



OECD-KDI Seminar on “Social Cohesion in Korea”

Comments on Thematic discussion notes

Room D

OECD Headquarters, Paris

Wednesday, 2nd May 2012

COMMENTS: Thematic Session 1
Income distribution and poverty among the working-age population and implications for social welfare policies

Please specify the exact definitions and data sources of the figures. Income distribution statistics are complicated and often incompatible across countries, and citations need to be precise. For example, how do you define 'working age', 18 to 64? 'Income distribution' refers to individualized yearly income for household members aged 18-64 or family income with heads in the ages? At many places I find the figures misleading. (All statistics should be from the KNSO. I noticed Going for growth 2012 includes some estimates from KLI panel data.)

Some statistics are for all ages and not for working age population. Much of international difference in income inequality is driven by generosity of pension payments. This is why we use working age income distribution or consumption instead of income. The cited Korea's relative poverty rate of 15.2% in 2009 is among all ages and not among working age.

Use one definition and avoid using income group means. The cited income gap of 10 to 1 is imprecise for the following reasons: i) it uses quarterly and not yearly incomes, ii) Income group averages especially at the top and bottom are imprecise, and iii) it uses an old income definition. The KNSO (Korea National Statistical Offices) publishes yearly incomes and their deciles from 1990-2011, which conform to OECD standards. It is recommended to use the data. Korea did not publish top 1% income share from tax returns data.

Income distribution improvement is a goal per se, and does not have to be rationalized with the need for opening the economy or holding up free market. Korea is already an open economy with FTAs with EU, US, and Chile. And I think saying that inequality threatens 'free' market is going too far. What is meant by a 'free market'? Do you mean an unregulated financial market? In an open and free economy, income equality is an important policy goal.

Causes for widening income gap are diverse and different across countries. Although there are common factors such as technology, globalization, and financial market openings, inequality development patterns are quite diverse among countries, which implies that different factors work at different degrees. [For example, Korea's income gap widening is between middle to bottom whereas the US widening is between middle and top - to be added.] Various literatures document this, where OECD publications are among them. And it is important to look into distinguishing features. Notwithstanding, this note states that it is a result of technological shift and seeks policy responses through tax and benefit reforms. I am left with an impression that diagnosis is tailored to prescription.

It is not high self-employment share but its stagnant income growth that dragged income growth at bottom. Business income share is high at top and bottom in all countries. Its share at bottom is high in Korea but I don't think it is the highest as other countries such as Turkey also have a very high SE sector. The role of self-employment is not very well understood but it does have a positive function in less institutionalized economies. (as noted by World Bank reports) It supported employment and income growth at bottom during the 1990s and contributed to equality in Korea. So it is not its high SE share but its competitiveness decline and lack of wage earning job opportunities that caused widening of middle to bottom income gap.

Whether the main driver behind rising income gaps is wage change or insufficient employment opportunities is in question. In the US mid to bottom gap stopped to grow as low skilled jobs grow, and mid to top gap enlarged with credit expansion. In Korea, bottom wage growth is solid at approximately 2% at p10

during 2000-07. But low skilled wage/salaried job growth is weak and the proportion of self-employed at bottom did not decline, widening mid-to-bottom gap. Thus income disparity is not entirely driven by technology. I do not believe either that Korea's top-bottom wage gap (p90/p10) is the highest among all OECD countries, because the shares of wage earners are still relatively small. For example, Germany has created 'one-euro' jobs. 'More and better jobs' is a tautological statement. 'Successful accomplishment of school to work transition' is another. Inequality naturally rises with ageing as gaps in earnings capacity widens with age but it is not of a policy concern.

EITC is not a major tool for tacking inequality. Not only Korea's EITC is small but also EITC generally do not significantly change inequality unless it is launched at a substantial scale. Reports from IMF and Sen-Stiglitz-Fitoussi allude, but do not go as far as arguing, that Korea's weak household income growth due to deteriorated terms of trade is related to income dispersion. We note that Greece and France are the only countries with no income gap widening in the 2000s. That is my concern for the title 'social policy implications for inequality' because implications of social policy implications cannot be anything but up-scaling social programs whereas the concern for the government is that both parties have already announced new social assistance programs amounting to 9% and 16% of GDP for the next five years in 11Apr2012 parliament election. The difference in sizes does not have much practical meaning, both being beyond what the budgeting offices are prepared for. The question is prioritizing the programs.

We have high expectations of what the OECD would suggest in the context of tax and benefit reform. The need for tax reforms has been much argued for, though the reform is difficult. Also prioritizing benefits is a pending issue. We are very curious and have high expectations upon what the OECD would put forward in this regard. Measuring redistribution effects of government spending requires a huge amount of work. I know of no recent work on this issue. Also the sources of tax and transfers statistic 7% and 2% need to be clarified. Again, provision of quality public services can mitigate effects of widening inequality but spending increase does not automatically guarantee better service provision. Child care support is a good example in Korea. Such points should be taken into account in policy suggestions.

Questions for discussion

- *How is Korea's inequality widening distinguished from those in other countries?*
 - *What policy framework is needed to alleviate the trend?*
- *How can Korea improve the redistributive power of its tax-benefit system?*
 - *Which tax and/or benefit reforms are the most promising to enable greater redistribution without unduly blunting incentives?*
- *How can the social safety net be improved and should the focus be on adequacy of benefits or access to them?*
 - *How should the social policy programs be prioritized?*
- *How can Korea improve the role of in-kind public services, such as health, education, housing and care services to reduce inequality?*
- *What should be the direction and strategy of reforming the existing social safety net?*