Why rates will likely rise in Korea?

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ECONOMY

Domestic industries should benefit from low unemployment and expansionary monetary and fiscal policies. Rising consumer confidence should filter through to a pickup in consumer spending, while the government measures to support housing demand should help boost home prices in 2014 after they declined in 2013. Faster GDP growth in 2014 will help reduce the output gap and lift prices. Low headline inflation and core price measures are increasing, which should help the dollar should help strengthen some of the pressure that exporters are facing from a weakening yen.

Korea enjoys solid investor demand relative to troubled Asian countries such as India and Indonesia because it follows the financial-system following the 1997-98 Asian financial crisis and has boosted foreign reserves and lowered external debt. Lower financial risk makes the ROK can focus on economic and price stability. The ROK will be concerned about slower growth rates, but not for too long for fear of causing financial imbalances, particularly after the credit and housing bubble during the 2000s. A forward-looking central bank should also preemptively hike rates as inflation accelerates to prevent it from becoming a bigger problem down the track. That said, risk to this forecast is to the downside. The falling yen is creating much angst among Korean authorities and the country’s exporters. Further yen weakness could thus erode Korea’s export competitiveness and cut profits. But we have been here before, and the central bank will probably intervene in foreign exchange markets to try and stem the currency’s gains and reduce volatility rather than cut rates.

Currency appreciation also has a negative impact on Korea because the world’s most intensive oil consumers and relies on imported petroleum, a stronger won should help lower the import bill and support manufacturing. It should also help rebalance the economy toward domestic growth, which could reduce Korea’s exposure to external shocks. Businesses can focus on cutting costs, innovation and improving productivity to drive growth, something President Park Geun-hye has been promoting recently. The bottom line is that rising rates are the result of a strengthening economy, which is a positive development.

GLOBAL ECONOMY

Juggling from theeltroping fevered financial markets around the world, it seems that 2014 will be one of the best years ever for global economy, and certainly the best since the beginning of the Great Recession. The surge of economic recovery is due to the major factor that the New Year inherited from 2013, especially in Europe. Risk premiums on the debts of the peripheral economies have come down steadily, and bond yields have recovered from their all-time lows.

Most economists anticipate that the global economy will grow at least one point percentage faster than in 2013. The renewed dynamism of the U.S. economy, notwithstanding recent rags in the employment outlook, will be a determining factor. In addition, Japan is also showing signs of becoming a sustainable contributor to global growth. Still, China continues to be the world’s most important source of growth. China continues to power higher on Europe and the United States.

In spite of the fact that the worst is probably behind us, one cannot be too optimistic about economic growth. The policies being implemented by most countries continue to be frustrated, mostly because austerity measures in a situation of extremely high unemployment and inflation with aftermath below one percent. The政策措施 at the national level continues to be on balancing budgets and repairing fundamentals, while at the European level most of the efforts are aimed at laying the foundations for a banking union.

A major topic in the spring session of the World Economic Forum that Europe is entering a phase of “secular stagnation”. This is the biggest fear among many observers and policymakers. It will take more than two or three years for austerity to deliver its promise, and the likelihood of a recession that might be more than 1.5 percent is not out of the question. The policy may not have the necessary fiscal and monetary stimulus that the world needs.

Meanwhile, the European Central Bank has recently indicated its willingness to tackle deflationary stagnation through the use of exceptional monetary policy tools. In countries where domestic demand is strong and the external sector can deliver growth in the short run. With a strong euro, this is difficult. Another option is to increase supply, offering a threat of supply-side economics, Germany prominently may be an example to others concerning ways to as stimulate demand from the European periphery.

The truth of the matter is that, in addition to Europe, the US continues to grow well below potential. In spite of the rise of oil prices, interest rates, investment is not growing fast enough to strengthen the stock of capital and to boost employment. The other danger is to see a new asset bubble emerge. Analysts wonder whether stock prices are reaching bubble-levels. Meanwhile, the real estate market has staged a strong comeback, with prices just 6 percent below the level in the first quarter of 2006. Higher and more stable levels of equity home may boost a nation in the form of greater consumption to be household.

One of the most dangerous threats to global stability lies in the level of private debt in China, a country that still lacks a modern banking system. Thus, there are many reasons to be concerned about the optimism of financial markets in the New Year. Significant risks remain.

Recovery or secular stagnation

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