Euro-vulnerable banks

GLOBAL ECONOMY

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The crisis did not originate in Europe, but it is proving most severe and intractable there. In terms of the real economy, Europe is registering the worst declines in output, highest unemployment, and highest rates of company bankruptcies.

In the financial sector, the convulsions in the market for European government debt are without precedent among developed countries, and the fragility of the banking system is worrisome.

Neutralizing the financial problems is crucial to the economic recovery. The stability of the eurozone is also at stake. The very viability of the common currency is now in question.

Banks in Europe are under pressure not just because of their exposure to bad loans to construction firms, real-estate developers and households. All banks in Europe continue to suffer, in spite of the help that both governments and the European Central Bank have made available to them since the beginning of the crisis. Italian and Spanish banks are among the worst hit, although the government has not yet had to rescue any of the biggest ones.

The situation in these countries is especially delicate because banks are the biggest intermediaries in the financial system. Unlike in the U.S. or the U.K., banks are the most important source of funds for companies, given the relative underdevelopment of the markets for corporate equity and debt.

It is not surprising that Italian and Spanish banks have taken advantage of the European Central Bank's funding lines to a much greater extent than other eurozone banks.

This effort to shore up their balance sheets has amounted to not much more than a "placebo effect" because of the devastating combination of financial problems and slow growth in the economy.

It is important to keep in mind that a significant share of the funds obtained by European banks from Frankfurt has been used to purchase government bonds.

Nobody expects moving forward the European Central Bank to offer such attractive funds to the banks in terms of the magnitude and the nature of the collateral. As a result, both the market for public debt and the market for bank equities are in for a slide.

Therefore, the trend is for a national compartmentalization of the market for government debt in Europe as more of it is held by banks of the same country, just the opposite of what many economists and analysts think would be necessary to save the euro.

This represents a most paradoxical situation in that the way in which the European Central Bank has intervened is having the effect of undermining the long-term viability of the common currency.

The perverse relationship between banks' balance sheets and the market for public debt in Europe creates a conundrum for the credit rating agencies.

They are concerned not only about the vicious cycle resulting from the increasingly domestic character of bond-holding within the currency union, but also about the lack of economic growth and the return to recession of several economies.

After nearly four years of crisis, it seems reasonable to predict that debt obligations won't be met without economic growth.

The IMF has noted that further deleveraging might lead to a deepening of the recession. Banks' core capital ratios will continue to deteriorate due to higher rates of non-performing loans, and we still have not figured out how to jump start wholesale financing for banks.

If bank recapitalization is necessary to generate confidence and to help credit flow to the real economy, someone must provide the funds.

Right now, with banks priced at 40 percent of their book value on average, the only source of fresh funds is the government, which takes us back to the problems in the market for public debt.

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Corporate tax and economic growth

STRATEGY

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Back to business as usual. The election is over. The new members of the National Assembly were chosen. Sooner or later, one of the political hot potatoes will be back on the table, again — corporate tax. Korea's top corporate tax rate is 22 percent.

The bone of contention is whether the current rate should be cut as promised or raised. The real question boils down to whether it makes the country a globally competitive place for investment.

The world's average corporate rate was hovering at almost 50 percent in the early 1980s and is now at around 25 percent. This is a result of an aggressive tax rates competition that has been ongoing over the last three decades. The trend has been one of the key contributing factors behind world economic growth over the same period. It's a fact not an argument.

To make the story simple, the truth is that investment is the key to sustainable economic growth. An investment decision is a long term one. We know the corporate tax rate has always been a key decision factor. Earnings mean "after-tax" profits at the end of the day.

That's why companies care about the rate. That's why our rate needs to remain and be kept competitive. Our economic future is at stake.

Who are our main competitors? It is obvious that we are not competing with the U.S., Canada, Japan or the U.K. We might do so in the far future but not in the foreseeable one.

We compete with Hong Kong, Singapore, Taiwan and potentially fast-growing Southeast Asian countries. It's a fierce competition. In recent years, Hong Kong cut the rate to 16.5 percent and the rates in both Singapore and Taiwan were reduced to 17 percent.

Korea is falling behind the competition. We need to do something about it, sooner than later. A sense of urgency and follow-up efforts are what we need now.

Above of all, a clear message should be sent about the goal and the competitors. The short-term goal is to make more investment, whether foreign or domestic, in Korea. The long-term fruit is a no brainer.

For that to happen, Korea should remain competitive enough to attract global players to the country. And we need to keep the corporate tax as competitive as at least those of our immediate competitors — Hong Kong, Singapore and Taiwan.

Twenty-two percent is at least 5 percentage points above. It's not competitive.

We should not underestimate a prediction that Asia is already leading the global economy. That's why Korea should be at least one step ahead of the curve.

The rules of the game should be made and kept transparent and predictable. What we hear quite often from multinational companies in Korea is that overall environment has improved but is still far from international standards.

They complain that public employees often go too far and tend to cross the line. It seems to them that Korea is not ethically competitive. This negative image about ethical standards should be improved quickly with real and serious efforts.

Global tax competitiveness is all about jobs and growth. It is not a symbolic or rhetoric issue. It's a question of "lead or perish."

The policy of today shapes where our economy will be tomorrow. When our policy is announced, it's a promise to the global business community.

If our promises are made to be broken, they won't be trusted. It's important for lawmakers and the government to make sure that our economic future is not something that can be on the table for political bargaining. We should never forget that our jobs and growth are at stake.

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Woman in charge

Going global

Chae Eun-mi
Managing director of FedEx Korea

We've reached a tipping point in how the world works. The largest economy in the world is no longer the economy of any one country — it is the economy of the global trade of goods and services.

Countries making an impact in the world of global trade are those connected to the global mainframe, not those that operate within the silos of their national geographies. Global trade has accelerated the formation of one world, one marketplace; a place where boundary-free commerce relies on worldwide connectivity.

The characteristic of global trade is also changing. Formerly small traders are becoming major trading powers, and trade is occurring with countries outside the traditional players. The biggest change is that an increasingly large part of world trade is comprised by trade with and among developing economies.

Since 1995, the United Nations Conference on Trade and Development has kept detailed data on the source and destination of exports. The data indicate that the proportion of exports originating in the developed world and the developing world stayed the same until around 1999. In other words, exports from both were growing at the same rate.

Since 1999, however, the developing world has been catching up. The developed world still grew: Between 2000 and 2009, total developed country goods exports rose by 66 percent. For developing countries, however, the figure was 147 percent.

Why so much emphasis on global trade? It helps businesses become more competitive by providing opportunities to expand businesses worldwide.

We cannot and should not stop this trend, but we can leverage the trend to strengthen our economic recovery, generate growth and create jobs.

There is no denying that Asia has become central in the world economy with the rapid growth from developing countries like India and China.

China will surpass the U.S. by 2017 in purchasing power parity terms and will account for twice the America's share of imports and exports by 2030, according to The Economist's forecast.

India is expected to become the third-largest economy next year. Aligned with the recently ratified KORUS FTA, Korea is also striving to further its status as a global trade hub sharing markets with the U.S. along with the ASEAN and EU pacts.

The increasing trend to trading across the border is beneficial to Korea because many of domestic business will be given an opportunity to become a major player in the global trade market.

Particularly, small- and medium-enterprises (herein, SMEs) in Korea are expected to experience a significant growth. According to a study by the Small and Medium Business Administration, in the year the KOREU FTA was ratified in 2011, exports from domestic SMEs to Europe were increased by over 18 percent.

Add to that the FTA between Korea and the U.S. is expected to create a $1.38 billion trade surplus for Korea, according to the Korea Institute for International Economic Policy and the Korea Development Institute. More specifically, SMEs in auto parts, textile, and electronics industries are expected to promote export and global business more vigorously.

Global trade is at the very heart of FedEx business. Our network is a critical enabler for the global supply chain. By facilitating global connections, FedEx believes when individual countries enable trade, they benefit not only to themselves, but also other nations with which they trade.

By improving market access and working to provide efficient customs procedures, FedEx contributes to enhanced opportunities for both importers and exporters.

In this increasingly crowded marketplace, being globally competitive requires having a global mindset and prioritizing connections. With access to the internet and access to FedEx, businesses can sell goods and services and find suppliers in virtually any market.