The remaking of Europe needed

GLOBAL ECONOMY

Mauro Guillen
Wharton School professor of management
Emilio Ontiveros
Universidad Autónoma de Madrid professor

The world enters the year 2012 awaiting a solution to the European crisis.

The decision by the European Central Bank to offer a 36-month liquidity facility for banks, for the first time, and the decision by the European Council to take steps towards tighter fiscal integration have been well received by financial markets.

The twin and interrelated problems of sovereign debt and deteriorating banking assets seem less acute now than a month ago.

If the single currency is to survive, there is little doubt that some form of fiscal unity needs to be accomplished. Such a union would signal to bondholders that they do not need to be so concerned about insolvency in the long run. It also reduces the risk that yet another country will need to be bailed out or to restructure its debt.

The good news on the financial front, however, may not be enough to spare the eurozone from entering a recession in 2012.

In part, the downturn is being caused by excessive fiscal austerity. In spite of the quantitative easing by the European Central Bank, credit conditions have not improved enough to help businesses invest and create jobs.

In countries in which households and firms depend on bank credit to a greater extent, the recession will be longer and deeper.

Credit is the lifeblood of the market economy. New innovative firms like the ones envisioned by Joseph Schumpeter as the engine of growth cannot play their role without credit.

> While Europe sorts out its internal problems, the rest of the global economy must think about alternative mechanisms for global growth.

A European recession will affect the global economy as a whole. The European Union represents some 30 percent of total the global output and nearly 35 percent of consumption. Countries that export manufactured goods or natural resources will suffer slower demand and possibly falling prices.

Asia, in particular, stands to lose the most, unless major economies like Japan, South Korea and China prop up their domestic consumption.

Europe's response to the sovereign debt crisis is in part limited by the fact that not all 27 member countries agree on what is needed to overcome the difficulties of the present time.

The United Kingdom has already announced that it is not in favor of tighter fiscal and political integration.

The parliaments of other member states may also impose limits or simply opt out. Rather than abandon these plans altogether, it would be better for Europe and for the global economy if a core group of countries, those in the monetary union, take steps toward more integration.

These important political decisions must be made during a time of crisis, when voters are disillusioned by the functioning of European institutions.

While Europe sorts out its internal problems, the rest of the global economy must think about alternative mechanisms for global growth and ways to encourage the Europeans to overcome their problems sooner rather than later.

The global economy needs a renewed commitment to free trade. It also needs the emerging economies to develop their domestic consumption markets faster, allowing their citizens to buy goods and services more freely. Otherwise, Europe's problems could easily become the world's.

Mauro F. Guillen is Director of the Lauder Institute at the Wharton School. Emilio Ontiveros is President of AFI and a Professor at Universidad Autonoma de Madrid.

Risks lie ahead for Korean economy

MACRO ECONOMY

Lee Myong-hwal
Director and senior research fellow
at Korea Institute of Finance

The year 2012 is one of the black dragon. Coming around once every 60 years in the lunar calendar, the Year of the Black Dragon has a special place in Korean history. The 1592 Japanese invasion into Korea is one example.

In 2011, the Korean economy experienced a slump, mainly due to global risk factors such as the eurozone's fiscal crisis, downgrade of the U.S. credit-rating and a delay in its economic recovery.

Unfortunately, the outlook for the Korean economy isn't any better for 2012. The eurozone's fiscal crisis will continue to slow Korean exports, and excessive household debts will weigh on domestic demands as would North Korea-related geopolitical risks.

These factors are expected to combine to produce an economic growth of only 3.7 percent in 2012, lower than that of 2011.

Korea's consumer price index (CPI) is expected to fall to about 3.1 percent as international oil and other commodity prices stabilize and global and domestic economies are slow to recover.

But due to the "transition effect" of high oil prices in 2011 that is still keeping Korea's underlying rate of inflation high, CPI is expected to be higher in the first half than in the second.

Korea's current account surplus is also expected to be down to about $12.8 billion as export growth slows along with the global economy.

Entering 2012, the continued flight-to-quality will most likely keep the value of the Korean won low against the U.S. dollar, but a steady reversal in global risk appetite and an economic recovery in the second half will raise the annual average exchange rate to around 1,100 won to the greenback.

> A protracted U.S. economic recovery can also weigh on the Korean economy, and so does the possibility of a hard landing in China.

Several global and domestic risk factors could bog down the Korean economy in 2012.

The eurozone's fiscal crisis poses a global risk that looks like it won't be going away anytime soon, which may cause instability in financial markets and a subsequent contraction in the real economy.

A protracted U.S. economic recovery can also weigh on the Korean economy, and so does the possibility of a hard landing in China.

With international restrictions on Iran, higher oil prices cannot be ruled out as it has the potential to fuel instability in the Middle East.

Domestically, the excessive level of household debt has the potential to deepen the economic slowdown by discouraging consumption and this could raise unemployment and hold down income growth, lowering the ability of households to service debt.

If this vicious cycle continues, Korea's household debt problem can spin out of control.

And since the sharp rise in household debt is largely concentrated in the non-banking sector, precautionary measures should be taken especially against any further deterioration of household debt by multiple, heavy borrowers.

In regards to foreign exchange risks, the eurozone fiscal crisis could trigger another liquidity shortage and fan risk aversion in the global financial markets.

With European banks having to recapitalize before June 2012, Korean banks could face foreign exchange liquidity challenges if European banks either deleverage or repatriate funds from emerging markets.

Korea's foreign exchange market will likely see heightened volatility as the exchange rate responds sensitively to any geopolitical developments coming out of North Korea.

In the longer term, issues surrounding Korea's fiscal soundness will likely come into force due to growing pressures to increase fiscal expenditures for social welfare programs.

In addition, Korea's low birthrate and an aging society are long-term economic headwinds that are holding back Korea's potential growth and increased employment.

Man in charge

What is your dream for the Year of Black Dragon?

Park Se-joon
Amway Korea president

We have just entered the new year of 2012. It is a Korean tradition to assign 12 different animal signs — cow, tiger, horse, monkey, and others — to each year in rotation.

This year is the Year of the Black Dragon which comes around every 60 years. In the East, the mystical imaginary animal is thought to have royal traits and appears in stories as a divine animal with goodwill. The black dragon, in particular, is considered the best of the kind, and there is a mythical belief that in the year of black dragon, babies with divine spirit are born.

Everybody has his or her own new year's wish, and many Koreans like to go to places where they can get a stunning view of the rising sun for their little wish-making rituals. In a survey by a Korean job portal asking people in their 20s and 30s about their new year's wishes, 45.6 percent of the respondents said they wanted to find work, get a promotion or change jobs.

As for the words of blessing they would like to hear most, every second person said "make lots of money." We can see that the tough conditions in the job market and consequent financial difficulties are one of the biggest problems facing our young generation.

The problem of unemployment is becoming a serious social issue that we now have a neologism "spec-poor" — short for "specification poor" referring to qualified graduates who have high English test scores and excellent academic records from reputable schools but still struggle to find jobs. Young Koreans of today are all in competition to secure better "specs," missing out on all romance and experience they deserve. On top of that, the global financial crisis hasn't made things any easier.

This is an agonizing situation for our youths. A survey found that eight out of 10 college students are obsessed with "spec" improvement and suffer from depression, lethargy, indigestion and other stomach disorders, headache, sociophobia and insomnia, among other conditions.

In order to resolve this problem of unemployment, the government, citizens and businesses must all join forces. Action is particularly required action on the part of businesses as important members of the society. It is the role and indeed responsibility of businesses to provide young people with more practical opportunities and substantial help to reach out to the world.

Employing talented people is also in the interest of businesses themselves for developing and managing human resources, one of the most important factors of corporate management. For example, companies can partner with universities to organize training specific to the demand of the industry. They should also absorb the young workforce by offering more internship opportunities. Global companies with sound infrastructure for nurturing talents must also take responsibility and initiative to address the issue of youth unemployment.

To this end, my company, Amway Korea, introduced a global internship program last year through which we have been hiring outstanding interns as our regular employees. Our one-on-one mentoring program, in particular, has helped provide hands-on training in a systematic way.

In addition, the trainees were given an opportunity to visit the headquarters of Amway Global in the U.S. where they worked with local interns on global projects, thus helping to improve their leadership skills.

Many economists are putting forward negative prospects for this year, and it looks like the unemployment problem is not going to be easy to tackle. Despite these circumstances, however, I would like to offer one piece of advice to young job-seekers: give plenty of thought to and maintain a clear vision about "your dream" instead of searching for security only. Encouraging young people to choose jobs as a means of fulfilling their dreams and to prioritize meaningful experience over the size of the company would be the key to reducing the level of youth unemployment.

The focus of Amway Korea's global internship program, therefore, is on helping young people who are embarking on their careers to develop and unleash their potential, rather than turning the spec-poor into the spec-rich. We are doing so in the hope of sending a message that those who work hard with a clear vision and goal will succeed.