exchange rate peaking at KRW1,285.7 to USD1 on 19 March. The currency subsequently stabilized toward the end of the month after the Bank of Korea announced a temporary currency swap agreement with the Federal Reserve for a period of at least 6 months. The currency remained in the KRW1,204–KRW1,236 to USD1 range during the rest of the review period.

Size and Composition

The Republic of Korea's LCY bond market grew 2.8% q-o-q to reach a size of KRW2,476.2 trillion (USD2,032.1 billion) at the end of March (**Table 1**). This was higher than the 1.6% q-o-q growth posted in Q4 2019. Growth in Q1 2020 was largely driven by the 4.2% q-o-q increase in the stock of government bonds. Meanwhile, the Republic of Korea's corporate bond segment grew at a slower pace of 1.9% q-o-q.

Government bonds. The size of the Republic of Korea's LCY government bond market rose 4.2% q-o-q to KRW992.3 trillion at the end of March. Growth was boosted by a 5.6% q-o-q expansion in the stock of central

government bonds to KRW645.9 trillion due to the surge in issuance in Q1 2020. The outstanding amount of Monetary Stabilization Bonds issued by the Bank of Korea inched up 1.0% q-o-q to KRW165.7 trillion. Outstanding bonds issued by government-related entities rose 2.5% q-o-q.

Issuance of central government bonds more than doubled in Q1 2020 to KRW42.5 trillion from KRW20.0 trillion in Q4 2019 as the government had a larger annual fiscal budget and a frontloading policy. High issuance volume were seen in the first 2 months of the year and surged even more in March as the government funded policy programs to address the economic impact of the COVID-19 pandemic. Issuance volume is expected to rise further the rest of the year as the government finances its supplementary budgets.

Corporate bonds. The Republic of Korea's LCY corporate bond market marginally grew 1.9% q-o-q to KRW1,483.8 trillion at the end of March on tepid issuance for the quarter. **Table 2** lists the top 30 LCY corporate bond issuers in the Republic of Korea, who together had an aggregate KRW922.1 trillion of bonds outstanding at the end of March, which accounted for 62.1% 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 KRW133.3 trillion.

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

	Outstanding Amount (billion)						Growth Rate (%)			
	Q1 2019		Q4 2019		Q1 2020		Q1 2019		Q1 2020	
	KRW	USD	KRW	USD	KRW	USD	q-o-q	y-o-y	q-o-q	y-o-y
Total	2,277,392	2,006	2,407,623	2,083	2,476,170	2,032	1.7	4.2	2.8	8.7
Government	930,886	820	951,912	824	992,346	814	1.9	1.7	4.2	6.6
Central Government Bonds	584,006	514	611,533	529	645,928	530	3.0	2.7	5.6	10.6
Central Bank Bonds	171,150	151	164,060	142	165,710	136	(0.3)	(2.1)	1.0	(3.2)
Others	175,730	155	176,319	153	180,708	148	0.3	2.5	2.5	2.8
Corporate	1,346,506	1,186	1,455,711	1,259	1,483,824	1,218	1.7	5.9	1.9	10.2

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

Notes:

1. Calculated using data from national sources.

2. Bloomberg LP end-of-period local currency–USD rates are used.

3. Growth rates are calculated from local currency base and do not include currency effects.

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

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.	Korea Housing Finance Corporation	133,287	109.4	Yes	No	No	Housing Finance
2.	Mirae Asset Daewoo Co.	75,016	61.6	No	Yes	No	Securities
3.	Korea Investment and Securities	68,135	55.9	No	No	No	Securities
4.	Industrial Bank of Korea	57,340	47.1	Yes	Yes	No	Banking
5.	KB Securities	55,090	45.2	No	No	No	Securities
6.	NH Investment & Securities	49,822	40.9	Yes	Yes	No	Securities
7.	Hana Financial Investment	46,860	38.5	No	No	No	Securities
8.	Samsung Securities	35,950	29.5	No	Yes	No	Securities
9.	Shinhan Bank	31,342	25.7	No	No	No	Banking
10.	Korea Land & Housing Corporation	29,700	24.4	Yes	No	No	Real Estate
11.	Korea Electric Power Corporation	28,456	23.4	Yes	Yes	No	Electricity, Energy, and Power
12.	Korea Expressway	23,100	19.0	Yes	No	No	Transport Infrastructure
13.	Woori Bank	21,290	17.5	Yes	Yes	No	Banking
14.	KEB Hana Bank	21,170	17.4	No	No	No	Banking
15.	Shinyoung Securities	19,625	16.1	No	Yes	No	Securities
16.	Korea Rail Network Authority	19,204	15.8	Yes	No	No	Transport Infrastructure
17.	Kookmin Bank	18,950	15.6	No	No	No	Banking
18.	The Export-Import Bank of Korea	18,444	15.1	Yes	No	No	Banking
19.	Hyundai Capital Services	17,440	14.3	No	No	No	Consumer Finance
20.	Shinhan Card	16,727	13.7	No	No	No	Credit Card
21.	Korea Deposit Insurance Corporation	15,280	12.5	Yes	No	No	Insurance
22.	Nonghyup Bank	15,145	12.4	Yes	No	No	Banking
23.	Korea SMEs and Startups Agency	15,038	12.3	Yes	No	No	SME Development
24.	Hanwha Investment and Securities	14,836	12.2	No	No	No	Securities
25.	KB Kookmin Bank Card	13,534	11.1	No	No	No	Consumer Finance
26.	Standard Chartered Bank Korea	13,290	10.9	No	No	No	Banking
27.	Korea Gas Corporation	13,090	10.7	Yes	Yes	No	Gas Utility
28.	Nonghyup	12,100	9.9	Yes	No	No	Banking
29.	Meritz Securities Co.	12,009	9.9	No	Yes	No	Securities
30.	Korea Student Aid Foundation	10,870	8.9	Yes	No	No	Student Loan
Total Top 30 LCY Corporate Issuers		922,140	756.8				
Total LCY Corporate Bonds		1,483,824	1,217.7				
Top 30 as % of Total LCY Corporate Bonds		62.1%	62.1%				

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 2020.

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.

The Republic of Korea's corporate bond market saw tepid issuance during Q1 2020, particularly in March, due to market volatility as a result of the COVID-19 pandemic. In addition, the continued pessimistic outlook in economic growth resulted in less borrowing by corporates during the quarter. **Table 3** lists the notable corporate bond issuances in Q1 2020. The market continues to be dominated by issuances from banks and financial institutions such as Woori Bank, Nonghyup Bank, and Mirae Asset Daewoo.

Investor Profile

Insurance companies and pension funds remained the largest holders of the Republic of Korea's LCY government bonds at the end of December 2019 with a share of 35.7%, which was slightly lower than their share of 36.0% in the same period in 2018 (**Figure 2**). General government and banks were next with shares of 17.6% and 17.4%, respectively. The share of the general government declined from 19.2% in December 2018, while that of

Table 3: Notable Local Currency Corporate Bond Issuance in the First Quarter of 2020

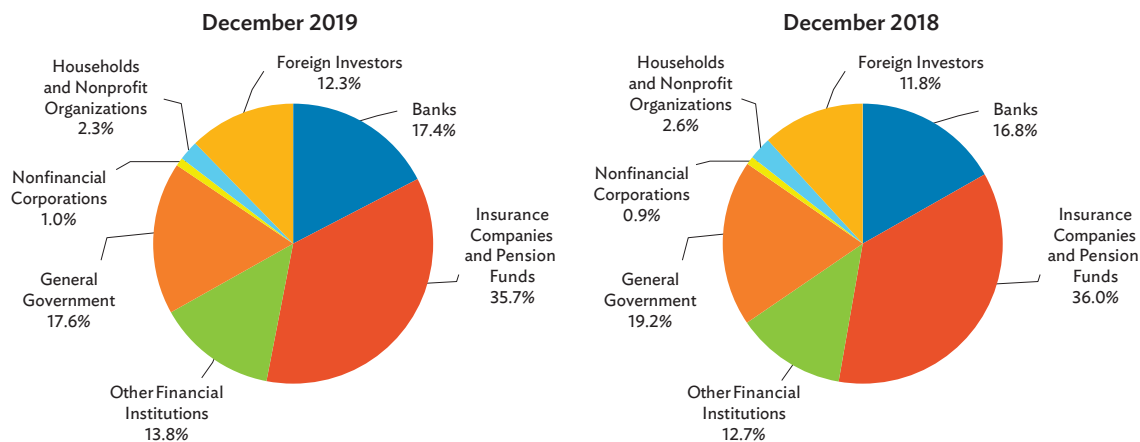
Corporate Issuers	Coupon Rate (%)	Issued Amount (KRW billion)
Woori Bank		
2-year bond	1.42	400
3-year bond	1.25	400
3-year bond	1.46	350
10-year bond	1.94	300
Nonghyup Bank		
2-year bond	1.50	380
5-year bond	1.62	300
10-year bond	2.38	300
Mirae Asset Daewoo		
3-year bond	1.80	350
6-year bond	3.00	500
SK Hynix		
3-year bond	1.61	340
5-year bond	1.72	360

Corporate Issuers	Coupon Rate (%)	Issued Amount (KRW billion)
National Agricultural Cooperative Federation		
3-year bond	1.51	300
5-year bond	1.62	400
Samsung Securities		
3-year bond	1.48	450
S-Oil Corp		
5-year bond	1.49	440
Kookmin Bank		
10-year bond	2.02	400
KB Financial Group		
10-year bond	2.21	370
LG Chem		
10-year bond	1.57	350
KEB Hana Bank		
10-year bond	2.32	350

KRW = Korean won.

Source: Based on data from Bloomberg LP.

Figure 2: Local Currency Government Bonds Investor Profile



Sources: AsianBondsOnline and the Bank of Korea.

banks marginally increased from 16.8%. The share of other financial institutions rose to 13.8% from 12.7% during the review period. Foreign holdings of LCY government bonds was up marginally to 12.3% from 11.8%.

Insurance companies and pension funds continued to be the largest investor group in the Republic of Korea's LCY corporate bond market with a share of 37.0% at the end of December 2019, a decline from its share of 39.2% in the same period in 2018 (**Figure 3**). Meanwhile, the share of other financial institutions rose to 35.8% from 33.3% during the same period. The share of the general government was barely changed at 13.6% at the end of December 2019, while the share of banks rose to 8.5% from 7.1%. The share of foreign investors remained negligible at 0.1%.

Foreign investor demand for the Republic of Korea's LCY bond market remained strong in the first 4 months of 2020 amid financial market volatility caused by the COVID-19 pandemic (**Figure 4**). The Republic of Korea remained a safe haven relative to its peers in the region as its LCY bond market registered net inflows of KRW4,623 billion in January. A decline to KRW570 billion in net inflows was registered in February, primarily due to risk aversion as domestic COVID-19 cases temporarily surged. However, foreign investors returned in March with net inflows of KRW3,581 billion, followed by a surge in net inflows of KRW7,383 billion in April.

The strong demand for the Republic of Korea's LCY bonds can be attributed to the high interest rate differential with the bond yields of similarly rated peers and with US Treasury yields after the Federal Reserve cut its rate to between 0% and 0.25%. The Republic of Korea also remained a safe haven given its high credit rating, robust external balances, the government's efforts to provide liquidity in the market, and its various programs to cushion the economic impact of the pandemic.

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

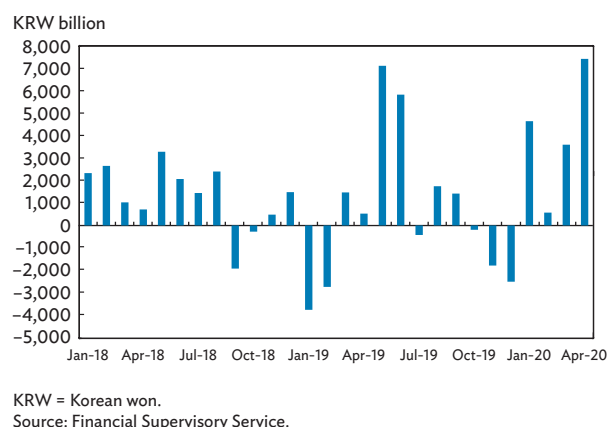
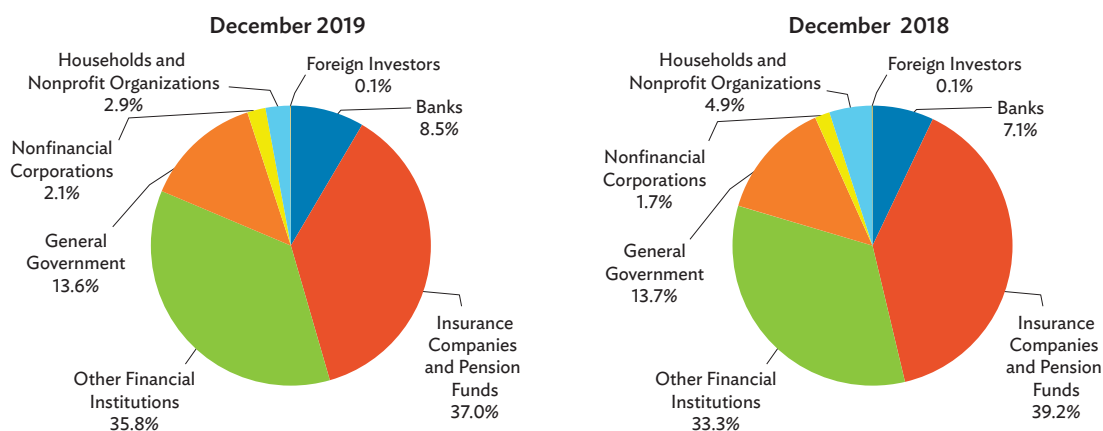


Figure 3: Local Currency Corporate Bonds Investor Profile



Sources: AsianBondsOnline and the Bank of Korea.

Ratings Update

On 11 February, Fitch Ratings affirmed the Republic of Korea's sovereign credit rating at AA– with a stable outlook. The rating affirmation was supported by the economy's steady macroeconomic prospects, which were to be further boosted by the government's fiscal stimulus, sound fiscal management, and robust external finances. Risks to the outlook remain and largely stem from rising cases of COVID-19 and geopolitical risks.

On 21 April, S&P Global affirmed the Republic of Korea's sovereign credit rating at AA and maintained its stable outlook. The rating agency stated that the economy may contract 1.5% in 2020, and it expects the fiscal deficit to widen this year due to fiscal measures being undertaken by the government to address the impact of the COVID-19 pandemic. The rating agency cited the Republic of Korea's strong economic prospects, with growth expected to rebound in 2021; the government's sound fiscal position amid years of surpluses; a favorable policy environment; and strong external metrics as reasons behind the affirmation.

Policy, Institutional, and Regulatory Developments

The Republic of Korea Announces Launch of Financial Support Package in Excess of KRW50 Trillion

On 19 March, the Government of the Republic of Korea announced the launch of a more than KRW50 trillion financial support package to aid businesses and households affected by the COVID-19 pandemic. The package includes nine programs focused on (i) providing liquidity to small businesses, special guarantees for small and medium-sized enterprise loans, guarantees for small merchants; (ii) deferment and or suspension of loan and interest payments by small and medium-sized enterprises and small businesses; and the (iii) creation

of a bond market stabilization fund and equity market stabilization fund.

The Bank of Korea Announces Measures to Boost Market Liquidity

On 26 March, the Bank of Korea announced measures to support market liquidity and stabilize financial markets. This included the conduct of weekly repo auctions for a period of 3 months. It also expanded the range of institutions eligible for the auctions from five to 16 nonbanks, eligible securities will now include eight bonds issued by public organizations, and eligible collateral has been extended to eight bonds issued by public organizations and bank debentures.

The Bank of Korea Launches Corporate Bond-Backed Lending Facility

On 16 April, the Bank of Korea launched the Corporate Bond-Backed Lending Facility to allow banks and non-bank financial institutions that can provide high-rated corporate bonds as collateral to access credit from the central bank. The facility will have a ceiling of KRW10 trillion and a term of 3 months; this can be adjusted after an assessment of financial market conditions.

National Assembly Passes KRW12.2 Trillion Supplementary Budget

On 30 April, the National Assembly passed the government's second supplementary budget, which was revised upward to KRW12.2 trillion from KRW7.6 trillion. As part of the government's financial support package, funds will be used to aid sectors affected by the COVID-19 pandemic, particularly financing of the household emergency relief program. KRW8.8 trillion will be sourced from spending restructuring, and the remaining KRW3.4 trillion will be raised via debt issuance.