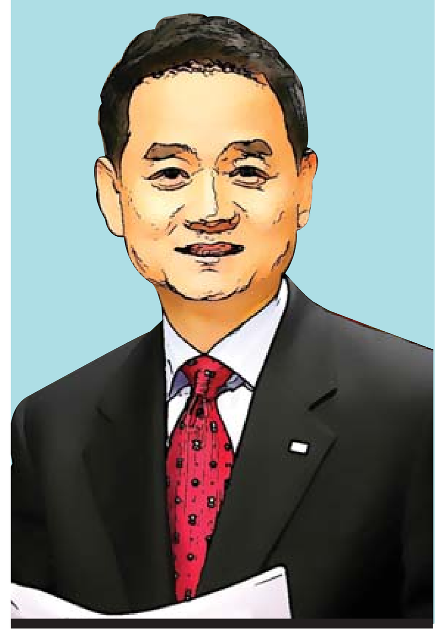
KOREAN MARKET

Koo Jae-sang

Korean market may bounce back in the second half



In 2012, the Korean stock market is likely to remain highly volatile. Europe is still kicking the can without finding pragmatic solutions. The coming February will be a stressful time for PIIGS (Portugal, Italy, Ireland, Greece and Spain) countries, especially Italy, as their bonds come to maturity. The debt maturity would be a factor in heightening the volatility in the market.

In the second half of 2012, however, as counter cyclical policies take effect in Europe and the U.S., the economic recovery will surface, beginning in Asia.

The U.S. would show a relatively sound economy with the growth rate at 1.5 to 2 percent. China is expected to grow 8 percent, slower than in previous years, but when the country's policy to boost domestic consumption takes effect, it could lead steady growth in Asia.

The stock market is likely to bounce back in the second half after falling in the first half. This means the bearish market of the first half could offer opportunities to mutual fund investors.

The global economic growth for 2012 is likely to stay near 3 percent due to the ongoing global economic downturn. However, the Korean stock market is holding up better than others as corporate earnings are growing faster than world economic growth.

We need to take interest in Korean companies with stable, sustainable growth based on their global competitiveness in the long-term while being aware of the global economic situation. KOSPI is anticipated to show a similar growth rate to those of individual Korean companies.

Due to macroeconomic uncertainties and the global slowdown, cyclical sectors and domestic consumption-related stocks have concerns over earnings visibility and growth. Instead, the following firms seem to be promising: companies which can achieve sustainable growth with unique positioning; companies which can achieve increase in market share leading to earnings growth; and multinational companies which have room for further growth due to their entry into emerging markets.

From a long-term perspective, these companies' value will grow sustainably as they could weather an economic downturn and have significant growth potential down the road.

Under such circumstances, investors may need to lower their target return on investment. Interest rates are likely to remain low for a considerable length of time, judging by government and household debts and sluggish demands caused by the stagnation in Europe.

The appropriate approach for achieving target return amid an era of low-interest rate will be diversifying the portfolio by putting capital into various kinds of assets, including equity funds during a market correction, exchange traded funds (ETFs) involving stellar companies, hedge funds that pursue stable profits, real estate and bonds-based funds.

Koo Jae-sang is CEO of Mirae Asset Global Investments.

GLOBAL MARKET

Patrick Artus

What will be the decisive factors for global markets?

We believe that the financial markets and the allocation of savings between regions and asset classes will primarily be influenced by three factors in 2012. The first factor, obviously, is the nature of the crisis in the eurozone and how fast it can be stopped, which has an impact on all risky asset prices, and which has led to a few assets being selected as safe-haven assets. The second factor is the size of the growth gap between the United States and the eurozone; if growth is far stronger in the United States, investors will head for the U.S. dollar and U.S. assets. Lastly, the third factor is the magnitude of the slowdown in growth in emerging countries, due to the weakness of the economies in OECD countries, and in certain cases, up to now, due to restrictive monetary policies and capital outflows. But monetary policies are starting to become more expansionary, and the exchange rates of emerging countries are depreciating. Nevertheless, if growth in emerging countries continues to slow down despite these developments, investors will switch out of emerging assets and into other assets, and this is already happening at the end of 2011.

Symmetrically, the eurozone crisis has generated safe-haven assets: the dollar, the yen, public debt issued by the United States, the United Kingdom, Sweden, Germany, the Netherlands and Finland.

At present, we do not have any clear idea of how the public debt markets of the troubled countries like Spain and Italy — which have substantial borrowing requirements — will be balanced in 2012: the ECB does not want to continue its purchases in the secondary market, banks and institutional investors are sellers, and the EFSF has very limited resources. But we also know that a default by a large euro-zone country or a break-up of the euro is unimaginable, because of the destructive effects this would have: capital losses on the external assets of the Northern countries, and defaults among banks, insurance companies and private-sector issuers as a consequence.

We could imagine a scenario where the eurozone crisis is still present in the first part of the year, after which it becomes imperative to end the crisis, leading to a renewed convergence between asset prices, especially between the interest rates of the Northern and Southern eurozone countries.

Let us now look at the situation relative to the United States and the eurozone. U.S. growth is and will be stronger than eurozone growth. This is mainly due to households' consumption behavior. The abundance of liquidity in the U.S. has probably encouraged households to consume part of their liquid savings, which

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explains the fall in the U.S. household savings rate.

The stimulation of consumption in the U.S. is leading to an improvement in the labor market, and therefore to a recovery that seems to be self-sustaining. The result could therefore be a considerable growth gap between the U.S. and the eurozone, which would drive investors to U.S. assets: equities, corporate bonds, commercial real estate, etc. The U.S. stock market is already significantly outperforming the European stock market.

Let us now look at the situation in emerging countries. Growth in emerging countries is decelerating due to the weakening of their exports, primarily due to the slowdown in exports to Europe. Their monetary policies are now becoming more expansionary; with, for example, the reduction in the reserve requirement ratio in China and the cut in Brazil's key intervention rate. However, boosting credit and activity will take time. Likewise, the depreciation of emerging countries' exchange rates against the dollar, which is due to capital outflows, will boost these countries' foreign trade, but only gradually.

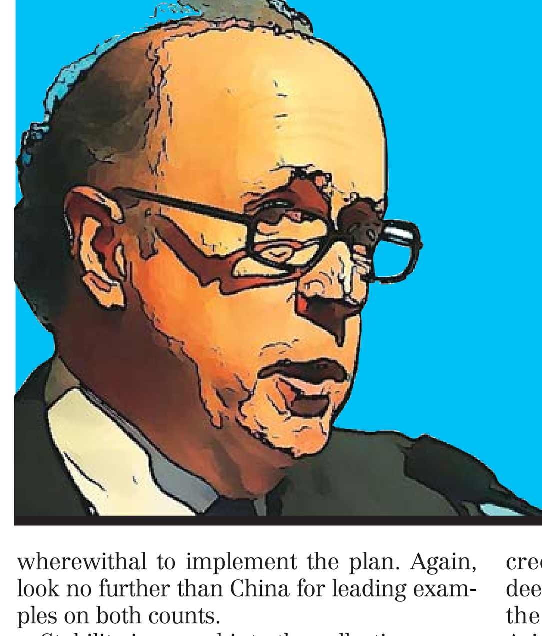
Accordingly, there will be a slowdown in emerging countries in 2012. These countries will therefore no longer be an Eldorado for investors where they can simultaneously find vigorous growth, exchange-rate appreciation and rising financial markets. If the loss of growth in emerging countries were to be too pronounced, investors might switch from emerging countries to OECD countries — and this has already started — on a more permanent basis, which would be a total reversal of the trend seen in the period 2002-2008.

Patrick Artus is the chief economist of Natixis.

GLOBAL ECONOMY

Stephen Roach

Asia will stay the course of its rapid ascendency



As the rich developed economies now languish in Japanese-like quagmires, there can be no mistaking the dynamism of Asia. The question is, "Can it continue?"

Collectively, the developing and newly industrialized economies of Asia now account for 28 percent of world output, according to the IMF's purchasing-power parity accounting metrics. That's more than 80 percent of the combined share of the United States and Europe. With growth in the gross domestic product of Asia's rapidly growing economies averaging about 8.5 percent in 2010-2011 — nearly three times the 3 percent growth elsewhere in the world — the region's economic power is in a league of its own.

Extrapolation, however, is always fraught with peril. Asia is hardly an exception. Japan, the region's first growth miracle, has been in tatters since the early 1990s. The widely heralded East Asian growth miracle faced a major crisis of its own in the late 1990s. And, now, with export-led Asia still heavily dependent on external demand in the crisis-battered developed world, and with China and India facing daunting tactical challenges of their own, there are no guarantees that Asia will stay its impressive course.

Out of crisis often comes opportunity. Such is the case for Asia. Yet its opportunities will be realized only if it deepens its focus on three key objectives — strategy, stability, and internal demand.

Strategy is Asia's greatest strength. Unlike the West, where the politics of short-term political cycles frame the policy debate in a dangerously myopic fashion, Asia has a much longer decision-making horizon.

China's five-year planning cycle is the most salient example of Asia's strategic approach to economic growth and development. Strategy is vacuous, however, if it is not accompanied by a commitment and the wherewithal to implement the plan. Again, look no further than China for leading examples on both counts.

Stability is seared into the collective mem-

> Seduced by the political economy of false prosperity, the West has squandered its strength. Driven by strategy and stability, Asia's rapidly growing economies offer great potential to fill the void.

ory of modern Asia. China's Cultural Revolution of the late 1960s and early 1970s, along with the Asian financial crisis of 1997-98, are important and painful examples of destabilizing threats to economic development.

For Asia, these are painful lessons learned. Unlike the West, which recently ignored instability at great peril — asset and credit bubbles in the United States and a deeply flawed currency union in Europe — the stability constraint is now central to Asia's strategic framework.

Internal demand is the third leg to the stool of Asia's opportunity. It is now time for this export-led region to wean itself from external demand in the crisis-torn developed world. A rebalancing toward internal demand is the only real option.

Here, there is nothing but upsides. For Asia's developing economies, internal private consumption currently stands at a record low of just 44 percent of pan-regional gross domestic product — fully ten percentage points lower than the share prevailing in 2000. In China, the share is a good deal lower — currently less than 35 percent.

Opportunities can either be seized or squandered. In recent years, we have seen glaring examples of both. Seduced by the political economy of false prosperity, the West has squandered its strength. Driven by strategy and stability, Asia's rapidly growing economies offer great potential to fill the void. The big "if" is whether Asia uncovers a new source of internal demand. China's pro-consumption 12th Five-Year Plan offers strong evidence that Asia will seize the opportunity and stay the course of its rapid ascendancy.

Stephen S. Roach, a member of the faculty at Yale University, is non-executive chairman of Morgan Stanley Asia and the author of The Next Asia.

MANAGEMENT STRATEGY

Mauro Guillen

2012: the year of emerging-market multinationals

The last five years have witnessed a sharp rise in the global activities of firms based in emerging economies. They have invested more than one trillion dollars outside their home countries, both in developed and developing countries. They presently account for more than half of all new foreign direct investment in the world, both in the form of greenfield establishment and acquisitions. And they now account for nearly 10 percent of new patents granted worldwide.

When historians examine the early years of the twenty-first century, they will most likely point to the rise of emerging-market multinationals as the most significant and consequential change. By comparison, the crisis of the euro or the financial implosion of 2008 will be regarded as minor events.

During 2012, emerging-market multinationals will continue to rewrite the rules of global competition. They have taught us very important lessons about the importance of efficiency, scale, niche thinking, political capabilities, and a host of other matters. They have applied these capabilities to both traditional and high-tech industries, ranging from food processing and beverages to mining, cement, steel, electronics and aircraft.

One of the most likely trends for the new year is a spike in mergers and acquisitions by emerging-market multinationals. There are several contextual factors that make it likely. First, emerging-market multinationals need more technology and know-how to sustain their expansion and move up the value chain. Second, they are eager to increase market access and market share in the most developed countries. Third, they tend to operate in industries that are relatively mature, some of them ripe for consolidation. And fourth, the large current account surpluses and increasingly strong currencies of emerging economies make it easier for their firms to invest abroad.

This phenomenon should trigger several kinds of soul-searching in developed countries. First, the rise of the emerging-market multinationals means that established multinationals are losing ground, at least in relative terms. Therefore, it is imperative that their sources of competitive advantage be identified, studied, and, whenever possible, emulated. Second, alliances and other types of agreements between emerging-market and established multinationals need to become more balanced. It is no longer the case, as in the recent past, that they only make sense when the former offer low costs and the latter the design and the technology. Alliances can now become a source of two-way learning. Third, established multinationals from developed countries must expect their emerging-market counterparts to compete for their managerial resources. The year 2012 will witness the beginning of a global race for managerial talent, with emerging-market multinationals being in a position to offer attractive jobs to the best managers because of their high-growth potential and financial resources.

The global economy of the 21st century is a far cry from the one we inherited from the twentieth. The rise of emerging-market multinationals will undoubtedly challenge most of our assumptions about global competition. This does not mean that the established multinationals from developed countries will be displaced by the emerging-market multinationals across the board. What it means is that the playing field has been fundamentally altered. New competitors and new ways of competing have transformed the global economy.

Mauro F. Guillen is the director of the Lauder Institute at the Wharton School.

2012 Business Focus Forum

In the spirit of the New Year, we invited 16 world-renowned economic experts and business leaders to share their insights. Most expect turbulent times ahead but they indicate that opportunities are also awaiting us. In short, the New Year will be a contrast of challenges and opportunities. Get a good grasp of what 2012 will look like from our forum — ED.

REGULATION

Cho Young-je

Step up monitoring of capital flows

The intensifying European debt crisis and mounting concerns on the global economic slowdown are weighing heavily on financial markets around the world. Domestically, the general business conditions have deteriorated for many small- and medium-sized enterprises and industries especially vulnerable in a downward economic cycle such as construction, shipbuilding and shipping. The soundness of household debt is coming under growing pressure as well.

Given the difficult market conditions that will likely prevail in 2012 for businesses and financial firms, the top priority for the Financial Supervisory Service (FSS) will be ensuring the safety and soundness of the key financial institutions and preserving the stability of the financial system. To this end, the FSS intends to step up its monitoring of capital flows and encourage domestic banks to secure more foreign currency liquidity as an additional buffer against external contagion risks. The FSS will also continue to keep a close watch on credit flows to small businesses and on the growth of household debt.

As rising inflation and interest rates impose an added burden to the economic hardship of many households, there is a growing need to pay particular attention to the economically disadvantaged and vulnerable segments of our society. For its part, the FSS will continue to take strong supervision and enforcement actions against abuses and conduct that harm consumers. Monitoring and supervision will be strengthened as well on private money lenders and consumer credit providers that prey on low-income borrowers who are often excluded from mainstream banking.

Efforts to improve consumer finance literacy and education will also continue in 2012. One is the "Citizen Bus Tour," which will travel around the country and offer financial advisory and education services to small shop owners and merchants who primarily operate in traditional marketplaces and rural commercial centers. The educational program called "Campus Finance Talk" that the FSS recently initiated to help college students better understand and manage personal finance will be expanded as well. Together with these efforts, more responsible corporate citizenship will be encouraged across the financial services industry.

Improving the efficacy of supervisory examination of financial institutions is another key objective for 2012 as the FSS steps up its supervision efforts to ensure the full compliance of financial institutions with laws, rules, and regulations for safety and soundness, upon which consumer protection depends.

Among others, the FSS intends to build up its examination resources and the intensity proportionate to the level of perceived risk as well as its highly focused thematic examination of large-size, high-risk mutual savings banks and problematic small consumer lenders.

Our supervisory examination will also focus on usurious interest rates, exorbitantly high service fees and financial product sales that fail to be fully disclosed. We will also monitor the practice of demanding deposits in return for a loan and other unlawful tie-in practices, from which consumers and small businesses often suffer. Financial firms' non-arm's length transactions with high ranked officials and businessmen, and anti-money laundering controls will be closely scrutinized as well.

With regard to examiners, the highest professional and ethical standards will be expected, and the IT and accounting specialists from outside will be involved in supervisory examinations to ensure a high level of quality. In addition, protection of private information and the security of electronic banking will be key areas of concern for the FSS in 2012.

Cho Young-je is a deputy governor of the Financial Supervisory Service.

OPERATION MANAGEMENT

Olaf Schatteman

Dynamic supply chains: a bridge over troubled waters

From a business standpoint, the first 10 years of the 21st Century have been anything but normal. Economic turmoil is almost constant. Currency valuations shift with the wind. Bank lending vacillates between lenient and tight fisted. What many people are now saying, in fact, is that this state of volatility may actually be reinforced in 2012: a New Normal characterized by abnormal business conditions.

According to a recent Accenture survey, executives are acutely aware — and quite concerned — about this apparently ceaseless state of sudden changes and rapidly shifting paradigms. Seventy percent of the 3,000-plus decision makers we polled expressed dissatisfaction with their company's ability to predict future performance. And more than 80 percent said they are worried about the resilience of their supply chains — the ability to adapt operationally to rapid changes in products, markets and currencies.

As we embark on 2012, several global and regional circumstances foreshadow ongoing uncertainty and volatility. The economic instability in Europe could have ripple effects in the United States that may reverberate from the Western world into Asia Pacific. While companies monitor the situation and undertake contingency planning, they also have heightened awareness of the concerns associated with natural disasters, as evidenced by the recent flooding in several countries across the region.

The impact of this New Normal on companies' supply chains is potentially huge. But what sort of changes should companies consider as a result? In our view, one of the best solutions is reinventing the supply chain as an adaptable, malleable ecosystem of processes, people, capital assets, technology and data.

Simply put, the "dynamic supply chain" we're proposing facilitates maneuverability in unpredictable markets. This may sound like something companies have always wanted, but the reality is that few organizations have achieved true supply chain dynamism. Most reside somewhere between the functional excellence and integrated enterprise stages. They've made tremendous progress but the emerging state of permanent volatility demands more.

Can a typical company justify the changes needed to create a dynamic supply chain? Most likely, yes, because today's state of permanent volatility can severely impede the operations of most organizations. Still, there are many questions companies can pose to help determine the intensity of their needs. For example, they can question their current level of adaptability. How nimbly does my supply chain organization react to changing customer demands?" or "How strong is our ability to respond smoothly to major disruptions?"

Another evaluation perspective might be strategic value. Could my supply chain be positioned less as a cost center and more as an enabler of key competitive capabilities? Lastly, companies might view the issue from a growth perspective. How prepared are we to operate in new or expanding global markets?

Addressing the above questions won't produce a final decision, but it could shed more light on the game-changing shifts occurring in the global business community, as well as on supply chain solutions that help respond to those changes in a profitable and competitively advantageous way.

No two dynamic supply chains will be precisely alike, even among industries, geographies or business units within the same company. There is a common trait, however: speed to outcome within each functional domain. There are also at least five universal components of any dynamic supply chain for a better future.

First is an adaptive operating model. This is a living, breathing design geared to ensuring that supply chains align with growth and innovation strategies, and embrace processes and systems that help companies rapidly scale or shutter operations based on short-notice demand signals.

Secondly, new skills in risk anticipation and mitigation. "Speed of response" is a critical characteristic of dynamic supply chains, and one way to get it is with advanced risk-prediction and -identification capabilities. Unfortunately, only 11 percent of the survey respondents actively manage supply chain risk and only 18 percent have formal supply chain risk management systems in place.

The third component is enhanced visibility and information acquisition. Maximizing responsiveness and adaptability means you excel at gathering, analyzing and applying information contributed by each link in the supply chain. Leveraging visibility and marshaling better information can also mean integrating your supply chain systems with pricing, promotion, sales and marketing applications.

Fourth is executional excellence. Companies focused on the development of dynamic supply chains don't overlook the importance of investing in core business processes.

And finally, supply chain sophistication and professionalism. It's essential that the organization as a whole understands all components of a dynamic supply chain strategy, and this means developing superior supply chain skills and ensuring that the entire company is receptive to new ways of operating.

Olaf Schatteman is managing director of Accenture Asia Pacific. Olaf has 15 years of Supply Chain experience. He has supported International clients in the area of strategic supply chain transformation.

KOREAN ECONOMY

Oh Suk-tae

Three key risks for Korean economy

The Korean economy is likely to experience a mild slowdown in 2012, and the GDP growth rate would fall to 3 percent from 3.5 percent prior.

European sovereign debt crisis will affect both exports and domestic demand. But the strength of emerging market economies will underpin exports, and consumption will be supported by the resilient job market and household credit growth.

Inflation will no longer be a key issue, as the headline inflation would fall to 3 percent from 4 percent thanks to stable food and energy prices. However, policymakers will not be active in boosting growth.

We expect only a nominal rate cut by 25 basis points by the Bank of Korea (BOK) as the monetary authorities would not completely give up the goal of interest rate normalization. The chances of a significant fiscal stimulus are rather slim considering the sustained emphasis on fiscal prudence.

The European crisis will continue to be the key risk factor. Direct impacts from Europe's economic troubles on Korea's exports will be limited, as those to Europe explain only 10 percent of total outbound shipments.

We actually worry more about the deterioration of external liquidity conditions due to the withdrawal of foreign currency lending by European banks.

Of course, the ratio of short-term debt to foreign exchange reserves, a widely-accepted indicator of external vulnerability, has declined significantly since

> Politics will be one of the key factors in the global economic outlook in 2012; Korea will not be an exception

the 2008 crisis. Korean banks successfully secured foreign exchange liquidity from non-continental-European banks in the second half of 2011 under a considerable stress in global markets.

The expansion of official foreign exchange swap with Japan and China also strengthened the second line of defence in case of emergencies. But we should continue to monitor developments of the European saga and its impact on foreign exchange liquidity and to prepare against the worst-case scenario like the bankruptcy of Lehman Brothers.

On the domestic side, the high ratio of self-employed people appears to be the Achilles' heel of the Korean economy. The share of self-employed people among the total workforce is much higher than in developed economies. We have long held the view that self-employed people are largely responsible for Korea's household debt problems.

This was confirmed by the recent Household Finance Survey, which showed that the household debt-to-income ratio is twice as high among the self-employed as among wage-earning workers. Household debt growth was also much higher among the self-employed than among wage-earners. Self-employed people tend to borrow more from riskier non-bank institutions, while salaried workers usually depend on banks.

Moreover, the recent strength in the labor market can be partly attributed to the rebound in the number of self-employed business people after a decline in the past five years. We should closely monitor the behavior of this group, as it appears crucial to jobs and credit, the two main drivers of domestic demand.

Last, but not least, the rise of medium-term uncertainty on the Korean peninsula due to Kim Jong-il's death should not be ignored. Admittedly, the apparent succession of power to Kim Jong-un will lower uncertainty in the very near term. But it is natural to expect a transition period of at least a few years, with a relative "power vacuum" in North Korea.

The possibility of market-unfriendly events like limited military attacks on the South could increase, while chances of any improvement in the relationship with North Korea are low.

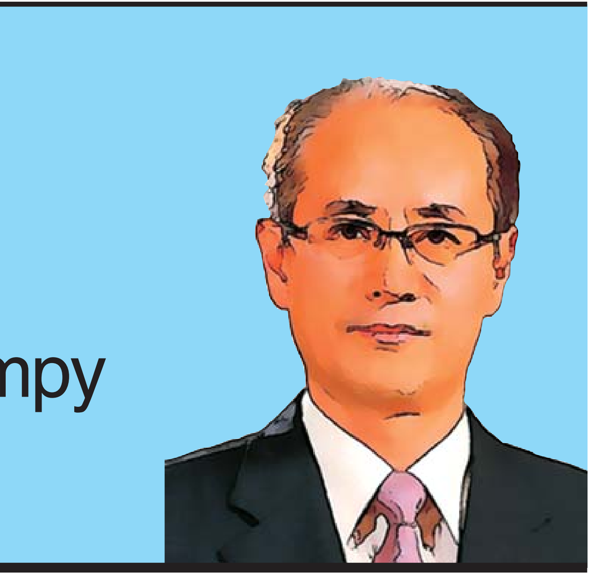
Politics will be one of the key factors in the global economic outlook in 2012; Korea will not be an exception, given the geopolitical risks surrounding North Korea as well as two key elections in the South.

Oh Suk-tae is the regional head of research at Standard Chartered First Bank Korea.

G20

Kim Jae-chun

G20 facing bumpy road ahead



"What on earth is the use of the G20 meetings for the global economy?" This comment typified the reactions of market pundits after last November's Cannes summit. There had been growing expectations from market participants that the elite group of 20 could reach an agreement on expanding IMF resources to tackle the eurozone sovereign debt crisis, but as it turned out, little progress was made. Worse, while the meeting was underway, the PIIGS (Portugal, Ireland, Italy, Greece and Spain) sovereign debt spread indicates that their credit risk widened to a record high amid the heightened uncertainty over Greek and Italian fiscal retrenchment.

The G20's policy coordination after the outbreak of the 2008 global financial crisis is regarded as a significant success. Its decisive actions played a major role in driving the recovery by dramatic fiscal expansion, monetary easing and financial regulatory reform to avoid financial market collapse and a second and global Great Depression. The G20 leaders came up with tangible solutions to jump-start the global economy at a series of five summits from Washington in 2008 to Seoul in November 2010.

The G20 Summit in 2012 is to be held in Mexico in June. With uncertainties at fever pitch on a further deterioration of the eurozone sovereign debt crisis and a double-dip recession of the world economy, the G20 leaders have little scope to present viable policy options. The Mexican Ministry of Finance and Banco de Mexico held a G20 high level seminar on Dec. 12 and 13, 2011 to debate the 2012 G20 agenda.

The G20 discussions this year are expected to take the following direction. First, the creation of global demand to ensure strong and sustainable growth is seen as the biggest issue. It is very likely that Mexico will steer the discussion toward growth promotion policies to heighten productivity involving long-term structural reforms and to unwind global imbalances by exchange rate adjustment.

Second, the discussion about the expansion of the IMF resources will be continued as an effort to strengthen the international financial architecture. The increase of IMF resources, which failed to be agreed to at the Cannes Summit, is expected to be on the agenda for this February's G20 meeting, with a divergence of opinions between the eurozone countries on the one hand and the emerging economies and non-eurozone advanced economies.

Thirdly, on financial regulatory reform issues, the emphasis is expected to be on countries' implementation of Basel III and the regulation of systematically important financial institutions (SIFIs), shadow banking and OTC derivatives.

Fourthly, the development agenda is likely to be discussed mostly in relation to green growth, climate change and food security.

As the premiere forum for the world economy, the G20 Summits are very important for Korea. They provide the opportunity to make its voice heard in a process of policy discussion and reconciliation bringing together the major advanced economies and emerging economies. Since Korea is not a member of the G7, the G20 is a platform open to us for international policy cooperation and we should press emphatically for it to take over some aspects of the G7's role.

At the upcoming G20 meetings in Mexico this year, we should build our policy capacity to further our national interests and to serve as a bridge between the advanced and the emerging economies. Also, we should steadfastly advocate a strategy of win-win growth, expanding domestic demand ourselves while strengthening export competitiveness. Thirdly, we should take an active initiative on further strengthening financial safety nets, improving macro-prudential policy framework and green growth. We cannot look to be welcomed across the threshold of the advanced economies without having scaled the heights of the G20.

Kim Jae-chun is a deputy governor of the Bank of Korea.