FIXED INCOME ISSUE REPORT

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August MPC Review

Still estimating terminal rate of 3.50%

- At the August Monetary Policy Committee (MPC) meeting, the Bank of Korea (BOK) raised the base rate by 25bps (from 2.75% to 3.00%). Considering the dissenting vote (in favor of freezing the base rate) and the dot plot (suggesting only one more hike over the next six months), the overall stance was dovish.
- Our baseline forecast for the terminal rate remains at 3.50%. The BOK is likely to hold the base rate steady through year-end before raising rates twice in 1H27 (once in January and once in April).
- Market vigilance towards MPC meetings will likely soften before tightening again in 2027. But as the BOK has substantially lifted its 2027 GDP growth forecast, we acknowledge that the terminal rate might be as high as 3.75%.

Excluding rate hike itself, MPC's stance dovish

The Bank of Korea's (BOK) Monetary Policy Committee (MPC) raised the base rate by 25bps (from 2.75% to 3.00%), a move that surprised markets, as expectations had leaned towards a hold. Bond yields rose sharply as a result.

Except for the rate hike itself and the BOK's significantly upgrading its GDP growth outlook, all other aspects of the statement were dovish. Committee member Hwang Geon-il dissented in favor of a freeze, and the dot plot suggests only one more rate hike over the next six months. Governor Shin Hyun-song characterized the back-to-back rate hike as an unusual departure from precedent, explaining that the preemptive action—aimed at nipping elevated inflation expectations in the bud—should enable a more moderate (less aggressive) tightening path. After reviewing both the dot plot and the governor's press conference, the bond market reversed course, with yields falling notably.

Still forecasting terminal rate of 3.50%; next hikes in January and April

Our forecast for the terminal rate remains at 3.50%. The BOK is likely to hold the base rate steady through year-end, but we now believe the next two rate hikes will happen in January and April (previously expected February and May). While we continue to view 3.50% as the most likely endpoint, given the BOK's substantial upward revision to its 2027 GDP growth forecast (from 2.1% to 2.9%), we need to be open to the possibility of an additional hike taking the terminal rate to 3.75%.

(Continued on the next page)

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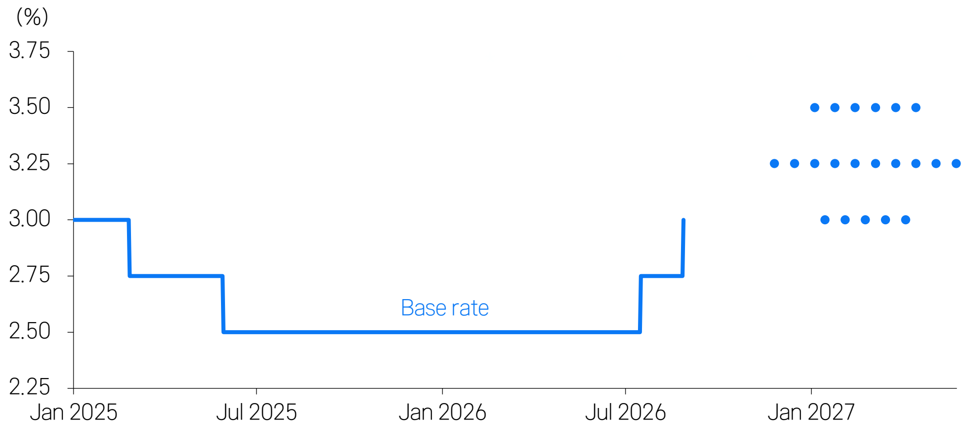
Relief rally hard to visualize

Immediately after the rate-hike announcement, the 3-year KTB yield touched 3.9% before sentiment shifted following a closer review of the dot plot and the press conference. As a result of the press conference, yields tumbled 6bps d-d on the 3-year KTB and 3bps d-d on the 10-year KTB, reflecting diminished market expectations for additional rate hikes before year-end. That said, the BOK's 2027 growth forecast of 2.9% and core inflation projection of 2.5% signal that the high-rate environment is unlikely to end anytime soon, limiting the scope of further bond-yield declines. The next catalysts for the bond market will be the budget bill and its impact on KTB issuances. For now, we estimate the 3-year KTB yield will range 3.60-3.80% and the 10-year KTB yield will range 4.10-4.40%.

BOK dot plot (as of Aug 2026)



Source: Bank of Korea

Economic outlook (as of Aug 2026)

	2026				2027			
	1H	2H	Annual	vs May	1H	2H	Annual	vs May
GDP growth (%)	3.8	3.0	3.3	[+0.7]	2.5	3.2	2.9	[+0.8]
• Private consumption	2.6	1.7	2.1	[+0.1]	3.1	2.5	2.3	[+0.2]
• Construction investment	-1.5	1.7	0.2	[-0.4]	2.6	1.3	1.9	[+0.4]
• Facilities investment	5.4	8.3	6.8	[+2.4]	4.7	4.7	4.7	[+2.0]
• Intellectual property products investment	3.7	3.7	3.7	[+0.2]	0.3	3.4	3.2	[+0.2]
• Goods exports	10.8	8.7	9.7	[+4.8]	4.8	4.5	4.6	[+1.3]
• Goods imports	9.7	9.8	9.8	[+6.8]	5.3	4.0	4.6	[+1.1]
CPI inflation (%)	2.5	2.8	2.7	[-]	2.3	2.2	2.3	[-]
• Core inflation	2.3	2.8	2.5	[+0.1]	2.6	2.4	2.5	[+0.2]
Current account (USD100mn)	1,910	2,590	4,500	[+2,000]	2,375	1,925	4,300	[+2,400]
• Goods balance	1,93[illegible]	2,733	4,672	[+2,000]	2,529	2,059	4,589	[+2,434]
• Services balance	-118	-252	-370	[-14]	-216	-255	-471	[-38]
• Primary & secondary income balance	89	108	198	[+14]	62	121	183	[+6]

Source: Bank of Korea

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