

Republic of Korea

Yield Movements

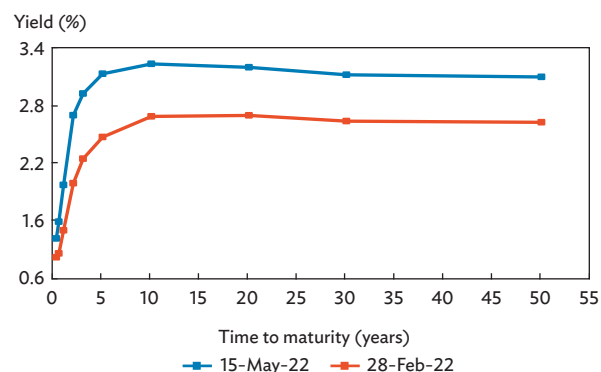
The Republic of Korea's local currency (LCY) government bond yields rose for all tenors between 28 February and 15 May (**Figure 1**). Yields for the 3-month through 1-year tenors rose 33 basis points (bps) on average. Meanwhile, yields for the 2-year through 5-year tenors surged 68 bps on average, with the 2-year tenor posting the largest increase at 71 bps. Yields for tenors of between 10 years and 50 years rose 50 bps on average. The spread between the 2-year and 10-year tenors fell to 53 bps from 70 bps during the review period, causing a slight flattening of the yield curve.

Yields rose across the curve during the review period amid rising global and domestic inflation, and monetary policy normalization by both the United States (US) Federal Reserve and the Bank of Korea (BOK). In its 15–16 March and 3–4 May monetary policy meetings, the US Federal Reserve raised the federal funds rate target range by 75 bps in total to a range of between 0.75% and 1.00%. In addition, the Federal Reserve in May signaled that further and larger rate hikes would be forthcoming to address inflation, and it announced the reduction of its bond holdings starting in June.

To address market yield volatility and as part of its market stabilization efforts, the BOK purchased KRW2.0 trillion worth of state bonds on 5 April. This was the second bond purchase of the year, following a KRW2.0 trillion purchase in February. However, volatility in US Treasuries continued to weigh on the domestic bond market.

On the domestic front, the BOK raised its base rate by 25 bps to 1.50% at its 14 April monetary policy meeting, with market expectations of further rate hikes amid the sharp rise in inflation. Inflation peaked at 4.8% in April, the highest since October 2008, from an average of 3.8% in the first quarter (Q1) of the year due to rising energy prices and supply chain disruptions. Subsequently, on 26 May, the BOK raised the base rate by another 25 bps to 1.75%. In addition, the central bank announced that inflation would remain at around the 5.0% level for the rest of the year and raised its 2022 and 2023 inflation forecasts to 4.5% and 2.9%, respectively, from the February forecasts of 3.1% and 2.0%. Meanwhile, 2022 and 2023 economic growth forecasts were lowered

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



Source: Based on data from Bloomberg LP.

to 2.7% and 2.4%, respectively, from the forecasts of 3.0% and 2.5% announced in February. Downside risks to the outlook include a prolonged Russian invasion of Ukraine, a slowdown in economic growth in the People's Republic of China, and faster-than-expected monetary policy normalization in the US.

Upward pressure on domestic yields also stemmed from bond oversupply concerns due to uncertainties on the fiscal policy of the newly elected government. However, concerns eased as the government announced in May that the financing of the proposed second supplementary budget of KRW59.4 trillion would not involve the additional issuance of government bonds. This led to a decline in yields after the announcement, slightly cushioning the surge in yields in March and April.

The Republic of Korea's economic growth slowed to 3.0% year-on-year (y-o-y) in Q1 2022 from 4.2% y-o-y in the fourth (Q4) of 2021, based on preliminary estimates by the BOK. The lower growth was primarily driven by the 3.5% y-o-y contraction in gross fixed capital formation, a reversal from the 1.4% y-o-y increase in the previous quarter. Both private and public consumption also posted lower annual increases in Q1 2022. Moreover, export growth slowed to 7.3% y-o-y from 7.9% y-o-y in the previous quarter. On a quarter-on-quarter (q-o-q) basis, domestic economic growth decelerated to 0.6% in Q1 2022 from 1.3% in Q4 2021.

Foreign demand for the Republic of Korea's LCY bonds remained strong in the first 2 months of the year, with the market recording net inflows of KRW3,673.0 billion and KRW3,950.0 billion, respectively. However, foreign inflows dropped to KRW279.0 billion in March and KRW36.0 billion in April due to the narrowing interest rate differential between US Treasuries and domestic government bonds and the continued depreciation of the Korean won. The Korean won was one of the weakest currencies in the region during the review period, depreciating 6.3% versus the US dollar to KRW1,283.8 per USD1.0 as of 15 May.

Size and Composition

The size of the Republic of Korea's LCY bond market reached KRW2,898.1 trillion (USD2.4 trillion) at the end of March (**Table 1**). Growth rose to 2.0% q-o-q in Q1 2022 from 1.5% q-o-q in the previous quarter, largely driven by the government sector as the corporate segment posted marginal growth. From the same period in 2021, the Republic of Korea's LCY bond market grew 7.5% y-o-y, slightly lower than the 7.9% y-o-y increase posted in Q4 2021.

Government bonds. Growth in the Republic of Korea's LCY government bond market accelerated to 3.4% q-o-q in Q1 2022 from 0.2% q-o-q in Q4 2021 to reach a size of KRW1,222.4 trillion at the end of March. The higher growth rate was solely driven by the 4.8% q-o-q rise in the stock of central government bonds, as both outstanding central bank bonds and other government bonds fell

during the quarter. Issuance of central government bonds surged 76.9% q-o-q in Q1 2022, in line with the government's frontloading policy program wherein 73% of the budget is allocated to be spent in the first half of the year. Meanwhile, Monetary Stabilization Bonds issued by the BOK declined 0.1% q-o-q as maturities exceeded issuance during the quarter, while outstanding bonds issued by other government-owned entities fell 0.3% q-o-q.

Corporate bonds. The Republic of Korea's LCY corporate bond market posted a marginal increase of 1.0% q-o-q to reach KRW1,675.7 trillion at the end of March. This was lower than the 2.4% q-o-q growth posted in the previous quarter. **Table 2** lists the top 30 LCY corporate bond issuers in the Republic of Korea at the end of March, which had aggregate outstanding bonds of KRW997.8 trillion and accounted for 59.5% of the total LCY corporate bond market. Companies from the financial sector continued to dominate the list with a share of 65.2% of the top 30's outstanding bonds. Korea Housing Finance Corporation remained the largest corporate issuer in the market with total bonds outstanding of KRW150.5 trillion at the end of Q1 2022. The Industrial Bank of Korea and Korea Investment and Securities were the next largest issuers at KRW78.6 trillion and KRW54.1 trillion, respectively.

The marginal growth in the Republic of Korea's corporate bond market in Q1 2022 was due to the 21.1% q-o-q decline in issuance to KRW135.5 billion from KRW171.8 billion in Q4 2021. Fewer companies issued

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

| | Outstanding Amount (billion) | | | | | | Growth Rate (%) | | | |
|--------------------------|------------------------------|-------|-----------|-------|-----------|-------|-----------------|-------|---------|--------|
| | Q1 2021 | | Q4 2021 | | Q1 2022 | | Q1 2021 | | Q1 2022 | |
| | KRW | USD | KRW | USD | KRW | USD | q-o-q | y-o-y | q-o-q | y-o-y |
| Total | 2,695,546 | 2,382 | 2,841,873 | 2,388 | 2,898,057 | 2,391 | 2.4 | 8.9 | 2.0 | 7.5 |
| Government | 1,122,368 | 992 | 1,182,573 | 994 | 1,222,359 | 1,009 | 4.0 | 13.1 | 3.4 | 8.9 |
| Central Government Bonds | 769,339 | 680 | 843,660 | 709 | 884,103 | 730 | 5.9 | 19.1 | 4.8 | 14.9 |
| Central Bank Bonds | 157,230 | 139 | 140,320 | 118 | 140,190 | 116 | (1.3) | (5.1) | (0.1) | (10.8) |
| Others | 195,799 | 173 | 198,592 | 167 | 198,065 | 163 | 1.5 | 8.4 | (0.3) | 1.2 |
| Corporate | 1,573,178 | 1,390 | 1,659,300 | 1,395 | 1,675,698 | 1,383 | 1.2 | 6.0 | 1.0 | 6.5 |

(-) = 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. Bloomberg LP end-of-period local currency-USD rates are used.
2. Growth rates are calculated from local currency base and do not include currency effects.
3. "Others" comprise Korea Development Bank Bonds, National Housing Bonds, and Seoul Metro Bonds.
4. Corporate bonds include equity-linked securities and derivatives-linked securities.

Sources: The Bank of Korea and KG Zeroin Corporation.

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 | 150,503 | 124.2 | Yes | No | No | Housing Finance |
| 2. | Industrial Bank of Korea | 78,620 | 64.9 | Yes | Yes | No | Banking |
| 3. | Korea Investment and Securities | 54,058 | 44.6 | No | No | No | Securities |
| 4. | Mirae Asset Securities Co. | 51,710 | 42.7 | No | Yes | No | Securities |
| 5. | Hana Financial Investment | 50,820 | 41.9 | No | No | No | Securities |
| 6. | KB Securities | 49,351 | 40.7 | No | No | No | Securities |
| 7. | Shinhan Investment Corporation | 46,172 | 38.1 | No | No | No | Securities |
| 8. | Meritz Securities Co. | 44,264 | 36.5 | No | Yes | No | Securities |
| 9. | Korea Electric Power Corporation | 39,600 | 32.7 | Yes | Yes | No | Electricity, Energy, and Power |
| 10. | NH Investment & Securities | 34,865 | 28.8 | Yes | Yes | No | Securities |
| 11. | Korea Land & Housing Corporation | 32,014 | 26.4 | Yes | No | No | Real Estate |
| 12. | Shinhan Bank | 29,392 | 24.3 | No | No | No | Banking |
| 13. | Samsung Securities | 29,022 | 23.9 | No | Yes | No | Securities |
| 14. | Korea Expressway | 26,990 | 22.3 | Yes | No | No | Transport Infrastructure |
| 15. | The Export-Import Bank of Korea | 26,670 | 22.0 | Yes | No | No | Banking |
| 16. | Woori Bank | 23,690 | 19.5 | Yes | Yes | No | Banking |
| 17. | KEB Hana Bank | 22,575 | 18.6 | No | No | No | Banking |
| 18. | NongHyup Bank | 20,220 | 16.7 | Yes | No | No | Banking |
| 19. | Korea SMEs and Startups Agency | 20,018 | 16.5 | Yes | No | No | SME Development |
| 20. | Kookmin Bank | 19,894 | 16.4 | No | No | No | Banking |
| 21. | Korea National Railway | 19,380 | 16.0 | Yes | No | No | Transport Infrastructure |
| 22. | Shinhan Card | 17,175 | 14.2 | No | No | No | Credit Card |
| 23. | Shinyoung Securities | 16,779 | 13.8 | No | Yes | No | Securities |
| 24. | Hanwha Investment and Securities | 15,283 | 12.6 | No | No | No | Securities |
| 25. | Hyundai Capital Services | 14,955 | 12.3 | No | No | No | Consumer Finance |
| 26. | KB Kookmin Bank Card | 14,695 | 12.1 | No | No | No | Consumer Finance |
| 27. | Standard Chartered Bank Korea | 13,130 | 10.8 | No | No | No | Banking |
| 28. | NongHyup | 12,830 | 10.6 | Yes | No | No | Banking |
| 29. | Samsung Card Co. | 11,958 | 9.9 | No | Yes | No | Credit Card |
| 30. | Shinhan Financial Group | 11,205 | 9.2 | No | Yes | No | Banking |
| Total Top 30 LCY Corporate Issuers | | 997,838 | 823.3 | | | | |
| Total LCY Corporate Bonds | | 1,675,698 | 1,382.7 | | | | |
| Top 30 as % of Total LCY Corporate Bonds | | 59.5% | 59.5% | | | | |

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 31 March 2022.

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.

in Q1 2022 due to high borrowing costs and increased market volatility. **Table 3** lists the notable corporate bond issuances in Q1 2022. Financial firms such as the Industrial Bank of Korea and the Export-Import Bank of Korea had the largest aggregate issuances for the quarter. Meanwhile, NongHyup Life Insurance had the single-largest issuance for the quarter.

Investor Profile

Government bonds. Insurance companies and pension funds continued to be the largest investor group in the Republic of Korea’s LCY government bond market at the end of December 2021 (**Figure 2**). However, its share declined to 34.3% from 35.7% in the same period in 2020.

Table 3: Notable Local Currency Corporate Bond Issuances in the First Quarter of 2022

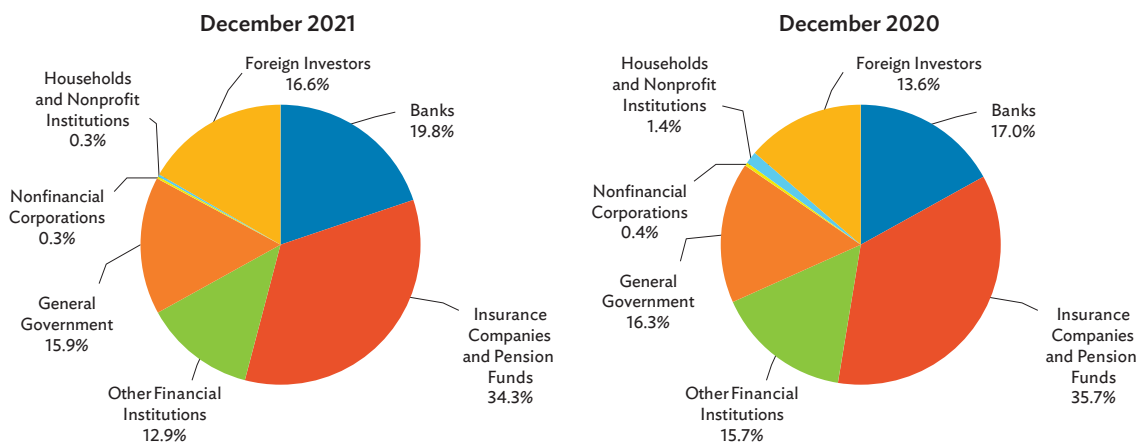
| Corporate Issuers | Coupon Rate (%) | Issued Amount (KRW billion) | Corporate Issuers | Coupon Rate (%) | Issued Amount (KRW billion) |
|--|-----------------|-----------------------------|---|-----------------|-----------------------------|
| Industrial Bank of Korea^a | | | Korea Electric Power^a | | |
| 6-month bond | - | 570 | 2-year bond | 2.73 | 200 |
| 6-month bond | - | 340 | 3-year bond | 2.50 | 270 |
| 9-month bond | - | 400 | 3-year bond | 2.89 | 210 |
| 1-year bond | - | 330 | 3-year bond | 2.89 | 200 |
| 1-year bond | 1.53 | 310 | 5-year bond | 3.03 | 300 |
| 1-year bond | 1.72 | 300 | 5-year bond | 2.69 | 280 |
| 10-year bond | 3.41 | 400 | 5-year bond | 2.53 | 200 |
| Export-Import Bank of Korea^a | | | 7-year bond | 2.83 | 200 |
| 6-month bond | - | 440 | 7-year bond | 2.75 | 200 |
| 6-month bond | - | 300 | NongHyup Life Insurance | | |
| 1-year bond | 1.71 | 420 | 10-year bond | 4.35 | 600 |
| 1-year bond | 1.44 | 360 | | | |
| 1-year bond | - | 300 | | | |
| 1.5-year bond | 2.12 | 330 | | | |
| 1.7-year bond | - | 310 | | | |

- = not available, 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



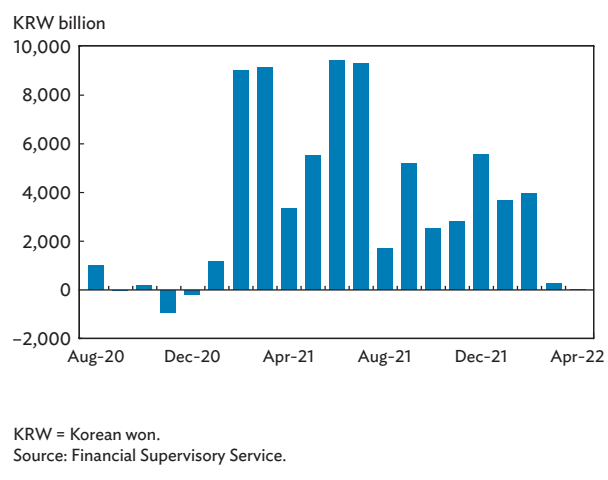
Source: AsianBondsOnline and The Bank of Korea.

Banks were the second-largest investor group with a share of 19.8% at the end of December, up from 17.0% in Q4 2020. Foreign investors surpassed both general government and other financial institutions as the third-largest group at the end of December. Foreign holdings rose to 16.6% in Q4 2021 from 13.6% in Q4 2020, as the domestic bond market registered high levels of foreign inflows in 2021.

Corporate bonds. Other financial institutions held the largest investor group share of the Republic of Korea’s LCY corporate bonds at the end of December with its share rising to 40.9% from 36.8% a year earlier (**Figure 3**). Meanwhile, the share of insurance companies and pension funds fell to 35.3% from 37.1%. The share of the general government was almost unchanged at 13.3% during the same period, while the share of foreign holders remained negligible.

Foreign fund flows. In January and February, the Republic of Korea’s LCY bond market posted net inflows of KRW3,673.0 billion and KRW3,950.0 billion, respectively (**Figure 4**). Foreign demand at the start of the year was driven by the relatively high interest rate differential of LCY bonds over US Treasuries and the stable Korean won. However, the rate hike by the Federal Reserve in March and expectations of faster-than-expected monetary policy normalization led to a sharper rise in US Treasury yields, narrowing the interest rate gap. The Korean won also depreciated versus the US dollar, reaching a low of KRW1,272.5 per

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

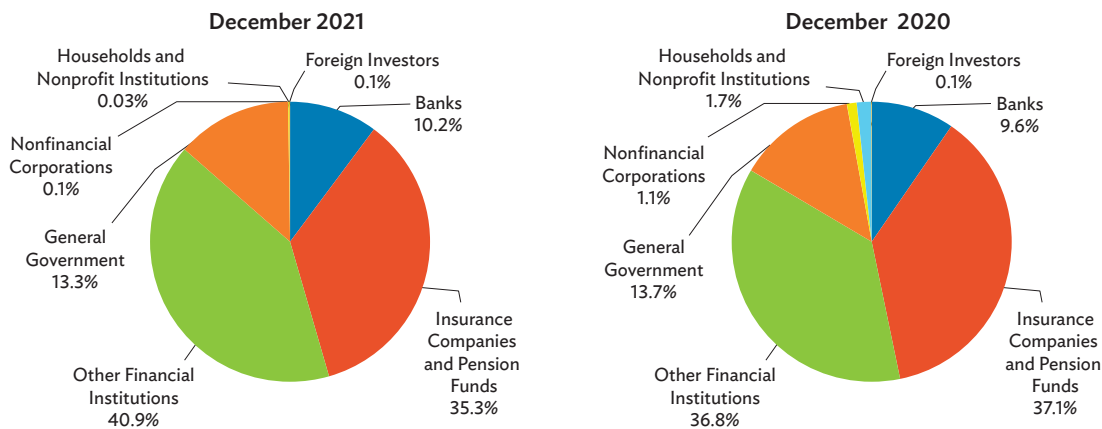


USD1.0 on 28 April. This resulted in a drop of foreign flows to KRW279.0 billion in March and further down to KRW36.0 billion in April. The foreign sell-off was most significant in bonds with remaining maturities of less than 1 year (**Figure 5**).

Ratings Update

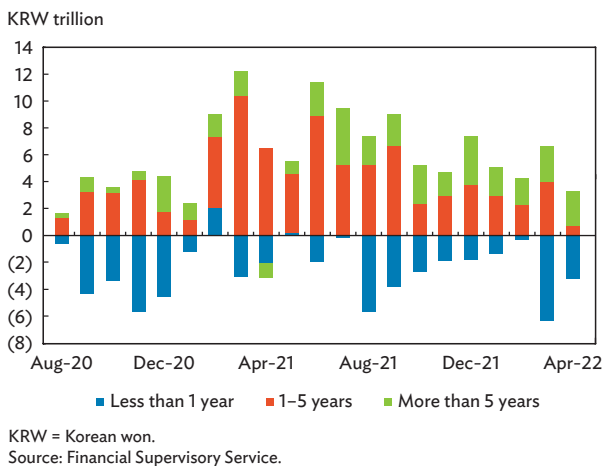
On 26 April, S&P Global Ratings affirmed the Republic of Korea’s sovereign credit ratings at AA with a stable outlook. The rating agency cited prudent policy decisions, solid fiscal conditions, and high monetary flexibility as the

Figure 3: Local Currency Corporate Bonds Investor Profile



Source: AsianBondsOnline and The Bank of Korea.

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



reasons behind the rating affirmation. The rating agency forecast 2022 gross domestic product (GDP) growth to be 2.5%, supported by exports and improved private spending. Downside risks to the growth outlook include continued high inflation from rising energy prices and high levels of household debt that may dampen consumption. Meanwhile, the fiscal deficit is expected to be 3.3% of GDP in 2022, with the government balance to return to surplus by 2024.

Policy, Institutional, and Regulatory Developments

The Republic of Korea’s National Assembly Passes the Second Supplementary Budget

On 29 May, the National Assembly passed the second supplementary budget of KRW62.0 trillion, which is to be largely allocated for programs involved in improving people’s livelihoods. These include, among others, programs to compensate small business owners hit hard by the pandemic (KRW28.7 trillion) and policies intended to ensure proper pandemic control and the gradual transition to the general health-care system (KRW7.1 trillion). The government also announced that financing for the proposed supplementary budget would not entail the issuance of government bonds. The resulting 2022 budget is expected to generate a consolidated fiscal deficit equivalent to 3.3% of GDP and a government-debt-to-GDP ratio of 49.7%.