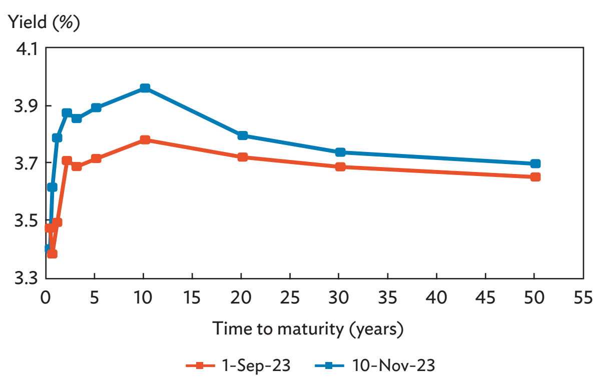
Republic of Korea

Yield Movements

Local currency (LCY) government bond yields in the Republic of Korea rose for most tenors between 1 September and 10 November on expectations of a prolonged tight monetary stance from the United States Federal Reserve (Figure 1). The Bank of Korea (BOK) at its 19 October monetary policy meeting kept the base rate at 3.50% amid higher inflation and growth uncertainties due to the Federal Reserve's signal of an extended period of elevated rates, rising household debt in the domestic market, and recent geopolitical tensions. These factors pushed up the yields during the review period. Market expectations of the BOK's continued restrictive monetary policy for the rest of the year also pushed up yields. The BOK stated that although inflation is expected to slow, it may remain above 3.0% for the remainder of the year, which is still higher than the 2.0% target.

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

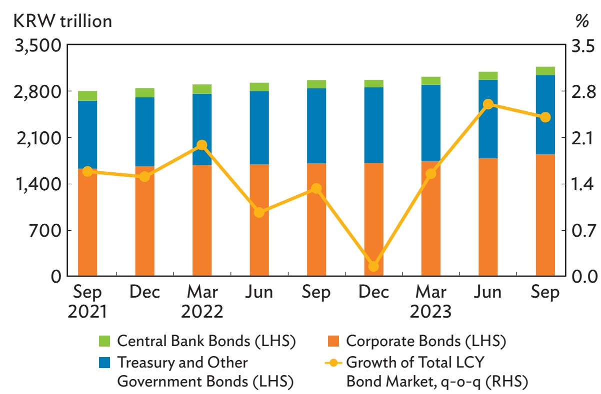


Source: Based on data from Bloomberg LP.

Local Currency Bond Market Size and Issuance

LCY bonds outstanding in the Republic of Korea rose 2.4% quarter-on-quarter (q-o-q) to KRW3,166.8 trillion at the end of the third quarter (Q3) of 2023, driven by growth in both the government and corporate bond segments. Corporate bonds continued to comprise more than half of total bonds outstanding in Q3 2023 and posted growth of 3.3% q-o-q, while government bonds outstanding rose at a slower pace of 1.2% q-o-q in Q3 2023 (**Figure 2**). Overall growth in Q3 2023 moderated from 2.6% q-o-q in the previous quarter due to a decline in quarterly issuances across all types of bonds.

Figure 2: Composition of Local Currency Bonds Outstanding in the Republic of Korea

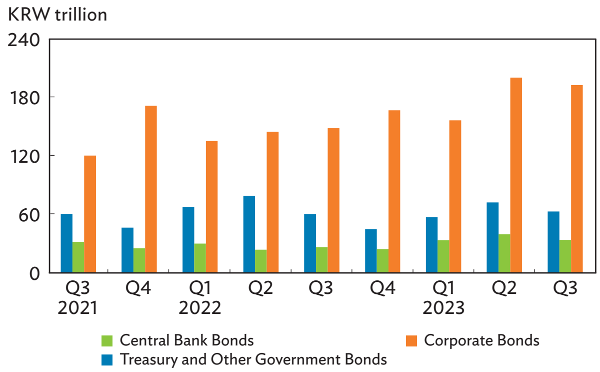


KRW = Korean won, LCY = local currency, LHS = left-hand side, q-o-q = quarter-on-quarter, RHS = right-hand side.

Sources: Bank of Korea and KG Zeroin Corp.

Total LCY bond issuance fell 7.2% q-o-q to KRW290.2 trillion in Q3 2023 as issuance declined for all bond segments. Government bonds issuance in Q3 2023 declined 12.9% q-o-q from a relatively high base in the second quarter of 2023 as the government had pursued a frontloading policy of releasing 65% of the 2023 budget in the first half of the year (**Figure 3**). Issuance of corporate bonds also fell, but at a slower pace of 3.8% q-o-q, due to higher borrowing costs amid a prolonged high-interest-rate environment. Corporate bond issuance in Q3 2023 continued to be dominated by banks and financial institutions.

Figure 3: Composition of Local Currency Bond Issuance in the Republic of Korea



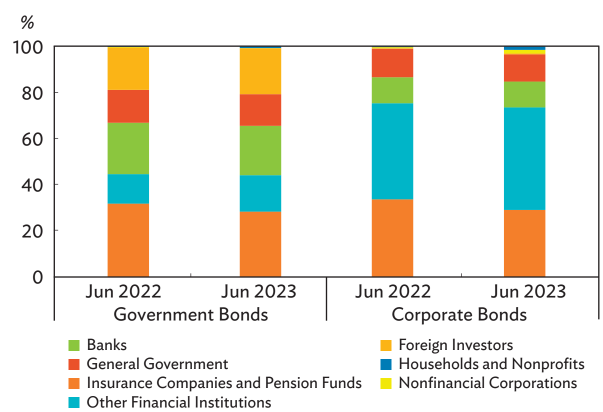
KRW = Korean won, Q1 = first quarter, Q2 = second quarter, Q3 = third quarter, Q4 = fourth quarter.

Sources: Bank of Korea and KG Zeroin Corp.

Investor Profile

Insurance companies and pension funds remained the largest investor group in the Republic of Korea's LCY bond market at the end of June 2023. They held a collective 28.4% share of the LCY bond market, but this was lower than their 32.3% share from a year ago. Insurance companies and pension funds accounted for more than 25% of all holdings in both the government and corporate bond markets (**Figure 4**). However, other financial institutions collectively had the largest holdings share in the corporate bond market at the end of June with 44.6% of the total. Foreign holdings in the LCY corporate bond market remained negligible in the second quarter of 2023, but foreign holdings in the LCY government bond market increased to 20.0% at the end of June from 18.4% a year earlier. Foreign holdings of LCY government bonds may have declined in Q3 2023 as bonds registered smaller net foreign inflows in July and reversed to net outflows in August and September. Foreign investors sold domestic bonds in recent months due to the weakening of the Korean won and the widening interest rate differential with US Treasuries, whose yields rose at a more rapid pace, making returns on Korean yields less attractive.

Figure 4: Local Currency Bonds Outstanding Investor Profile



Sources: *AsianBondsOnline* and Bank of Korea.