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Emerging Markets
Asia

Korea Macro View

Weak Recovery Increases Likelihood of Further Monetary Easing

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- **Sharp decline of Aug IP hints recovery pace in 3Q14 remains sluggish** — The decline of industrial production in Aug was sharper than expected and that seems to bring 3Q14 IP growth to at a negative territory on QoQ terms even if Sep IP is expected to rebound meaningfully. The upward trending inventory to shipment ratio also bodes ill for production activities in the coming months.

- **Two main risks: slowing down of China/euro area and weakening JPY** — Exports in Sep showed a brisk rebound of 6.8%YoY from -0.2% a month ago. However, our recent downgrade of China (-0.2%p) and euro area (-0.3%p) growth is expected to lower exports growth by c2%p in the coming 12 months. Given high export similarity, further JPY weakness is also a downside risk to exports and profits in the manufacturing sector. As the JPY weakens against the KRW by 10%, exports are expected to decline by 1.8%p while a 10% increase of USDJPY is likely to shrink manufacturing's sales and profitability by 1.45% and 0.21%ppts.

- **We cut 2014E and 2015E growth to 3.6% and 3.8%, respectively** — Given the weaker-than-expected recovery pace amid subdued economic sentiment and aforementioned headwinds to exports, we revise down 2014 and 2015 growth forecasts by 0.3%p and 0.2%p to 3.6% and 3.8%. Particularly, real GDP growth is likely to fall further to 3.3%YoY in 3Q14 from 3.5% in 2Q14 and expected to stay at below 4% on YoY terms until 2Q15 as facilities investment and exports remain weaker. Meanwhile, job growth in 2015 is likely to slow to 350K on a YoY basis and the jobless rate is expected to fall to 3.3% in 2015 from 3.5% in 2014. With three consecutive years of economic growth below 3.7%, in our view, potential growth in 2014-15 declined to 3.5~3.6%, leading to the negative output gap dissipating in 2Q15.

- **Subdued inflation but gradual pick-up expected** — As we witnessed in Sep, weak crude oil prices and favorable weather seem to lead deflationary pressures to remain for a while, weighing on inflationary pressures from other industrial goods and services. Reflecting that, we cut annual inflation in 2014 and 2015 to 1.4% and 2.2%, -0.2%p and -0.4%p from the previous forecast, respectively. Headline inflation is likely to stay below 2% to the end-1H15 but rise faster to low-3% in 4Q15 on the back of positive output gap and low base in 2H14.

- **Policy rate cut in Oct and the first rate hike in 2015 could be delayed** — On top of the government pressures, continuing low inflation at low-1% and weaker than expected recovery in 3Q14 is likely to lead the BoK to cut the rate at Oct MPC meeting. We do not think another rate cut could happen in the near term on the back of the expected slow but steady economic recovery and sentiment. We expect a rate hike in 4Q15 by 25bps but do not rule out extra rate cuts in 2015 in case recovery slows or JPY weakens faster than our expectation.

See Appendix A-1 for Analyst Certification, Important Disclosures and non-US research analyst disclosures.

Weak Recovery, Another Rate Cut in Oct

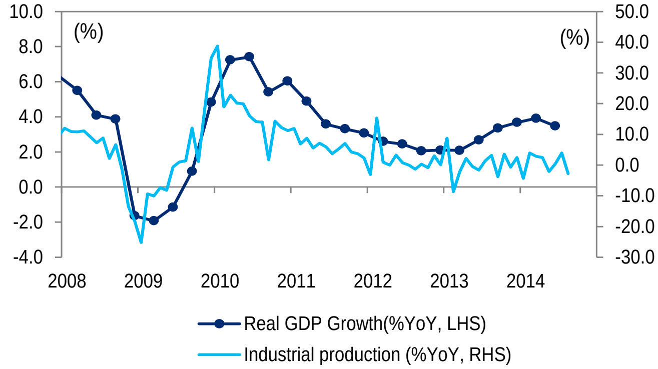
The sharp contraction of Aug IP hints the recovery of the economy remains weaker than expected despite taking into account temporary factors such as holidays. The government's fiscal stimulus and the BoK rate cut in Aug seem not to trigger meaningful recovery of the economy yet. Furthermore, sluggish Chinese and European economy and expected further weakening of JPY casts a dim outlook on the Korean economy. Reflecting these, we downgrade 2014 and 2015 growth forecast by 0.3%p and 0.2%p to 3.6% and 3.8%, respectively. Considering weaker-than-expected growth and continued government's pressure to the BoK to coordinate policy, we changed our call for the policy rate from no change to additional 25 bps cut in Oct in this year. We expect the BoK to hold its policy rate until the first rate hike in 4Q15 by 25bps. However, we also do not rule out delay of the rate hike or additional rate cuts in 2015 if weakening of JPY is faster than our expectation and economic recovery is not satisfactory.

Delayed recovery of production and sentiment

The decline of industrial production in Aug was sharper than expected even if we account for the shifts of summary holidays of main industries to end of Aug from early Sep a year ago. Sep IP is expected to rebound meaningfully but the disappointing Aug reading is likely to bring 3Q14 IP growth to at a negative territory on QoQ terms following -0.9% in 2Q14 albeit the YoY growth could inch up on the back of base effect. Furthermore, the downward sloping utilization ratio, which fell to the record low level since May 2009, and upward trending inventory to shipment ratio in the Figure 2 bodes ill for production activities in the coming months.

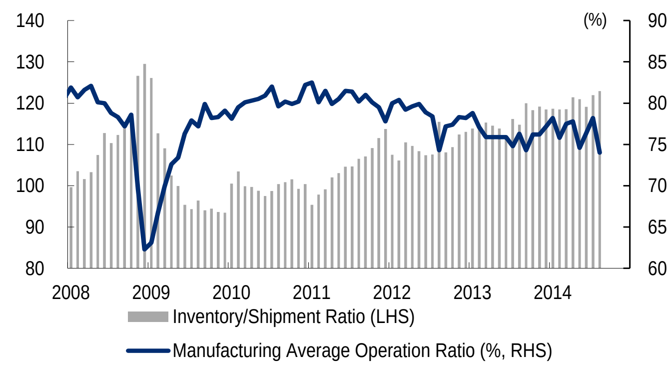
To bolster economic sentiments and recovery, the government prepared stimulus measures from Jul and implemented KRW40.7trn of packages. The BoK also cut the policy rate, called base rate applied on 7-day RPs, as policy coordination with the government in Aug. Despite these accommodative measures, the recovery pace turns out to remain weak without meaningful improvement of economic sentiments. The subdued economic sentiments, particularly consumer sentiments seem to weigh on the recovery of domestic demand. The only part of the economy which responses as the policy intended is the property market. On the back of easing regulations of DTI and LTV in Jul and low interest rate, housing transactions in Jul-Aug increased by 77.3%YoY and nationwide housing price rose by 0.3%QoQ and 1.8%YoY. However, we note that Cheonse (Korean rent) price continue to stay on an up-trend and YoY increase outpace the housing price. The reconstruction of apartments and households' weak conviction on sustainable recovery of the property market seem to support demand for Cheonse.

Figure 1. Industrial production and Real GDP growth



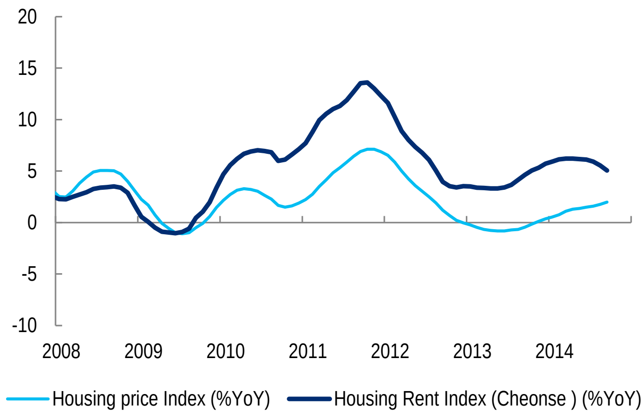
Source BoK, Statistics Korea, CEIC, Citi Research

Figure 2. Inventory/shipment ratio and manufacturing operation ratio



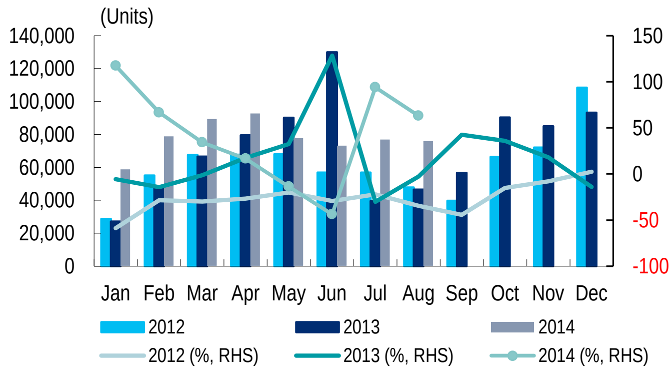
Source: Statistics Korea, CEIC, Citi Research

Figure 3. Housing price and rent (Cheonse) price index



Source: Kookmin Bank, Citi Research

Figure 4. Housing Transactions



Source: MoLIT, Citi Research

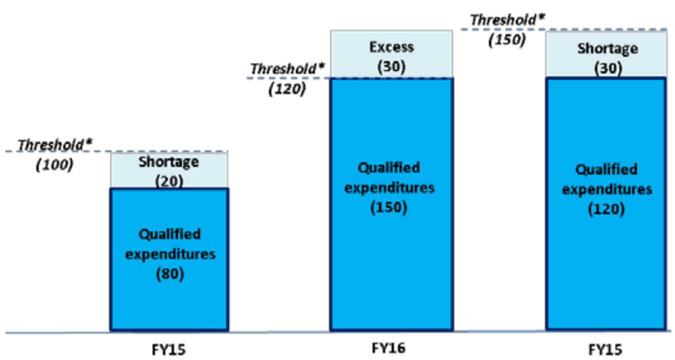
In Jul-Aug, the service activities and retail sales growth bottomed out from the aftermath of the ferry sinking incident in Apr which resulted in flat growth of the former and -0.5%QoQ sa for the latter. We expect them to improve further but the recovery pace is likely to slow on the back of the subdued sentiments and lukewarm nominal wage growth as well. During the first eight months of this year, nominal wage had just increased by 2.4%, 1.5%p lower than that of 2013. Furthermore, the resilient job growth (YTD 2014: 585K YoY) was mostly from the service sectors (75% of total job growth) where the average nominal wage is 10% lower than manufacturing. In particular, we note that nominal wages in the accommodation & food service and human health and social work activity sectors, which contributed 59% of overall service industry job growth, had continued to decline in this year. Furthermore, unlike the high expectation that the government's plan to tax on excessive cash reserves of corporate could increase dividend income or wage, in our view, the policy impacts are not likely to be materialized in the near term since. The corporates can delay the increase of wage or dividend payout by passing over the tax burden to 2016 as Figure 5 and 6 illustrate.

Figure 5. The Government Plan to Tax on excessive corporate cash reserves

■ businesses must spend a certain amount on investments, wage increases and dividend payments, or be subject to a tax (10%) on excessive corporate reserve
■ Applicable to businesses with an excess of 50 billion won in equity capital and large conglomerates subject to restrictions on cross-shareholdings
■ Businesses will be able to choose between either A or B methods for this tax and must adhere to these methods for 3 years
A: [income x base rate α(60-80%) - (investment + employee wage increase + dividends, and etc.*)] x 10% tax rate
B: [income x base rate β(20-40%) - (employee wage increase + dividends, and etc.*)] x 10% tax rate

Source: MoSF, Citi Research

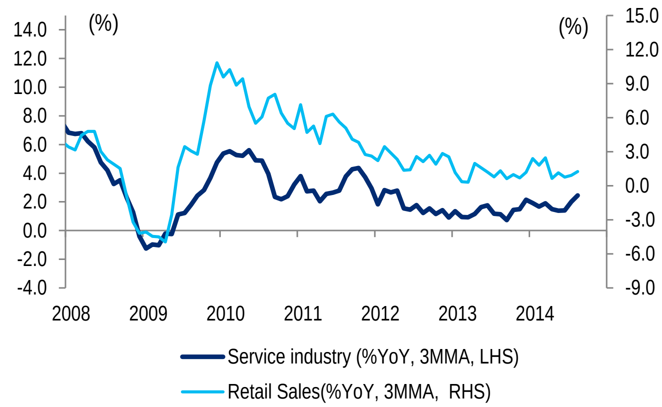
Figure 6. Shortage in FY15 can be offset against the excess in FY16 : No tax due when filling FY16 CIT return



Note: (*) Threshold is set by the two types of base tax rate (α &β) and net income of a corporate. Shortage means the qualified spending is less than the threshold.
 1) Shortage in FY15 can be offset against the excess in FY16: No tax due when filing FY16 CIT return. 2) Remaining net excess of 10 (=30-20) in FY16 can be carried over: Not tax due when filing FY17. 3) Net shortage for FY17 is 20=(30-10) and it carries over to FY18: Tax due for FY17 will depend on the shortage/excess of FY18 when filing FY18 CIT return

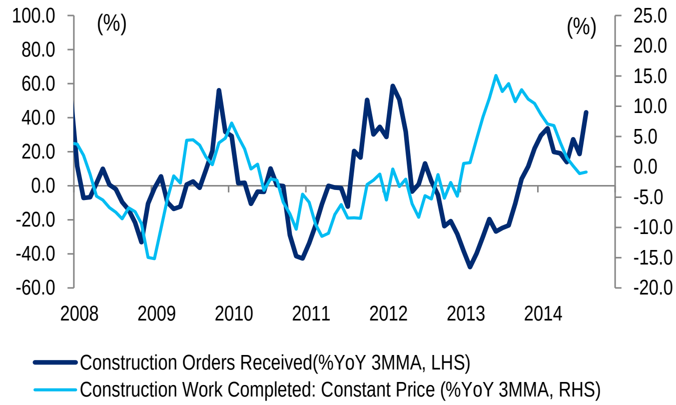
Source: MoSF, Citi Research

Figure 7. Service industry and Retail sales



Source: BoK, Statistics Korea, CEIC, Citi Research

Figure 8. Construction order and Construction completed

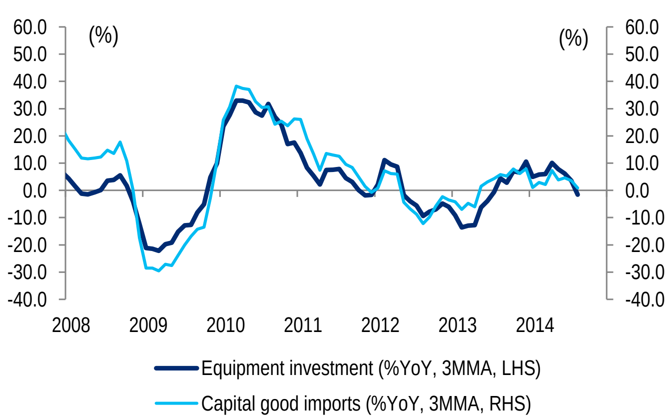


Source: BoK, Statistics Korea, CEIC, Citi Research

Investments also remained weak

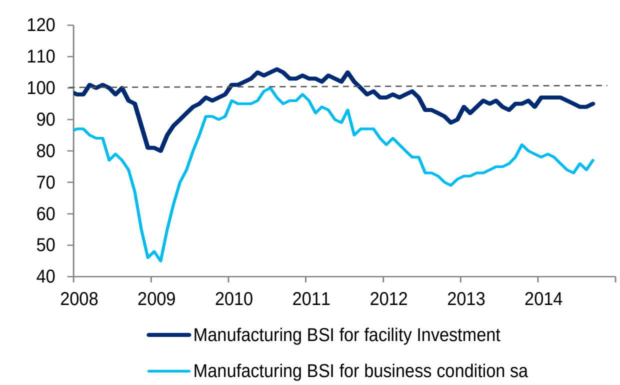
The readings on equipment investments and construction completed also lagged behind of our forecasted path. The former plunged by -10.6%MoM sa and -9.8%YoY in Aug. In Sep, equipment investment is expected to rebound from the previous month's sharp retreat on the back of a resilient recovery of capital goods import and machinery order received in Sep. However, manufacturing BSI for future facility investment in Sep had remained flat at 95, below the benchmark 100, over the last three months, suggesting sentiment for the investment still remains sluggish. Furthermore, the high base in 4Q14 (10.9%YoY) will be another factor to lower the YoY growth in 4Q14 even if the growth momentum of facilities investment restores. The sluggishness of construction investment has been mostly due to civil engineering since residential construction growth had remained robust in 2Q14 and Jul-Aug. The construction order received, a leading indicator, in Sep also declined sharply as that of civil engineering fell by 30.6%YoY. However, we have a bit brighter prospects for construction investment than facilities investment on the back of the government's extra spending on SOC and social safety in 2015 that could support activities in civil engineering sectors.

Figure 9. Equipment investment and capital goods imports



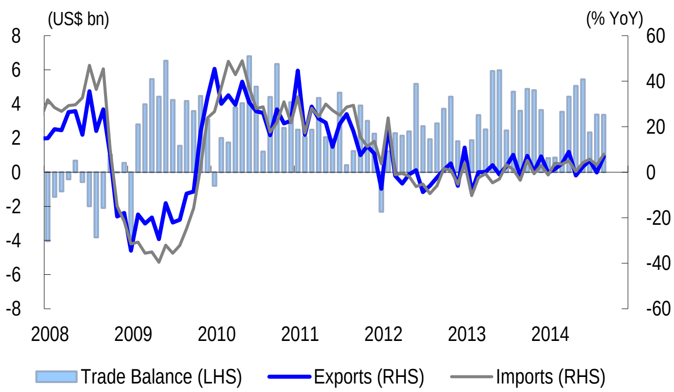
Source: BoK, Statistics Korea, CEIC, Citi Research

Figure 10. Manufacturing BSI for facility investment and business condition



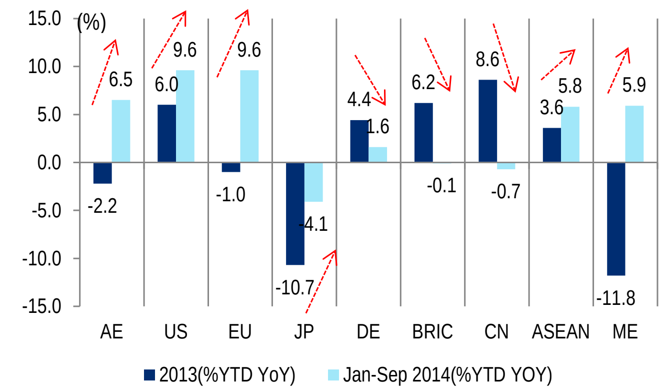
Source: BoK, Statistics Korea, CEIC, Citi Research

Figure 11. Exports, Imports, and Trade balance



Source: KITA, Statistics Korea, CEIC, Citi Research

Figure 12. Exports by destination

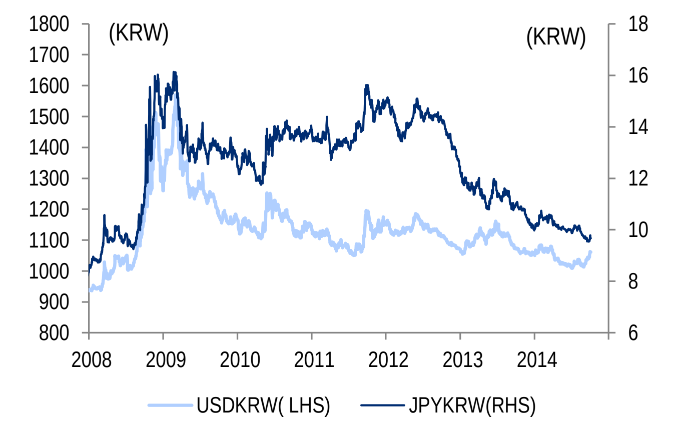


Source: KITA, Statistics Korea, CEIC, Citi Research

Two major hurdles for recovery of exports

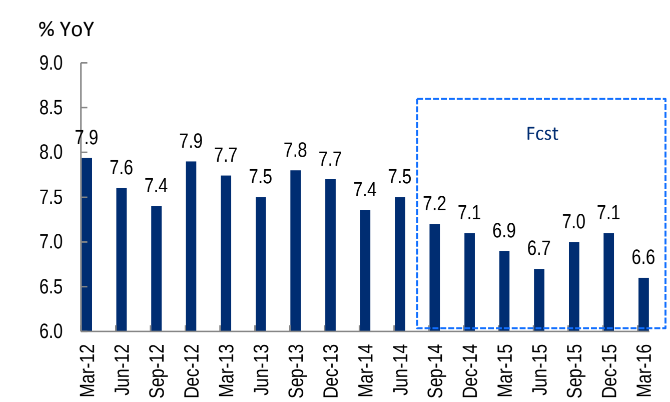
Exports in Sep showed a brisk rebound of 6.8%YoY from -0.2% a month ago on the back of upswing in exports to the US and ending of the four straight months of YoY contraction of exports to China. We expect exports going forward (3Q14: 3.9%YoY. 4Q14: 6.2%YoY, 2015: 7.6%) to expand faster than 1H14 (2.5%YoY) as exports to the US likely remain strong and exports of major products such as semi-conductor and auto also expected to continue to increase. However, exports recovery is likely to be weighed by two major factors: 1) slowing down of major trade partners, particularly China and Euro area, and 2) further weakening of the JPY against the KRW. Recently we downgraded growth forecasts for China by 0.2%p for 2014 and 2015 to 6.9% and 6.8% respectively. For the euro area, we had cut the growth rate by 0.3%p for both 2014 and 2015 during last two months to 0.8% and 1.4%, respectively. As of Sep 2014, the share of exports to China is 25% and that to the euro area is 9.5%. We expect the slowdown of two economies is likely to lower export growth by around 2%ppt. Meanwhile, Korean exports have become less vulnerable to appreciation of KRW since oversea production of main export goods has expanded and the proportion of capital goods (incl. intermediate goods) exports has increased while that of final consumer goods has fallen.

Figure 13. USDKRW and JPYKRW



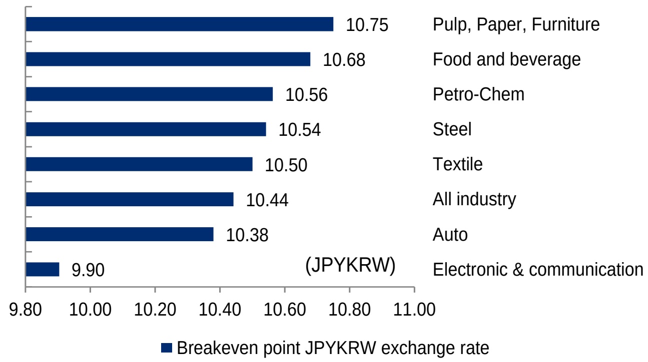
Source: Bloomberg, Citi Research

Figure 14. Chinese Real GDP growth rate (%YoY)



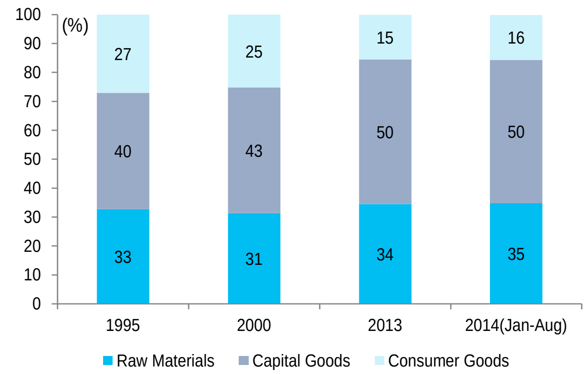
Source: CEIC, Citi Research

Figure 15. Major industry's breakeven point JPYKRW exchange rate



Note : Survey from 146 companies in Sep 2014, the largest by the amount of sales
Source: Federation of Korean Industries, The Korea Economic Daily, Citi Research

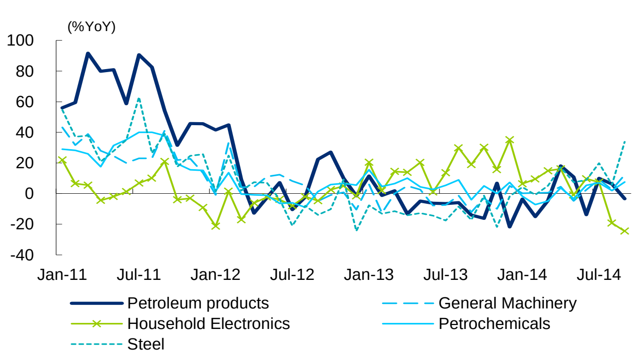
Figure 16. Export composition by goods characteristics



Source: KITA, Citi Research

However, further strengthening of the KRW against the JPY appears to be another hurdle for exports going forward, given the high similarity with Japanese export goods. According to our research, the export similarity of Korea with Japan as of 2012 was 67.2%, the second highest after Germany, 82.2%, among the 16 countries studied – see Downside Risk Materializing: Further JPY Weakness. Particularly, petroleum products, autos, machineries, metal (incl. steel), and electronic products are known to have the high similarity and have remained sluggish since JPY started to weaken against KRW in early 2011. A recent survey from the Federation of Korea Industry reported that the average level of break-even JPYKRW was 10.44, which is far above current 9.8. We think that level is somewhat exaggerated but reflects industries' worries over JPY weakness. Further weakening of the JPY is going to increase the likelihood of meaningful negative impacts to exports as we can see in the following studies. A study at the Korea Institute for Industrial Economics & Trade showed that Korea exports will decrease by 1.8%ppts when JPY weakens 10% against KRW. Research from the Institute for International Trade reported that 10% depreciation of the JPY against the USD will cut sales of manufacturing by 1.45% and profits by 0.21%p. In particular, those losses of large corporations are bigger than SMEs because of their larger shares in total exports. The petro-chemical sector is expected to experience the largest sales' loss on the back of larger proportion of exports, esp. to Japan, while the largest profit loss will occur in steel and metal sector due to unit price declines as price competition intensifies.

Figure 17. Exports growth by major product



Source: KITA, MoTIE, CEIC, Citi Research

Figure 18. Impact of 10% increase in USDJPY to Korean Manufacturing

Manufacturing		
By size of firms	Sales Growth (%)	Profits (%p)
Large Corp	-1.66	-0.26
SMEs	-0.91	-0.14
By sectors		
All manufacturing	-1.45	-0.21
Textile, Cloth, Leather	-0.99	-0.16
Petro Chemical	-1.76	-0.05
Steel & Metal	-0.79	-0.70
electronics	-1.57	-0.28
Industrial Machinery	-1.50	-0.36
Auto	-1.58	-0.14

Note: Profits are the ratio of operating profit to sales
Source: Institute of International Trade, BoK, Citi Research

Figure 19. Revised 2014-2015 Economic Forecasts

	2011	2012	2013	2014							2015		
	Annual	Annual	Annual	1Q	2Q	1H	3QF	4QF	2HF	Annual F	1HF	2HF	Annual F
GDP (%YoY)	3.7	2.3	3.0	3.9	3.5	3.7	3.3	3.6	3.5	3.6	3.8	3.9	3.8
(%QoQ s.a.)				*0.9*	*0.5*		*0.9*	*1.2*					
Private Consumption	2.9	1.9	2.0	2.5	1.5	2.0	1.7	2.3	2.0	2.0	3.4	3.4	3.4
Government Consumption	2.2	3.4	2.7	2.9	1.7	2.3	3.0	4.1	3.5	2.9	5.1	3.1	4.1
Fixed Capital Formation	0.8	-0.5	4.2	5.9	3.4	4.5	3.1	4.8	4.0	4.2	0.8	5.6	5.0
Construction	-3.4	-3.9	6.7	4.3	0.2	1.9	0.3	6.5	3.5	2.8	4.4	5.6	3.3
Facilities Investment	4.7	0.1	-1.5	7.3	7.7	7.5	4.6	-0.7	1.8	4.6	2.9	3.7	4.7
Intellectual Property Products	6.9	8.6	7.3	7.3	5.7	6.5	8.6	9.4	9.0	7.8	3.0	6.4	9.2
Exports of Goods & Services	15.1	5.1	4.3	4.5	3.7	4.1	5.6	5.7	5.6	4.9	5.6	8.1	6.9
Imports of Goods & Services	14.3	2.4	1.6	3.5	2.7	3.1	4.9	5.2	5.1	4.1	4.9	8.3	6.6
CPI	4.0	2.2	1.3	1.1	1.6	1.4	1.4	1.4	1.4	1.4	1.6	2.8	2.2
Core CPI	3.2	1.7	1.6	1.9	2.2	2.1	2.2	1.7	1.9	2.0	2.0	2.7	2.4
Unemployment Rate (% s.a.)	3.4	3.2	3.1	3.5	3.7	3.6	3.4	3.3	3.4	3.5	3.4	3.3	3.3

Source: BoK, Statistics Korea, CEIC, Citi Research

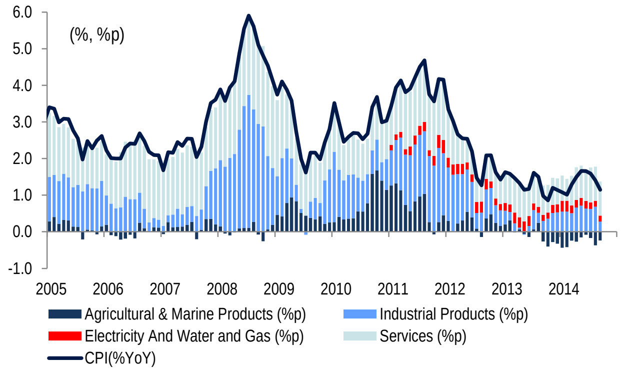
Economic growth unlikely exceeds 4% in 2015

Given the recovery pace weaker than expected amidst subdued economic sentiment and aforementioned headwinds to exports, **we revise down 2014 and 2015 growth forecasts by 0.3%p and 0.2%p to 3.6% and 3.8%. Particularly, real GDP growth in is likely to fall further to 3.3%YoY 3Q14 from 3.5% in 2Q14** and expected to stay below 4% on YoY term until 2Q15 even if we assume c1% of QoQ growth as facilities investment and exports remain weaker than previously expected. Meanwhile, we leave the forecast for private consumption expenditure unchanged since the accommodative fiscal and monetary measures is likely to offset the drags due to the delay of economic sentiments and impacts of reduced growth momentum from export industries. Meanwhile, job growth in 2015 is likely to slow to 350K on YoY basis on the back of the based effect of a hefty increase of over 500K YoY in 2014. As the government continues to pursue efforts to increase the employment ratio of females and the over 60s, the unemployment rate is expected to fall to 3.3% in 2015 from 3.5% in 2014. With this revised growth path, the negative output gap is expected to narrow slowly until 1Q15, and then the output gap is likely to shift to the positive territory in 2Q15. **Downward revision to our 2015 growth forecast does not change the time the output gap turns from negative to positive since the recent three-year period of anemic economic growth below 3.7% is likely to have edged down the potential growth rate to around 3.5~3.6%.**

Inflation to remain below 2% for a while

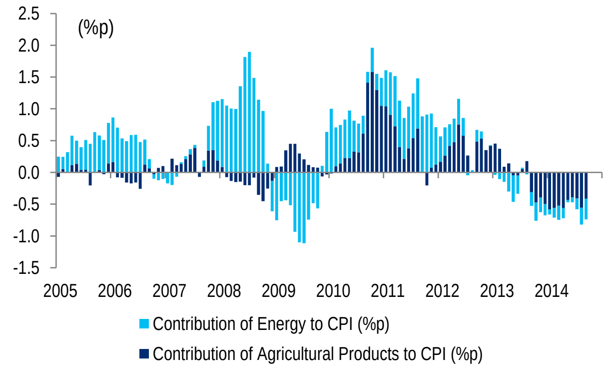
Headline inflation in Sep shifted to decline on a MoM basis by -0.1% and fell sharply by 0.3%p to 1.1% on the back of deflationary pressures from oils and agricultural goods. Oils price decline contributed -0.1%p and -0.3%p to MoM and YoY headline inflation respectively. Meanwhile, MoM inflation of agricultural goods slowed to 1.8% from 3.9% in Aug and YoY deflation continued by posting -9.8% (contributing -0.4%p to headline inflation). Seasonality also factored in the sharp decline of headline inflation due to the reduced travel fees after the Chuseok holidays.

Figure 20. Inflation and component's contribution



Source: BoK, Statistics Korea, CEIC, Citi Research

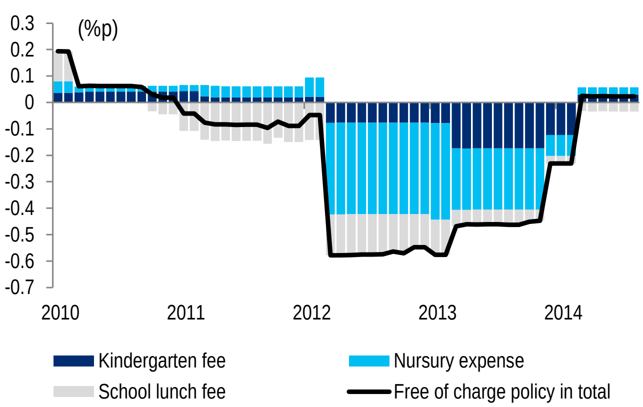
Figure 21. Agricultural products and Energy's contribution to CPI



Source: Statistics Korea, CEIC, Citi Research

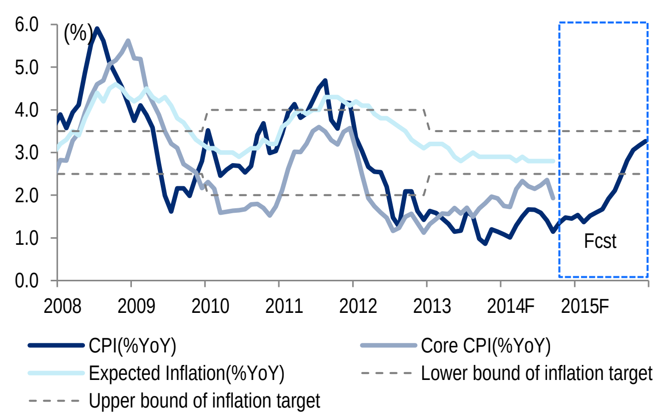
Considering recent weakness of crude oil prices and favorable weather, the deflationary pressures from the supply side is likely to continue to weigh on inflationary pressures from other goods, such as processed foods and other services. However, headline inflation in 4Q14 is likely to post 1.4%YoY as MoM inflation remains flat, given the low base a year ago (4Q13: 1.1%YoY). With this, **we expect annual inflation in 2014 to register 1.4%, 0.2%ppts lower than the previous forecast. The supply-side deflationary pressures to continue for a while and downward revision of economic growth in 2015 also led us to cut 2015 inflation to 2.2% from 2.6%.** Particularly, headline inflation is likely to remain below 2% to the end of 1H15 and rises faster to low-3% in 4Q15 on the back of the positive output gap albeit not large, and a low base in 2H14. We still expect the government to pursue public service tariff hikes in 2015 to consolidate the balance sheets of the government-owned enterprises and local government. Even if it is a one-off shock, tobacco price hike early next year is also another factor to level-up YoY headline inflation. If the government raise the price by KRW2,000 per a pack, headline inflation is going to rise by 0.6%p. In our view, the increase is likely to be limited to KRW1,500 during the discussions at the National Assembly and that will raise headline inflation by 0.5%p. The government plans to continue to increase welfare policies in 2015 which could bring deflationary pressures as we saw in 2012-13 (Figure 22) but, in our view, the deflation pressure is not likely to remain high on the back of base effects.

Figure 22. The contributions of government policy to CPI inflation



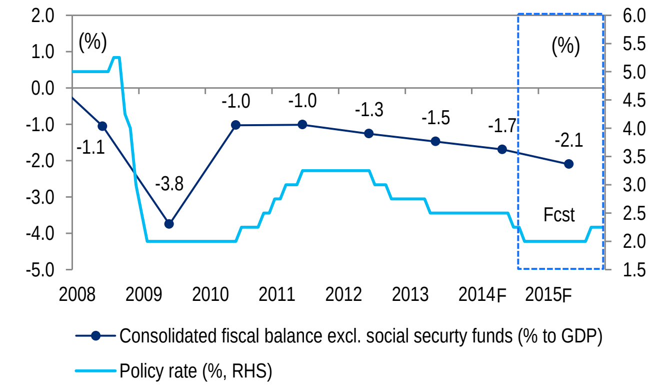
Source: BoK, Statistics Korea, CEIC, Citi Research

Figure 23. CPI inflation, Core CPI inflation, Expectation, and Target



Source: Source: BoK, Statistics Korea, CEIC, Citi Research

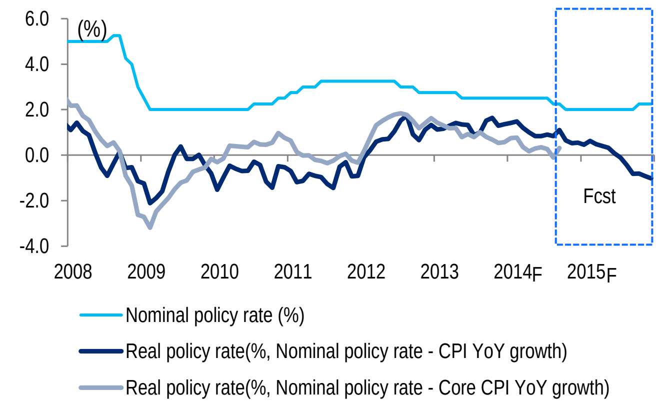
Figure 24. Fiscal balance and BoK's policy rate



Note : 2014's fiscal balance is MoSF's estimate

Source: MoSF, BoK, Statistics Korea, CEIC, Citi Research

Figure 25. Real policy rate



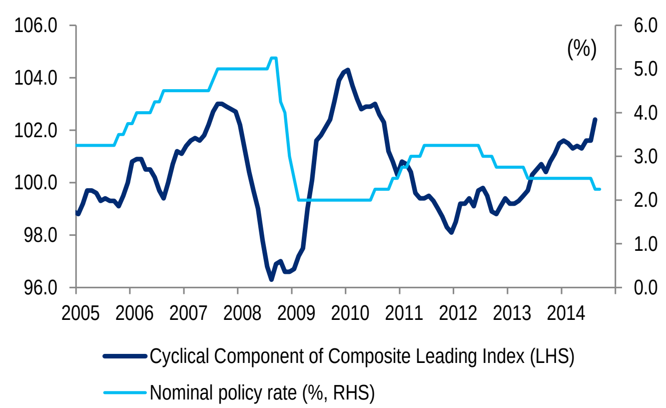
Source: BoK, Statistics Korea, CEIC, Citi Research

The BoK to cut the rate in Oct and hold in 2014

The BoK is likely to cut the policy rate in Oct by 25bps after pausing a month following the 25bps cut in Aug on the back of continued subdued inflation as well as weaker-than-expected recovery in 3Q14 – see [Sharp IP Decline in Aug; We Now Expect a BoK Rate Cut in Oct](). On top of that, the government pressure for the BoK to cut the rate alongside its fiscal stimulus is another main reason for the rate cut. As in Figure 24, the BoK has kept pace with the government along with economic situation. As the government plans to expand its spending, widening the fiscal deficit in 2015 by 2.1% of nominal GDP, the BoK is likely to pursue a more accommodative stance than now.

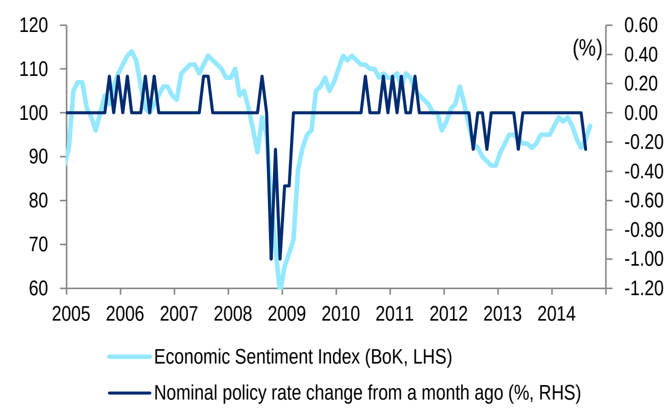
Further rate cut in the near term is not likely. Amidst weak recovery of economy and economic sentiments, as we can see in Figure 26 and 27, cyclical component of leading indicator and economic sentiment show sign of improving recently. Based on the BoK's previous response functions to cyclical components of leading indicators and economic sentiment, we believe the BoK has to hold the rate or prepare for rate hikes, not rate cuts.

Figure 26. Cyclical Component of Leading indicator and policy rate



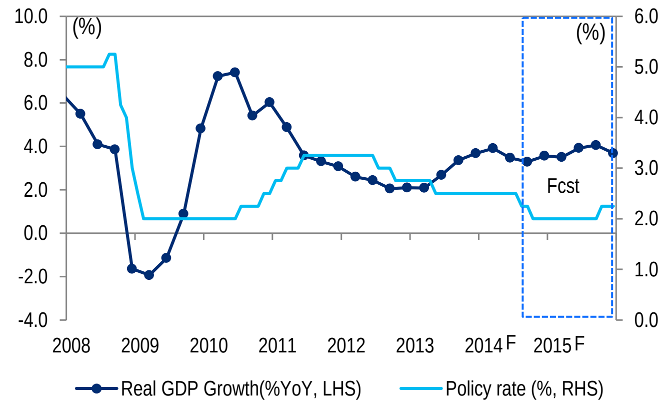
Source: BoK, Statistics Korea, CEIC, Citi Research

Figure 27. Economic Sentiment index and policy rate change



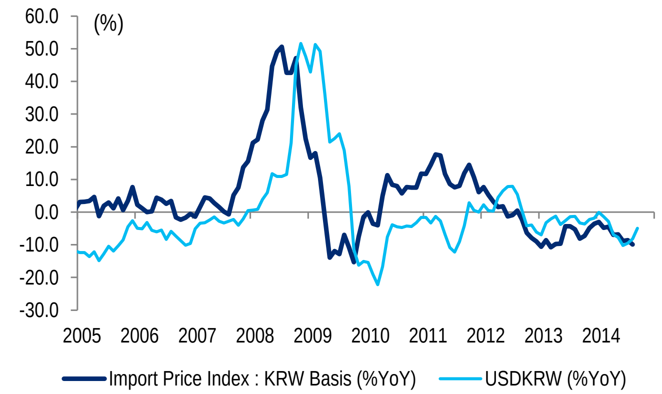
Source: BoK, Statistics Korea, CEIC, Citi Research

Figure 28. Real GDP growth(%YoY) and BoK's policy rate



Source: BoK, Statistics Korea, CEIC, Citi Research

Figure 29. Import price index in KRW and USDKRW exchange rate



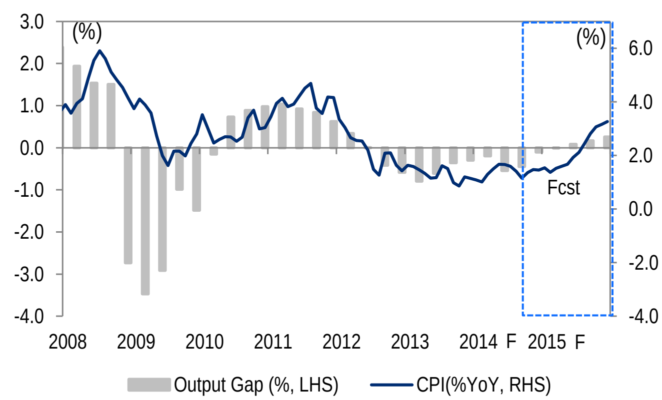
Source: BoK, Statistics Korea, CEIC, Citi Research

The policy rate cut in Oct will support the recovery of economy in the coming quarters by stimulating consumptions and investments, albeit gradually. In particular, the monetary easing is going to help recovery of domestic demand in 2H15 as the policy rate falls to negative in real terms. The BoK is expected to cut 2014-15 growth and inflation forecasts and announce on Oct 15. Some speculate that the rate cut may come in Nov as the BoK cut the rate in Aug after its downward growth revision in Jul. We do not rule out the possibility but current weaker-than-expected inflation and JPY increase the likelihood of rate cut in Oct.

Rate hike starts in 4Q15 but depends on JPY

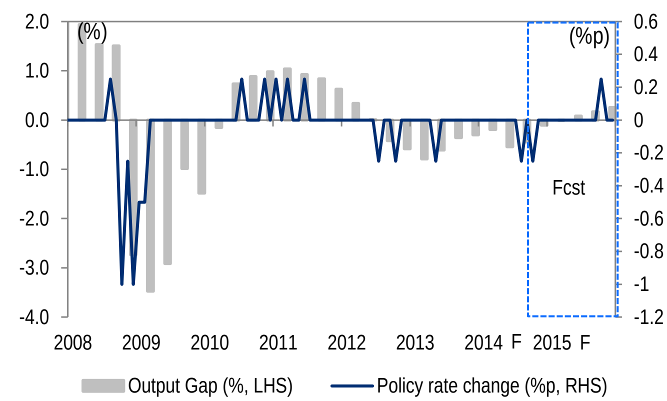
In 2015, we still believe the BoK will start a rate hike cycle. Before we revise down growth and inflation forecast for 2015, we thought the BoK would raise the rate twice each by 25bps in 3Q15 and 4Q15. **We now, however, expect the BoK to delay the rate hike in 4Q15, just once by 25bps, leading the policy rate to post 2.25% at the end of 2015.** Even if inflation remained subdued at below 2% until 1H15, it seems to rise faster in 2H15 on the back of the shift of output gap to positive and low base in 2H14.

Figure 30. Output gap and CPI headline inflation



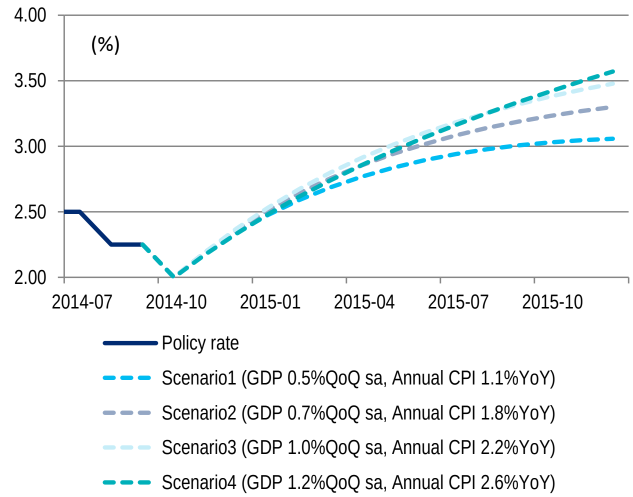
Source: BoK, Statistics Korea, CEIC, Citi Research

Figure 31. Output gap and BoK's policy rate change



Note : Output gap(%) = {(gdp – potential gdp)/potential gdp} * 100
Source: BoK, Statistics Korea, CEIC, Citi Research

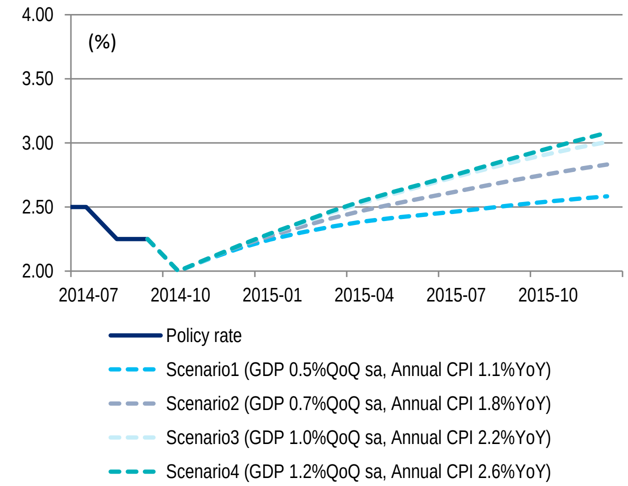
Figure 32. The Policy Rate Forecasted from Augmented Taylor Rule 1



Note: The x and y in scenario (x, y) refer average of QoQ sa real GDP growth and annual headline CPI inflation in 2015 respectively

Source: BoK, Citi Research

Figure 33. The Policy Rate Forecasted from Augmented Taylor Rule 2



Note: The x and y in scenario (x, y) refer average of QoQ sa real GDP growth and annual headline CPI inflation in 2015 respectively. Augmented Taylor Rule 2 used Federal fund rate as one of the independent variables.

Source: BoK, Citi Research

Based on our growth forecast in 2015, we projected appropriate policy rates using our Taylor rule equations and found that our policy rate path is at the very accommodative levels. Figure 32 and 33 illustrate the projected rate path to the end of 2015 after a 25bps cut in Oct. We conducted Taylor rule simulations by varying the growth (QoQ terms on average: from 0.5% to 1.2%) and inflation (Annual CPI YoY terms: from 1.1% to 2.6%) in 2015. In general, the Taylor rule projection with Federal funds rate provided lower forecast than the one without it and the all of simulation results show that appropriate policy rate level at end-2015 is higher than 2.25%. The Federal funds rate augmented Taylor rule predicts 2.58% at end of 2015 if average of QoQ growth rate is 0.5% and annual CPI inflation is 1.1% in 2015. Meanwhile, when those of **growth rate and inflation are 1.0% and 2.2% respectively, which is our baseline forecast, the policy rate by the Talyor rule at the end of 2015 is 3.0%.**

If the KRW strengthen against the JPY excessively and economic recovery is not satisfactory, however, we cannot rule out the delay of the rate hike or extra rate cuts in 2015. We recently adjusted our annual forecast of USDKRW from 1,017 to 1,029 and that could increase headline inflation by c0.1%p by lifting up import prices. The weakening of the KRW against the USD was also taking account of further weakening of the JPY against the USD; USDJPY in 2015: Sep 114 vs. Aug 108. Therefore, if JPY weakens faster than our forecast, the FX authorities are likely to be more concerned about the JPYKRW pair and intervene the market more actively to level up USDKRW. Given that they do not have other measures to deter JPY weakness other than market intervention, the BoK may consider further accommodative stance. Another possibility of that is the economic recovery pace below 1.0% of quarter-on-quarter growth in this quarter and next quarter. The Minister of Finance recently said the economy will gain growth momentum to continue 1%QoQ in the following quarters on the back of boosting measures implemented. If the recovery pace in 2015 is not enough to stratify the government forecast, the government is likely to put additional pressures for the BoK’s monetary easing. However, for now, our baseline forecast for the rate is 25bps cut in Oct and no rate change until 25bps hike in 4Q15.

Appendix A-1

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