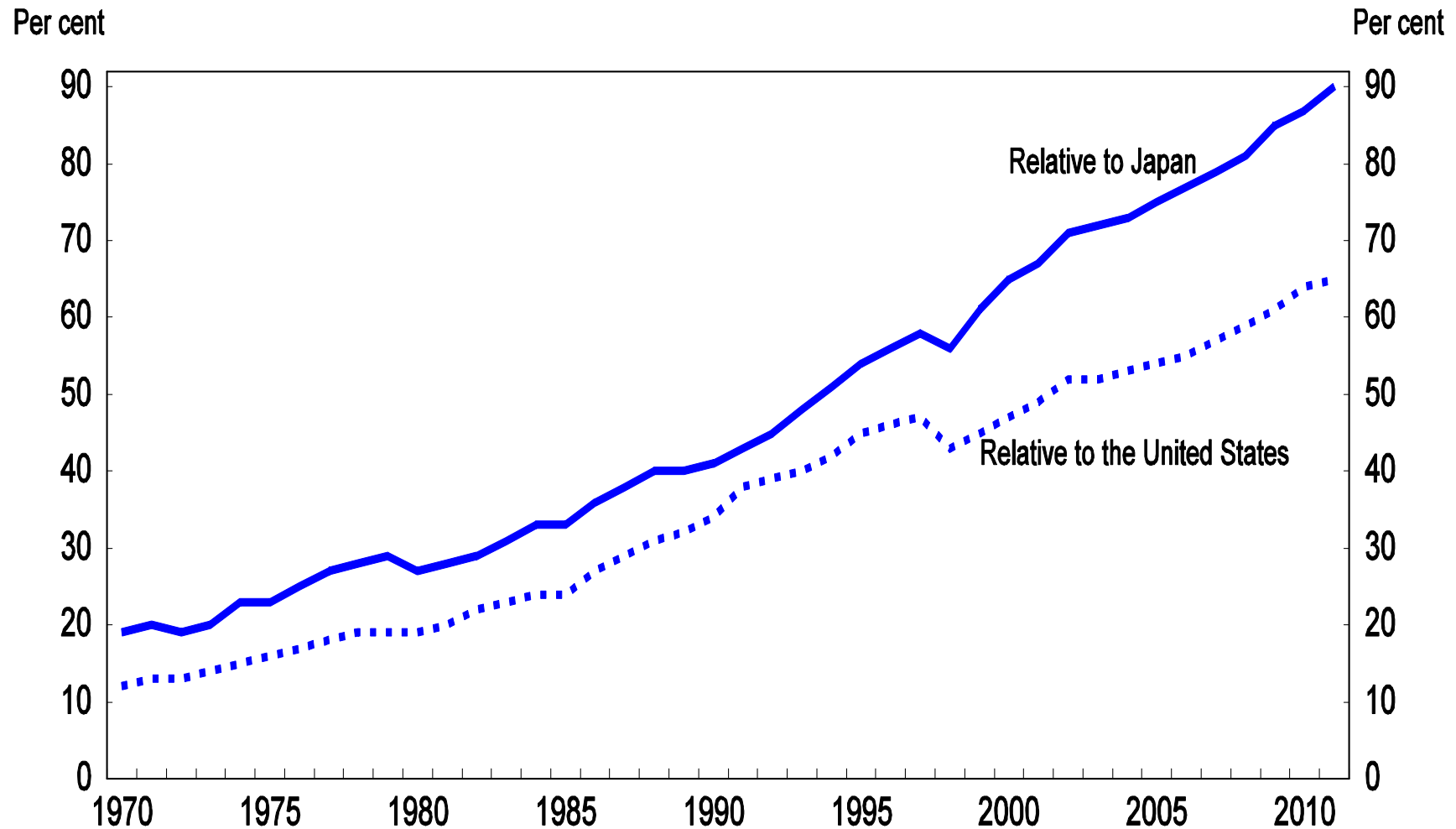


# **Enhancing social cohesion in Korea**

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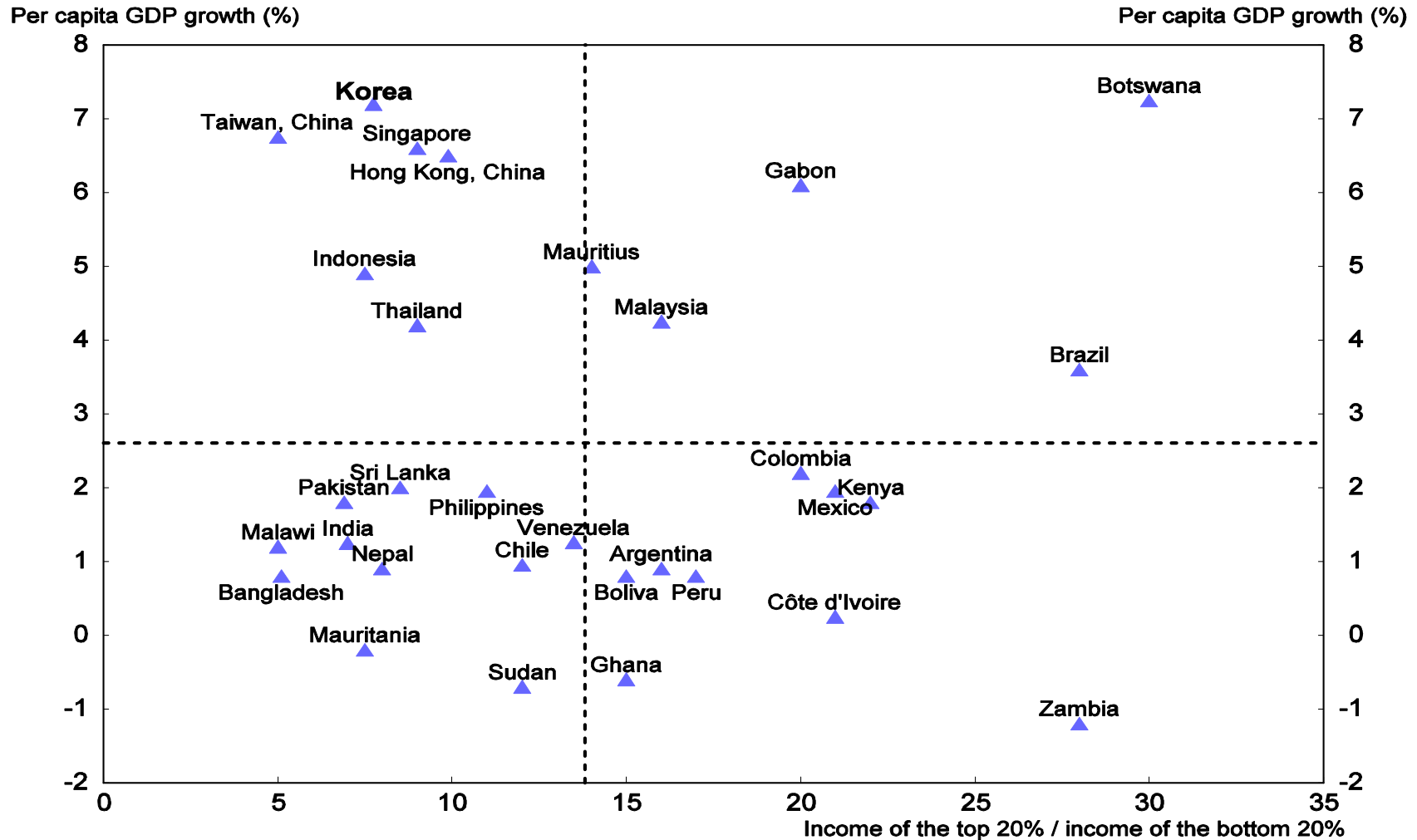
# Korea's per capita income is converging rapidly to the high-income countries<sup>1</sup>



1. Using 2005 purchasing power parity exchange rates.  
Source: OECD (2013), *Going for Growth 2013*, forthcoming.

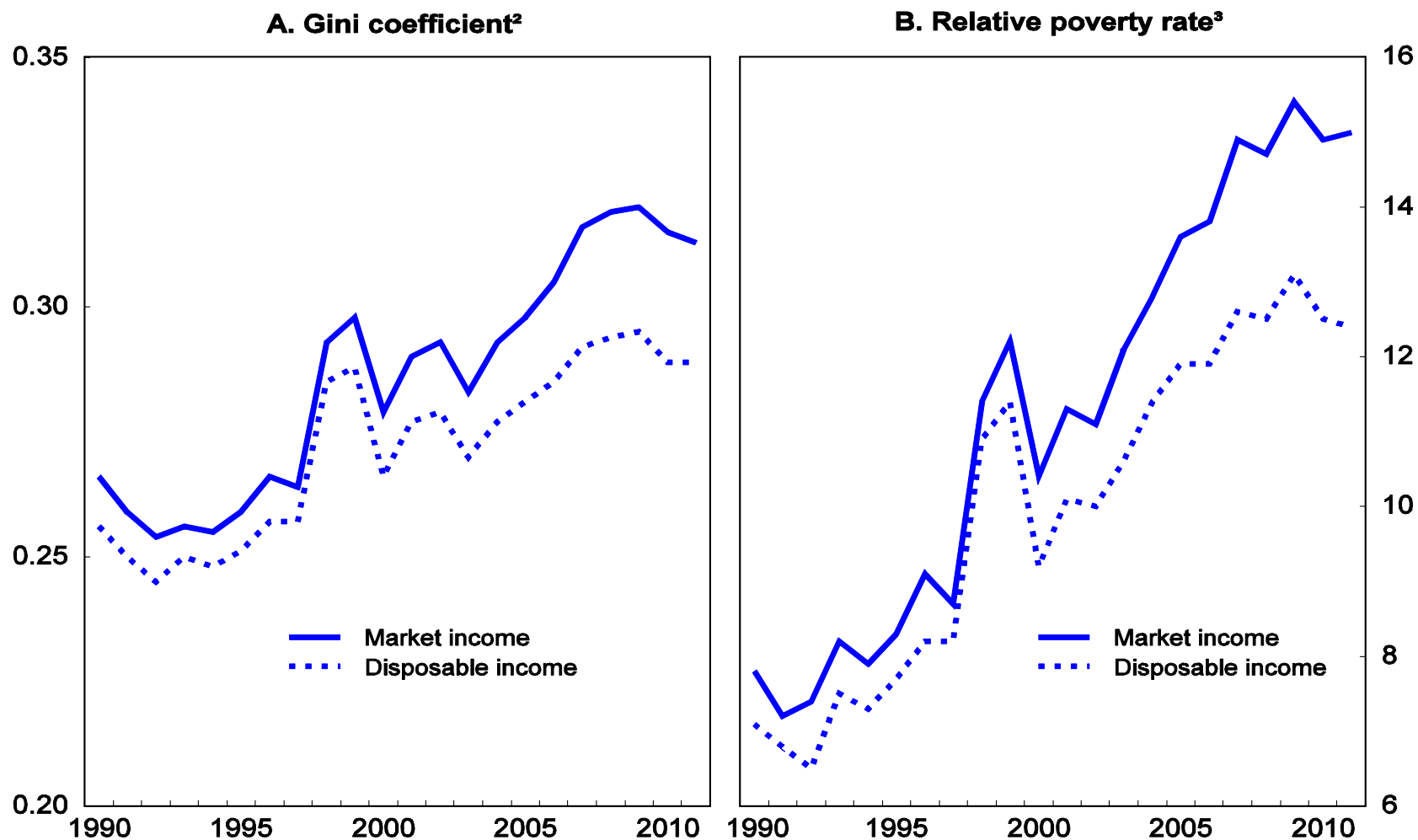
# Korea combined rapid growth with an equitable income distribution during its high-growth period

Between 1965 and 1989



Source: World Bank (1993), *The East Asian Miracle: Economic Growth and Public Policy*, World Bank Policy Research Reports, Oxford University Press, 30 September, Washington, DC.

# Inequality in Korea has been increasing since the mid-1990s<sup>1</sup>



1. For urban households with at least two persons.

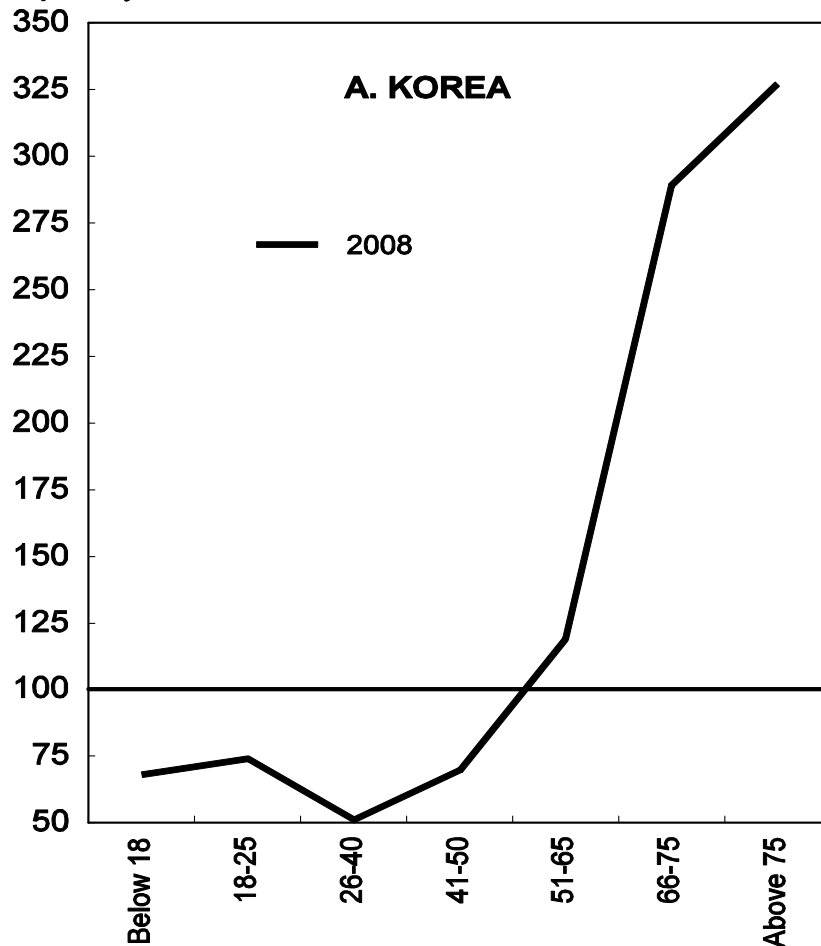
2. The Gini coefficient can range from 0 (perfect equality) to 1 (perfect inequality).

3. Relative poverty is defined as the share of the population that lives on less than half of the median income.

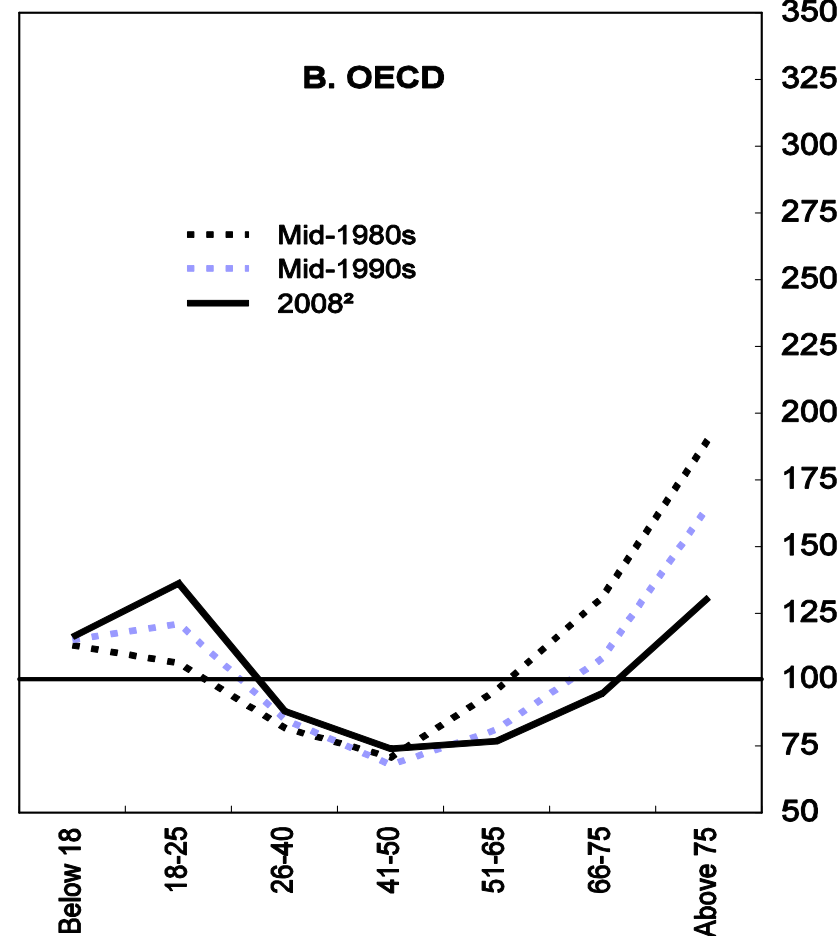
Source: Statistics Korea.

# The poverty rate in Korea is exceptionally high among the elderly<sup>1</sup>

Total poverty rate = 100



Total poverty rate = 100

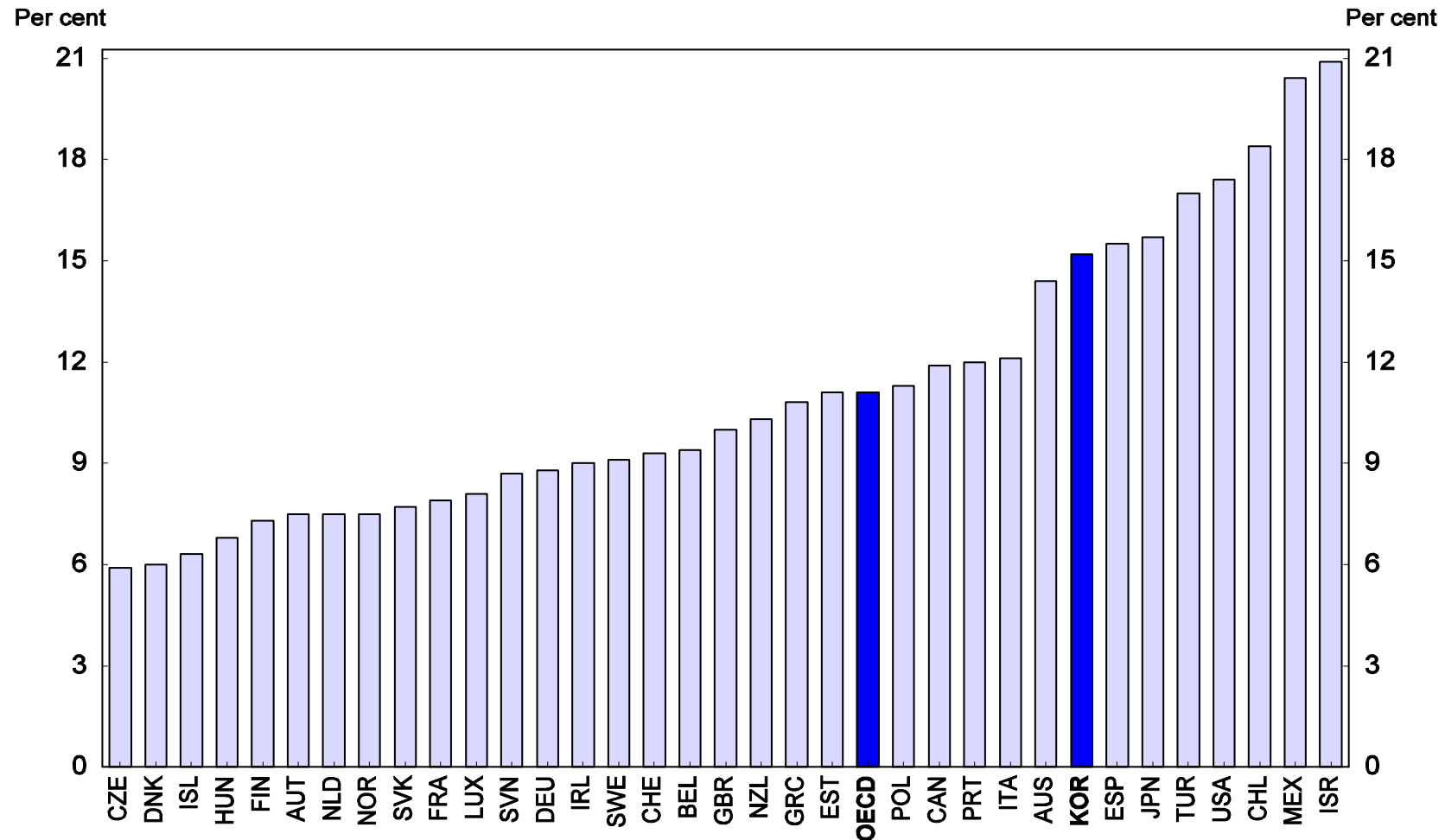


1. The figure shows the poverty rate for each age group using an index, with the rate for the entire population set at 100. The poverty threshold is set at 50% of median income of the entire population. The OECD average includes 20 member countries.
2. Data refer to the most recent year in the late-2000s (2008 for most countries).


Source: OECD Database on Income Distribution and Poverty ([www.oecd.org/els/social/inequality](http://www.oecd.org/els/social/inequality)).

# Korea's relative poverty rate in the eighth highest in the OECD

In per cent of total population in 2011 or latest year available<sup>1</sup>



1. The poverty rate is defined as the share of individuals with equivalised disposable income less than 50% of the median for the entire population. The income concept used is that of household disposable income adjusted for household size. Data for Chile are for 2009.  
 Source: OECD Database on Income Distribution and Poverty ([www.oecd.org/els/social/inequality](http://www.oecd.org/els/social/inequality)).

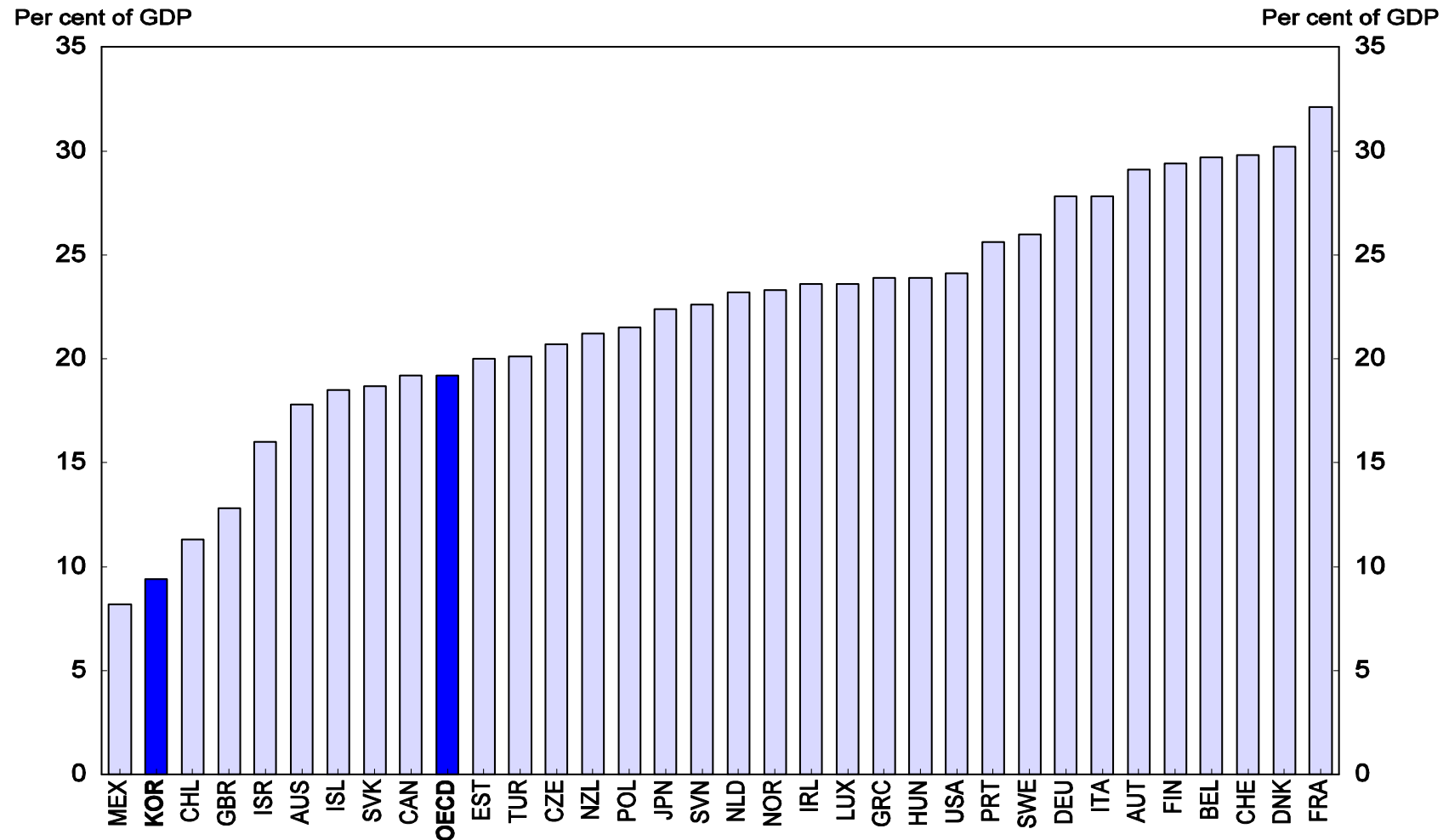


As Korea has become increasingly integrated in a globalised economy, it has faced many of the same forces that have led to rising inequality in other countries. Yet, Korea stands out for a number of reasons:

1. Its low level of social spending, which has only a small redistributive effect.
2. Labor market dualism results in large wage gaps between regular and non-regular workers.
3. Low productivity in services, leading to large wage gaps.
4. A high level of private spending on education and health.

# Social spending is low in Korea

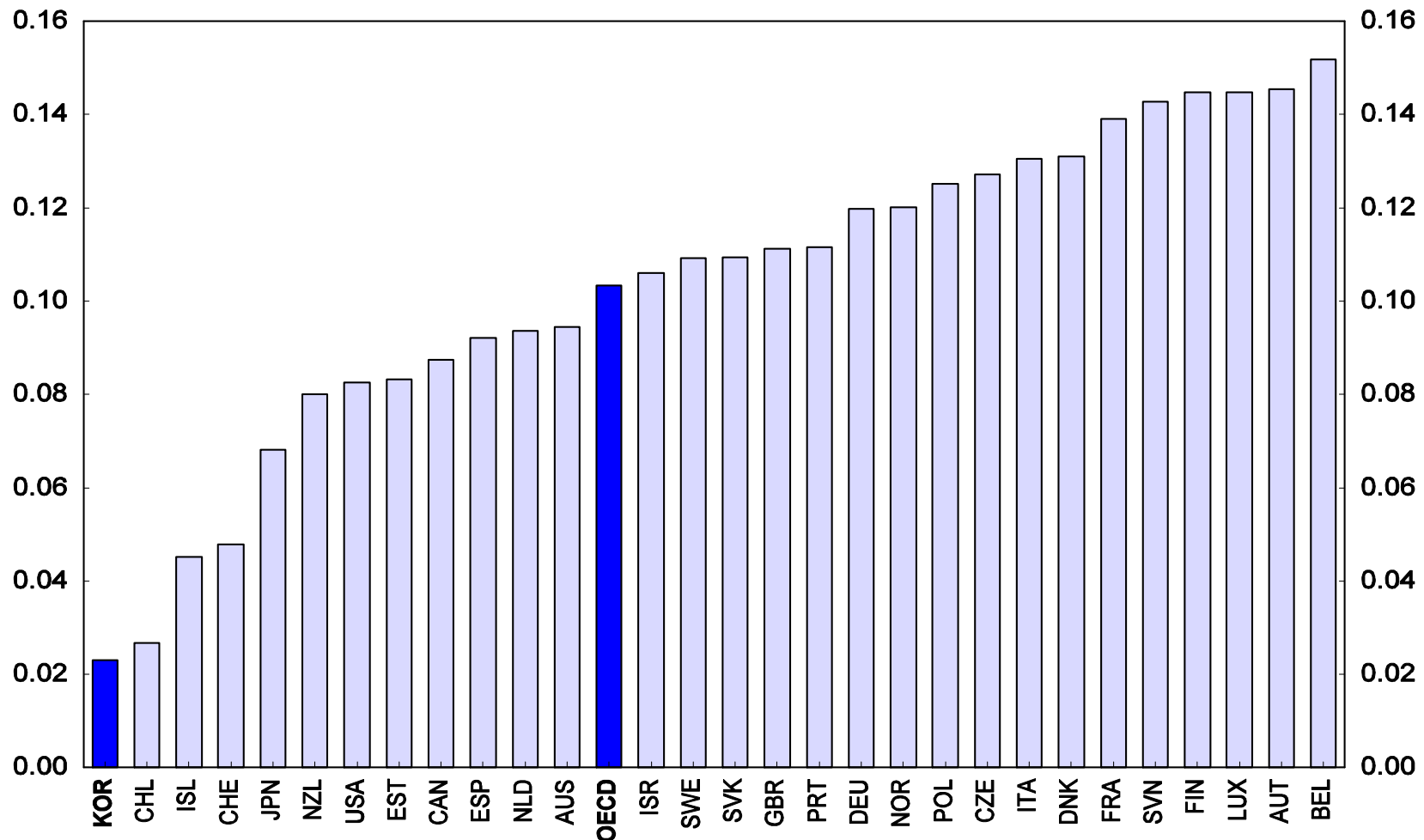
As a per cent of GDP in 2009



Source: OECD Social Expenditure Database.

# Social spending has little redistributive impact

Difference between inequality of market income and disposable income based on the Gini coefficient in 2008



Source: OECD Database on Income Distribution and Poverty ([www.oecd.org/els/social/inequality](http://www.oecd.org/els/social/inequality)).

# Korea's dualistic labor market is segmented between regular and non-regular workers

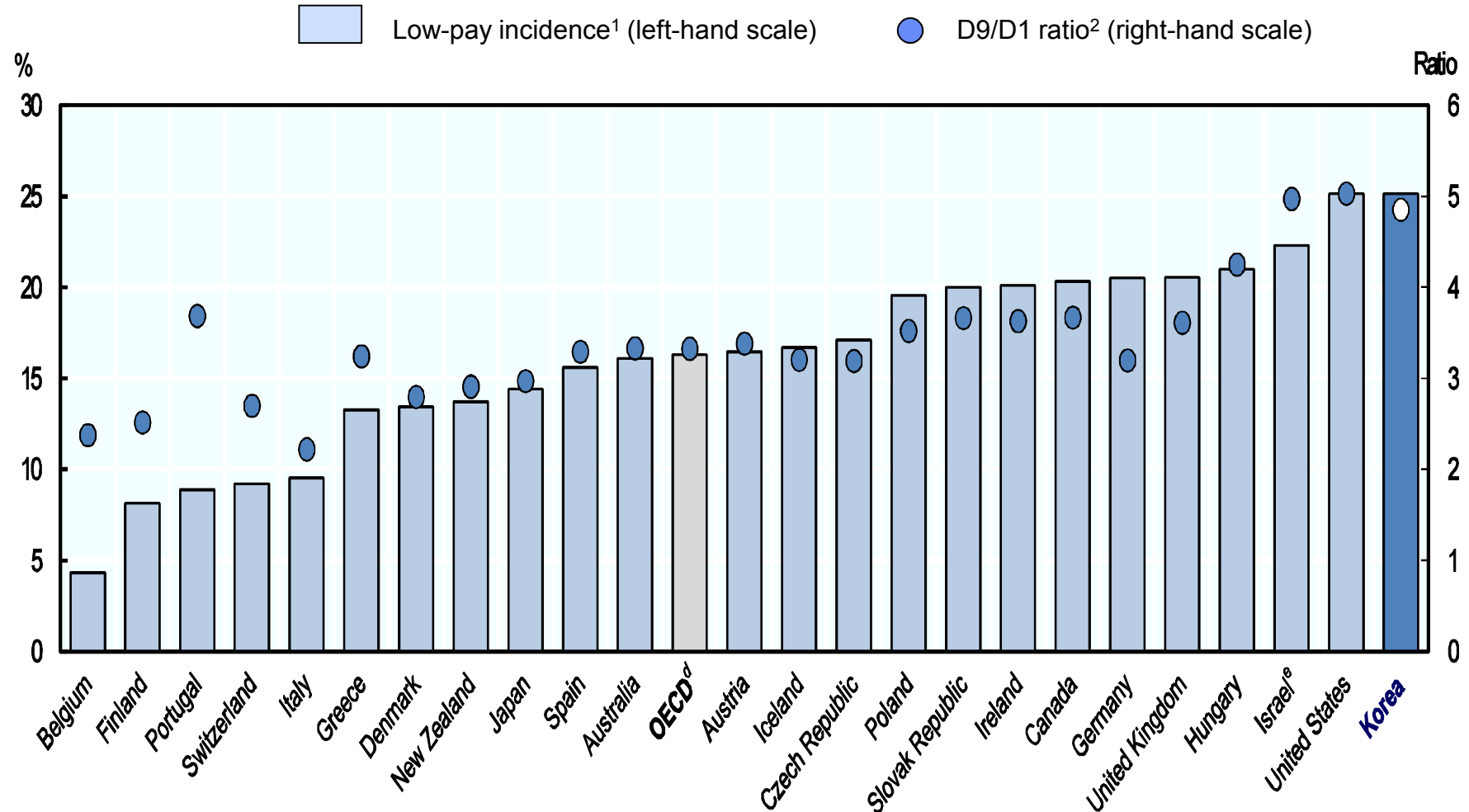
Year	Wage workers	Non-regular workers		of which <sup>1</sup>					
				Temporary workers			Part-time workers	Atypical workers	
				With fixed-term contract	With open-ended contract, expect job to continue	With open-ended contract, but could be dismissed		Dispatched	Others
Thousand	Thousand	Per cent	Per cent	Per cent	Per cent	Per cent	Per cent	Per cent	
2003	14 149	4 606	32.6	52.2	5.4	7.9	20.2	2.1	34.3
2005	14 968	5 483	36.6	49.8	5.5	10.7	19.0	2.1	32.6
2007	15 882	5 703	35.9	44.4	9.7	8.1	21.1	3.1	35.7
2009	16 479	5 754	34.9	48.9	3.0	9.1	24.8	2.9	36.8
2011	17 510	5 995	34.2	44.5	5.7	7.3	28.4	3.3	37.2

1. The sum of the categories of non-regular workers exceed 100% due to double-counting.

Source: Statistics Korea, *Survey on Economically Active Population*.

# Labor market dualism has led to increased wage dispersion

The incidence of low-paid work<sup>1</sup> and earnings dispersion<sup>2</sup> in 2011 or latest year available

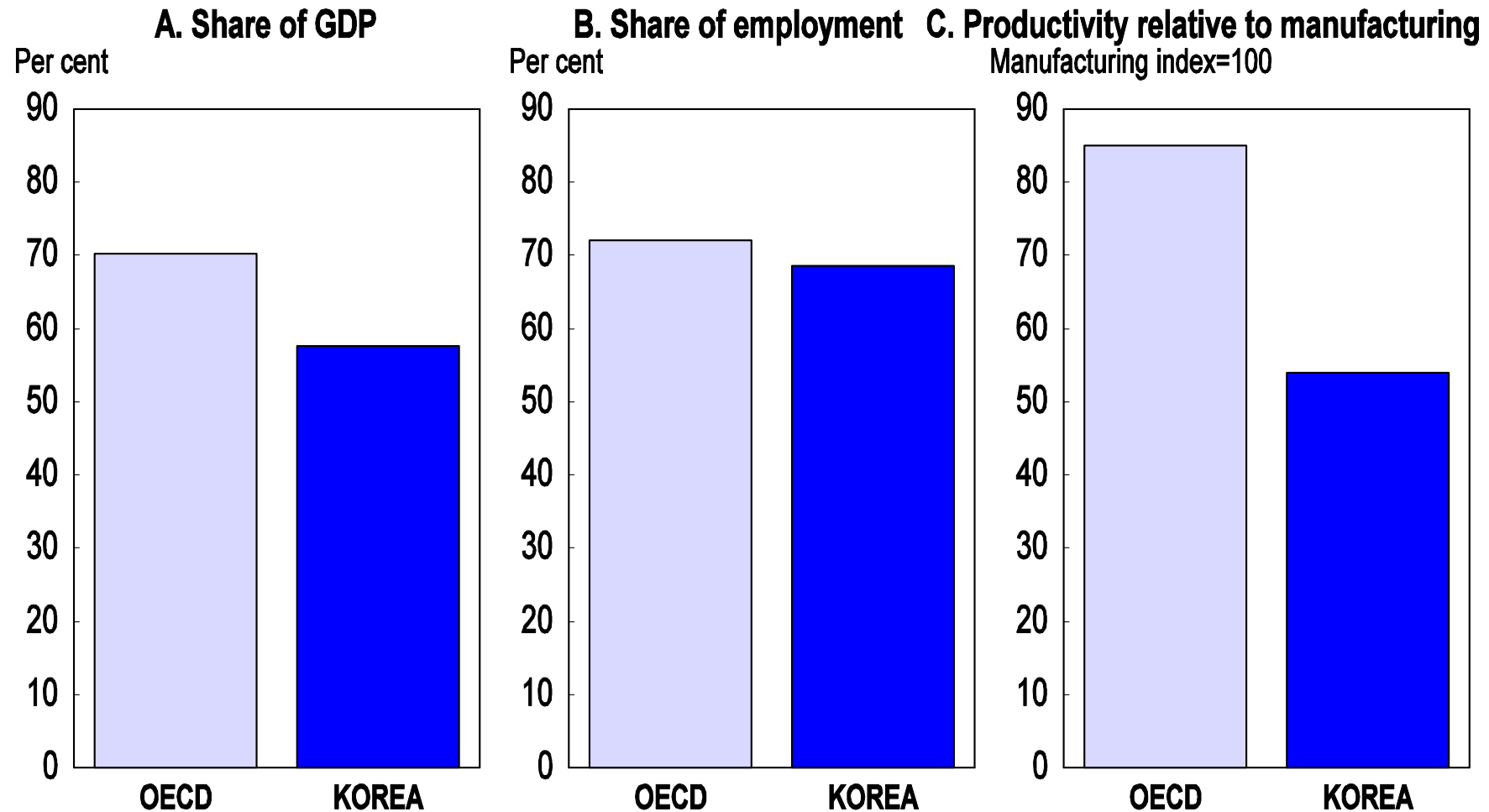


1. The incidence of low pay refers to the share of full-time workers earning less than two-thirds of median earnings. Earnings include both fixed pay and bonuses, except for Japan where it is limited to fixed pay. When only fixed pay is considered for Korea, the incidence of low pay declines to 22%, still substantially higher than the 14% rate in Japan.

2. Earnings dispersion is measured by the ratio of 9th to 1st deciles limits of earnings for full-time workers.

Source: OECD Earnings Distribution Database.

# Low productivity in services in Korea reinforces inequality<sup>1</sup>

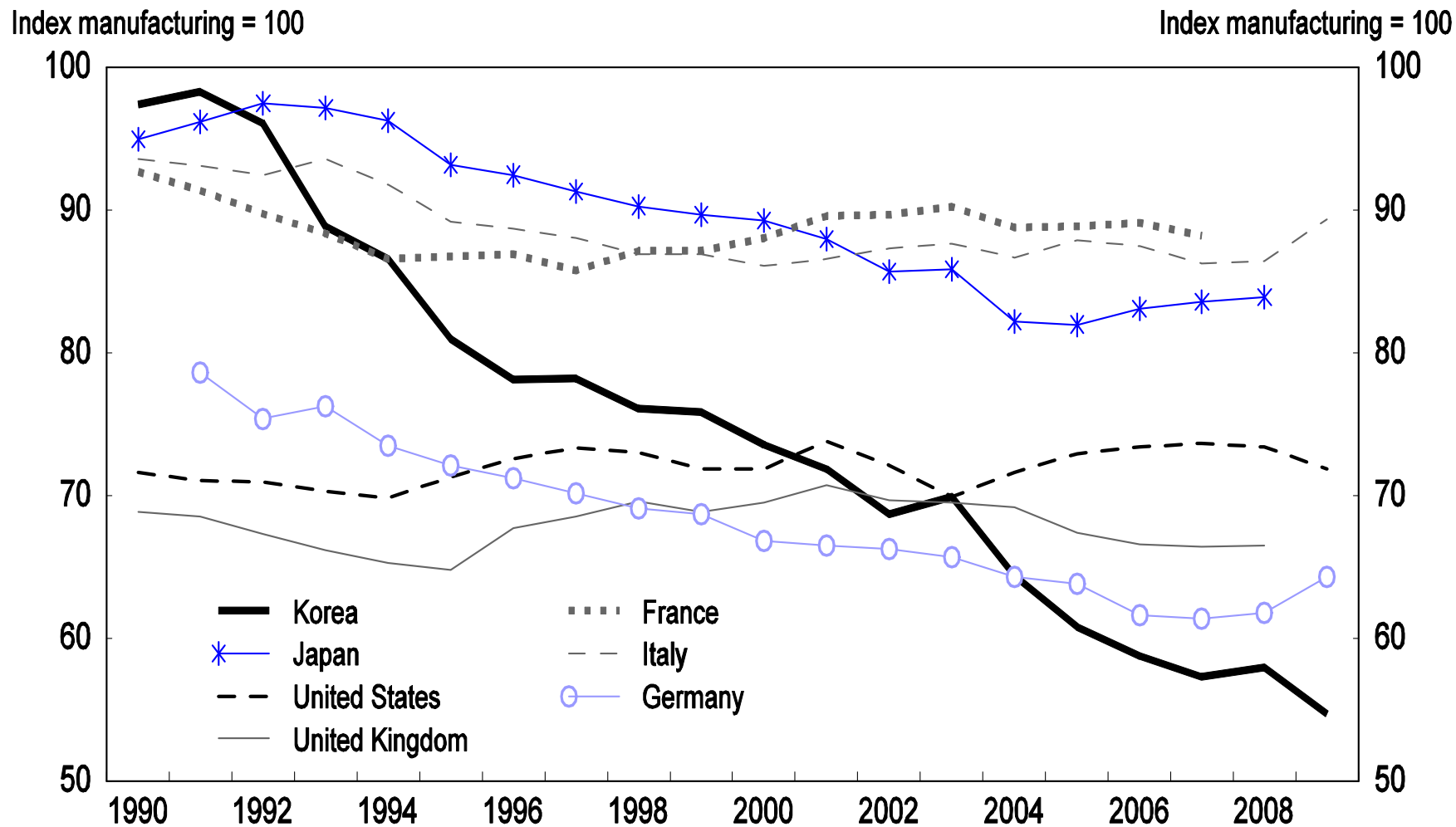


1. Unweighted averages for OECD of the 34 Member countries.

Source: OECD National Accounts Database (QNA) for Panel A and (SNA) for Panel B, and OECD STAN Indicators Database for Panel C.

# The widening wage gap between manufacturing and services is large compared to other OECD countries

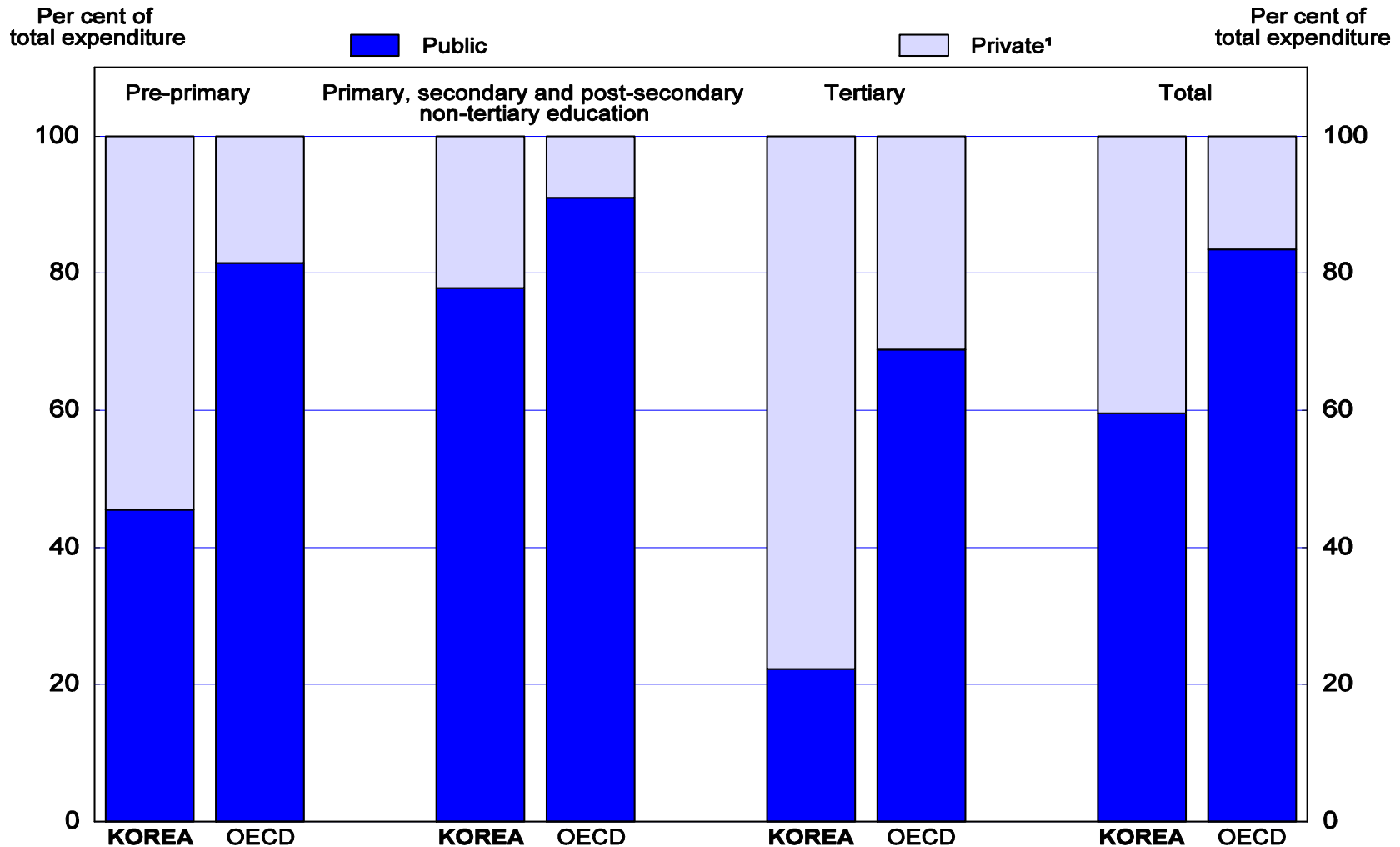
Wages at firms with more than 300 workers = 100



Source: OECD STAN Database for Structural Analysis.

# The large share of private spending in education increases the impact of socio-economic factors on educational outcomes

In 2009



1. For primary, secondary and tertiary education based on full-time equivalents. The figures do not include spending on private after-school institutions, such as *hagwons*.  
 Source: OECD (2012), *Education at a Glance: OECD Indicators*, OECD Publishing, Paris.

## Why is enhancing social cohesion so urgent?

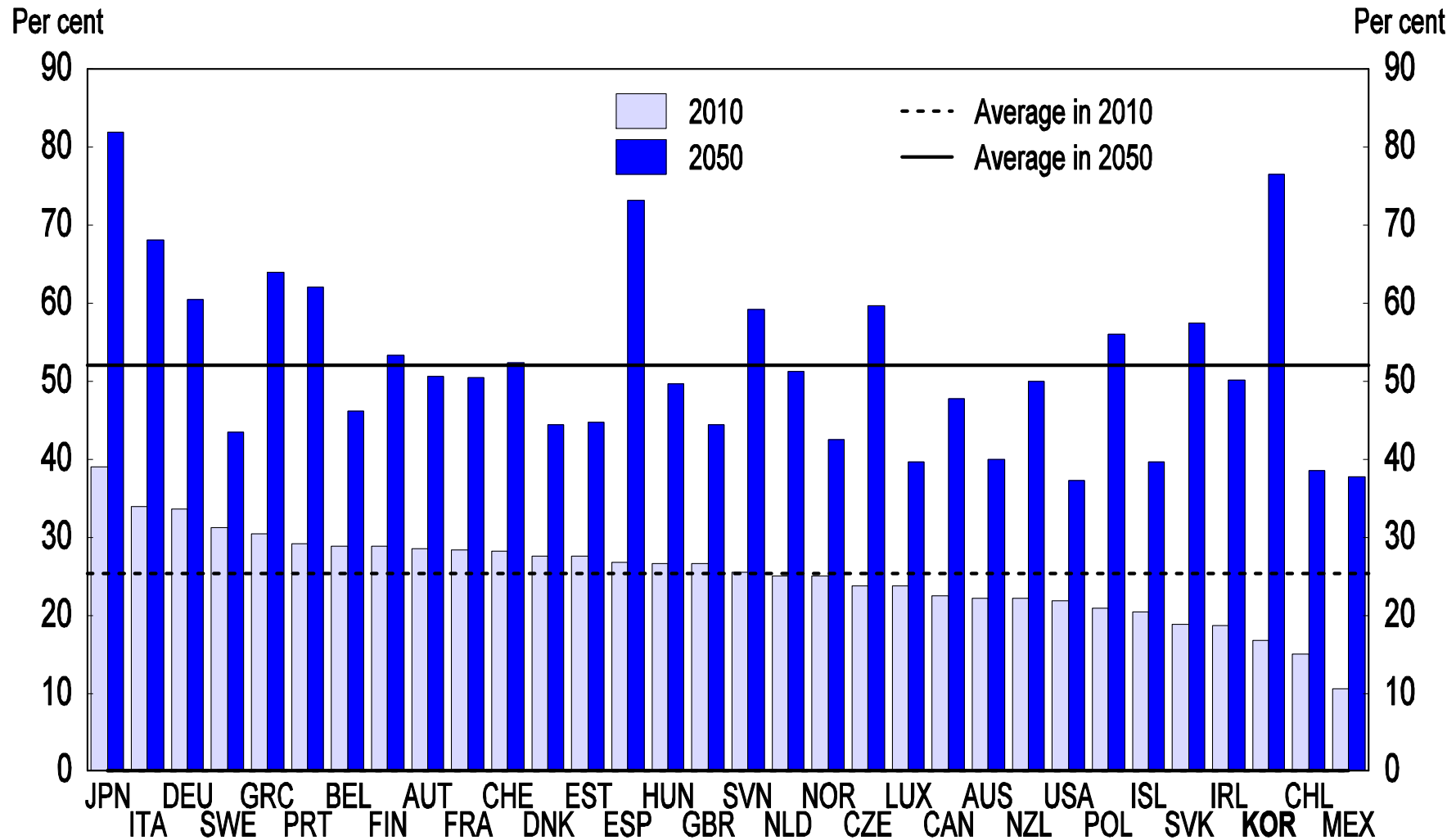
1. Failing to address inequality risks allowing the social compact – the foundation of economic progress -- to unravel.
2. Income inequality can have a corrosive effect on social mobility. Young people who see no future for themselves feel increasingly disenfranchised.
3. Given Korea's demographic situation, it needs to make the most of its human resources and can not allow a marginalized lower class to develop.

## Korea faces special changes in addressing social cohesion

1. Korea is projected to have the fastest population aging in the OECD area.
2. Korea faces the potential cost of economic rapprochement with North Korea.

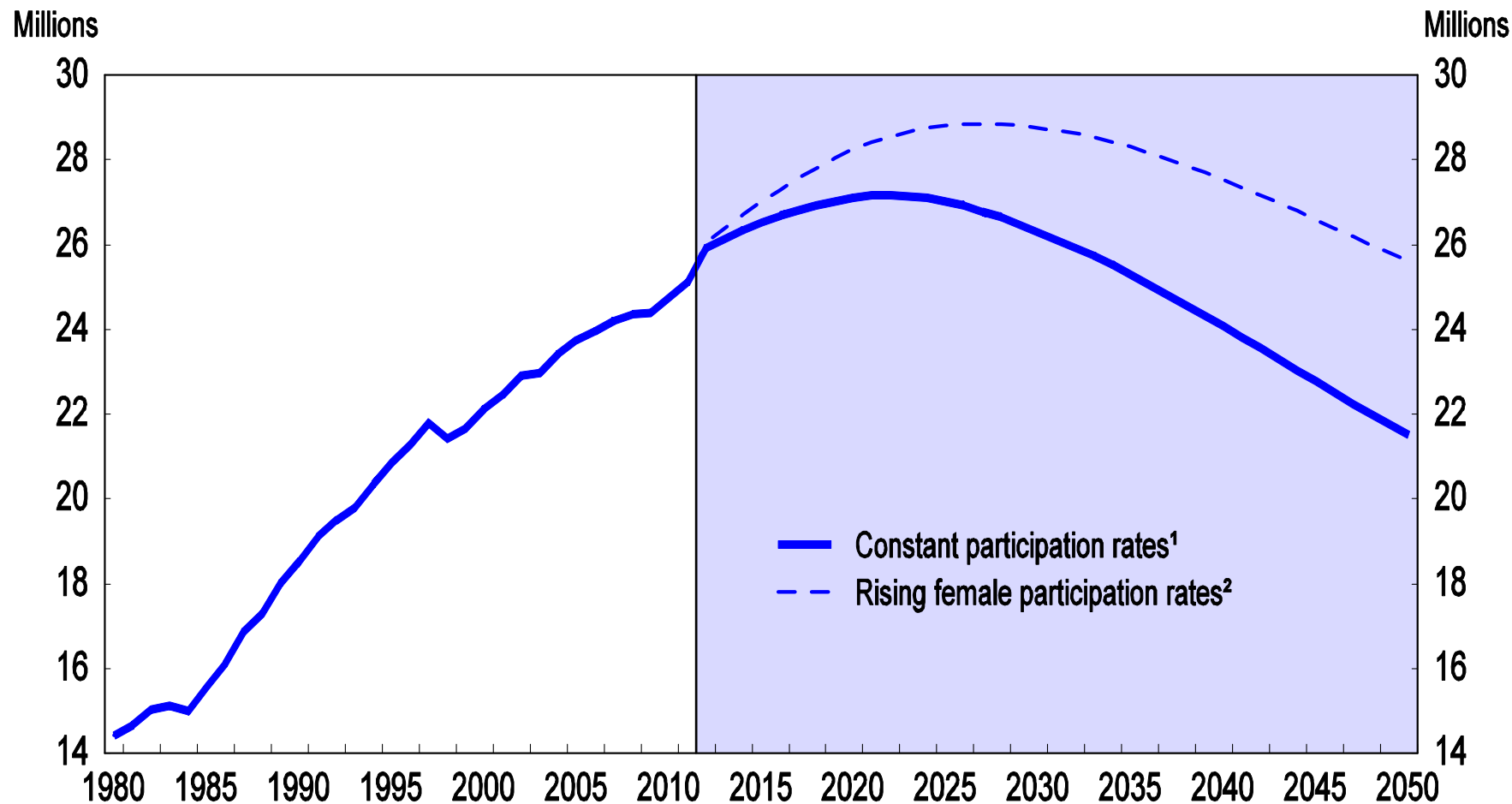
# Population aging in Korea will be the most rapid among OECD countries

Population aged 65 and over as a share of the population aged 20 to 64



Source: Statistics Korea, *Population Projection for Korea* (2011 version) and *OECD Demography and Population Database*.

# Korea's labor force will shrink significantly



1. The participation rates for men and women are assumed to remain at their current levels for each age group.

2. Female participation rates are assumed to reach current male rates in each age group by 2050.

Source: Statistics Korea, *Population Projection for Korea* (2011 version) and *Economically Active Population Survey*, and OECD calculations.

# The economic impact of possible rapprochement with North Korea may be very large

<b>Comparison of North and South Korea in 2010</b>			
	(A) North Korea	(B) South Korea	Ratio (B/A)
Population (millions)	24.2	48.9	2.0
GNI (trillion won)	30.0	1173.1	39.1
GNI per capita (million won)	1.2	24.0	20.0
Total trade (billion US\$)	6.1	891.6	146.2
Exports	2.6	466.4	179.4
Imports	3.5	425.2	121.5
<i>Of which: inter-Korean exports<sup>1</sup></i>	1.0	0.9	0.9
<b>Industrial statistics (2009)</b>			
Power generation (billion kWh)	23.5	433.6	18.6
Steel production (million tonnes)	1.3	48.6	37.4
Cement production (million tonnes)	6.1	50.1	8.2
<b>Agricultural production (2009)</b>			
Rice (million tonnes)	1.9	4.9	2.6
Fertiliser (million tonnes)	0.5	2.6	5.2

1. North Korean exports to the South in Panel A, and South Korean exports to the North in Panel B. The latter includes USD 23 million of non-commercial exports, primarily humanitarian aid in the form of commodities such as rice and fertiliser. Such aid peaked in 2006 at USD 421 million.

Source: Statistics Korea.

# Given these challenges, it is crucial that Korea:

## 1. Maintain a sound fiscal position

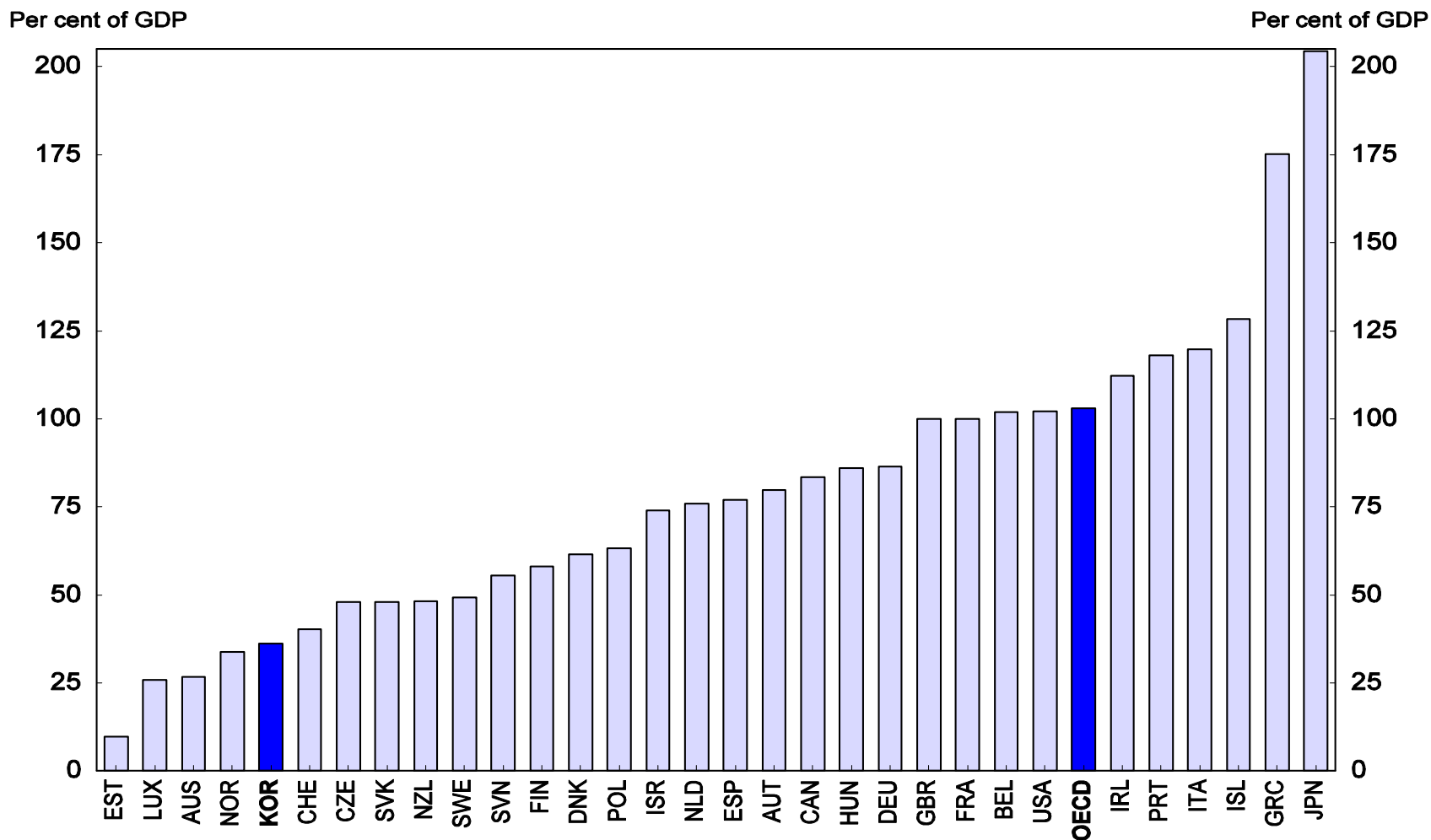
- Use well-targeted and effective social spending to reduce inequality and poverty.
- Implement reforms, for example in the labor market, the service sector and in education, to address the fundamental causes of inequality. In particular, break down labor market dualism and reduce the role of *hagwon* in education.

## 2. Sustain economic growth

- Implement wide-ranging reforms to sustain labor inputs and productivity.
- Limit the economic impact of higher social spending and taxes on economic growth.

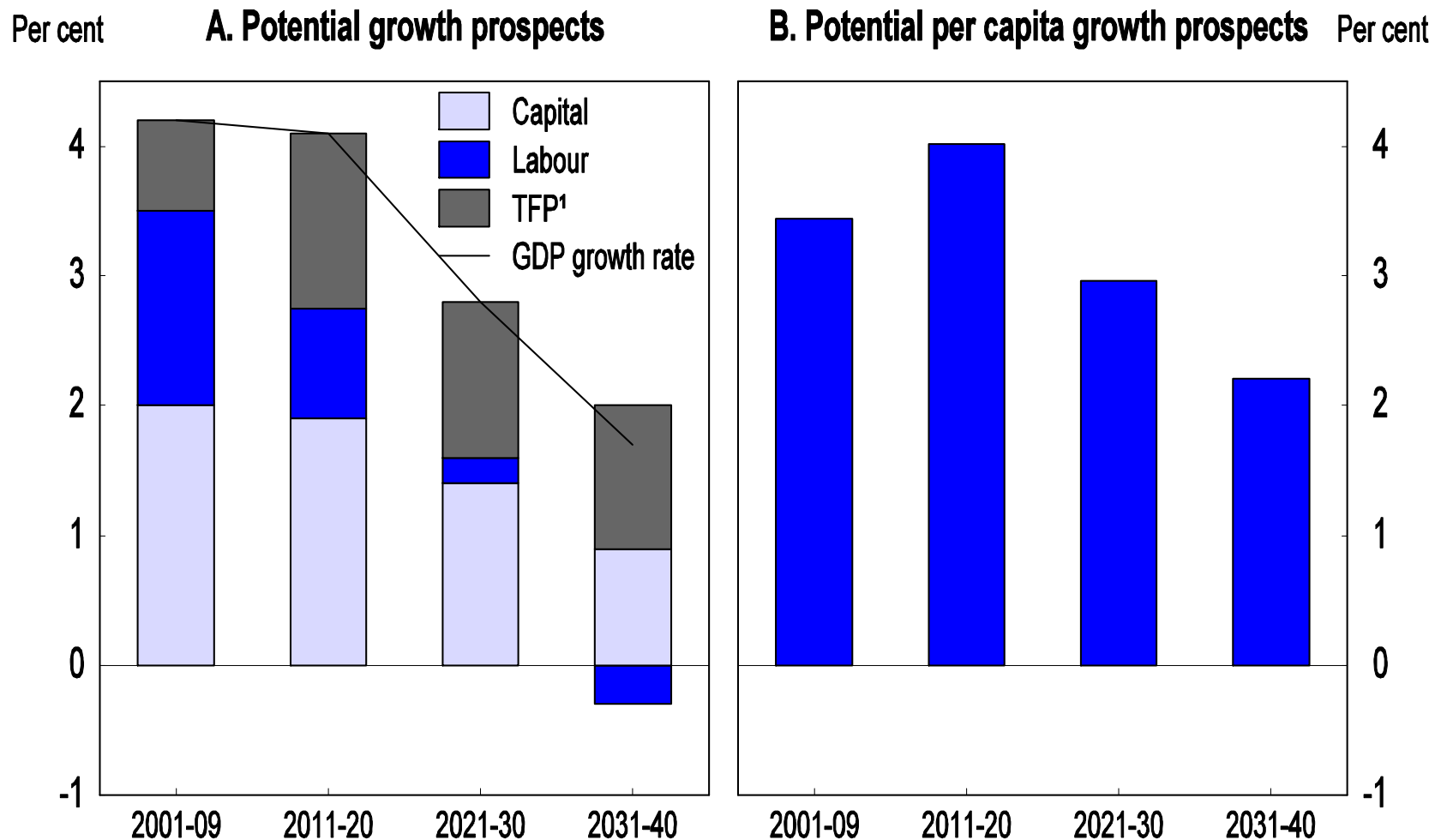
# Korea's public debt is relatively low

Gross public debt as a per cent of GDP in 2011



Source: OECD, Economic Outlook Database.

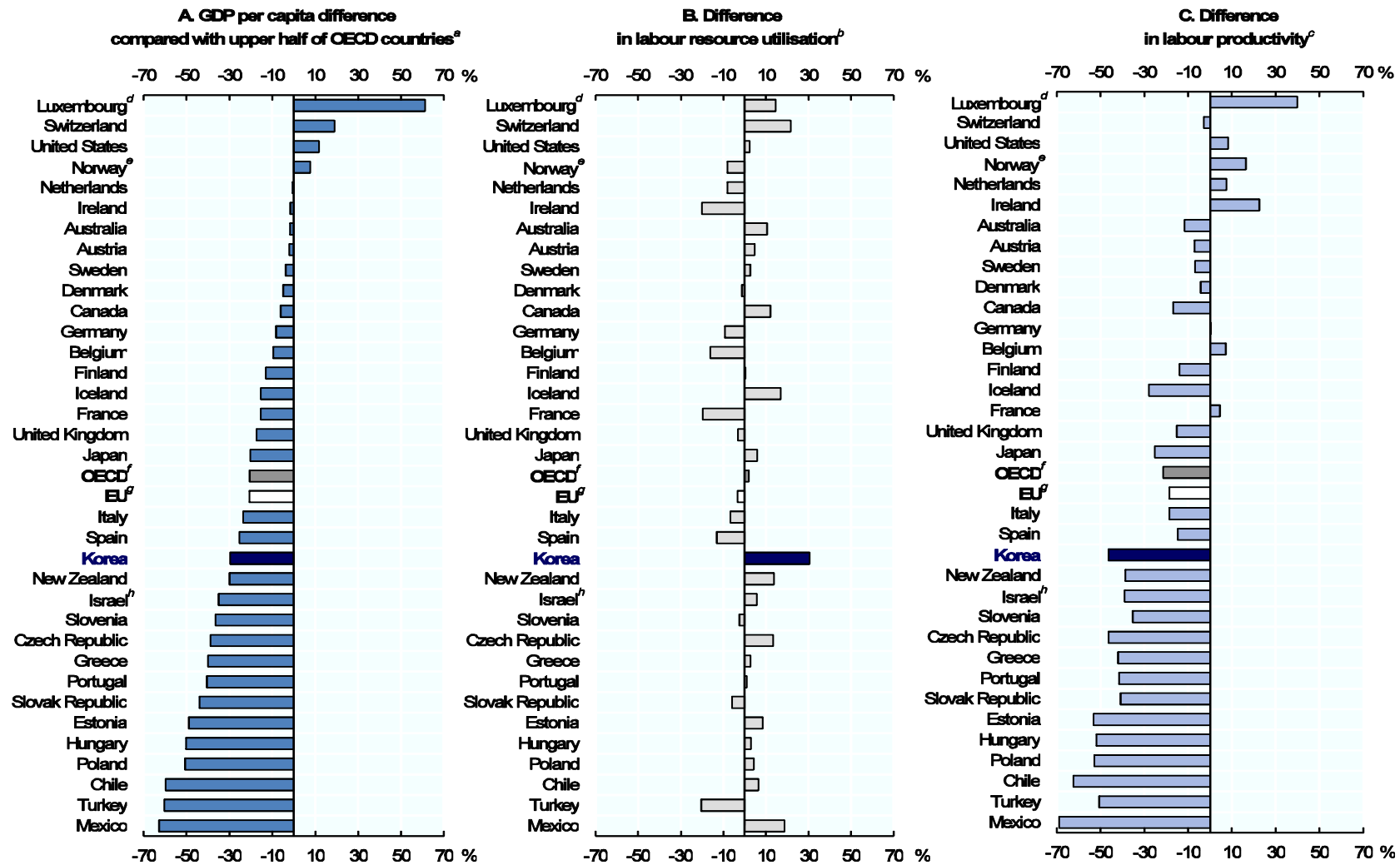
# Potential growth is projected to slow to less than 2% per year in the 2030s



1. Total factor productivity.  
Source: Korea Development Institute.

# Explaining differences in income

In 2011

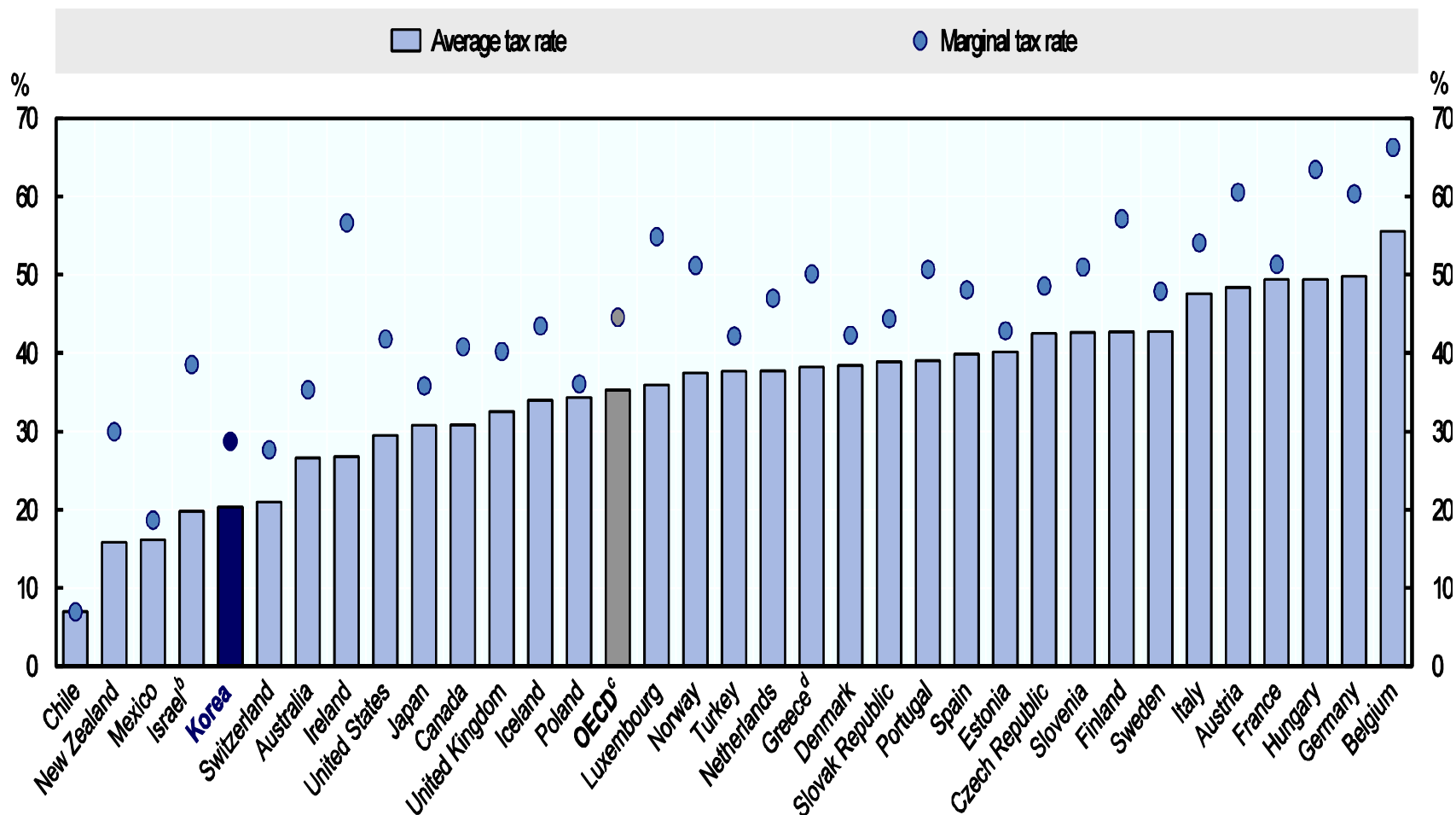


1. Using 2011 PPP exchange rates.

Source: OECD (2013), *Going for Growth 2013*, forthcoming.

# Average and marginal tax wedges on labor are low in Korea<sup>1</sup>

As a per cent of gross labor costs in 2011 for a worker with average earnings



a. The tax wedge measures the difference between total labor compensation paid by the employer and the net take-home pay of employees as a ratio of total labor compensation.

b. Information on data for Israel is available at: <http://dx.doi.org/10.1787/888932315602>.

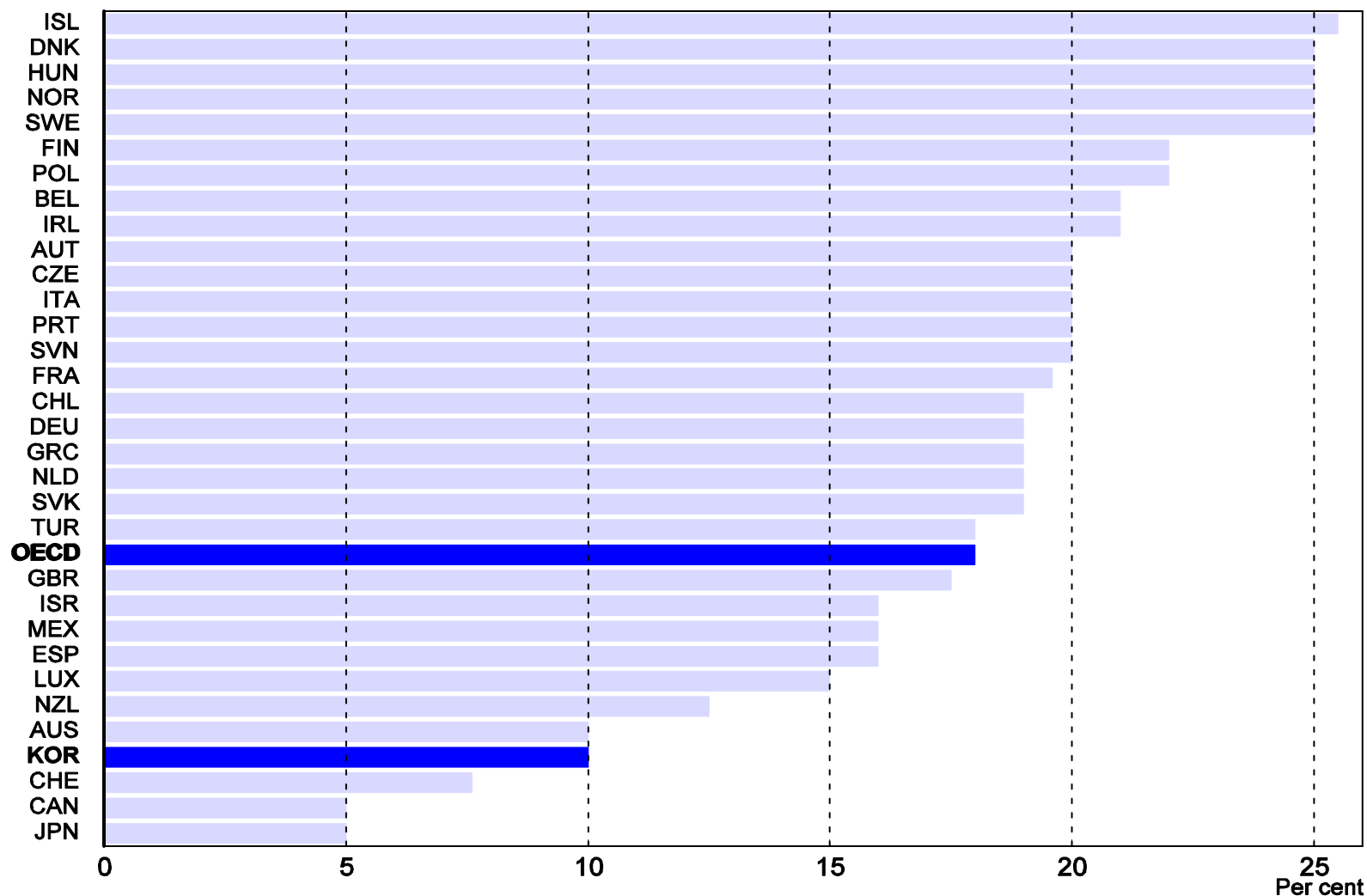
c. Unweighted average of 34 OECD countries' data shown in the chart above.

d. For Greece, data refer to 2010.

Source: OECD Taxing Wages Database ([www.oecd.org/ctp/taxdatabase](http://www.oecd.org/ctp/taxdatabase)).

# Value-added tax rates in OECD countries

In 2010



Source: OECD (2011), *Consumption Tax Trends 2010*.

# Summary

1. Korea was characterized by a high level of income equality during its high-growth era, but has faced rising inequality since the mid-1990s.
2. A variety of special factors contribute to inequality and relative poverty in Korea.
3. A high and rising level of inequality risks weakening the social compact and social mobility, which would also have adverse consequences for growth.
4. Rapid population ageing and the potential cost of economic rapprochement with North Korea are challenges for Korea.
5. It is crucial to maintain Korea's sound fiscal position.
5. It is important to address fundamental causes of inequality and poverty (i.e. labor market dualism, low productivity and wages in services, and problems in the education sector, such as *hagwons*).
6. Well-targeted and effective social spending should be financed primarily by indirect taxes so as to limit the negative labor market impact associated with taxes on labor.