

Republic of Korea

Yield Movements

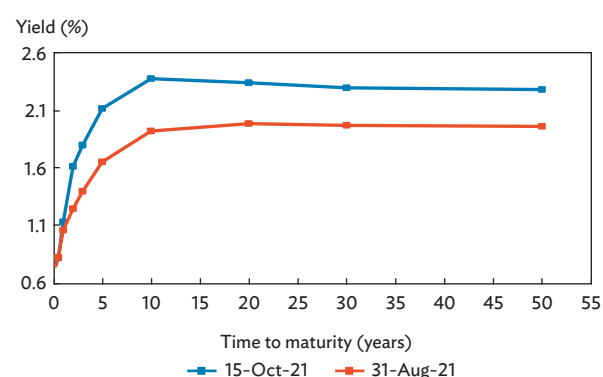
The Republic of Korea's local currency (LCY) government bond yields surged for most tenors between 31 August and 15 October (**Figure 1**). Yields for the 3-month and 6-month paper were mostly unchanged, while the 1-year bond yield increased 7 basis points (bps). Yields for tenors between 2 years and 50 years surged 38 bps on average, with the 5-year and 10-year bonds posting the largest increases at 46 bps and 45 bps, respectively. The yield spread between the 2-year and 10-year tenors rose to 75 bps from 67 bps during the review period.

Short-term government bond yields remained range-bound during the review period, following a spike in yields the week before the Bank of Korea's monetary policy meeting on 26 August, when the central bank raised its base rate to 0.75%. Yields barely moved thereafter given expectations that the central bank would maintain its policy rate at its October monetary policy meeting. On 12 October, as expected, the Bank of Korea kept the base rate steady.

The rise in yields for tenors of 2 years and longer continued throughout the review period on heightened expectations of another rate hike by the Bank of Korea in November, its last monetary policy meeting for the year. Subsequently on 25 November, the Bank of Korea raised the base rate by 25 bps to 1.00%. The domestic economy is forecast to continue its recovery supported by an improvement in consumption, exports, and investment. The growth forecast for 2021 was maintained at 4.0%. Meanwhile, inflation is expected to be well above the 2.0% level, with the central bank raising its forecast for 2021 to 2.3% from its August projection of 2.1%. The central bank also stated that it will assess when to further adjust the degree of monetary policy accommodation given sound economic growth and inflation running above the target level, driving expectations of further rate hikes in 2022.

Moreover, domestic yields tracked the rise in global yields as the United States (US) Federal Reserve is expected to announce tapering measures as early as at its November meeting. In addition, foreign selling of Korea Treasury Bond futures also contributed to the rise in domestic yields. This was driven by the weakening of the Korean won that resulted in smaller capital gains,

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



Source: Based on data from Bloomberg LP.

making the instrument less attractive to foreign investors. The domestic currency depreciated 1.9% during the review period to KRW1,182.3 per USD1.0 on 15 October, and reaching a low of KRW1,198.9 per USD1.0 on 12 October due to the continued strengthening of the US dollar and foreign outflows from the equities market.

On 3 September, the government submitted its 2022 budget proposal to the National Assembly for approval. The budget amounts to KRW604.4 trillion, a 13.7% increase from the original 2021 budget and an 8.3% increase when including all supplementary budgets passed in 2021. The budget is also expected to result in lesser issuance of deficit-financing bonds in 2022 compared to 2021, easing bond oversupply concerns. However, this was not enough to drive down yields as the rise in global yields weighed more on the domestic bond market.

The Republic of Korea's economic growth moderated to 4.0% year-on-year (y-o-y) in the third quarter (Q3) of 2021 from 6.0% y-o-y in the second quarter (Q2), based on advance estimates by the Bank of Korea. The slower growth was driven by the lower annual increase in private consumption of 3.2% y-o-y from 3.7% y-o-y in Q2 2021 due to stricter social distancing measures imposed during the quarter. Gross fixed capital formation growth slowed in Q3 2021 to 1.8% y-o-y from 3.8% y-o-y. Export growth also slumped to 6.9% y-o-y from a surge of 22.4% y-o-y in Q2 2021. Meanwhile, government spending posted accelerated growth of 6.3% y-o-y from 5.3% y-o-y. Consumer price inflation in the Republic of Korea

remained high at 2.6% y-o-y in both July and August, slightly easing to 2.5% y-o-y in September. In October, inflation surged to 3.2% y-o-y, the highest since January 2012, mainly driven by accelerated annual increases in the prices of utilities, transport, and communication.

Foreign demand for the Republic of Korea's LCY bonds remained strong in the month of July, with registered net inflows of KRW9,290 billion. However, inflows dropped in August to KRW1,689 billion as foreign investors sold domestic bonds due to the rise in short-term yields leading up to the Bank of Korea's rate hike on 26 August. Foreign inflows recovered in September to KRW5,172 billion, however, inflows were capped due to increased expectations of further tightening measures by the central bank and the possibility of tapering by the US Federal Reserve as early as November. Subsequently on its 2–3 November meeting, the Federal Reserve announced that it would begin tapering its asset purchases starting in November.

Size and Composition

The Republic of Korea's LCY bond market grew 1.6% quarter-on-quarter (q-o-q) to reach a size of KRW2,799.9 trillion (USD2,364.6 billion) at the end of Q3 2021 (Table 1). This was slower than the 2.3% q-o-q expansion posted in the previous quarter. The growth was largely driven by the government bond market as the corporate segment grew at a slower pace. From the same period in 2020, the Republic of Korea's bond market rose 7.6% y-o-y, slower than the 7.9% y-o-y growth posted in Q2 2021.

Government bonds. The Republic of Korea's LCY government bond market rose 1.9% q-o-q in Q3 2021 to KRW1,179.7 trillion (USD996.3 billion). However, this was lower than the 3.2% q-o-q growth posted in the previous quarter. Growth continued to stem from the rise in the stock of central government bonds, which expanded 3.0% q-o-q to KRW831.7 trillion. Meanwhile, the outstanding size of Monetary Stabilization Bonds issued by the Bank of Korea declined 2.1% q-o-q to KRW151.1 trillion. The outstanding bonds issued by other government-owned entities inched up 0.3% q-o-q to KRW197.0 trillion.

Issuance of government bonds dropped 19.0% q-o-q to KRW92.5 trillion in Q3 2021, as both issuance of central government bonds (–29.0% q-o-q) and central bank bonds (–9.1% q-o-q) declined during the quarter. The lower issuance of central government bonds during the quarter was due to a high base in Q2 2021 in line with the government's frontloading policy in the first half of the year. Bonds issued by other government owned-entities also fell 6.8% q-o-q.

Foreign Exchange Stabilization Bonds. The Republic of Korea issued USD1.3 billion worth of Foreign Exchange Stabilization Bonds on 7 October. These bonds are issued to promote foreign exchange market stability through accumulation of foreign exchange reserves, and the resulting rates will also serve as a guide for prospective companies planning to issue bonds offshore. The bond offer was conducted via a dual-tranche issuance comprising USD500.0 million worth of 10-year bonds priced at 1.796% (25-bps spread over

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

	Outstanding Amount (billion)						Growth Rate (%)			
	Q3 2020		Q2 2021		Q3 2021		Q3 2020		Q3 2021	
	KRW	USD	KRW	USD	KRW	USD	q-o-q	y-o-y	q-o-q	y-o-y
Total	2,602,081	2,224	2,756,445	2,447	2,799,920	2,365	1.9	9.8	1.6	7.6
Government	1,069,062	914	1,158,252	1,028	1,179,746	996	3.0	12.1	1.9	10.4
Central Government Bonds	707,681	605	807,725	717	831,745	702	4.2	16.6	3.0	17.5
Central Bank Bonds	166,750	143	154,230	137	151,050	128	(1.3)	(2.5)	(2.1)	(9.4)
Others	194,631	166	196,297	174	196,951	166	2.3	10.7	0.3	1.2
Corporate	1,533,019	1,310	1,598,193	1,419	1,620,174	1,368	1.1	8.2	1.4	5.7

() = negative, KRW = Korean won, q-o-q = quarter-on-quarter, Q2 = second quarter, Q3 = third 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 KG Zeroin Corporation.

the 10-year US Treasury) and EUR700.0 million worth of 5-year bonds priced at -0.053% (13 bps spread over the 5-year benchmark euro mid-swap). The euro tranche was also a green bond issuance listed on the Frankfurt Stock Exchange and, eventually, on the London Stock Exchange.

Corporate bonds. The outstanding size of the Republic of Korea's LCY corporate bond market inched up 1.4% q-o-q to KRW1,620.2 trillion (USD1,368.3 billion), with growth slightly lower than the 1.6% q-o-q increase posted in the previous quarter. **Table 2** lists the top 30 LCY corporate bond issuers in the Republic of Korea, with aggregate

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	153,269	129.4	Yes	No	No	Housing Finance
2. Industrial Bank of Korea	70,250	59.3	Yes	Yes	No	Banking
3. Mirae Asset Securities Co.	60,133	50.8	No	Yes	No	Securities
4. Korea Investment and Securities	56,780	48.0	No	No	No	Securities
5. Hana Financial Investment	50,209	42.4	No	No	No	Securities
6. KB Securities	49,620	41.9	No	No	No	Securities
7. Shinhan Investment Corporation	40,377	34.1	No	No	No	Securities
8. NH Investment & Securities	34,075	28.8	Yes	Yes	No	Securities
9. Korea Electric Power Corporation	30,610	25.9	Yes	Yes	No	Electricity, Energy, and Power
10. Korea Land & Housing Corporation	30,533	25.8	Yes	No	No	Real Estate
11. Samsung Securities	30,341	25.6	No	Yes	No	Securities
12. Meritz Securities Co.	29,079	24.6	No	Yes	No	Securities
13. Shinhan Bank	28,992	24.5	No	No	No	Banking
14. Korea Expressway	25,670	21.7	Yes	No	No	Transport Infrastructure
15. The Export-Import Bank of Korea	23,630	20.0	Yes	No	No	Banking
16. Woori Bank	22,520	19.0	Yes	Yes	No	Banking
17. Kookmin Bank	21,704	18.3	No	No	No	Banking
18. KEB Hana Bank	20,815	17.6	No	No	No	Banking
19. NongHyup Bank	19,320	16.3	Yes	No	No	Banking
20. Korea SMEs and Startups Agency	19,228	16.2	Yes	No	No	SME Development
21. Korea National Railway	19,050	16.1	Yes	No	No	Transport Infrastructure
22. Shinyoung Securities	17,784	15.0	No	Yes	No	Securities
23. Hanwha Investment and Securities	17,378	14.7	No	No	No	Securities
24. Shinhan Card	16,185	13.7	No	No	No	Credit Card
25. KB Kookmin Bank Card	14,350	12.1	No	No	No	Consumer Finance
26. Hyundai Capital Services	14,205	12.0	No	No	No	Consumer Finance
27. Standard Chartered Bank Korea	13,760	11.6	No	No	No	Banking
28. NongHyup	13,580	11.5	Yes	No	No	Banking
29. Samsung Card Co.	12,088	10.2	No	Yes	No	Credit Card
30. Shinhan Financial Group	10,865	9.2	No	Yes	No	Banking
Total Top 30 LCY Corporate Issuers	966,401	816				
Total LCY Corporate Bonds	1,620,174	1,368.3				
Top 30 as % of Total LCY Corporate Bonds	59.6%	59.6%				

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

Notes:

1. Data as of 30 September 2021.

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 KG Zeroin Corporation data.

bonds outstanding of KRW966.4 trillion at the end of September, accounting for 59.6% of the total LCY corporate bond market. Financial institutions, particularly banks and securities and investment firms, continued to comprise a majority of the list and had a collective share of 65.3% of the total volume. Korea Housing Finance Corporation, a government-related institution providing financial assistance for social housing, remained the largest single-largest corporate bond issuer with outstanding bonds of KRW153.3 trillion. Industrial Bank of Korea and Mirae Asset Securities followed with total bonds outstanding of KRW70.2 trillion and KRW60.1 trillion, respectively.

The slower q-o-q growth in the Republic of Korea's corporate bond market was driven by the decline in issuance of 19.9% q-o-q to KRW120.6 trillion from KRW150.5 trillion in the previous quarter. All categories—special public entities, financial debentures, and private companies—posted q-o-q decreases. Firms borrowed less during the quarter, particularly in the month of August, due to the spike in yields leading up to the Bank of Korea rate hike. **Table 3** lists the notable corporate bond issuances in Q2 2021. Financial firms such as Kookmin Bank, Woori Bank, and NongHyup Bank had the largest issuances during the quarter.

Investor Profile

Insurance companies and pension funds remained the top holders of the Republic of Korea's LCY government bonds with a market share of 34.1% at the end of June 2021, almost at par with 34.2% in June 2020 (**Figure 2**). Banks were the second-largest investor group with a share of 19.1%, up from 16.7% in Q2 2020. The shares of general government and other financial institutions fell in Q2 2021 to 16.2% and 14.6%, respectively, from 16.5% and 16.0% in the same period in 2020. Foreign holdings of LCY government bonds rose to 15.4% at the end June 2021 from 13.0% in the previous year, as high levels of foreign inflows were registered in the first half of 2021.

In Q2 2021, other financial institutions continued to surpass insurance companies and pension funds as the largest investor group of the Republic of Korea's LCY corporate bond market (**Figure 3**). The share of other financial institutions jumped to 40.2% from 37.4% in the same period in 2020, while the share of insurance companies and pension funds fell to 35.5% from 37.2%. The respective shares of the general government and banks increased to 14.3% and 9.5%. Meanwhile, the share of foreign holders remained negligible at 0.1%.

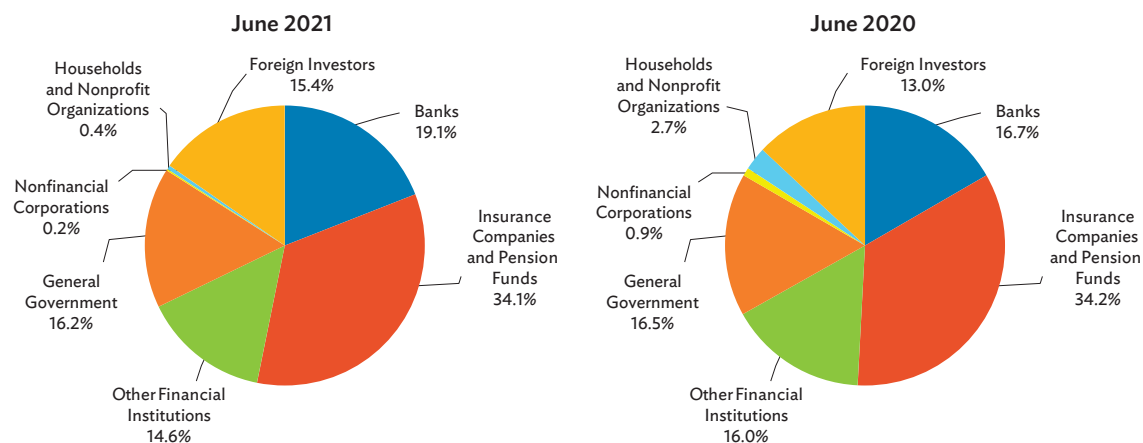
Table 3: Notable Local Currency Corporate Bond Issuances in the Third Quarter of 2021

Corporate Issuers	Coupon Rate (%)	Issued Amount (KRW billion)	Corporate Issuers	Coupon Rate (%)	Issued Amount (KRW billion)
Kookmin Bank ^a			NongHyup Bank ^a		
1-year bond	1.14	530	1-year bond	1.11	700
1-year bond	1.10	400	1-year bond	1.14	550
1-year bond	1.11	400	1-year bond	1.23	480
1-year bond	1.12	380	1-year bond	0.13	340
1-year bond	1.07	380	1-year bond	1.09	300
1-year bond	1.14	370	Sinbo Securitization Specialty ^a		
1-year bond	1.10	350	3-year bond	1.77	609
1-year bond	1.10	300	3-year bond	2.01	326
1-year bond	1.15	270	Shinhan Bank ^a		
1-year bond	1.15	250	1-year bond	1.17	480
Woori Bank ^a			1-year bond	1.11	240
1-year bond	1.10	590	1-year bond	1.14	200
1-year bond	1.10	500	Kyobo Life Insurance		
1-year bond	1.15	300	30-year bond	3.72	470
1-year bond	1.10	300	Cube Banpo Securitization		
1-year bond	1.55	280	4-year bond	1.88	400
1-year bond	0.13	280	Samsung Biologics		
1-year bond	1.13	250	3-year bond	1.89	380
1-year bond	1.12	250			
3-year bond	1.58	300			

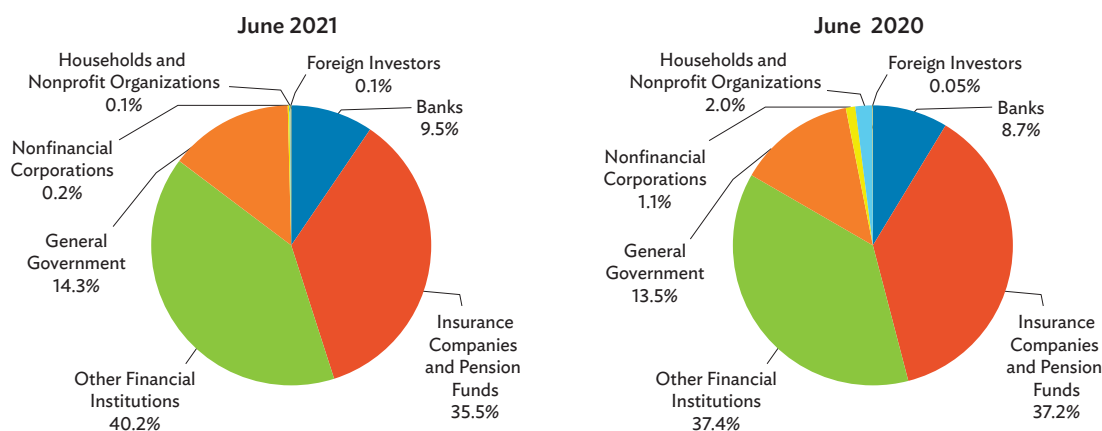
KRW = Korean won.

^a Multiple issuance of the same tenor indicates issuance on different dates.

Source: Based on data from Bloomberg LP.

Figure 2: Local Currency Government Bonds Investor Profile


Source: AsianBondsOnline and The Bank of Korea.

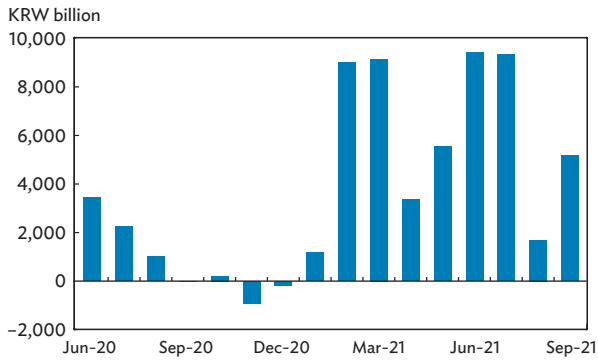
Figure 3: Local Currency Corporate Bonds Investor Profile


Source: AsianBondsOnline and The Bank of Korea.

Net foreign inflows into the Republic of Korea's LCY bond market remained high in July with another record volume of KRW9,290 billion, the second-highest level for the year (**Figure 4**). However, net inflows fell to KRW1,689 billion in August as net foreign purchases of longer-tenor bonds were offset by the net outflows from short-term bonds (**Figure 5**). Foreign investors sold Korean LCY bonds, particularly those with tenors of less than 1 year, amid a surge in short-term yields leading up to the rate hike

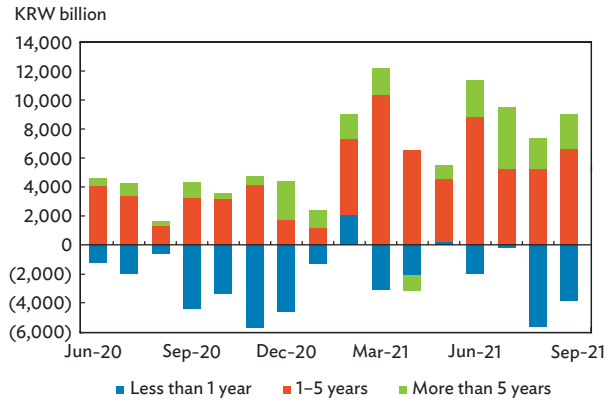
by the Bank of Korea in its 26 August monetary policy meeting. Foreign inflows recovered in September to KRW5,172 billion. However, this was capped by the continued outflows from the short-term bond segment, which were driven by expectations of another rate hike by the Bank of Korea before the year ends and the Federal Reserve announcement of possible tightening measures beginning as early as November.

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



KRW = Korean won.
Source: Financial Supervisory Service.

Figure 5: Net Foreign Investment in Local Currency Bonds in the Republic of Korea by Remaining Maturity



KRW = Korean won.
Source: Financial Supervisory Service.

Policy, Institutional, and Regulatory Developments

The Government of the Republic of Korea Passes 2022 Budget Proposal

On 3 September, the Government of the Republic of Korea passed for approval to the National Assembly its 2022 budget proposal of KRW604.4 trillion. The proposed budget is 8.3% higher than the original 2021 budget of KRW558.0 trillion, and almost at par with the revised KRW604.9 trillion budget that includes all supplementary budgets passed during the year. The budget aims to aid citizens and society in the recovery from the pandemic, promote inclusive growth, and prepare for a post-pandemic economy. The 2022 budget is also expected to reduce the fiscal deficit by KRW20.0 trillion as tax revenues are expected to improve on the back of the continued economic recovery. The fiscal deficit as a percentage of gross domestic product is forecast to decline to 2.6% in 2022 from 4.4% in 2021.