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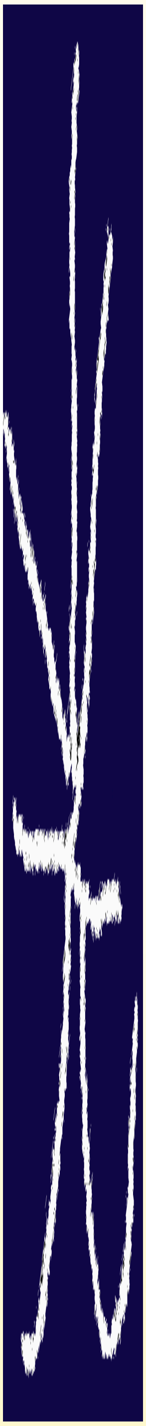

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THE FINANCIAL CRISIS: ADDRESS STRUCTURAL PROBLEMS IMMEDIATELY

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The subprime loan crisis triggered by the burst of the American housing bubble is rapidly spilling over to the global market and the real economy, causing serious damage to both. The global economy, which just in 2005 enjoyed the greatest prosperity since the end of World War II, has suddenly hit a downturn, with 2009 expected to be the worst year in the post-war period.

Countries around the world are making utmost efforts to normalize financial markets and pull their economies out of the slump by mapping out various financial and fiscal policies. However, it will only be after 2010, at the earliest, that the global economy will show signs of recovery.

The current crisis is a historic experience in terms of the dramatic speed at which it has degenerated and the impact its damage has caused. Equally important is that the crisis is directly linked to medium- and long-term structural problems in the global economy. A huge mountain lies behind the crisis. The structural problems are fourfold.

The first is global imbalances. For the past decade and more, the huge household consumption of the United States has generated worldwide demand. On the other hand, the expansion of the US current account deficits had intensified international capital exchange. Together these created a boom in the global economy. The world had gained from the expanding global imbalances even while alarmed by them. The crisis has put an end to this fragile boom. US households can no longer afford to fall deeper into debt to continue spending. On the other hand, Asia, Europe and the Middle East can no longer expand their exports on the back of US consumption. How should the over-consuming and over-saving countries each change their growth models and industrial structures? Are the plans viable?

The second is financial reform. The crisis meant a major setback for the existing paradigm of financial capitalism. Financial institutions' business models that rely on leverage must be improved. The regulation and supervision of commodities and markets without transparency and players without accountability must be strengthened. Business ethics have hit a low and must be restored. At the same time, financial protectionism and financial nationalism must be resisted. Financial reform based on the lessons learned from the experience of this crisis is of crucial significance in maintaining capitalism as a viable economic system.

The third is the future of the international currency system. For the past six decades, the global economy has operated under the dollar standard system where the US dollar served as the key currency. However, amid the rapid increase of US net indebtedness and the weakening of the US financial industry due to this crisis, the US dollar's hegemonic position as the world’s key currency is being threatened. Yet no currency is likely to replace the dollar. Under such circumstances, the instability of international currency will increase. Led by the International Monetary Fund (IMF), the international community needs to establish an international crisis management system that can respond to unexpected events.

The fourth is responding to the changing global balance of power. Economic and geopolitical factors have been undermining the unipolar world order centered on the United States. The current crisis has just accelerated the pace. The European Union (EU), the BRICs (Brazil, Russia, India and China) and oil-producing countries are increasing their influence. The global center of gravity is shifting away from the G7 framework and broadening. Above all, the rise of China has been remarkable. In a few decades, the US and China may be waging a battle for supremacy over ideology and politico-economic systems.

The current economic crisis will end eventually. Yet the world will never be the same. It is rapidly plunging into a whirlpool of huge historic change toward the middle of the 21st century. We must begin making necessary preparations as early as possible.

The G5 and G7 that once led the global economy are no longer groups exercising leadership with adequate capabilities and authority. However, the newly created group of 20 countries that met in Washington, DC last November (G20) is not perfect either. This is because the members of a group expected to play a leading role must possess not only some influence on the global economy but also the will and ability to contribute to the development of the global economy. However, we cannot afford to waste time now on trying to create another forum that might best serve the purpose. We have no choice but to find an effective way of managing the G20 by trial and error with a view to producing substantive results. The effects of the current crisis differ among the United States, Britain, continental Europe, Asia and oil-producing countries. So do the priorities of remedies.

For example, the biggest problem for Japan is not the bursting of the financial bubble but the slump of the real economy caused by the bursting of the export bubble. Therefore, the recent measures adopted by Japan to take advantage of its relatively strong financial power – such as the offer of an additional $100 billion loan to the International Monetary Fund (IMF), the provision of further finance to the Asian Development Bank (ADB) and the expansion of loans to Asian countries through the Chiang Mai Initiative – are extremely meaningful contributions to the international community.

When they meet at the London summit in April, the G20's leaders must make clear what each of them can do to expand credit and imports, the most pressing tasks facing the global economy.

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