CAN MARKET INTEREST RATES STAY LOW?

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In January, the series of record-breaking interest rate drops ended. The 3-year corporate bond rate continued to drop close to 7.0% in early January, but soon after it rebounded to above 8.0%. In spite of this fluctuation, interest rates still remains at a historically low level, a single-digit number. There are two reasons for this recent fluctuation of interest rates. First, the sudden news of the outbreak of the Brazilian financial crisis made the domestic financial market unstable. Even though the impact did not remain strong for a long time, however, it was sufficient to temporarily shake the positive mood toward a fast recovery of the Korean economy. While short-term interest rates such as the RP and call rates stayed at a low level around 6%, longer term interest rates like the 3-year corporate bond yield went up, reflecting expected risk in the future. Second, the worry over the speed of drops in interest rates spread in the financial market. For example, the 3-year corporate bond yield was 11.9 at the end of last September, but dropped to 10.00%, 9.25% and 8.00% at the end of following months. Thanks to these fast drops, the stock market exploded and real estate market also showed signs of recovery. This sudden boom in the asset markets caused worry over financial bubbles and, as a result, reactional sentiment has risen in the market.

Although these factors stopped the continuous drops in interest rates, the basic economic and policy environments are still solid to keep record low interest rates. First, the government and the Bank of Korea share a strong consensus to keep interest rates low in order to boost the economy. The BOK dropped the RP rate again below the 6.0% level early February. Second, there is sufficient liquidity in the financial market. Basically, this is due to the abundant money supply and sluggish demand of money from business sector. Third, the restriction on bond issuance of big companies is pulling down the bond supply in the market. As long as this restriction is valid and economy is not significantly recovering, there will be no significant pressure to push up the interest rates. It seems clear that major interest rate indicators will stay under 10%, for a while. This trend will be sustained during the next month unless there are other shocks from the international market. VIP

〈Table〉 Major Interest Rates

(End of Period, %)

	1997	1998		1999	
		Nov.	Dec.	Jan.	Feb. 4
Corporate Bond Yield(3 yr.)	28.98	9.25	8.00	8.13	8.10
CP Rate(91 days)	35.00	7.90	7.90	7.12	6.70
Call Rate(1 day)	35.00	7.16	6.53	6.15	5.85