

South Korea Economics

Capital Outflow Pressure, KRW Weakness, and BoK's Faster Hikes

CITI'S TAKE

In May-June, capital outflow pressure from foreign equity investors has accelerated while Korean exporters appear to keep high USD conversion ratio to KRW. On monetary policy, we maintain our view of BoK's rate hiking cycle being 25bps each in July 2026, October 2026, January 2027, and April 2027, towards a 3.5% terminal rate. However, **the risks should be tilted to a faster-than-expected BoK rate hiking cycle (e.g. back-to-back hikes in 3Q26 or a surprising 25bps hike at the unexpected ad-hoc June MPB meeting)**, as a strong KOSPI rally could raise the risks of KRW weakness and a housing market rally ([note](#)). BoK Governor Shin recently anticipated that a narrowing of the US-Korea interest rate differential will likely alleviate KRW depreciation pressure via the NDF market and carry trade ([note](#)).

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[1] **BoK foreign reserves:** In May, BoK foreign reserves declined by US\$0.9bn to US\$426.9bn. BoK noted, the monthly contraction is attributable to market stabilization measures such as BoK/NPS FX swaps ([press release](#)). The monthly decline of foreign reserves excluding FX valuation effects would be only around -US\$0.7bn (vs. April: +US\$1.0bn; March: -US\$1.8bn; February: +US\$1.4bn; January: -US\$4.8bn; December: -US\$4.4bn), on our estimates.

[2] **BoK's forward position & NPS FX hedging:** In April, BoK's long forward position has gradually increased by +US\$1.9bn (vs. March: +US\$1.0bn; February: +US\$1.2bn). In our view, the NPS FX hedging may have been gradually implemented via both BoK/NPS FX swap and market since late December 2025. The National Pension Service (NPS) has recently eased the burden of USD procurement in 2H26 by changing NPS asset allocation target for 2026 ([note](#)).

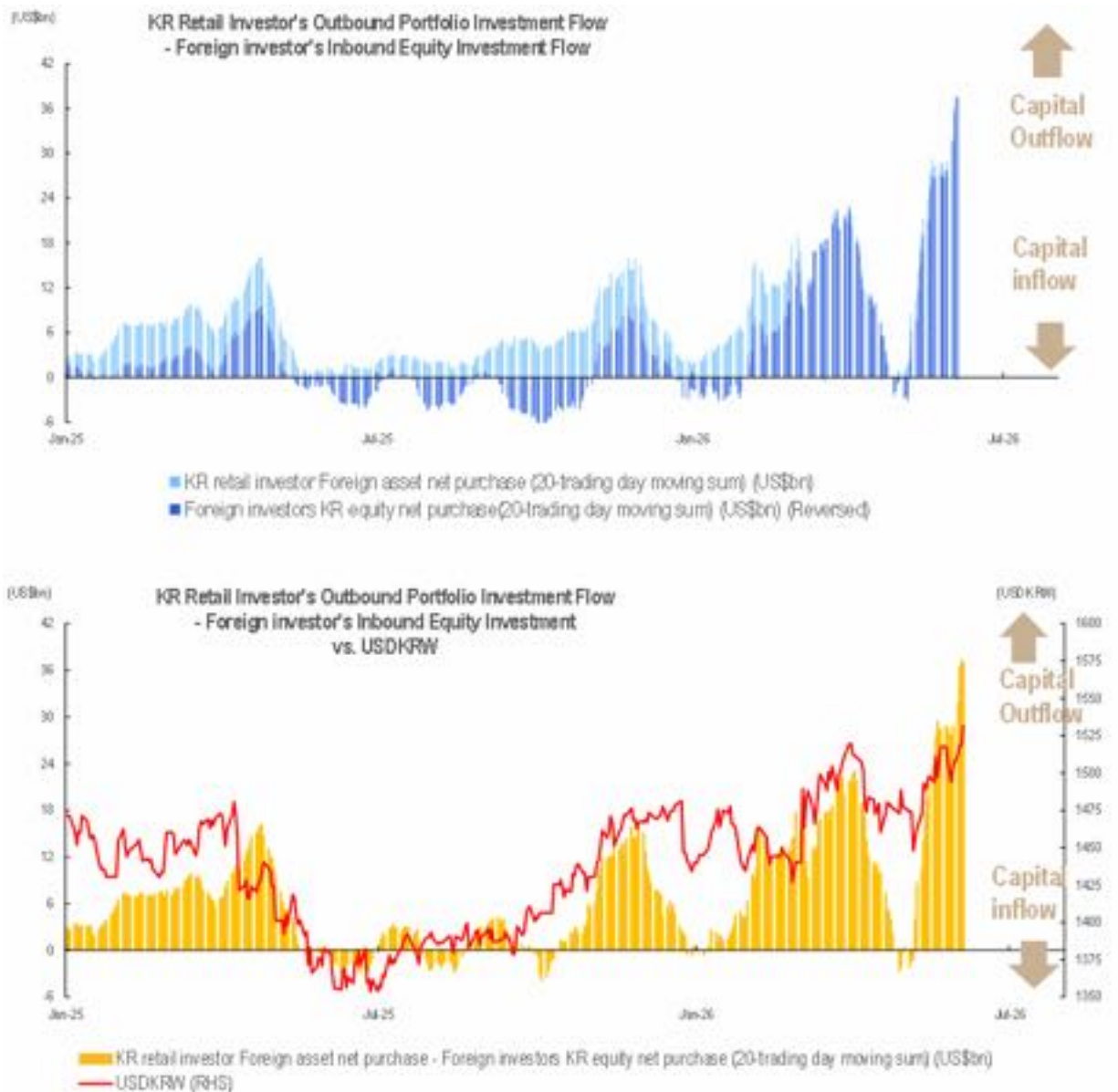
[3] **Foreign equity investors:** Capital outflow pressure from foreign equity investors has accelerated **-US\$12.1bn over June 1st to June 5th** (vs. May: -US\$27.9b; April: +US\$0.6bn), led by rebalancing and profit taking. Over January-May'26, foreign equity investors' Korean equity exposure has cumulatively surged by US\$0.98trn to US\$1.89trn while foreign equity investors cumulatively sold US\$76.4bn of Korean equities. Foreign equity investors' share of Korean equity market rose to 37.7% at end-May'26 (vs. December'25: 32.9%). Citi EM FX & Rates Strategy team noted valuation effect outweighs flow impact ([note](#)).

[4] **Korean retail investors:** Korean retail investors' purchases of foreign securities declined (June 1st to 4th: -US\$1.1bn; May: +US\$0.9bn; April: +US\$0.2bn, March: +US\$1.4bn) as Korean retail investors are purchasing Korean equities instead, effectively digesting foreign equity investors' selloff.

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[5] **Korean exporters and conversion ratio:** Korean exporters appear to be keeping high USD conversion ratio to KRW led by the semiconductor exports boom, in our view. Our proxy for conversion (Foreign Currency Deposit in South Korea as % of 12-month sum of Exports) suggests active USD conversion trends by exporters. We estimate the nominal amount of semiconductor exports to increase further in coming quarters. We keep our 2026E current account surplus at 12.8% of GDP (vs. 2025: 6.6% of GDP) ([note](#)).

Figure 1. Capital outflow pressure from foreign equity investors has accelerated



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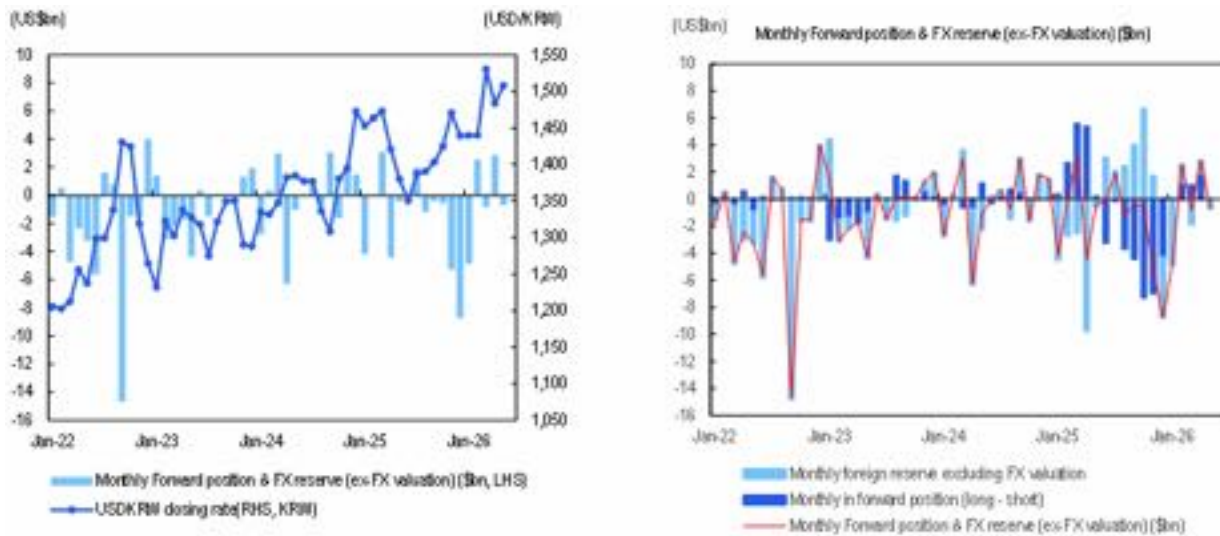
Figure 2. In January'26-May'26, foreign equity investors' Korean equity exposure has cumulatively surged by US\$0.98trn to US\$1.89trn; Foreign equity investors' share of Korean equity market rose to 37.7% at end-May'26 (vs. December'25: 32.9%).



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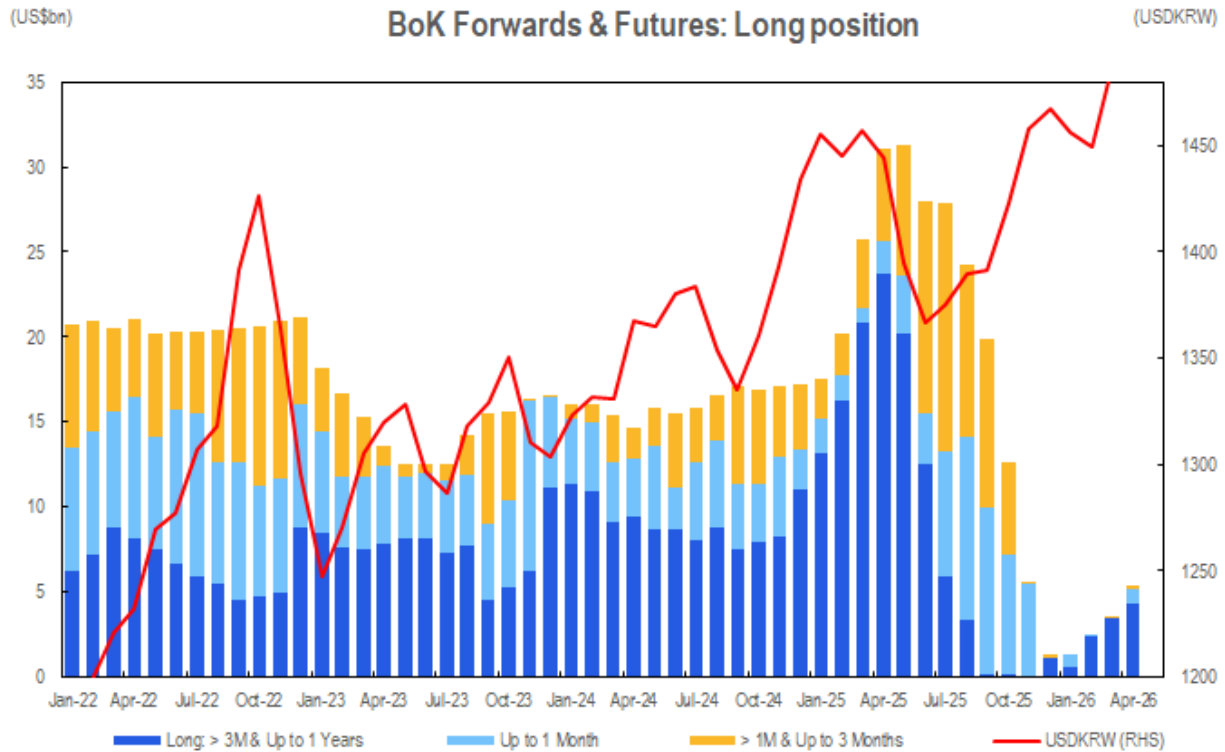
Figure 3. The monthly decline of foreign reserves excluding FX valuation effects would be only around -US\$0.7bn (vs. April: +US\$1.0bn; March: -US\$1.8bn; February: +US\$1.4bn; January: -US\$4.8bn; December: -US\$4.4bn), on our estimates.



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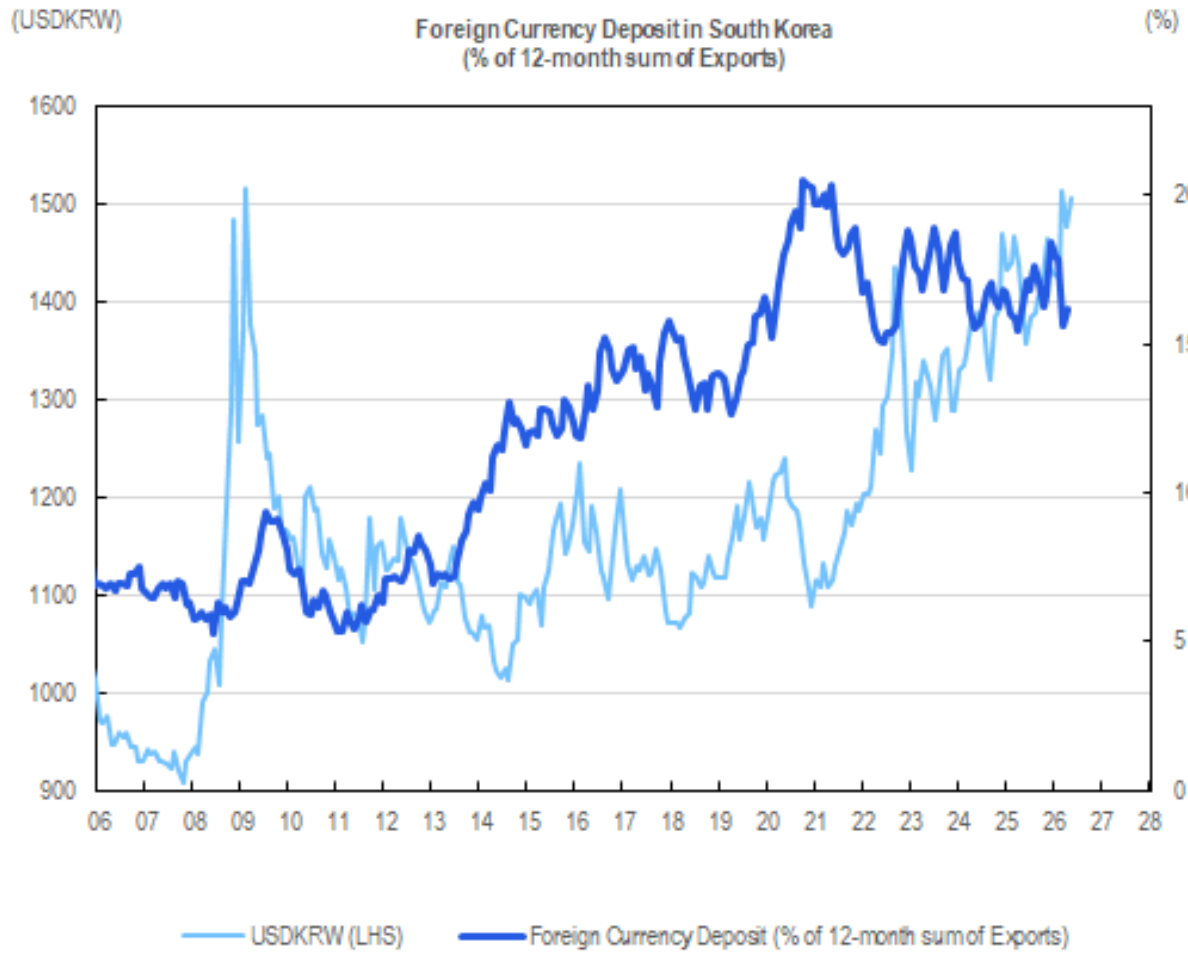
Figure 4. In April, BoK's long forward position has gradually increased by +US\$1.9bn (vs. March: +US\$1.0bn; February: +US\$1.2bn).



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Figure 5. Our proxy for conversion (Foreign Currency Deposit in South Korea as % of 12-month sum of Exports) suggests active USD conversion trends by exporters



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Figure 6. The capital gain by domestic retail equity investors could accelerate the Greater Seoul area housing market rally.



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