

# Lee Says Bank of Korea Shouldn't Delay Rate Increases

By Seyoon Kim

Dec. 10 (Bloomberg) -- Bank of Korea Governor Lee Seong Tae said the central bank shouldn't wait too long before gradually raising interest rates, provided the recovery maintains momentum.

"Saying monetary policy will for some time focus on reviving the economy doesn't mean rates won't move," Lee said in Seoul today after leaving the seven-day repurchase rate at 2%. Maintaining borrowing costs at that level a year from now would be "unimaginable" if the economy keeps growing more than 1% each quarter or about 5% annually, he said.

Gross domestic product grew 3.2% in the third quarter, the fastest pace in more than seven years, as companies including Samsung Electronics Co. and LG Electronics Inc. reported a jump in profits. Lower rates have boosted borrowing by consumers, with bank lending to households rising for a second straight month in November on increased mortgage loans.

"The head of Korea's central bank made it clear where he wants rates to go: up, and the sooner the better," said Frederic Neumann, senior Asia economist at HSBC Holdings Plc in Hong Kong, wrote in a note. "The strong upward revision to the third-quarter GDP numbers recently has strengthened the argument for earlier tightening since it means that Korea's economy is coasting closer to potential than previously assumed."

President Lee Myung Bak's administration increased spending and accelerated outlays to cushion the economy from the worst global recession since World War II. The central bank cut the benchmark rate by 3.25 percentage points between October 2008 and February, the most aggressive easing since it began setting a policy rate a decade ago.

## Cloudy Outlook

The central bank said it would "maintain the accommodative policy stance for the time being." While the economy remains on a "recovery trend" as exports and consumer spending improve, there "remains uncertainty" about the growth outlook, it said in a statement. Today's rate decision was forecast by all 17 economists surveyed by Bloomberg News.

The benchmark Kospi stock index erased earlier losses to close up 1.1% at 1,652.73 at 3 p.m. in Seoul. The gauge has gained more than 16 percent over the past six months. The won (KRW) closed at 1,165.50 KRW/USD, near a two-week low. It climbed 5% in the past three months, the best performer among 10 Asia-Pacific currencies, along with the Australian dollar. The KRW has appreciated by 7.5% against the USD in 2009. Asia-Pacific currencies have been appreciating against the USD. During the past three months, the Japanese yen climbed 4.3% against the USD, while the worst performer of the group was the Taiwanese dollar, which appreciated 1% against the USD.

## Boosted Borrowing

Governor Lee indicated he wants to avoid delaying a rate increase for too long because that might mean the bank would have to tighten credit more sharply later on.

"We can't suddenly normalize monetary policy in one step," he said. "We need a process to normalize. Timing is important and we have to consider that it takes about six months to a year" before changes in monetary policy become effective.

The International Monetary Fund this week raised its forecast for gross domestic product growth in 2010 to 4.5% from 3.6%.

Kwon Young Sun, an economist at Nomura International Ltd. in Hong Kong said the expiry of Governor Lee's term on March 31 would make it difficult for the bank to raise rates early next year because his leadership role on the monetary policy committee may weaken. Regional elections in June may add pressure to leave rates low to ensure the recovery isn't choked off, he added.

### **Too Early**

Both President Lee and Finance Minister Yoon Jeung Hyun say it's too early to pursue an "exit strategy" to policy measures taken to stimulate the economy, as risks remain.

Industrial production unexpectedly dropped 3.8% in October from September and inflation remained below the central bank's target of between 2.5% and 3.5% for a sixth straight month in November. Manufacturers' confidence slipped to the lowest level in four months and consumer confidence dropped for the first time in eight months in November.

The recovery "has been quite strong, but there have been some signs that it might slow in the coming months -- that's what the governor's worried about," said Alaistair Chan, an economist with Moody's Economy.com in Sydney.

"I don't think there's going to be a problem on the inflation side, for a while at least," said Chan, who predicts a rate increase in "mid-2010."

Reserve Bank of Australia Governor Glenn Stevens last week raised the benchmark interest rate by a quarter percentage point to 3.75%. He is the only policy maker in the world to have raised interest rates three times this year. This policy has made the AUD the best performer among Asia-Pacific currencies in 2009. The AUD has appreciated 23% against the USD in 2009.

New Zealand's Reserve Bank Governor Alan Bollard said today that he may raise rates from a record-low 2.5% "around the middle of 2010," sooner than he had previously indicated.

The Bank of Korea last month widened its inflation target range for the next three years, providing scope for policy makers to keep interest rates low. The goal for 2010 to 2012 will be 3%, plus or minus 1%, it said on Nov. 26. The current target is 3%, plus or minus 0.5%.