

Korea 1Q GDP, economic upturn begins

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1Q17 GDP expanded 0.9% QoQ (2.7% YoY)

Korea's 1Q17 GDP gain accelerated to 0.9% QoQ (2.7% YoY). The figure surpassed the consensus but was less than our forecast of 1.2% QoQ (2.9% YoY). The gap was mainly due to investment demand that was much stronger than we expected, leading to estimate-beating demand for imported goods. Therefore, even though 1Q GDP growth was less than we estimated, it is more than enough to provide an optimistic outlook for the economy.

There are signs of recovery among every GDP indicator. Facilities and construction investment along with private consumer spending posted higher figures than our estimates. A favorable cycle for the semiconductor industry led the growth of facilities investment. Accelerated inventory buildup contributed to GDP growing 0.3%p more than the previous quarter. Facilities investment and the inventory cycle contributed to downward revisions for growth rates in 2016 but they are now the main drivers of this year's optimistic outlook. In particular, a strong export recovery is leading the upswing for facilities investment and the inventory cycle.

Construction investment expanded 5.3% QoQ, relieving concerns about a rapid downturn for the construction industry. Shipments of intermediary goods for construction have been recovering since the beginning of the year along with the homebuilding permit area, a leading indicator of the housing market. Hence, we believe the construction sector is set for a soft landing in 2H17.

However, the rise of private consumer spending is slower than expected. In QoQ terms, private consumer spending improved only 0.4%, less than GDP growth. The fact that consumer growth is particularly low despite the 2.3% QoQ increase in gross domestic income indicates no change to households' preference for savings.

Yet, the recent consumer sentiment index indicates a recovering trend and therefore we forecast more rapid growth for private consumer spending in 2H17. The April Consumer Confidence Index climbed to 101.2 and topped the important 100 benchmark. Thus, we expect to see private consumer spending rise at a similar pace as GDP.

Table1. Spending component growth figures

(% YoY, % QoQ)

Category	2016				2017
	1Q	2Q	3Q	4Q	1Q
Gross domestic product	0.5	0.9	0.5	0.5	0.9
(% YoY)	2.9	3.4	2.6	2.4	2.7
Private spending	-0.1	0.8	0.6	0.2	0.4
Gov't spending	1.4	0.6	0.9	0.6	0.5
Construction investment	7.6	3.1	2.2	-1.2	5.3
Facilities investment	-7.0	2.6	0.9	5.9	4.3
IP products investment	0.2	1.3	0.5	0.6	-0.2
Change in inventory	-0.5	-0.1	0.1	0.1	0.3
Exports	-0.6	1.0	1.0	-0.1	1.9
Imports	-1.5	2.2	2.6	-0.1	4.3
Gross domestic income	3.0	-0.1	-0.5	0.8	2.3
(% YoY)	5.7	4.7	3.3	3.1	2.4

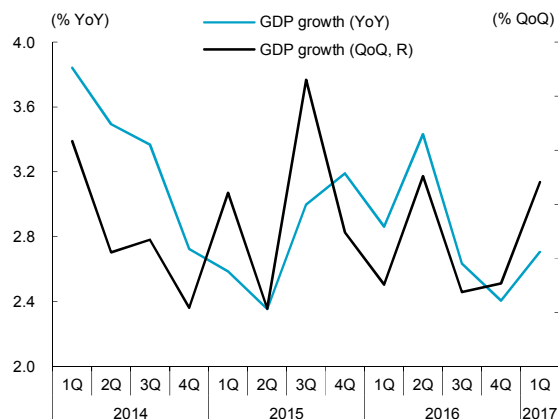
Note: Change in inventory indicates its contribution to GDP (%)
Source: Bank of Korea, KIS

Recovery led by exports and investment, further spurred by consumer spending

While exports and investment played major roles to prop up the economy in 1H17, the recovery will be led mainly by consumer spending in 2H17. A global economic upturn led by the US is continuing and Korean new government will announce the new economic policies focused on bolstering the economy after the presidential election. As such, our forecast for GDP growth is 2.9%. We believe the economy will expand ~3% in 2H17.

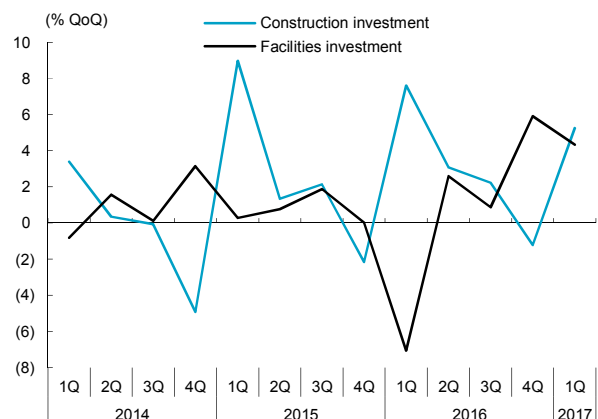
Accordingly, the actual rate will come close to the potential growth rate. The output gap will reach the finance-neutral level. Hence, inflationary pressure will rise as we enter the second half of the year. Higher commodity prices will contribute less to domestic price levels while revived demand contributes more to inflation.

Figure 1. GDP growth



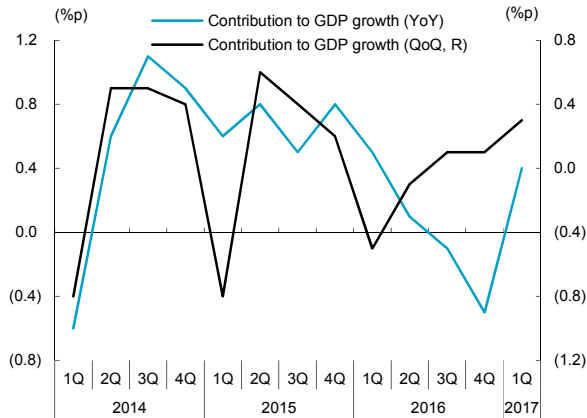
Source: CEIC, Korea Investment & Securities

Figure 2. Construction and facilities investment



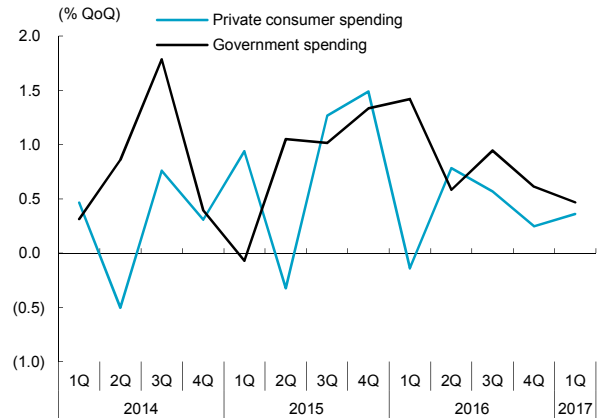
Source: CEIC, Korea Investment & Securities

Figure 3. Inventory contribution to GDP growth



Source: CEIC, Korea Investment & Securities

Figure 4. Private consumer and government spending



Source: CEIC, Korea Investment & Securities

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