

# New Year Speech

January 2, 2018

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Governor

The Bank of Korea

Dear fellow members of the Bank of Korea!

Today we start our first tasks of 2018, filled with new hope and resolve. I would like to begin by expressing my heartfelt gratitude to all of you, for so faithfully carrying out your duties throughout the last year even in the midst of difficult conditions.

Last year the trend of growth in our economy picked up gradually, even despite the worsening of our trade conditions vis-à-vis major countries and the increase in North Korea risks, as our exports and facilities investment showed buoyancy in line with the global economic recovery. This improvement can also be said to have owed in large part to the Bank of Korea's accommodative monetary policy to this time. With regard to consumer price inflation, the upward pressures on the demand side were not large last year, but under the influence of supply-side factors including the rising international oil prices, the annual rate of inflation was around our target level of 2%. Given the forecast that the economy would continue to grow at its potential rate going forward as well, and that inflation would approach the target level, conditions were also built up under which the degree of monetary policy accommodation could be adjusted. Judging that holding the Base Rate at the current level under these circumstances could lead to a further expansion in the real degree of accommodation which could entail an increased risk of financial imbalances accumulating, the Monetary Policy Board raised the Base Rate by 25 basis points last November.

The Bank of Korea, while devoting efforts to maintaining market stability whenever factors causing financial or foreign exchange market unrest arose, at the

same time also endeavored last year to expand its bilateral currency swap agreements with foreign central banks so as to strengthen the multi-layered global financial safety nets. The extensions of its currency swap agreements with the Reserve Bank of Australia and the Peoples' Bank of China, and the establishment of a new standing currency swap agreement with Canada, a vehicle currency country, can be considered particularly valuable achievements reaped directly by the Bank itself last year.

Dear members of the Bank of Korea!

This year the Korean economy appears likely to maintain its trend of solid growth, thanks for example to a continuation of the global economic recovery and to the government's expansion of its fiscal expenditures. However, a look at domestic and external conditions finds there to be a variety of potential risks in many places. If major country central banks, following the US Federal Reserve, reduce the degrees of their monetary policy accommodation due to the strengthening of their economic recoveries, then there is a possibility that a shrink in the volume of global liquidity could destabilize the international financial market and thereby constrain the global economy's recovery. There is also a chance of the growth in world trade slowing, due to worsening trade conditions in consequence of strengthened protectionism in major countries. The possibility also remains that, as North Korea risks surface occasionally, they can cause expanded financial market volatility and negatively affect economic sentiments.

On the top of this, the structural problems that are limiting our economy's vitality also continue to exist, among them our low birthrate and population aging, the deepening of our segmented labor market and of the income imbalances, the

buildup of household debt, and the delay in our development of next generation high-tech industries.

Under these circumstances, if we want our economy to take one more leap forward, while also sustaining the momentum of our current economic recovery, we have to continue our reform efforts to improve the make-up of our economy and expand its growth potential. And I think that the present time, when the trend of growth is recovering and fiscal policy is being operated expansively, is a suitable one for pushing ahead with reform. The government and private economic actors will have to cooperate on this, so as to avoid missing a golden opportunity.

Dear members of the Bank of Korea!

Let me talk now about the main tasks that the Bank of Korea will have focus on carrying out this year.

We will need to conduct our monetary policy so as to ensure that sustainable growth continues and consumer price inflation can be stabilized at the target level over a medium-term horizon. Given the forecast that the demand side inflationary pressures will not be high, even though the economy's solid trend of growth will continue this year as well, it will be desirable to maintain our accommodative monetary policy stance for the time being. At the same time, we should pay more attention to the possibility that the prolongation of this stance will cause a deepening of our financial imbalances, and the cumulative effects of these imbalances on growth and inflation over the medium- to long-term horizon. Keeping this in mind, we should judge carefully whether it is necessary to adjust its accommodative monetary policy

stance further, based upon close examination of future growth and price trends and conditions related to financial stability. In addition, inasmuch as the monetary policy operating conditions and transmission effects are now differing greatly from those in the past, we will have to deliberate more carefully and carry out research on measures that can enhance our monetary policy's effectiveness.

During this year we will have to again examine the operating conditions of our inflation targeting system, which will be newly set with effect from 2019. We will have to systematically analyze any changes in the inflation dynamics, such as the trends of inflation and the relationship between growth and prices, and carefully examine whether there might not be points needing improvement in relation to the inflation target level, the method of setting the target, our responsibility for policy explanation, etc.

As I have stressed on many occasions until now, in order to effectively operate a well-timed monetary policy, the enhancement of our precision in economic forecasting is more important than anything. Amid the rapid changes in the conditions surrounding our economy, the cause and effect relationships between economic variables are changing. And with the development of industrial technology and the progress of globalization the interrelationships among individual economies are evolving in complex ways. In line with this, while we on the one hand expand our database necessary for economic analysis, we will also need to endeavor to constantly improve our methods of analysis and our forecasting models, and ensure thereby that we can more accurately predict macroeconomic variables such as growth and prices. And on this foundation, we will have to deliver consistent policy signals to economic agents as we carry out our policies.

Our efforts to secure a solid level of financial stability must also be strengthened further. We must closely examine factors causing financial unrest at home and abroad, trends of capital flows, and so on, and through timely implementation of market stabilizing measures where necessary, maintain the stability of our financial and foreign exchange markets. With regard to household debt, the pace of its growth is expected to gradually slow thanks to the government's efforts for housing market and household debt stabilization. However, we should not neglect the fact that the total household debt volume is high, and that it is still increasing faster than household income, which may hinder the sustainable growth of our economy and financial stability. It may be difficult within a short period of time to resolve the problem of household debt, but over the medium- to long-term it is necessary to maintain the rate of growth in debt at no more than that in income.

The payment and settlement environment is changing greatly now, as technologies such as big data, artificial intelligence and biometric authentication come to be adopted in the financial industry. In these circumstances the Bank of Korea must devote special efforts to advancing the payment and settlement systems and heightening their safety. The work of constructing the next generation BOK-Wire, in order among other things to enhance financial institutions' convenience in making funds transfers, will have to be carried out with insights peering ahead 20 or 30 years into the future. We will in addition have to work harder to strengthen the resilience of the BOK-Wire businesses against cyber risks and natural disasters as well.

Fathoming the depth and the breadth of the changes taking place in the financial sphere due to the recent digital innovations is not easy. Research on ways of

applying distributed ledger technology to payment and settlement has been increasing rapidly, led by central banks in major countries and commercial banks. There is a possibility that cryptocurrency transactions, which are showing signs of overheating around the world, will work as risks to financial stability, and we will therefore also have to continue considering measures for dealing with those risks. We should also keep participating actively in the related discussions in international society and with the domestic ministries and institutions concerned, while steadily carrying out studies of the effects of digital innovation on financial stability and monetary policy, and of the possibility of digital currency issuance by the central bank.

Dear fellow members of the Bank of Korea!

Efforts are currently proliferating to eradicate corruption throughout our society as a whole, and to make it an upright one. We are confident that we have always put an emphasis on principles and fairness, and managed ourselves strictly, but a look at it from the lofty standpoint of the public, which is demanding high levels of morality and transparency of the central bank, may find there to be some areas in which we have fallen short. And therefore, in carrying out our duties, we will have to check again one more time to see whether there might not be practices that we engage in that can be judged as unreasonable, and if so make bold efforts to correct them.

Our policy conditions and our business environment are changing incessantly. In this situation, if our ways of thinking and patterns of behavior remain stuck in the past we will face difficulties in fulfilling all of the duties entrusted to us. We have to constantly ask ourselves what the roles being demanded of the central bank are, right now in particular, what policy alternatives related to pending economic issues we can

propose, and how we should communicate with economic agents about our monetary policy directions. Meanwhile, if we carry out our duties passively, for the reason that predicting the directions and the timings of future changes is difficult, then it will be difficult to propose policy alternatives that will help our economy to develop. We will have to exert courage individually, and work with enterprising spirits like 'First Penguins', taking single steps at a time forward and challenging the environment.

But even if an organization's members all devote their best efforts in their own individual spheres, unless they can overcome the 'Silo Effects' of focusing solely on their own or their own departments' performances it will be difficult for the organization as a whole to develop. We therefore have to work to increase staff communication – between superiors and subordinates, between co-workers, and between departments – and through a broadening of understandings fix into place a healthy organizational culture characterized by mutual respect and care for one other. I cannot stress enough that we will have to design an elaborate assessment and compensation framework, and operate it to ensure that our organizational and personnel system can well support the development of such a culture.

My fellow Bank of Korea family members!

At this time last January, we started our new year with a special determination compared to any other time, to overcome the many difficulties that we faced. Our economy has fortunately been showing a steady trend of growth, so that we have been able escape certain worries that we initially had, but we cannot be complacent and let down our guards at any time. I ask that during this year as well all of us, as central bankers, go forward with self-esteem and a sense of mission and do our very best in

fulfilling the duties entrusted to us. As we welcome this new year of the Golden Dog, I want to wish all of you here at the Bank of Korea, and your families, a year filled with health and happiness.

Thank you.

January 2, 2018

Governor

Juyeol Lee