

Juyeol Lee: New Year speech

New Year's address by Mr Juyeol Lee, Governor of the Bank of Korea, at the Bank of Korea, Seoul, 4 January 2016.

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Dear fellow members of the Bank of Korea,

Today is the first day of work in 2016, which we greet with new hopes and resolutions. I wish you and your families a happy new year full of good health and blessings. Let me also express my sincere appreciation to all of you for faithfully carrying out your duties last year.

Looking back, we have of course never had any easy years, but last year the Korean economy went through many truly great difficulties. On top of the continuous slump from the beginning of last year in exports, which have led economic growth, we also witnessed a rapid contraction in consumption due to the unexpected outbreak of MERS. Financial and foreign exchange market volatilities increased greatly as well, driven by the uncertainties concerning the timing of the US Federal Reserve's policy rate hike and by the economic unrest in emerging market economies (EMEs) including China.

Against this backdrop the Bank of Korea eased its monetary policy further, by cutting the Base Rate on two more occasions following the cuts in 2014, and by raising the total ceiling of its Bank Intermediated Lending Support Facility to a large extent. We also worked actively to stabilize the markets, by strengthening our monitoring of financial and foreign exchange markets at home and abroad and by making efforts to prevent any excessive expansion in the volatility of price variables.

However, our economic conditions were not satisfactory, as economic growth fell short of its potential and inflation remained below the target range.

The recent low growth and low inflation are worldwide trends, and are attributable largely to factors not easily dealt with through monetary policy such as sluggishness in global demand, declines in international oil prices and changes in economic structures. The Bank of Korea, which has the mandate of pursuing macroeconomic stability while paying attention to financial stability, had to be alert to the possibility of its accommodative policy stance pursued over a long period of time causing other adverse effects via the accumulation of financial imbalances. Nevertheless, we have to also look humbly back, and ask whether there was any room for improvement in terms of our assessments of economic conditions, our policy responses, and our communication efforts.

Dear members of the Bank of Korea,

This year our economy is expected to maintain a modest trend of growth, thanks to the continuing recovery of the global economy and to improvements in our households' real purchasing power. Looking at domestic and external conditions, however, there are various potential risk factors that could undermine the smooth recovery of our economy.

Externally, as international capital movements will likely expand due to both the weakening of economic growth in China and the continuous decoupling of monetary policies among major countries, EMEs having weak economic fundamentals could face economic crises. If these concerns are realized, the international financial markets could turn unstable again, and the global economic recovery could weaken.

Domestically, our economy faces still unresolved structural problems that could undermine its vitality, including low fertility and population aging, inter-sectoral imbalances, and the dual structure of the labor market. In addition, as the greatly increased household and corporate debts are affected by the US Federal Reserve's monetary policy normalization, they could cause consumption and investment sentiment to contract and work as a factor undermining financial system stability.

Under these circumstances, the main tasks for Korea to focus on, as a small open economy, are improving its economic fundamentals and boosting its growth potential. The prerequisite for this is structural reform. This is not an easy task, because it leads to pain and sacrifice in the short-term while there are also conflicts of interests among the economic agents concerned.

If we keep pushing this reform ahead with perseverance, however, we can reap fruits that will compensate us sufficiently for the pains that we must undergo. In particular, a successful structural reform will help our economy to achieve faster growth than others once external conditions improve, through the creation of new growth engines and through the restoration of virtuous cycles between exports and domestic demand and between growth and employment.

Structural reform can also help to mitigate the negative effects on our economy of the expansion in volatility in the international financial market. As you are all well aware, one international credit rating agency recently upgraded Korea's rating to the levels of advanced countries. And one of the main rationales for its decision was its positive assessment of our efforts for structural reform.

Dear fellow members of the Bank of Korea,

I would like to touch now on the major tasks that we will need to focus on this year.

First of all, since we have newly set the inflation target, in consideration of the appropriate inflation level for our economy in the medium- to long-term, we need to do our utmost to steer consumer price inflation close to this target over a medium-term horizon. The new inflation target has been set as a point target rather than a range, which is considered a more advanced method adopted by major developed countries. There are many merits to the point target: it not only effectively stabilizes the inflation expectations of economic agents, but also allows the central bank to conduct monetary policy in a more flexible manner, taking into account inflation as well as economic and financial conditions. We need to get the message across to economic agents concerning the background to this change, and the characteristics of our new inflation target. At the same time, we should devote every effort to fulfilling our responsibility of explaining to the public any cases where inflation deviates from the target to excessive extents or for excessive periods of time.

This year, under the new inflation target, in order to sustain the trend of recovery of economic growth we will maintain our accommodative monetary policy stance, while also paying attention to financial stability. Given the moderate pace of our economic recovery and our low inflationary pressures, it is necessary for the time being that we very closely monitor macroeconomic trends, while also being mindful of the downside risks to growth and inflation.

Secondly, we should also step up our efforts to enhance the predictability and effectiveness of our monetary policy. In this regard, the most important thing is increasing the accuracy of our economic forecasting. The unpredictability of economic dynamics has risen enormously, owing to changes in the cause and effect relationships among economic variables and to the rising interconnectedness across economies in line with globalization. We thus face limitations in narrowing the forecast errors. But if the accuracy of our economic forecasts is inadequate, it will be hard to maintain monetary policy efficiency or communication consistency. This is why we need to redouble our efforts to strengthen our forecasting capabilities.

To strengthen our explanations of the backgrounds to our policy decisions, we also need to enrich the content of the Monetary Policy Statements and expand the scope of the Monetary Policy Board meeting materials released to the public. In addition, in order to secure the appropriate time horizons for deciding on our monetary policies, and to strengthen the linkage between monetary policy and our economic forecasts, we plan to reorganize the framework for Monetary Policy Board meeting operation, with effect from next year. We need to thoroughly prepare so that this can be achieved without delay. In particular, as the annual number of monetary policy decision meetings will be reduced, we need to devote more efforts to strengthening our communication with the market.

We need to pay greater attention to financial stability this year. First, we should seek measures to ensure a soft-landing of the household debt problem, by cooperating closely with the government and the regulatory authorities. Liquidity and fund flows through open market operations should be properly managed, to prevent companies from suffering having financing difficulties in the processes of restructuring. Since it is likely that the high volatility in our financial and FX markets will continue this year, we have to thoroughly monitor international financial market conditions and capital flow trends, and if necessary implement our comprehensive Contingency Plan to ensure market stability, in a timely manner.

Meanwhile, as IT and finance become integrated, FinTech, big data and the uses of blockchain technology are becoming global trends. In line with this, we need to carefully examine how these changes will affect our policy environment, and in particular the stability of our payment and financial systems. We also need to conduct an in-depth study of how Internet-only Banks, whose launch is scheduled for this year, will evolve in the future, and what changes they will bring to the monetary policy transmission channels and bank management environment.

Dear fellow members of the Bank of Korea,

As our economy remains in a difficult situation, and the economic and social environments change rapidly, there have been diverse and sometimes conflicting demands from various areas of society regarding the central bank's role. In this situation, in order for the Bank of Korea to meet the nation's expectations and fulfill the role entrusted to it, we need to make ground-breaking improvements in our ways of perceiving reality and carrying out our duties, as well as in our methods of policy operation.

People tend to remain complacent in keeping to what they are used to and comfortable with, and it is thus very difficult to break from old mind-sets and practices. I am well aware that our Bank of Korea staff members have made enormous efforts to adapt to the changing external environment. However, there does remain much room for improvement still, and so we need to strengthen our dynamism for change. This can of course not be done in a day. We have to work continuously to improve the relevant systems for increasing our recruitment of external talent and promoting efficiency and competition in our personnel management.

Our society demands of us that we have much higher levels of integrity and stronger senses of vocation than is necessary in other workplaces. And so it is a basic responsibility of ours that we comply fully with the regulations and principles regarding our duties. Further, as members of a central bank with strict self-discipline and a strong sense of responsibility, we need to put the public interests before our own personal interests, and respect our organizational values.

Meanwhile, our organizational culture of respecting and caring for each other is a longstanding tradition that we have cultivated ever since the Bank of Korea was established. Although the environment surrounding us is changing rapidly, we have to work to maintain and further develop this proud tradition going forward.

Dear fellow BOK members,

There are substantial concerns that the Korean economy could face huge difficulties this year. However, a crisis that is foreseen is no longer a crisis. If we are not too absorbed in pessimism, and prepare for approaching difficulties with optimistic and active attitudes, we can help our Korean economy to overcome any troubles it may face and to take itself one-step further to a higher level.

I hope that you will fully demonstrate your strong competence and potential again this year, to show that the Bank of Korea is indispensable to the development of our national economy.

I look forward as well to your beginning this new year with renewed vigour and determination, and I wish you all happiness and fulfillment.

Thank you.