



# ECONOMIC GOVERNANCE AND POVERTY REDUCTION IN SOUTH KOREA

By

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## **Abstract**

In this paper we examine the links between economic governance, viewed as the structure and practice of economic policy-making and management, and poverty elimination efforts. By examining the qualitative and historical links making up the economic governance-poverty nexus in South Korea, we extend the line of research broached by Evans and Rauch (1999) to consider the relation of Korea's capacities for economic governance to the incidence of poverty and inequality there.

Based primarily on field interviews with past and present officials in the economic and social bureaucracy, as well as with relevant academics and civil society associations, this research finds that with democratisation, and particularly during the Kim Young Sam administration (1993-97), the growing flirtation with neo-liberal economics (for various reasons and from various sources) resulted in the abandonment of strategic economic planning, and with it, the further marginalisation of concerns with inequality and social welfare within the economic bureaucracy. More specifically, the restructuring of the economic bureaucracy over the 1990s—first with the demise of the Economic Planning Board and the subsumption of some of its functions within the Ministry of Finance and Economy and second with the breakdown of that ministry in 1998—led to a decline in support for progressive, social welfare ideas from within the economic bureaucracy. While the issues of inequality and welfare forced their way onto the government's agenda during the economic crisis (as a result of rising unemployment), this effort was politically driven by the President and was not a 'normal' and thus stable feature of the country's system of economic governance. Consequently, the future direction that Korea takes with regards to economic governance and poverty is likely to revolve around the ability for policy-makers and social welfare advocates to significantly develop the notion of 'productive welfare' (or other 'third way' notions) through a broad based policy dialogue that can achieve consensus and support by all those involved in economic governance.

The structure of the paper is as follows: We begin by briefly examining the country's record on poverty from the 1960s through to the present day. We then turn to examine the state's institutional capacities for economic governance, detailing the historical evolution of Korea's institutions. This institutional historiography is meant to inform the penultimate section where we present an analysis of the effects Korea's system of economic governance may have had on its poverty reduction efforts in the years immediately following the Asian Financial Crisis in late 1997. Finally, we conclude with some of the general issues that arise from analysis the economic governance-poverty nexus.

## **1. INTRODUCTION**

In the research linking economic growth to state institutional capacities for economic governance, the Republic of Korea (South Korea) has emerged as one of the exemplary cases. Among the factors that have led to its extraordinary growth record since the late 1960s, governance capacities (including bureaucratic competence) seem to have been decisive (Evans and Rauch 1999, Rauch and Evans 2000). While South Korea's industrialisation and growth record has not been unique - in that it was matched by Taiwan, Singapore and Hong Kong <sup>1</sup> - what was unusual was that from the early 1970s through to the late 1990s, poverty reduction - verging on elimination - seemed to have gone hand in hand with economic growth without any significant government commitment to anti-poverty policies. Along with Taiwan, South Korea appeared to be the prime example of how poverty could be eliminated merely as a by product of economic growth and it was internationally touted as such by the World Bank and similar agencies.<sup>2</sup>

In this paper we examine the links between economic governance, viewed as the structure and practice of economic policy making and management, and poverty elimination efforts. The line of research broached by Evans and Rauch is extended by examining the relation of South Korea's capacities for economic governance to the incidence of poverty and inequality there. We begin by briefly examining the country's record on poverty from the 1960s through to the present day. We then turn to examine the state's institutional capacities for economic governance, detailing the historical evolution of Korea's institutions. This institutional historiography informs the penultimate section where we present an analysis of the effects Korea's system of economic governance may have had on its poverty reduction efforts in the years immediately following the Asian Financial Crisis of late 1997. In the conclusion we identify the main issues that arise from this analysis of the economic governance-poverty nexus.

## **2. POVERTY RECORD**

South Korea has experienced one of the most dramatic declines in absolute poverty that the world has seen. In the 1950s the majority of its people lived in absolute poverty. Even as late as the mid-1960s, between 60-70 percent of the population was estimated to be living in poverty (PSPD/UNDP 2000). Hunger and deprivation were widespread and with much of the country's economy and infrastructure destroyed during the Korean War (1950-53), it looked as though its population – still largely a peasantry in the 1960s – would be impoverished for many years to come. By the mid-1990s, however, absolute poverty had dramatically declined to levels as low as 3.4 percent of the population (Park 2001). Indeed, by 1999, the Korean averages for poverty in single-person households was comparable to other OECD countries (OECD 2000). These

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<sup>1</sup> Not to mention, in an earlier period, the USSR and Japan.

<sup>2</sup> The other East Asian 'tigers', Hong Kong and Singapore, both had indirect anti-poverty policies which operated in the guise of public housing programmes and in the case of Hong Kong, the 'administered' control of food prices (Castells et al 1990, Schiffer 1991, Henderson 1993).

declines in income poverty have been matched by gains in human development. The average life expectancy of Koreans increased from 55 in 1962 to 72 in 1998; infant mortality dropped from 7% in 1962 to .9% in 1998 (World Bank, 1999). By 1998 its human development index had reached 0.854 and was ranked 31<sup>st</sup> in the world (UNDP, 2000).

Much of the ‘miracle’ underlying Korea’s historical success in economic growth and poverty reduction (without explicit poverty reduction policies)<sup>3</sup> undoubtedly stem from both its engagement with land reform in the late 1940s, coupled with its ability to successfully pursue an export-oriented industrialisation strategy in the mid 1960s through to the 70s. The Agricultural Land Reform Amendment Act (ALRAA), brought into effect in March 1950, directly and indirectly facilitated a vast transfer of arable land ownership to the peasantry. Unlike most land reforms, this was an exercise that genuinely returned ‘land to the tiller.’ It dramatically increased the share of agricultural value added that was returned to labour and was associated with major improvements in productivity. The rural underclass were allowed to repay the loans advances for their land primarily in terms of a proportion of their annual crop yield. As the government’s annual stock of rice was then sold at regulated levels far below market price and these funds used to pay back the former landlords for their properties, the former landlords were effectively made to sell their properties for less than their worth thus contributing to significant levels of income redistribution (Jeon and Kim 2000).<sup>4</sup> Alongside land reform, significant levels of poverty reduction came equally from changes in economic development strategy under the second five-year economic development plan (1967-1971). While having first attempted a development strategy based on “import substitution” (substituting the import of cement, refined oil, and fertilizer for example with investment in the production of these items domestically) under President Park Jung Hee, Korea was able to pursue a different strategy based on “export-oriented industrialisation” which generated greater levels of economic growth and reinvestment that, in turn, enabled large numbers of the peasantry to migrate to urban areas and enter into low paid work as manual labourers.

While the broad picture and basic story concerning the decline in absolute poverty is clear, the empirical details needed to fully substantiate poverty reduction in Korea are harder to confirm. Surprisingly, given the seeming relation of South Korea's economic 'miracle' to poverty reduction, poverty has been regarded as something of a 'non issue' and has historically received little attention and priority within government or academic circles. While the ravages wrought by the country's economic crisis subsequent to 1997 have dramatically raised the profile of the poor in government agencies, even now there is still no official poverty line nor a consensus on how it should be measured.

The social consequences of the economic crisis of 1997 has raised many concerns. Amongst these the widespread beliefs that growth would continue and poverty would decline, have been shaken. The crisis showed that growth was not guaranteed forever.

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<sup>3</sup> As reported in the literature, and as many of our interviewees pointed out, at the microlevel social security through the ‘miracle’ was provided by the family unit.

<sup>4</sup> Despite concerns that politically dominant regions received preferential treatment, recent research has confirmed that regional income inequality in Korea has not worsened; an important prerequisite for assuring that economic growth actually leads to poverty reduction. For instance, Yoon (2000) has found that at least during over the 1986–95, available GINI co-efficient data suggests that regional income distribution has been relatively egalitarian and not distributed across the regions in a distorted manner.

Those who held steadfast to the assumption that economic growth automatically reduced poverty, however, continued to believe that this pattern would re-assert itself when growth returned. When the economy began to grow again in 1999, and reductions in unemployment and poverty were evident from official statistics, these views seemed to be substantiated.

Our interviews with those in the relevant Government agencies (October-November 2001) have confirmed that absolute poverty<sup>5</sup> has returned to pre-crisis levels (and may be falling even further). Proponents of the economic 'miracle'/poverty reduction (or 'trickle-down') thesis, however, fail to appreciate that underlying the poverty statistics in South Korea is an important and longstanding debate about the methods and measures used to calculate the poverty indices and thus a controversy about the actual levels of absolute and relative poverty in the country.

The debate around poverty statistics concerns both the nature of the surveys employed and methods used for calculation. Most researchers use the official Minimum Cost of Living (MCL) basket to measure poverty. The MCL is employed by the government as a working definition of the poverty line for purposes of budgeting and administering social assistance benefits. Calculations began in 1973 and were conducted annually until 1989 when the Korean Institute of Health and Social Affairs (KIHASA), the government agency which calculates the MCL, conducted surveys only at five year intervals. The annual figures are derived by adjusting for inflation (OECD 2000).

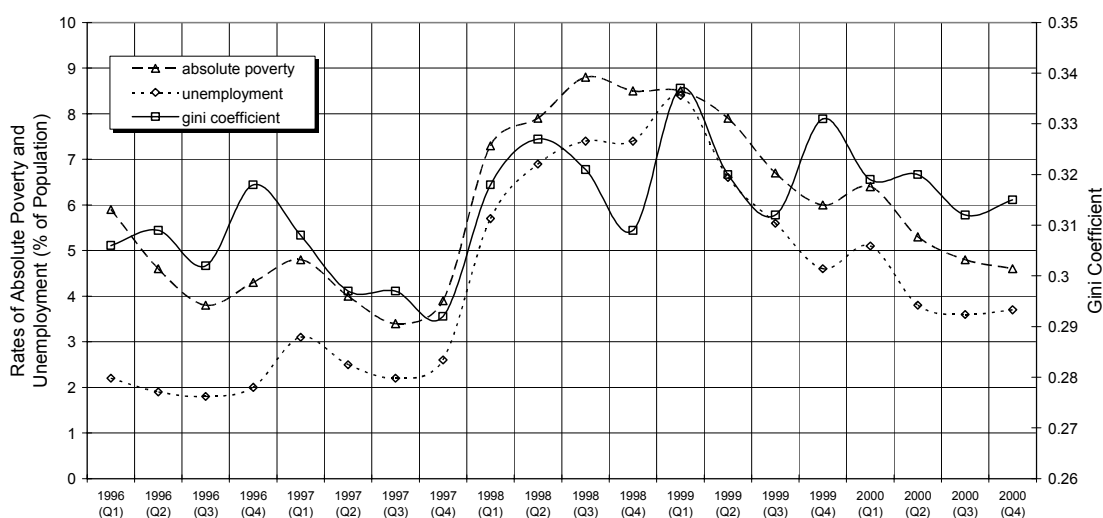
In the debate over poverty statistics, one of the major concerns expressed by interview respondents within the government research institutes, non-governmental organisations (NGOs) and even some of those in the economic bureaucracy itself, is that the current survey, from whose data the MCL is calculated, focuses only on earnings. Problematically, this excludes both the unemployed and, importantly in the South Korean context, the self-employed.<sup>6</sup> Consequently, at the height of the crisis in the first quarter of 1999, official accounts recognised that up to 8.5 percent of the population had become poor; an increase of 4.6 percent on the figure for the fourth quarter of 1997 (Figure 1). Alternative calculations, focussing on household expenditures rather than income, however, have recently shown that just prior to the crisis in the first quarter of 1997, 13.7 percent of the population was below the MCL (a decline of two percent since 1996). A year later (the first quarter of 1998), however, this alternative calculation suggests that poverty had increased to 23.5 percent of the population (PSPD/UNDP 2000), two to three times the maximum rate that has been officially reported.

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<sup>5</sup> Absolute poverty occurs when a person is unable to meet their minimum basic needs. For a discussion and bibliography see World Bank (2000).

<sup>6</sup> While unemployment has been low for most of the 1990s, ranging between 2 and 3 percent of the labour force prior to the crisis (see figure 4), the self-employed population have consistently constituted well over a quarter of the labour market throughout the 1990s. For instance, in 1990 28 percent of the labour force was self-employed with a slightly increase to 28.8 percent by 1999 (OECD 2000).

Figure 1. Poverty and Unemployment in Korea, 1996-2000



Source: Park, NH (2001) Poverty Rates and Poverty Line in Korea.

Field interviews confirmed that while the nature of poverty statistics underlies the ongoing debate, the conflicts between the government and anti-poverty advocates in academia and civil society have recently become oriented less towards attempts to revise official poverty statistics and survey methods, and more to getting the current (Kim Dae Jung) government to significantly raise the budget for social assistance. Currently, the social safety net assumes that a little over 3 percent of the population need support. Accordingly, some civil organisations have lobbied the government arguing that the budget should aim to assist 8 percent of the population; the share of the population officially reported as below the MCL at the height of the Financial Crisis.

The reason the debate has tended to veer away from calls for a fundamental reform in the process of calculating the statistics, lies in two government counter arguments. Firstly, the government has argued that calculation based on household expenditure will overestimate the incidence of absolute poverty because it will allow those who are not poor to be included as if they were.<sup>7</sup> Secondly, it appears that the government has contemplated, on several occasions, improvements in data gathering to capture the self-employed (for taxation purposes). Yet it has backed-off from pursuing significant reforms to include the self-employed as previous attempts to incorporate the self-employed in surveys have performed badly and were thus not cost effective from the government's perspective.<sup>8</sup>

Given the likelihood that expenditure-based statistics are indeed prone to overestimation, and that it is not feasible to reform surveys to attempt to capture the self-employed, the government has maintained its position to err on the conservative

<sup>7</sup> The government's example being those that spend their money frivolously on non-essential items.

<sup>8</sup> One social welfare specialist reported that the government was only been able to capture around 23 percent of the total self-employed income estimated to exist by the treasury. As the costs of initiating major reforms in existing statistical surveys were not offset by the potential increases in taxation, the government has consequently decreased its interest in pursuing statistical reforms to capture the self-employed.

side of poverty estimates and persist with current statistical conventions. As a consequence, this means that the most accurate assessments of the incidence of poverty probably lie somewhere between the government's estimates and those of its major critics.

Policy analysts in Korea seem to have assumed that, with economic growth, poverty would decline to almost zero by the early years of the 21<sup>st</sup> Century. It is evident, however, that the rate at which poverty was declining began to slow after the great improvements that had been achieved between the 1960s and 1980s. By 1991, 7.6 percent of the population – and perhaps much more – could still be judged to be in absolute poverty (Kwon, 1998). While the widespread belief that absolute poverty had drastically declined in Korea by the mid 1990s appears to be broadly correct, the problems in methodology and the consequent extent of the statistical discrepancies, casts doubt on the prevailing view that economic growth, in and of itself, leads to poverty reduction, even in the country considered the best case scenario for this argument.

Scepticism about the view that there is a direct relation between economic growth and poverty reduction can be further justified from the South Korean experience. At the height of the country's economic success, official data suggested that absolute poverty had been virtually eliminated. Actual levels of absolute poverty, however, are unlikely to have been that low given that the destitute, homeless, disabled, mentally ill, elderly in rural areas and low-income self-employed are, at best, only partly captured by official statistics. In addition, there are concerns about the independence of the National Statistical Office and a widespread belief among Korean specialists on inequality and poverty that relevant government data is unreliable.<sup>9</sup>

Furthermore, when one considers South Korea's performance on relative poverty, the influence of economic growth on income inequality has not been overly impressive. For instance, the official figures show that just before the crisis, South Korea had a GINI co-efficient of 0.292. This rose to 0.337 at the height of the crisis before trailing back down to 0.315 in the fourth quarter of 2000 (Figure 1). This suggests that at the height of the crisis, income inequality reached levels comparable to the mid 1960s (the period when South Korea also experienced the highest rates of absolute poverty) when estimates of inequality were 0.33 in 1964 (Martellaro 1989) and 0.343 in 1965 (Choo

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<sup>9</sup> Our scepticism derives from three findings. The first is the fact that the provision of statistical data was, and remains, not only a monopoly of the government's National Statistical Office (NSO), but it only became publicly accessible in the 1990s. Secondly, the NSO's independence was queried by many interview respondents who felt that the impartiality of its activities was compromised by the fact that its head was formerly appointed by the Ministry of Finance and Economy (MOFE) and is now appointed by the President (on the recommendation of MOFE). For instance, one former government researcher confirmed that the current head of the NSO comes from MOFE and that given the post is a political appointment, the head of the NSO typically remains in post for relatively short periods. Given that statistical posts are generally regarded as less prestigious than posts in the government think tanks, they tend not to attract the best applicants. Thirdly, several respondents offered anecdotal evidence and indeed personal accounts that suggest that under authoritarian and - to a lesser extent - democratic regimes also, the government may at times have sought to 'manage' statistical data in such a way as to place itself in a favourable light. For instance, some trade unionists have reported in interviews that recent employment rates and job creation statistics have been deliberately overestimated. Furthermore, one former Korea Development Institute (KDI) researcher recalled incidences where new findings on income inequality were directly suppressed by senior Economic Planning Board (EPB) managers in the early 1990s, ultimately underestimating levels of relative poverty.

1982). Furthermore, even towards the end of the crisis, income inequality had still not returned to the levels reached in the late 1960s, which one study conservatively estimated to have been 0.305 in 1968 (Jain 1975).

While great strides have been made in terms of the reduction of absolute poverty in South Korea the case that absolute poverty has been virtually eliminated needs to be challenged. In terms of relative poverty, then there is little evidence of this reducing given the similarity in GINI co-efficients in the late 1960s and 1990s. If this is so, then the argument that assumes a direct link between economic growth and poverty reduction (that is, without the mediation of poverty reduction policies) seems to be difficult to sustain given that South Korea has been seen as an emblematic case. While we will return to these issues in the conclusion, we now proceed to examine South Korea's system of economic governance.

### **3. ECONOMIC GOVERNANCE IN SOUTH KOREA, 1961-2001**

Subsequent to the military coup in 1961 and the heavily state-influenced form of economic development that it set in train, South Korea has seen remarkable advances in economic performance and social welfare. Underlying the Korean 'miracle' was a model of capacity-building aimed at engendering the 'developmental state' with an institutional apparatus organised to provide a coherent and effective system of policy formulation and implementation.<sup>10</sup> In this section, we attempt a broad description of the institutions of economic governance, their configuration and how they have developed over time. Four major developmental phases can be identified to capture changes in the composition and configuration of South Korea's governing institutions (see Figure 2). Each will be discussed in turn below.

Prefacing the argument developed in the following sections, economic governance through to the present day must be understood within the context of the institutional legacies of the authoritarianism which dominated the country's political and economic life from the early 1960s through to the onset of democratisation in the late 1980s. Successive military regimes shaped Korean policy-making not only with a strong tendency towards centralised decision-making and autocratic management, but also with a relatively stable institutional structure. While the former remain in place (in spite of democratisation), we will argue that institutional stability has been less evident in over the past ten years or so.

More specifically, authoritarianism has left its mark on Korean economic governance through two dominant organisational characteristics. These are, the ultimate power of the President and his office - the *Cheong Wa Dae* or 'Blue House' - and a system of policy formulation and implementation that is functionally separated into two parallel structures: the ministries on the one hand and the government think tanks on the other (see Figure 2).

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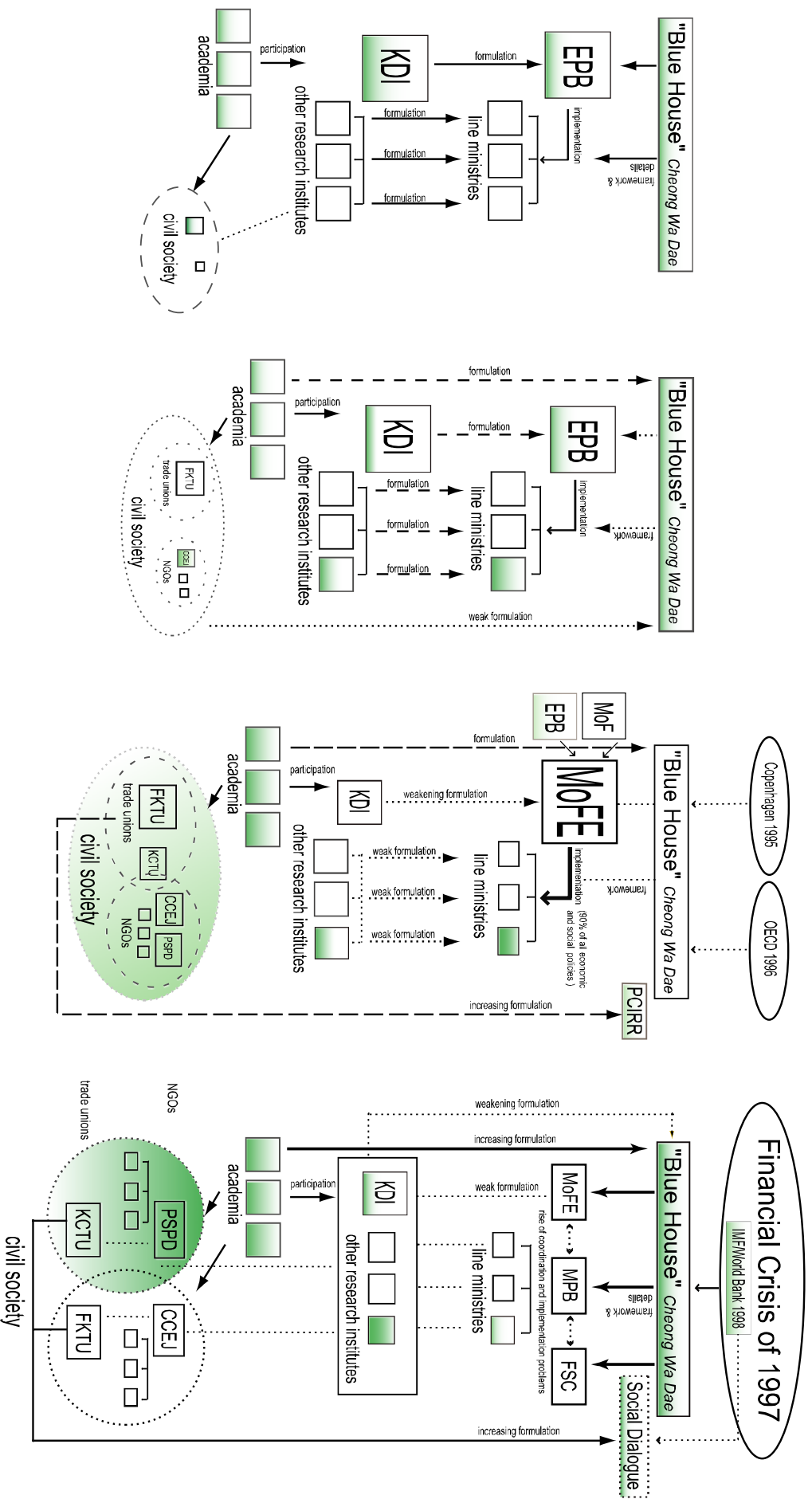
<sup>10</sup> For some of the most important analyses of this phenomenon, see Amsden (1989), Woo (1991), Chang (1994) and Kim (1997). South Korea, of course, was not the only East Asian country to pursue this route to economic development. Taiwan, Hong Kong, Singapore and - less effectively - Malaysia, all crafted their own versions of the 'developmental state' model, as did Japan before them. On the larger regional picture see the essays collected in Appelbaum and Henderson (1992).



In this section, we will argue that in the years following democratisation in 1987, there has been a gradual emergence of civil organisations and an increasing role for academic experts in policy-making. Simultaneously, however, the encroachment of globalising processes and with them, neo-liberal economic ideas, have spelled the end of coherent economic planning in South Korea. The economic bureaucracy and its exercise of power, has been transformed and with this the earlier structural connections between the ministries and their associated research institutions - crucial to effective economic planning - have been broken.

Notwithstanding the changes in South Korea's political economy and the makeover of its governing institutions, however, our findings suggest that the managerial style and organisational strategies fostered under the authoritarian regimes, continue to remain at the heart of economic governance.

Figure 2. Institutional Organisation and Evolution of Policy Formulation & Implementation, South Korea 1961-2001



Note:  Shading represents the institutional location and strength of poverty-related activities

Authoritarian Legacy and the Developmental State 1961-87

Democratization and the Rise of Civil Society 1987-93

Globalisation, Neo-Liberalism and the SuperMinistry 1993-97

Crisis Restructuring and the return of Productive Welfare 1997-2001

### 3.1 Authoritarianism and the Developmental State, 1961-1987

Historically, economic governance in South Korea has been highly centralised. From the military coup in 1961 - led by Park Chung Hee - through to the early 1990s, it was driven by the interplay of two dominant institutional features: the economic bureaucracy and the ultimate power of the President (Cheng et al 1998). In this section, we first sketch some of the key issues associated with the emergence of 'state-directed' capitalism in South Korea before turning to examine in more detail the mechanisms of economic governance and related matters.

The 'developmental state' established by the Park regime had three important goals. First, economic development was promoted as the top priority of the government. Comprehensive blueprints for economic development were drawn up and implemented. Second, reforms were instituted within the government bureaucracy to assist in economic planning. In particular, the Economic Planning Board (EPB) was created and subsequently expanded and strengthened. Third, vital resources for economic development, including domestic and foreign capital, became closely regulated by the state<sup>11</sup>. These institutional reforms produced a troika of economic ministries, with the EPB at its centre and the Ministry of Finance and the Ministry of Trade and Industry supporting the EPB. The relative autonomy in decision-making provided to these ministries and the centralized control and coordination by the EPB were similar to the privileges and power given to the Ministry of International Trade and Industry (MITI) and the Ministry of Finance in Japan (Kim, E.M. 1998).

The EPB's mission included the formulation of long-term economic development plans, their implementation and management, and the control of both domestic and foreign capital (through the nationalization of banks and direction of the national budget). While it was the most prestigious government agency throughout the 1960s and 1970s, and continued to exercise significant power through to the onset of democratisation in the late 1980s, at no time did its remit include a direct concern for poverty reduction<sup>12</sup>.

The EPB was established by amalgamating various plan-oriented departments scattered throughout the pre-existing bureaucracy and soon consisted of five bureaux<sup>13</sup> and nineteen departments, employing about 600 government officials. It was headed by an assistant minister who, in December 1963, was elevated to hold, simultaneously, the position of deputy prime minister (Choi 1991). This ensured that

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<sup>11</sup> Castells (1992) refers to these reforms, and their equivalents in Taiwan and Singapore, as part of a 'political economy of survival'. In other words, they were driven largely by geo-political threats to the respective regimes, which in the case of South Korea were posed by the Kim Il Sung regime in North Korea.

<sup>12</sup> In that sense, among others, it was very unlike Malaysia's Economic Planning Unit for which it was a model (see Henderson et al 2002).

<sup>13</sup> These included the Bureaux of Comprehensive Planning, Material Resource Mobilization (from the Ministry of Construction), Statistics (from the Ministry of Internal Affairs), Budget (from the Ministry of Finance) and Supply. The latter enabled the EPB to control the procurement, supply, and management of all domestic and foreign capital and goods.

other ministries usually fell into line when EPB sought to 'coordinate' their plans and actions (EPB 1982).<sup>14</sup>

The development plans developed by the Park regime were implemented in a semi-militaristic, manner. The state forcibly intervened in the market and while it did not have recourse to significant levels of state ownership<sup>15</sup>, it sought to be omnipresent in the market. There were two ways in which the South Korean state enforced its economic policies. Firstly, it used a series of mechanisms to discipline the *chaebol* (large conglomerates). For much of the 1960s and 1970s it was clearly the dominant partner in its loose alliance with the *chaebol*. Rather than allow them to respond to 'market signals' the military government forced cooperation in its development plans from the business leaders.<sup>16</sup> As development proceeded and by the late 1970s, however, the relationship between the state and the *chaebol* became more symbiotic. Through to the early 1990s, however, the state continued to control domestic and foreign capital - and the *chaebol's* access to both - and it used its power to enforce strict guidelines for domestic loans. The *chaebol* had to compete with one another to receive subsequent, low interest credit from the state, which was provided only to support government-approved initiatives consistent with national development plans (Mardon 1990, Woo 1991)<sup>17</sup>. While there was undoubtedly corruption involved in South Korean state-business relations, it took a 'developmental' form - with positive consequences - rather than the 'predatory' or 'acquisitive' and (literally) counter-productive forms of corruption typical of many other developing countries (Henderson 1999).

The second way in which the state used authoritarian means to achieve its economic goals was the repression of industrial workers. The state's policies were intended to keep wages low and to limit, and indeed prohibit, labour unions (Cho, H. 1993, Choi 1989). The lack of minimum-wage legislation prior to 1988 and the poor enforcement of laws relating to working conditions resulted in significant levels of worker exploitation (Song 1991). The police and the Korean Central Intelligence Agency were used to monitor labour activities and extensive force was used to prevent or control strikes (Ogle 1990)<sup>18</sup>.

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<sup>14</sup> While elevating the rank of the EPB minister to Deputy Prime Minister did provide the EPB with a formal authority, via the budget, over the coordination and executing economic development plans, it did not necessarily elevate the EPB minister above the other economic ministers. For instance, while ministers were required to consult with the EPB head prior to initiating major economic policies, when their policy proposals did not affect the budget, other economic ministers often tended not to consult the deputy prime minister prior to initiating policy proposals (Choi 1991).

<sup>15</sup> In addition to the banks and utilities, only steel - in the form of the sector's largest company, POSCO - was state owned.

<sup>16</sup> Initially under threat of indictment on charges of having illicitly accumulated wealth under the former Rhee and Chang Myon regimes.

<sup>17</sup> Given that the *chaebol* were wholly-owned by family dynasties who resisted recourse to the capital market (under-developed anyway in South Korea) for investment funds, state control of credit (and the 'socialisation' of investment risk associated with it) proved to be a decisive - and largely successful - development tool. In addition to Woo's (1991) book on South Korea, see Zysman (1983) and Whitley (1992) for some of the theoretical issues behind such strategies.

<sup>18</sup> While the repression of labour movements was, and remains, fairly general in the developing world, South Korea witnessed some of East Asia's most brutal incidents and these probably contributed to the emergence of a labour movement there that was, until recently, the most militant in the entire continent. On the issues involved in the rise of trade union militancy in South Korea, see Deyo (1989).

Under an authoritarian state, the centralisation of military control would have deep-seated effects upon the structure of the bureaucracy in general, and the structure of economic decision-making in particular (Cheng et al, 1998). As we turn to next, militaristic forms of hierarchy and regimentation would equally define the institutional structures and governing mechanisms for policy formulation and implementation.

### Mechanics of Economic Governance

From interviews with senior officials in the economic bureaucracy as well as government researchers, academics and civil activists, economic governance under the authoritarian regimes seems to have been conducted via a relatively stable institutional configuration which governed the process of policy formulation and implementation (see Figure 2).

In post-coup Korea, the function of formulating policies was organisationally separated from their implementation. With regard to policy formulation, one dominant feature of economic governance was the role of policy 'experts'. Under authoritarianism, there were isolated cases where advocates in NGOs succeeded in providing input into the policy formulation. Where they did, such NGOs seem to have lost their independence, becoming converted into quasi governmental agencies.<sup>19</sup> Generally speaking, however, 'independent' policy expertise and formulation capacity existed only in academia. In these cases, the most desirable career path involved progress from the top universities into the government research institutes.

Korea began systematically developing its research institutes in the 1960s. Each new institute was conceived in relation to a particular ministry that would completely fund their respective activities.<sup>20</sup> In turn, the corresponding ministry was the primary, if not exclusive, recipient of their policy advice.

Several interviews confirmed that very close relations existed between the ministries and the research institutes. Anecdotal accounts describe how working relationships were sufficiently intimate and the number of researchers limited enough, to enable both the policy-makers and the experts to engage in mutual dialogue and learning. Under authoritarianism, such close arrangements between researchers and their bureaucratic clients possibly developed because the number of individuals with the necessary academic qualifications were in short supply during the formative years of the post-coup bureaucracy, and because policy-making issues were focussed almost exclusively on the goals of economic development. As one respondent put it, during this period, 'the bureaucrats and researchers could engage in a common language oriented towards a common goal'. Such arrangements also attest to the fact that under authoritarianism, as several respondents indicated, the formulation of policies was perhaps the primary challenge faced by economic planners given that military dictatorship and its control over the *chaebol*, labour organisations and the media, let alone the bureaucracy, meant that the implementation of policies was able to proceed

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<sup>19</sup> Similar developments have taken place in Malaysia. See Henderson et al 2002.

<sup>20</sup> It should be noted that, at least initially, not all ministries had a corresponding think tank. The social ministries developed corresponding research institutes later than the economic ministries, which may have reflected their lower status in the ministerial pecking order.

relatively unchallenged, notwithstanding the rise of student and other opposition movements from the mid-1970s onwards.

The main bastion of research expertise was the Korean Development Institute (KDI). The KDI was established in 1971 by President Park and was charged with formulating and designing both the five-year economic plans which framed economic development at the macro level, as well as, from 1972, engaging in the formulation of social policy (Kwon 1999). The latter, however, as far as both the KDI and senior levels of the bureaucracy were concerned, was very much a secondary focus. The institutional position and power of the KDI relative to the other think tanks directly mirrored that of the EPB and its near absolute power over all the line ministries engaged in policy implementation.<sup>21</sup>

The Economic Planning Board was the epitome of the bureaucratic structure of policy-making during Korea's development era (early 1960s to late 1980s). It embodied the governance practices and style of national economic management long established under authoritarian rule, namely the centralisation of decision-making located in what was in effect, a relatively autonomous 'super-ministry'. At an organisational level, the autonomy of the EPB was oriented towards developing a form of economic governance through which the authoritative coordination of economic and social policies was possible. At an operational level, the EPB's autonomy insulated officials from the bulk of the bureaucracy (with the exception of the Presidential Office) and the undemocratic, repressive state ensured that it was insulated from any oppositional movements that might develop in civil society. It was free, therefore, to implement policies in whatever way was deemed necessary for economic development. Among other things this meant that EPB officials were free to mediate between the owners of the *chaebol* so that the government could selectively target one or another of them so as to direct resources in order to optimise the possibilities for economic growth (Kim, H-R. 2000a).

While the parallel structures between research think tanks and the ministries established a longstanding institutional configuration governing policy formulation and implementation, it should be noted that the story of economic governance under authoritarian rule is equally, if not more so, a story about the most powerful decision-making figure of all, the President. It seems clear that despite the autonomy given to the economic bureaucracy in coordinating policy formulation and implementation, the delegation of power to the machinery of government in general, was of a second order to the ultimate authority bestowed on the President. At times, the role of the President in economic governance has been both to provide the framework within which policies are formulated, as well as to provide the developmental goals around which economic and social policies are implemented. At other times, however, the power of the President was used to circumvent the executive-legislative divide, intervening in policy-making processes in such a way as to specify the content of policies as well

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<sup>21</sup> While the EPB was the lead agency in the economic bureaucracy, the Ministry of Finance and the Ministry of Commerce and Industry (MCI) were also significant agencies making up the troika of economic governance. As one senior official described it, 'the MOF's power lay in the collection of taxes and supervision of financial institutions. The MCI, while the lesser of the three, was influential especially as industrial and trade policies were central to the government's strategy throughout most of the development period'.

(Cheng et al 1998). As will be clear from later sections, this feature of governance has persisted through to the present day.

Over and above the actual mechanics of policy formulation and implementation described here, there is an issue important to our concerns that seems very clear. While there was some attention to matters of social welfare during the authoritarian period, poverty and inequality did not figure as a significant issue for economic policy. Only with regard to price controls in the domestic market (Amsden 1989), which would have helped the poor, is there any evidence of a concern for poverty within economic policy-making. Beyond this it appears that the planners of Korea's 'economic miracle' assumed that the 'trickle down' effects of economic growth, and the support mechanisms of the family, would provide social security and reduce deprivation.

### **3.2 Democratisation and the rise of civil society, 1987-1993**

While not immediately upsetting the institutional structure, the beginnings of political democratisation in 1987 represented a key moment in the evolution of South Korea's economic governance. Democratisation was fostered by, and in turn continued to foster, the rise of diverse social movements engaged, at times, in vehement challenges to centralised, authoritarian forms of policy-making. With democratisation, such movements became more able to diversify their efforts and began to target specific policy areas - especially those concerned with social welfare - that had previously been a low priority for the Government. Additionally democratisation opened an institutional space for the formal political expression of interests that had been mobilised in civil society. With this development the institutions of economic governance were confronted with the need to transform the roles and functions that had been inherited from the authoritarian era (Kim, K.R. 2000a).<sup>22</sup>

With President Roh Tae Woo's administration (1988-92) there began to be signs of change within the economic bureaucracy. In particular, our respondents reported that with the beginnings of democratisation, the onus in the policy process began to shift from the earlier stress on policy formulation (addressed above) to a greater priority for policy implementation.

Reflecting the shift in emphasis towards policy implementation, several respondents felt that soon after democratisation, the relative importance of the government think tanks began to decline. By the beginning of the 1990s, it seems that the close personal connections that once characterised the relations between the bureaucrats and the research institutes, had begun to wane. Leading think tanks such as KDI had become a victim of their own success. They began to attract large numbers of US-trained, and thus neo-classical economists, producing voluminous and increasingly academically-

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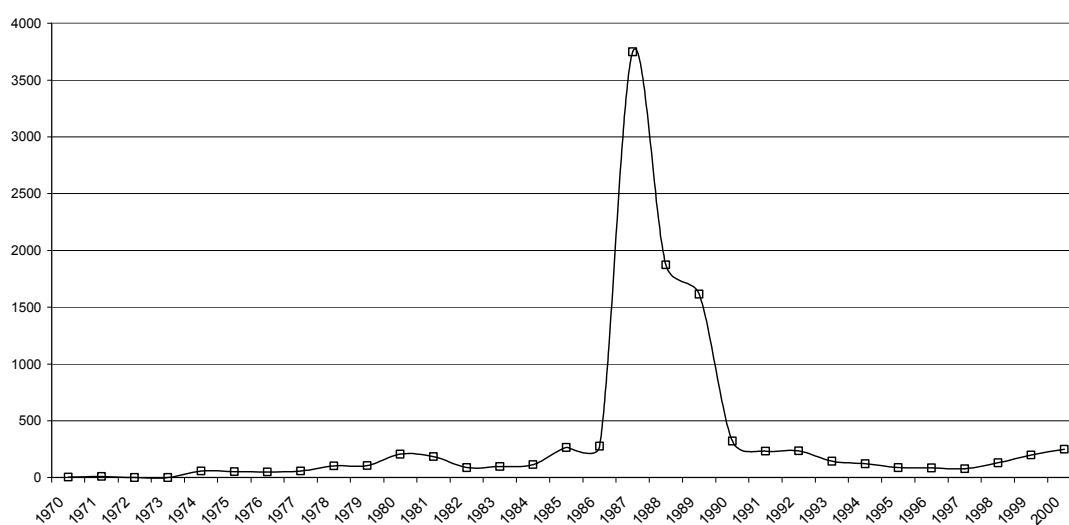
<sup>22</sup> Such a transformation was not an inevitable product of democratisation, however. As the Singaporean experience has shown, authoritarianism and democracy can go hand in hand such that the economic bureaucracy of the state can continue to be insulated not only from the political process in civil society, but also from its representations in the legislature. On the Singapore case see Rodan (1989) and Koh (1997).

oriented research reports, which, according to one official, were less accessible and less relevant to the tasks faced by the economic managers.

To grasp the new changes facing policymakers, we need look beyond the formal layers of the developmental state. The rapid development of an organised civil society (the rise of independent and militant trade unions, for instance) represented a critical development driving the shift in the focus of South Korea's governing institutions and ultimately challenging the stable institutional arrangements that supported authoritarian policy-making. Control over the media, and thus of public opinion and debate, could no longer be relied upon. Furthermore, the autonomy of the decision-making process (itself largely a derivative of the state's capacity to repress the development of effective forms of civil organisation), could no longer prevent the development of non-governmental organisations that actively sought to redress a number of social issues that previously had been subordinated to their struggle for democracy.

Associated with the emergence of formal democracy, a key transformation in civil society was the development of the labour movement that had previously been a prime target for state repression. There was an upsurge in union membership and activity, venting workers' dissatisfaction that had built-up under authoritarianism. With the onset of democratisation, the number of labour disputes increased tenfold (Figure 3). Along with workers' dissatisfaction with the government, activists increasingly challenged the monopolistic trade union structure itself. A number of enterprise unions moved to create rival union federation centres, breaking away from the Federation of Korean Trade Unions, the 'yellow union', which has long been the only officially-tolerated national forum for union activity, and one that was compliant with the wishes of both management and government. These more militant factions eventually (1995) amalgamated to form a rival trade union (discussed further in the next section).

Figure 3: Strikes and Lockouts, South Korea 1970-2000



Source: ILO Laboursta Database



Whereas civil movements were largely suppressed under authoritarianism<sup>23</sup> democratisation created the space for a dramatic expansion of NGOs. For instance, 74 percent of the NGOs currently in South Korea were established after 1987, 35 percent during the Roh administration (1987-92) and 39 percent during the Kim Young Sam government (1993-97) (Kim, H.R. 2000b). Having achieved political democratisation, the focus of the NGOs turned to a range of social issues including income disparity, real estate speculation, and economic justice (Kim, H.R. 2000b). One of the most notable and successful civil society developments during this period was the inception of the Citizen's Coalition for Economic Justice (CCEJ).

The CCEJ was the first major NGO to tackle social welfare issues. Its members urged the government to change policies over housing eviction and lobbied for the need to build more homes (a need the government responded to with its New Town Policy in the early 1990s). Furthermore, the CCEJ pressured the government to prevent land speculation. As one CCEJ member recalled, their original campaigns attempted to introduce more transparency in land deals given that over the previous decades, five percent of the population, especially the owners of the large *chaebol* had, in their estimation, come to own in excess of 60 percent of the land in South Korea (also see Henderson 1999).

Support from academics appears to have been central to the development of the new civil organisations. For a number of NGOs, university professors (between 250 and 300 currently work with the People's Solidarity for Participatory Democracy (PSPD), for instance) helped their expansion by bringing to them both technical competency in areas such as economics and law as well as credibility in policy-making circles. Academic expertise was also central to the labour movement particularly when the reform of labour law became a matter for public debate for the first time.<sup>24</sup>

Successful university academics had always tended to move into public service (in preference to the private sector). Under the authoritarian regimes, their influence in the structure of policy-making was largely confined to positions in the state research institutes such as KDI. With democratisation, however, several respondents felt that policy-makers - including the President's Office - began to use selected academics from Korea's elite universities as key advisors.

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<sup>23</sup> Most infamously when the police attacked a demonstration in Kwangju in 1980, leaving a death toll estimated at anywhere between 200 and 2000. One NGO that was tolerated by the authoritarian regimes was the 'Wednesday Group'. This was a small voluntary organisation of doctors, academics and civil servants which, in the late 1950s early 1960s met every Wednesday to discuss concerns over medical insurance. After the military coup of 1961, future President but then chairman of the Health and Social Affairs committee of the Supreme Council for National Reconstruction, Park Chung-Hee, resumed efforts initiated in December 1960 by the first Minister of Health and Social Affairs to establish this group as a formal Committee for Social Security (CSS), transforming this once civil organisation into an official advisory committee to support his later attempts as President to introduce the first social welfare programmes in Korea (see Kwon 1999). The CSS would then again ultimately transform into the Korean Institute for Health and Social Affairs (KIHASA), a fully-fledged governmental think tank operating under the auspices of the Ministry of Health and Social Welfare.

<sup>24</sup> For instance, in the creation of the Labour Law Review Committee in 1992, several university professors joined alongside members of the FKTU and the Korean Employers' Foundation to help draft revisions to the labour laws (Choi 2000).

### 3.3 Globalisation, neo-liberalism and the new 'Super-Ministry', 1993-1997

Where the Roh administration (1988-1992) was engrossed in managing the transition to democracy, the Kim Young Sam administration (1993-1997) sought to make its mark by 'modernising' the economy. Partly driven by its perceived need to be seen as a good global economic citizen, as a prelude to membership of the OECD (achieved in 1996), the Kim Young Sam administration instituted policies that were designed to change South Korea's image from that of a developing economy 'piloted' by an interventionist state, to an image of the country as a mature and developed economy governed by market forces and a relatively disengaged, economically liberal state. In furtherance of this aim, the Kim government introduced *Segyehwa*, which can loosely translated as 'Globalisation Policy'.

Although there were 43 projects covered by *Segyehwa*, their primary goal was to further market liberalisation. The government liberalised exchange rates, abolished various protectionist measures (including on the import of rice) and liberalised regulations on domestic and international capital investments (Park 1996). Additionally, the government reduced the size of the state bureaucracy, justifying its actions by means of neo-liberal 'small state' rhetoric.<sup>25</sup>

In many ways Korea's experience with globalisation represented a distinct juncture in economic governance, fuelled by an effort to hasten the liberalisation process and restructure its governing institutions. As Kim (2000a:568) argues, in executing reforms, 'the government overlooked the possibility that withdrawing state intervention [in the interests] of deregulation [might] rather dismantle the foundation for economic governance'. Indeed, interviewees inside the economic bureaucracy offered similar views, confirming that liberalisation occurred 'too fast' and without the introduction of the sorts of financial sector regulations that could have prevented the excess credit that was one of the causes of the economic crisis.<sup>26</sup>

Particularly detrimental to the country's economic policy-making capacity, and thus - arguably - its long term economic health, was the abolition of the Economic Planning Board as an autonomous unit. Two of its key divisions - the Supervisory Board of Financial Affairs and the Department of Planning and Budget - were transferred to the Ministry of Finance, creating a new 'super-ministry', the Ministry of Finance and

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<sup>25</sup> Under Kim Young Sam, the limited government initiative aimed to reduce the civil service by 10 percent over the course of his five-year term. In the event, moves to reduce the number of civil servants extended into the Kim Dae Jung administration, clashing with efforts to expand the social protection system and with it, the pressures for increases in staff. For instance, some respondents have commented upon the coordination problems between the Ministry of Planning and Budget (MPB) and the Ministry of Government Administration and Home Affairs (MOGAHA) over the implementation of the National Basic Livelihood Security Act passed in 2000. On the one hand the MPB attempted to increase the workforce allocated to NBLIS implementation given that workload ratios were roughly 500 cases for each civil servant. On the other, however, the MOGAHA resisted MPB moves to expand staff numbers given its opposing mandate to reduce the number of civil servants.

<sup>26</sup> While most of the excess credit flowed to the *chaebol* (as we indicate below), substantial amounts also ended up fuelling an economic bubble driven by a consumption boom on overseas travel and luxury items. For instance, debt associated with travel accounts jumped from US\$0.57 billion in 1993 to US\$1.19 billion in 1995 and then to US\$2.6 billion in 1996, while the current account deficit increased from US\$3.8 billion in 1994 to US\$8.5 in 1995 and US\$23.7 in 1996 (Lee 2000).

Economy (MOFE).<sup>27</sup> Several respondents confirmed that in creating this super-ministry, the government had eroded its capacity for checks and balances in the policy-making processes (a verdict that would be confirmed after the crisis). As a consequence, the institutional mechanisms were in place for South Korea's subsequently rapid shift from a long-term planning to a short term, finance-driven, form of economic governance.

Alongside changes in the economic bureaucracy, the role played by the research institutes in policy formulation was also changing. Along with the finance-led economic bureaucracy, several respondents felt that the Korea Development Institute had also begun to concentrate its research focus on areas such as public finance rather than social welfare. As one former senior KDI researcher confirmed, by the mid 1990s, concerns over social welfare in general, and poverty and inequality in particular, had disappeared from KDI activities (leaving these issues to more specialist institutes such as the Korea Labour Institute and the Korea Institute for Health and Social Affairs). Furthermore, responses from several policy-makers expressed views that research organisations such as KDI had a much depreciated role, tending to become 'merely' think tanks rather than key policy-formulating agencies in their own right.

Beyond the bureaucracy, organisations within Korean civil society continued to grow in size and to some extent in political influence (although with signs of increasing polarisation and internal differentiation that would become increasingly apparent after the economic crisis). For instance in 1994, the People's Solidarity for Participatory Democracy (PSPD) was established. Focusing on all aspects of social welfare, the rapid growth of the PSPD appears to have motivated the CCEJ to retreat from its original concerns over social welfare (particularly housing and land speculation). Rather, during the 1990s, the CCEJ began to mobilise efforts to promote its own views on economic reform more generally. As one housing expert indicated, the CCEJ's original focus now seems to have been marginalised as it has come to be dominated by neo-classical (and largely American trained) economists who have tended to emphasize their view on market reform.

In the labour movement, the trade unionists which had broken away from the Federation of Korean Trade Unions to set up rival organisations, by 1995 had merged their efforts and established the Korean Confederation of Trade Unions (KCTU). The nature of the KCTU leadership has been a key to the more militant approach taken by the organisation. Many of the leaders were trained by early activists and socialists, themselves experiencing state repression during the drive to promote Korea's heavy industries in the 1970s. Their militant approach and critical stance towards the government, delayed their official recognition until 1999.<sup>28</sup>

The influence of civil organisations upon policy-makers also grew as significant moves to formalise the institutional channels for social dialogue ensued. For instance, the government created the Industrial Relations Reform Commission (IRRC) in 1996

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<sup>27</sup> According to former EPB personnel, this treatment was effected with no internal debate or forewarning, leaving most staff to learn of the decision from Kim Young Sam's televised address. The EPB's social planning division, however, was not transferred to the MOFE.

<sup>28</sup> It should be noted that trade union militancy was one of the key factors driving the upward movement of manual workers' wages from the late 1980s and speeding up the 'trickle down' of growth.

(Choi 2000). As the successor to the Labour Law Review Committee created four years earlier, the IRRC was given a specific two-year mandate to build a consensus concerning revision in the labour law and report its proposals to the President. Unlike its predecessor, the IRRC promoted widespread public debate. Yet the benefits of expanding the social dialogue were ultimately overshadowed by covert redrafting of the IRRC proposals. Under pressure from the *chaebol* and other employers, last minute reforms to the labour law ignored union arguments for job security and promoted the standard neo-liberal concerns with labour market 'flexibility'. The workers' response was a general strike in December 1996 which resulted in the repeal of the new labour laws.

### 3.4 Crisis and the reform of economic governance, 1997-2001

With hindsight, it is clear that it is courting disaster to liberalise an economy and undertake associated bureaucratic reforms, as did the South Korean government, without, at the same time, building an institutional capacity to manage the now freer markets. Some analysts have argued that by failing to build the state's capacity for market oversight, the Kim Young Sam government was unable to manage the adjustment from a relatively planned to a more market-driven economy (Kim, H.R. 2000a; Lee 2000).<sup>29</sup> Nowhere was this more clear than in the case of the merchant banks which expanded dramatically from the late 1980s and became one of the principal sources of the economic crisis of the late 1990s.

Throughout the developmental era, the relationship between the government and the *chaebol* has been that of implicit risk-sharing partners, with local financial institutions serving as facilitators for the national drive for industrialisation. The state's 'management' of the *chaebol* was institutionally centred on the EPB and practically on loans in support of policy initiatives coupled with restrictions on the flows of foreign capital and interest rate manipulations.<sup>30</sup> Between 1961 and 1982 the government owned all the major banks and directed policy loans to government priority sectors such as in exports and heavy chemical industries.<sup>31</sup> Even after the privatisation of the commercial banks in 1982, they were subject to tight regulation until the early 1990s. The share of government-approved policy loans in total commercial bank loans, for instance, remained around 60 percent between 1987-91 (see Table 1)

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<sup>29</sup> Lee (2000) has argued that following the crisis, economic policy decision-making became increasingly politicised (a view supported by our analysis). As a consequence, many market actors lobbied officials to further weaken the already weak mechanisms charged with regulating the newly liberalised economy.

<sup>30</sup> There was, of course, much more to it than this, including, apparently, draconian laws designed to limit capital flows into speculative (as distinct from productive) investments. For a summary of the policy instruments used by South Korean governments during the 'developmental era', see Henderson (1993).

<sup>31</sup> During the heavy chemical industrialization drive in the 1970s, for instance, policy loans constituted about 50 percent of total domestic credit (Kim, E.M. et al 2000).

Table 1: Share of Policy Loans by Deposit Money Banks (DMBs) and Non-Bank Financial Institutions (NBFIs)

(Unit: %)

	1973-81	1982-86	1987-91	Average during entire period 1973-91
<b>DMB loans (A)</b>				
Government funds	7.5	7.4	8.0	7.6
National Investment Fund	4.3	5.1	3.0	4.2
Foreign currency loans	21.1	19.7	19.4	20.3
Export loans	21.3	16.9	5.1	16.2
Commercial bills discounted	8.0	13.9	16.5	11.6
Special funds for SMCs	5.9	5.6	6.5	6.0
Loans for AFL	6.1	5.3	7.4	6.2
Housing loans	8.0	13.1	14.1	10.8
Other	17.7	13.1	20.0	17.1
Policy Loans Total	100.0	100.0	100.0	100.0
<b>NBFI loans (B)</b>				
KDB loans	91.9	71.7	83.7	84.8
(National Investment Fund)	(25.7)*	(18.5)	(7.9)	(19.5)
EXIM loans	8.1	28.3	16.3	15.2
(National Investment Fund)	(2.5)*	(4.7)	(2.3)	(3.0)
Policy Loans Total	100.0	100.0	100.0	100.0
(A)/DMB loans	63.0	59.4	59.5	61.2
(B)/NBFI loans	48.0	32.3	15.3	35.9
((A)+(B))/domestic credit	48.9	40.8	30.9	42.4

Notes:

- 1) Figures are annual averages.
- 2) \* : Annual average during 1974-1981.
- 3) Includes loans for imports of key raw materials, loans on mutual installment, loans for machinery, equipment loans to the export industry, special equipment funds, and special long-term loans.

Sources: National Statistical Office, Korean Economic Indicators, various issues; Bank of Korea, Monthly Bulletin, various issues. Quoted from Cho, Yoon Je and Kim, Joon-Kyung (1995)

With the privatisation of the banks and in spite of restrictions on the size of individual share holdings<sup>32</sup>, it was the *chaebol* that eventually became dominant amongst the largest shareholders (see Table 2).

<sup>32</sup> In 1982, when the privatization of the banking sector was implemented, a ceiling of 8 percent was imposed on individual ownership of nationwide commercial banks in order to prevent any single shareholder exerting excessive influence over a bank's management. This restriction was further strengthened when the ceiling was lowered to 4 percent in 1994. Despite this restriction, however, the ownership distribution of South Korean banks became as concentrated as those elsewhere, such as the USA. By the end of 1996, the combined shares of large shareholders (those owning more than one percent of the total voting stock) of nationwide banks amounted to an average of over 39 percent. For local banks, whose ownership structure is much more concentrated than nationwide banks, due to a higher ceiling, the combined shares of large shareholders was nearly 50 percent (Table 2) (Kim, E.M. et al 2000).

Table 2: Share of Banks Owned by the Top 30 Chaebol

(As of the end of 1996, Unit:%)

<i>Chaebol</i>	Ownership Share for Each Bank
1. Hyundai	Korea First Bank(2.20), Hanvit Bank(2.00), Seoul Bank(1.99), Kangwon Bank(11.89)
2. Samsung	Chohung Bank(2.81), Commercial Bank(7.03), Korea First Bank(3.96), Hanil Bank(4.76), Seoul Bank(3.77), Korea exchange Bank(1.05), Shinhan Bank(3.36), KorAm Bank(1.02), Hana Bank(3.42), Peace Bank(1.28), Daegu Bank(5.65), Pusan Bank(1.02), Kyonggi Bank(1.57), Jeonbook Bank(1.20), Kangwon Bank(1.22), Kyung nam Bank(2.38)
3. LG	Korea First Bank(3.03), Hanil Bank(2.47), Boram Bank(7.58), Cheju Bank(1.80)
4. Daewoo	KorAm Bank(18.56)
5. SK	Kyonggi Bank(3.42)
6. Ssangyong	Chohung Bank(1.98), Korea Exchange Bank(1.04), Hana Bank(1.52), Kookmin Bank(1.96)
7. Hanjin	
8. Kia	Kyonggi Bank(5.63)
9. Hanwha	Korea First Bank(1.04)
10. Lotte	Chungchong Bank(16.49), Pusan Bank(23.93)
11. Kumho	Kwangju Bank(7.87)
12. Doosan	Boram Bank(11.34)
13. Daelim	Hanil Bank(3.57)
14. Hanbo	
15. DongAh	Seoul Bank(1.50), Cheju Bank(2.31)
16. Halla	
17. Hyosung	Hana Bank(5.16), Kyungnam Bank(11.57)
18. Dongkuk Steel	Seoul Bank(1.27), Pusan Bank(3.85), Kyungnam Bank(3.92)
19. Jinro	Hana Bank(3.51)
20. Kolon	Boram Bank(5.80)
21. Tongyang	Donghwa Bank(1.03)
22. Hansol	
23. Dongbu	Cheju Bank(1.06), Chungbuk Bank(1.74)
24. Kohab	
25. Haitai	
26. Sammi	
27. Hanil	
28. Kukdong-Construction	
29. New Core	
30. Byucksan	

Source: The Bank Supervisory Board (Kim et. al 2000).

More importantly - because they were crucial to the onset of financial turmoil in 1997 - the non-banking financial institutions (NBFIs) were largely free of ownership restrictions. As a result, many NBFIs came to be owned and controlled by the *chaebol*. By 1997, the 70 largest *chaebol* owned a total of 114 NBFIs (an average of five

NBFIs each in the case of the 5 largest *chaebol* ) concentrated in securities, merchant banking, insurance and installment credit (see Table 3)!

Table 3: Number of Non-Banking Financial Institutions Owned by the Top 70 Chaebol

(As of the end of 1997, Unit: number of firms)

	Top 5 Chaebols	Top 6-30 Chaebols	Top 31-70 Chaebols	Total
Merchant Bank (29)	3	7	4	14
Securities (26)	6	5	1	12
Investment Trust (24)	4	6	0	10
Life Insurance (31)	2	4	8	14
Fire & Marine Insurance (13)	2	3	0	5
Installment Credit (26)	2	7	3	12
Mutual Saving & Finance (219)	1	5	12	18
Venture Capital (56)	3	4	6	13
Credit Card (7)	3	1	0	4
Finance & Factoring (46)	3	4	5	12
Total (487)	29	46	39	114

Notes:

- 1) The rank of *chaebol* is based on total borrowings.
- 2) The figure in the parentheses represents the total number of financial institutions at each financial sector.
- 3) Leasing companies are excluded as they are owned by banks.

Source: National Information and Credit Evaluation Inc.

In spite of the highly concentrated ownership structure of the NBFIs, financial supervision was lax. While the principal regulator and supervisor of NBFIs was notionally the Ministry of Finance and Economy, only a small and ineffective working-level unit was assigned to the supervisory role. In short, the NBFIs were under the strong influence of *chaebol* while government supervision had become all but absent (Kim, E.M. et al 2000).

The policy loans and the state's sharing of investment risk associated with them, then, certainly contributed to rapid industrialisation, but also encouraged heavy corporate leverage - with debt-equity ratios of up to 5:1 - and the creation of an 'immature' banking sector.<sup>33</sup> With (a) the abandonment of strategic economic planning and the weakening of financial regulation that resulted from the demise of the EPB with (b) the liberalisation of financial markets associated with the 'globalisation policy', (c) the explosion of short-term credit and (d) the fact that both the 'real' economy and the financial sector were largely owned by the *chaebol* anyway (who were themselves the

<sup>33</sup> What principally drove the need for such high levels of corporate leverage, however, was the aggressive competition among the *chaebol* themselves. It should be borne in mind that while debt-equity ratios of even 1:1 were (and are) inconceivable in capital market-financed forms of capitalism (such as in Britain and the United States), the South Korean ratios were fairly typical by Japanese (and other East Asian) corporate standards. Indeed their economic 'miracles' that would have been inconceivable without such high debt-equity ratios and the risk-sharing associated with them.

major beneficiaries of the loans) and in the South Korean context, you had a disaster waiting to happen. By 1997 when debt-equity ratios had reached over 20:1, as they were for some *chaebol*, and bankruptcies began to ensue<sup>34</sup>, financial panic - given the dynamics of 'mad money' (Strange 1998) - and the economic and social devastation it wrought, was inevitable. It seems clear from the South Korean case that a principal determinant - at the global economic moment when it mattered most - was *under*-regulation not over-regulation as has been argued across East Asia (see Chang 1998, Chang et al 1998, Henderson 1999).

### Dilemmas of post-crisis reform

As the government looked for the causes of and scapegoats for the crisis, one view was that the concentration of policy-making powers and information in the Ministry of Finance and Economy was, in part, to blame for the lack of early detection of the sign of impending economic demise. Indeed, there is evidence that at least some of the senior bureaucrats in the economic bureaucracy, the Ministry of Commerce and the Bank of Korea in particular, had raised concerns prior to the crisis and that the MOFE, despite having control over all of the main policy-making tools and comprehensive access to information, did not react to these concerns. Thus, the emerging verdict was that this new lead agency in the economic bureaucracy was culpable for failing to prevent, if not helping to precipitate, the crisis.<sup>35</sup> As a consequence, one of the first tasks of the current (from 1998) Kim Dae Jung administration was to restructure the state bureaucracy once more.

In terms of the economic agencies, the most notable target of the government reform effort was the rationalisation of macroeconomic functions and a restructuring of the Ministry of Finance and Economy. MOFE was deprived of two critical responsibilities - budgetary and financial supervision - but it was left in charge of taxation and related financial policies. In reorganising responsibilities, two further agencies were introduced into the economic bureaucracy, the Ministry of Planning and Budget (MPB) and the Financial Supervisory Commission (FSC).

In creating the Financial Supervisory Commission, the government consolidated several agencies previously charged with supervising the banks, securities companies, and insurance firms. Reporting directly to the President, the agency took over regulatory reforms and supervision of both the financial and corporate sector.

The Ministry of Planning and Budget was created in mid 1999 through the merger of the Board of Planning and Budget and the Budget Office (both of which had been created in early 1998). The MPB was given responsibility for the planning of all national policies as well as the management of the national budget. As a consequence, MPB officials now engage in the planning, budgeting, implementation

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<sup>34</sup> By the end of 1996, debt-equity ratios for some of the larger, but less prominent *chaebol*, were 21:1 for Halla, 32:1 for Sammi and a staggering 86:1 for Jinro (Henderson 1999).

<sup>35</sup> The backlash against the MOFE 'super-ministry' was underlined by a special parliamentary committee on the crisis chaired by the Minister of Commerce. Indeed, the Deputy Prime Minister (head of the MOFE) was prosecuted and his post as Deputy PM was (temporarily) disbanded in 1998.



and evaluation stages for all economic and social policies where the budget is concerned.<sup>36</sup>

With the rationalisation and reorganisation of the economic bureaucracy, policy coordination has become even more crucial to effective national economic management. Unfortunately, however, effective coordination among the state's economic agencies continues to be problematic. Interview evidence from within the economic bureaucracy suggests that the coordination problems are seen as a product of the contestation associated with democratisation more than as a product of bureaucratic reforms. Other respondents, however, report that the presentation of economic policies for public consumption is increasingly disjointed and inconsistent, implying that at least part of the problem derives from the structure of the bureaucracy and the inter-agency competition that it is generating.

Other evidence suggests that recent reforms have indeed failed to deal with the problems of policy coordination and may even have exacerbated them. In terms of monetary policy, for instance, the reforms may have actually increased coordination problems by creating a system where the authority to manage monetary and financial policy is divided among three agencies: the Bank of Korea, the Ministry of Finance and Economy, and the Financial Supervisory Commission.<sup>37</sup>

Indeed, the reform effort as a whole has been faced with organisational change and implementation problems. For instance, while one problematic super-ministry (MOFE) was being restructured, another was being created, this time in charge of overall government administration. The Ministry of Government Administration and Home Affairs (MOGAHA) was created in 1998.<sup>38</sup> Inundated with projects and responsibilities, during the second wave of public sector reforms in 1999, the government reversed tack, this time attempting to take responsibilities for civil service reform away from MOGAHA, and locate them in a new dedicated agency: the Civil Service Commission. The transfer of reform implementation responsibilities to the Civil Service Commission, however, have proved problematic, seemingly because MOGAHA has resisted the dilution of its power.

If the institutional reforms exacerbated coordination problems at the level of implementation, they had similar implications for the process of policy formulation. In 1998, the ministries and their research institutes were formally separated. In the reorganisation, all research institutes (over 50 fifty large organisations) were placed under the jurisdiction of the Prime Minister's Office (PMO)—the much weaker

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<sup>36</sup> According to one official, the MPB's role in policy-making begins with meeting the ministries involved in a particular policy initiative. Only in the case of a disagreement will the MPB consult with the research institutes for advice. Once a budget is agreed upon by the ministries and the MPB, the budget is presented to the general assembly of Parliament. After Parliamentary approval, the MPB oversees the implementation of the policies and monitors expenditure.

<sup>37</sup> In terms of monetary policy, attempts to rationalise the financial system were pursued through changes in the Central Bank. Where the Bank of Korea was originally set up to facilitate the state's economic development plans and serve as the government's bank, comprehensive reform in the Bank of Korea Act immediately after the onset of the crisis sought to increase the Central Bank's independence from the government, giving it an increasing role in financial supervision. For instance, in 1998, the Bank became responsible for monetary policy and inflation, losing previous functions such as market supervision that was transferred to the FSC.

<sup>38</sup> By merging the previous Ministries of Government Administration and Home Affairs.

counterpart to the Presidential 'Blue House'. The restructuring required that each institute's policy- output be reported to the PMO. Furthermore, the funding mechanisms for the research institutes were changed. On the one hand, the majority of research funding would now come from the PMO. On the other hand, research funding was to be increasingly distributed on a competitive contract basis.<sup>39</sup>

Officially, the rationale for severing the ties between the ministries and their respective research organisations was to remove the possibility of bias in the formulation of policies (which was assumed to have played a part in facilitating the crisis). While several interviews confirmed that the links between the research institutes and the ministries had been weakening, anyway, during the 1990s, the restructuring does not seem to have consummated this trend by completely de-linking the research institutes from the ministries. A common view from both policy-makers and researchers is that the former system still operates, albeit at an informal level. The ministries still remain the primary recipient of policy outputs of their former research institutes and in practice still provide the guidelines for policy research. The problem now is that with the duplication of institutional management (having to report to two 'masters'), the work load of the research institutes has increased without a compensatory growth in staff numbers.

While it seems clear that the government's institutional responses to the crisis have not fragmented the economic bureaucracy, it does appear that the policy-making process may now be more contested within the bureaucracy - as a result of internecine competition between the various agencies - and thus less coherent than was previously the case. Attesting to these developments, the coordinating role of the Deputy Prime Minister was revived in 2001.<sup>40</sup>

### Developments in civil society

In the wake of the crisis there is evidence of growing rifts between the organisations of civil society. For instance, the Citizen's Coalition for Economic Justice, once the largest of the NGOs and the first to pursue social welfare concerns, appears to have lost ground to the People's Solidarity for Participatory Democracy. Currently the largest NGO (with over 13,400 members and an annual budget of 1.8 billion won<sup>41</sup>), the PSPD mobilises around social welfare from an opposing position to the CCEJ. While responses from PSPD staff downplay the extent of the rivalry, claiming that the two organisations work in different areas, there has been public opposition to increased social welfare expenditure by some CCEJ executives. This contrasts with PSPD support for increases in welfare expenditure.

If the principal NGOs mobilising around social welfare do not speak to the government with a coherent voice, neither does organised labour. Our interviews suggest that the historic ideological and political differences between the Federation

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<sup>39</sup> For instance, the Korea Rural Economic Institute, once under the Ministry of Agriculture (MOA), now receives 50 percent of its funding from the PMO, 25 percent from MOA contracts, and 25 percent from projects initiated by other ministries.

<sup>40</sup> Unlike the previous structure, the coordinating role of the DPM is now filled by two individuals, namely, the Minister for Education and Human Resources as well as by the Minister of Finance and Economy.

<sup>41</sup> About 957,000 GBP or 1.36 million USD.

of Korean Trade Unions (FKTU) and the Korean Confederation of Trade Unions remain and that the experiences of economic crisis seem to have done little to alter the situation. While particular issues sometimes result in a 'common front', for the most part mutual distrust prevents the coherent response to business and government policy that might otherwise have been anticipated.

The rifts between civil society, more generally, and the government that were moderated in the early years of democratisation, also re-emerged after the crisis. Initially, however, the experiments in social dialogue of the 1990s were extended in 1998 when the KCTU was invited, for the first time, to participate in the new Tripartite Commission on collective bargaining (Lee and Lee 2000).<sup>42</sup> After three weeks of negotiations, a compromise was reached; the government promised to create a workplace council for civil servants and to allow teachers to unionise. They promised to improve union rights and to give unions full rights to participate in political activity. Furthermore, the government also promised to spend more on unemployment and social welfare. In return, the unions accepted a new redundancy system, effectively endorsing the government's longstanding goal to increase labour market flexibility in the *chaebol*.

Notwithstanding this apparent success, however, evidence suggests that the strength of the social dialogue has been both limited and ephemeral. In the latter half of 1998, labour disputes erupted over the restructuring of the banking and corporate sectors. In early 1999, both labour federations withdrew from the Tripartite Commission and in May of that year the Seoul Subway Union initiated a week-long walkout in protest over public sector reform. While the agreements reached by the Tripartite Commission were passed into law, interviews with both government and trade union officials suggest that social dialogue has effectively come to a halt.

#### **4. ANALYSIS: ECONOMIC GOVERNANCE AND POVERTY**

Given that official statistical accounts suggest that the economic and social impact of the crisis has been contained by the Kim Dae Jung administration, this suggests that government reforms have been successful in balancing economic and social needs in the recovery effort. Indeed, the recovery in the country has been much more rapid than has been the case in regional neighbours – Thailand, Malaysia, Indonesia. Furthermore, this has been achieved in the context of South Korea's first explicit attempts at poverty reduction. Accordingly, in this section, we discuss South Korea's evolving institutions of economic governance in order to understand their relationship to social welfare policies in general and to poverty alleviation in particular.

The poverty counter-measures initiated under the Kim Dae Jung administration were two-fold and, by South Korean standards, they represent a radical shift in policy. They involved reforms to the social insurance system and the development of social assistance programmes.<sup>43</sup> In terms of poverty reduction, the most notable reform in

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<sup>42</sup> Yet as one KCTU member remarked, both the FKTU and the Korea Employer's Federation had full access to negotiation meetings in the social dialogue council while the KCTU did not.

<sup>43</sup> See Kim, Y.M. (2001) for further details.

social insurance concerned the Employment Insurance System (EIS).<sup>44</sup> The government resisted efforts by MOFE to privatise parts of the system (a continuation of pursuits initiated under the previous administration). Rather, the government chose to preserve the public management structure, expand its coverage, increase benefits, and introduce labour market measures previously unknown in South Korea. For instance, coverage was expanded to all wage-earning employees including non-standard workers (ie. temporary and part-time workers). By 2000, the EIS covered 55.1 percent of the workforce, compared with only 33.1 percent in late 1997. However, despite this extension in coverage, no more than 11 percent of the unemployed population received unemployment benefits at the peak of the crisis in 1999 (Park et al 2001). Alongside increases in the level of benefit and allowance period, the government also introduced new forms of active labour market programmes, such as job training, as well as more traditional 'passive' measures such as unemployment payments.<sup>45</sup>

Beyond reforms to the social insurance system, the development of social safety nets targeting those hardest hit by the economic crisis (the poor and unemployed), were more significant anti-poverty measures. The government, for instance, temporarily increased the funds given to job training for the unemployed, loans for the jobless to secure a livelihood, and temporary livelihood protection programmes for the poor. In 1999, the government allocated over 4,365.4 billion Won (then about £2.36 billion) or 59.5 percent of the total unemployment budget to these four programmes. By 2000, conditions were improving with official unemployment levels declining dramatically from a high of 8.4 percent in the first quarter of 1999, to 5.1 percent at the start of 2000 and 3.7 percent by the end of the year (see Figure 4). The government curtailed these safety net expenditures in 2000, reducing their budgetary allocation by 45 percent to 2,410 billion won (then about £1.3 billion), as well as discontinuing the temporary livelihood protection programme.

While the social safety nets introduced immediately after the crisis were only conceived of as a temporary response, in line with World Bank recommendations, the government did enact a lasting institutional reform of the social insurance system. In October 2000, the government overhauled existing laws and established the National Basic Livelihood Security law (NBLs). Reforms focused primarily on two aspects: eligibility requirements and conditionalities. Firstly, the government repealed the existing eligibility requirement which had formerly excluded those between 18 and 65 years of age as well as individuals, or any age other than children, who were able to

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<sup>44</sup> Given the dramatic rise in unemployment, reform in the employment insurance system was particularly important for poverty reduction. Yet to differing degrees, each pillar of the social insurance system was reformed under the Kim Dae Jung administration. For instance, modest reforms to the pension system attempted to expand coverage to the entire population by introducing schemes for the urban self-employed. This improved pension coverage from 43.7 percent in 1997 to 75.8 percent of the economically active population in 1999 (Yang 2000). On the other hand, the most extensive reform efforts were targeted on the Health Insurance System. Along with a slight extension to the scope of health insurance benefits, the government attempted an ambitious merger of over 420 health insurance societies - each independently managed and having different contribution rates - into a single, publicly-managed insurance plan with a nationally unified contribution rate. Yet reports from some trade union officials claim that these reforms were a 'disaster' and reform debates have since focussed on the development of private health insurance since 90 percent of hospitals are already privately owned.

<sup>45</sup> 'Traditional', that is, for other countries. Although active labour market policies were first introduced after the crisis, passive measures have continued to receive higher budgetary allocations.

work (ie. the vast majority of the population). Under the new law, eligibility was limited only by income level and value of assets. At present, this means anyone earning less than 260,000 won per month (roughly £138), and who possesses less than 30 million won in assets (roughly £16,000), is covered under the NBLS. Secondly the government introduced 'workfare' conditionalities into the livelihood protection system. Given drastic increases in public expenditure for the poor following the crisis (see Table 4), Korea's economic agencies and especially the Ministry of Planning and Budget, insisted on conditionalities requiring able-bodied claimants to participate in job training or self-support programmes.<sup>46</sup>

Table 4: Livelihood Protection Budget (1996–1999)

	<i>1996</i>	<i>1997</i>	<i>1998</i>	<i>1999</i>
Absolute Budget	3,606	4,357	5,749	11,353
Rate of Increase	-	20.8	31.9	97.5

(unit: hundred million Won, %)

Source: PSPD (2000)

In summary, the Kim Dae-Jung administration initiated Korea's first concerted attempts to tackle poverty and income inequality through a rapid expansion of social expenditures coupled with developments in the social protection system.

Furthermore, his government advanced the idea of 'Productive Welfare' as a new macro-economic framework in which social welfare and poverty were to be key considerations in economic management (discussed further in section 4.2). Indeed, the priority now given to poverty-related issues by economic managers is underlined by the fact that some of these policy issues have been raised - and proposals made - within the main coordinating forum for the economic bureaucracy: the economic policies coordination meeting of the 'Blue House'.

Yet while advances in poverty reduction and welfare policy-making have emerged alongside recent developments in economic governance (at times emerging from the economic bureaucracy itself), the link between economic governance and poverty in contemporary Korea, is not as straightforward as it may at first seem. In order to show how and why this is the case, we need to consider arrangements from an earlier period in South Korea's system of economic governance.

#### **4.1 The Economic Planning Board as welfare's 'relative' ally**

Following the introduction of South Korea's 'Globalisation Policy' in late 1994, as indicated earlier, the then President, Kim Young Sam, authorised the merger of the

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<sup>46</sup> While reflecting the 'neo-liberal' orientation of many in the economic bureaucracy, the use of conditionalities in National Basic Livelihood Standards Act is less stringent than workfare policies in the US context (cf. Kim, Y.M. 2001 and Peck 2001). For instance, under the U.S. Personal Responsibility and Work Opportunity Reconciliation Act of 1996, recipients are required to enter the workforce within two years and end assistance within five years. Furthermore, the NBLS introduced self-support programmes as a complement to workfare programmes.

Economic Planning Board into the Ministry of Finance (MOF). Crucially, by removing control over economic planning from EPB heads and transferring it to MOF directors, Korea abruptly shifted from a planning to a finance-driven form of economic governance. Evidence suggests that the introduction of *Segyehwa* ('globalisation policy') and associated reforms effectively marginalised the support for the development of social welfare programmes that had been emerging from within the economic bureaucracy.<sup>47</sup>

Unlike the MOF, the EPB had always operated with a much wider remit than economic policy *per se*.<sup>48</sup> Indeed, it played an important role in the development of the early versions of the social protection system and was active in the formulation and implementation of social policy more generally.<sup>49</sup> The development of the Employment Insurance System, initiated in 1995, was a case in point and it is worth exploring in some detail.

It seems that the EPB was the first government agency to recognise the need for unemployment insurance in the early 1970s (Yoo 1999), but it was not until the early 1990s that opposition to the idea, from elsewhere in the government apparatus, was overcome. With support from the Ministry of Labor, the EPB publicly acknowledged the necessity for an employment insurance system as part of its 7<sup>th</sup> Five Year Plan (1992-1997).<sup>50</sup> At the time, this initiative was opposed by other economic agencies, such as the Ministry of Commerce, as well as influential organisations such as the Korea Employers Federation (KEF). These groups argued that there was little to warrant a policy initiative that would increase the financial burden on firms (especially small and medium sized enterprises) given that the unemployment rate had fallen to 2.3 percent by 1991 and had been declining for over a decade (see Figure 4).

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<sup>47</sup> This can be seen from the structure of the new Ministry of Finance and Economy, which did not incorporate the social development planning division of the EPB when it absorbed the latter.

<sup>48</sup> The involvement of South Korea's economic managers in social policy formulation appears to have stemmed, at least in part, from executive decisions. President Park's appointment of the Minister of Social Welfare to the head the EPB in the late 1970s was one important development in this sense. With the rise of the Chun administration (1980–1986) following the assassination of Park in October 1979, the government was faced with the task of balancing both economic and military interests. The military, through the National Security Council, began to promote the idea of building a welfare state as a way of legitimating military rule, while the larger goal of economic development continued to be promoted by Chun's closest economic advisors (Kwon 1999). It appears that the solution taken by Chun was to invest a greater degree of control over social policy formulation in his economic managers, thus merging efforts to develop a semblance of a welfare state (it was never intended to be more than that) with a renewed focus of economic development. Ultimately, while the support for building a welfare state soon dissipated as military rhetoric changed tack, the EPB continued to pursue the social welfare 'project'; a role that the EPB would retain until the elimination of its autonomy.

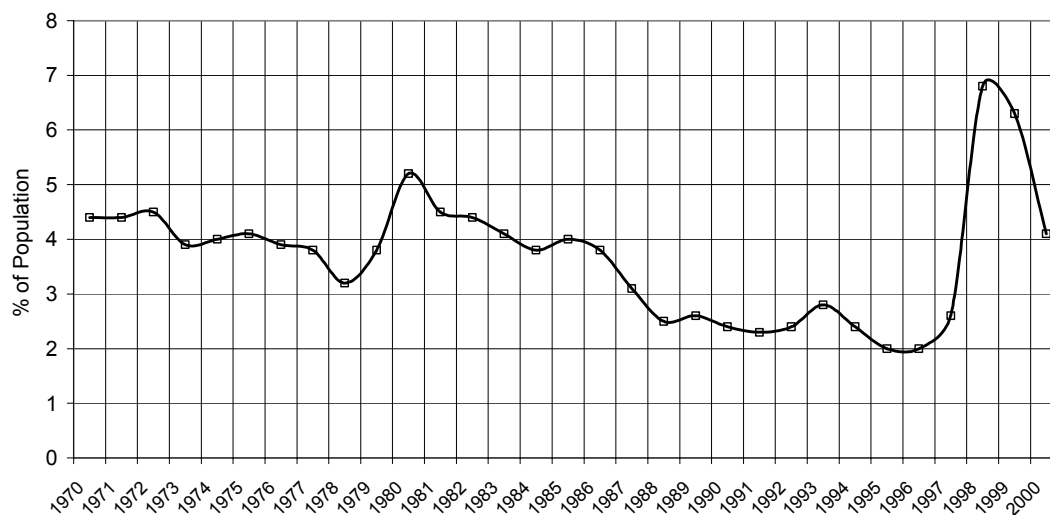
<sup>49</sup> This is not to detract attention from the overarching fact that throughout the developmental era, advances in social welfare have always emerged from Presidential initiatives to gain legitimacy for their newly-elected administrations (Kwon 1999). While the role of the President has been paramount in supporting social welfare, the EPB often took ultimate responsibility for the administration of social welfare programmes and participated in their actual design. Indeed, on occasion, it took Presidential intervention to prevent the EPB from taking responsibility for social welfare programmes. The control of the health insurance programme of 1975 (when President Park sided with the Minister of Health and Social Affairs against the interests of the EPB) was a case in point (Kwon 1999: 57).

<sup>50</sup> As in state-socialist societies, South Korea (and indeed, Taiwan) organised its economic planning in terms of a series of five year plans, each of them emphasizing (hence organising the development effort in support of) particular strategic initiatives (textiles, heavy industry, chemicals etc.).

Interview responses from one of the designers of the EIS confirmed that unlike the Ministry of Finance, which had barely been engaged in its formulation, the EPB's authority, even in matters of *social* policy-making, allowed it to 'nose-in' on a number of issues - even technical ones - that were strictly the preserve of the Ministry of Labor.

The EPB's efforts in developing the EIS, arose in part from concerns about the likely impact on employment of the collapse of labour-intensive industries such as shoes, rubber, and textiles in the early 1990s. Additionally, however, it wished to circumvent an alternative Ministry of Labor plan to introduce an 'employment adjustment subsidy' which the EPB considered to be harmful to its wider interests in managing the need for industrial restructuring. The EPB's proposals ultimately triumphed against the opposition of the Ministries of Commerce and the KEF when support from the President ensured that proposals to develop the EIS were incorporated in the 'New Economy' Five-Year Plan announced in mid 1993.

Figure 4: Unemployment Rate: Korea 1970 - 2000



Source: National Statistics Office

While the role of the EPB in designing the Employment Insurance System was clearly affected by changing political sentiments under the Kim Young Sam administration, its historic engagement in social policy areas was not altogether surprising given its own organisational history and intellectual culture. As early as the mid 1970s, Korea's economic planners had become interested in including social welfare analysis in their remit.<sup>51</sup> While concerns over income distribution became an important issue for the economic planners, due to the rapid growth and concentration of wealth in the *chaebol*, their attempts to integrate economic and social analysis also reflected the background and thinking of key individuals within the EPB itself.

For instance, interviews with former EPB officials confirmed that while economists sympathetic to social welfare initiatives were in the minority among EPB staff, its

<sup>51</sup> As a former official recalled, the EPB often considered that data from the GINI co-efficient (which measures income inequality) to be one of the most important sources of evidence for the analysis and formulation of economic policy.

social planning division did foster a number of individuals with both specialised training and a genuine interest in advancing social welfare alongside economic development. When political sentiments were supportive, individuals receptive to social welfare concerns were able to take key positions within the EPB. One case in point occurred in the mid 1970s when Shin Hyun Hwak became head of the EPB. Coming from his previous post as Minister for Social Welfare, his appointment was an important political gesture when the country was in the midst of a drive for economic growth. Indeed, in his new capacity, it appears that Shin was instrumental in getting the 'social' dimension incorporated into the very name of the 4<sup>th</sup> Five-Year Plan in 1977 which was entitled, the 'Economic and Social Development Plan'.<sup>52</sup>

With the invocation of the 'globalisation policy' in 1994 and the expulsion of long-term planning from the core of national economic management, the experience in, and receptiveness to, social concerns by the economic managers appears to have dissipated along with social welfare's 'relative ally' in the economic bureaucracy: the EPB. An important reason for this was an important sub-text to the merger of the EPB and the Ministry of Finance: their oft-remarked intellectual rivalry. Being the more progressive economic agency, the EPB was often pitted against the longstanding conservatism of the MOF. Indeed, interviews suggest that South Korea's financial managers had previously resisted two attempts by the EPB to send teams into the MOF to transform their economic conservatism. Once the MOF's had absorbed the EPB, the former's conservatism was secure.<sup>53</sup>

## **4.2 Social welfare in a global era: implications of a finance-driven economic bureaucracy**

Historically, all four 'pillars' making up South Korea's present social insurance system, were developed under the EPB (the last of these being the Employment Insurance System enacted in 1995). In the years following the EPB's demise and the creation of the Ministry of Finance and Economy in 1995, the institutional structure for co-ordinating economic and social policy has changed. It now effectively marginalises social considerations. For example, social welfare inputs from agencies such as the Ministry of Health and Social Affairs are not a feature (nor ever were) of the Economic Ministers' Committee and as one senior official confirmed, representatives of the social welfare ministries are rarely invited to its meetings.<sup>54</sup>

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<sup>52</sup> Reports from some former EPB officials confirmed that while the name change did reflect changes in the ideas and analysis being used in economic planning, it did not signify a major policy turn or in the relative prioritisation of social policy vis-à-vis economic policy. Furthermore, other respondents reported that the name change reflected the fact that many social welfare initiatives were already in the planning stage and the title of the 4<sup>th</sup> Five-Year Plan merely reflected these developments.

<sup>53</sup> While many EPB officials, at this point, left for other civil service posts - particularly in the research institutes - there were notable exceptions. For instance, one senior official, Lee Ki-Oh became both the Economic Secretary in the Blue House as well as the Minister of Finance and Economy (considered the two most powerful positions in economic policy-making). The present Deputy Minister in the MOFE is also a former EPB official.

<sup>54</sup> Standing members of the economic committee include the heads of the Ministry of Planning and Budget, the Financial Supervisory Commission, the Ministry of Finance and Economy, the Ministry of Commerce and Industry, the economic secretary in the Blue House, and the Chief economic advisor to the President. Unlike the other social ministries, the Ministry of Labor is often present in the economic coordination meetings, signifying the importance that labour issues have acquired following the crisis.



Similarly, even within the Blue House, the social secretariat is not linked to the economic secretariat and they pursue their respective remits in relative isolation from one another. While the EPB previously co-ordinated economic and social policy-making, any routine co-ordination that now exists seems to arise primarily in negotiations over the budget. Whereas welfare issues, certainly from at least the mid 1970s, had a presence in minds of economic policy-makers (though it is important not to over-stress its significance for them), now it appears that it has largely been exorcised from the concerns of their successors.

When attempting to evaluate the poverty counter-measures pursued after the financial crisis, one must first recognise that the government's pre-crisis 'social safety net' was minimal. Korea had historically pursued the development of a social security system and not a safety net. By the beginning of the crisis, the formal social protection system was comprised of a minimal social insurance system, supported by a livelihood protection system that provided stipends to the aged, poor and incapacitated along with rudimentary social welfare services.<sup>55</sup> Consequently, post-crisis efforts to build a more comprehensive social safety net represented, amongst other things, a change in the very language of Korean social policymaking.<sup>56</sup> As much as anything else, this reflected the government's need to adopt the social welfare *lingua franca* of the international community, following its acceptance of financial aid from the World Bank in 1998.<sup>57</sup>

With the crisis and the rapid growth of unemployment to unprecedented levels, the government was clearly pressed to come up with a swift solution. Interview responses from policy experts - and, indeed, from some officials - confirmed that the government's response was inadequate. This was largely because of a glaring lack of attention - and appropriate resource commitments - to building the capacity (in terms of personnel and services) that was required to implement anti-poverty strategies.<sup>58</sup> If these reports are accurate, then most of the new welfare policies pursued after the crisis must have resulted in much wasted expenditure given the absence of an appropriate institutional capacity for implementing the policies.

For instance, as one respondent indicated, the application of those aspects of the social safety net that could not be administered routinely according to simple criteria (the

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As well as the formal economic coordination meetings, which currently occur about every two weeks, there are often bi-weekly informal discussions on economic affairs.

<sup>55</sup> One senior Korean official indicated that when the IMF analysed the country's social safety net in the late 1990s, they concluded that it provided about two-thirds of the average support levels of the US and UK (which have among the less generous levels of provision in the advanced economies) but far below the levels of the Scandinavian countries.

<sup>56</sup> While social safety nets are used by the IMF and the World Bank to refer to temporary cash or in-kind transfer programmes for the poor and unemployed, in Korea the term does not necessarily refer to poverty counter-measures. Rather, it tends to encompass all forms of social protection and welfare (Kim, Y.M. 2001).

<sup>57</sup> World Bank Structural Adjustment loans require that government efforts meet at least one of three criteria: the reallocation of public expenditures in favour of the poor; the elimination of distortions and regulations that disadvantage the poor and limit their income-generating opportunities; and/or the development of social safety nets that protect the most vulnerable members of the population.

<sup>58</sup> The workload for welfare officers in Korea is much higher than in most OECD countries. For instance, recent estimates place the average caseload-to-staff ratio in Korea at roughly 280 cases per social worker, compared with averages between 60 and 100 in Belgium and Norway or against ranges of 80 to 120 in the Netherlands and Switzerland (OECD, 2000).

level of administrative capacity and duties that had developed under the existing system of social insurance), was severely constrained because of limitations in terms of manpower, training and restrictions on the exercise of authority. In practice, this meant that certain projects - public works for example - which require minimal numbers of staff to process large numbers of simple applications - were reported to have been more successful and better implemented than many of the new benefit policies. New benefit programmes often required significantly more staff to process claims precisely because more complex forms of information-gathering and monitoring were required to verify the financial situation of claimants. Given that more complex administrative procedures were unnecessary for the application of the former social insurance system, and that the former system was never subject to the level of claims seen during the economic crisis, the new 'productive welfare' programmes seem to have degenerated into welfare 'handouts' due to administrative and logistical limitations. For instance, of the 1.5 million targeted beneficiaries under the new National Basic Livelihood Security System in 2000, roughly 1.1 million (75 percent) were immediately classified as unable to work, thus receiving financial support with no conditions attached. Of the 381,000 beneficiaries that were classified as able to work, only about 4 percent (60,000) of the total target population were ultimately given benefits with some 'productive welfare' conditionality (MOL 2000). The capacity to deliver means-tested social benefits involving claimant conditionalities could not be created overnight.

As the NBLIS case illustrates, much of the social safety net established after the crisis may have become, in effect, welfare disbursements. Despite policy rhetoric and the incorporation of active labour market conditionalities into the livelihood protection system, many policies have not been given adequate attention in terms of the capacity-building needed to effectively administer the new and expanded programmes. One important reason for this outcome may lie in how the institutions of economic governance have evolved over the 1990s.

Whereas South Korea's economic managers had once played an important and at times proactive role in social welfare, available evidence suggests that this is no longer the case. Rather, under the current Kim Dae Jung administration, social welfare developments appear to have been driven by the President with little support (and, surprisingly for Korea, with some resistance) from many in the economic bureaucracy. The predominant role of the President in post-crisis social welfare reform becomes clear when attention is given to the institutional development of the notion of 'productive welfare'.

In late 1998, newly-elected President, Kim Dae Jung, asked Kim Yoo-Bae, then the Blue House presidential secretary for welfare and labour, to put together a small team (the 'Quality of Life Committee') to develop the concept of productive welfare into a policy platform. Interestingly, this concept was reported to have first entered political discourse in the earlier Kim Young Sam administration (1993-1997) after President Kim Young Sam had attended the Copenhagen Summit in early 1995.<sup>59</sup> Failing to gain a consensus and political momentum, the concept remained at the fringe of political discourse under the guise of 'balanced welfare' before re-emerging again as

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<sup>59</sup> In his recent book, Kim Dae Jung claims to have first come up with the notion of 'productive welfare' in the 1950s (Office of the President of the Republic of Korea, 2000).

'productive welfare' towards the end of the 1990s.<sup>60</sup> Furthermore, a number of respondents confirmed that the concept, as before, was developed with relatively little support or input from either members of the economic bureaucracy or even from the major social welfare NGOs.<sup>61</sup>

Evidence suggests that efforts to establish the notion of productive welfare—itsself little understood and, if reports are correct, of little relevance to the day-to-day activities of the bureaucrats—was a propaganda ploy by the new administration designed to ease public opposition to the reforms (and their consequences for unemployment) that would be needed to overcome the economic crisis.<sup>62</sup> Some respondents also felt that the concept was intended as a political crisis-management strategy. Specifically, they thought, it was aimed at appeasing opposition from those in the economic bureaucracy who feared that Korea would succumb to the supposed 'welfare disease' that had slowed down rates of economic growth in Western nations.

Further underlining the primacy of the chief executive in advancing social welfare after the crisis, opposition to Kim Dae Jung's attempts to expand the social safety net extends beyond the economic bureaucracy. The National Basic Livelihoods Standards Act, passed in November 2000, is a case in point. Attempts to update the NBLS were opposed not just by many in the economic bureaucracy, but even by senior officials in Ministry of Labor (MOL). As one respondent explained, the MOL opposed efforts to upgrade the existing Livelihoods Protection System because labour officials felt that government poverty counter-measures should place greater emphasis on employment generation, emphasising individual self-reliance over government welfare handouts.<sup>63</sup> Given that in 1999, the budget for livelihood protection (which, as mentioned above, effectively became a form of welfare handouts with little or conditionalities attached) had risen to over 11 billion Won (then roughly £6m or \$9.6m) - an amazing 97.5 percent increase from levels in 1998 - this MOL concern was understandable.

Resistance to social welfare developments, however, have not only come from within the economic bureaucracy. Some NGOs have opposed efforts to expand social expenditures, clearly showing the divisions that have developed within civil society. For instance, one senior member of the Citizen's Coalition for Economic Justice, a

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<sup>60</sup> One of the key people involved in the historical development of Productive Welfare was Kyungbae Chung, currently the President of the Korean Institute for Health and Social Affairs. He has been personally engaged in the development of the concept of "Balanced Welfare" for over ten years and was himself a member of the President's Blue House team on Productive Welfare.

<sup>61</sup> While a few respondents suggested that NGOs such as the People's Solidarity for Participatory Democracy may have contributed to the development of productive welfare, interviews with PSPD staff confirmed that this was not the case.

<sup>62</sup> While this was the first time that a Korean President had officially outlined their plans for the direction of welfare policy, many respondents felt that productive welfare lacked any relevance for policymakers, nor did it have any concrete impact on social policy change. Kim YM (2001) describes the concept as 'a hodgepodge of various different ideas ranging from state welfarism and neoliberalism to the Third Way and welfare pluralism...', ultimately concluding that '...it does not seem an appropriate research direction to try to identify the character of the DJ administration's social welfare policy focusing on productive welfare.'

<sup>63</sup> One important context to the MOL's opposition the Livelihood Protection System was reported to be a constraint of the IMF negotiations which only gave room for two policy options, public assistance or employment measures. Not unsurprisingly then, the MOL argued for employment measures over public assistance.

civil organisation strongly supported by many academic economists, was reported to have publicly opposed the policies pursued by Korea's main social welfare NGO, the People's Solidarity for Participatory Democracy, arguing that their attempts to increase welfare expenditures would only be a waste of government funds.

Furthermore, the Bretton Woods agencies and their equivalents are often attributed with influencing social welfare policies in neo-liberal directions (see Deacon 1997). Yet we have found little evidence to suggest that their role in formulating and directing social policies in South Korea was significant. On the one hand, many social welfare advocates in Korea have argued that the recent reforms are indeed neo-liberal in orientation, using a number of industrial and labour policies as examples (for instance, Kim and Bak 1998; Jang 1998). While gaining headway under Kim Young Sam's globalisation policy, some argue that neo-liberalism has further influenced policy-makers through the bailout conditionalities imposed by the Bretton Woods institutions (eg. Pieper and Taylor 1998). Against these claims, others have argued that social welfare policies under Kim Dae Jung actually enhance the role of the state in welfare provision rather than withdraw it from such functions (Kim, Y.M. 2001).<sup>64</sup> Our research tends to support the latter argument, suggesting that Korea's internal governing dynamics have played a greater role in shaping social and economic policy-making ideas and determining how, in practice, they are pursued.

Firstly, interview responses revealed a broad consensus affirming the claim that while the Bretton Woods institutions have influenced social and economic policies in a general sense, their level of influence was greatest during the developmental period of the 1970s and early 1980s.<sup>65</sup> By the mid 1980s, Korea's balance of payments were healthy and consultations with the international financial institutions were reported to be declining. Thus, with the exception of the economic crisis, international agencies appeared to have played only a minor advisory role for the last decade.

Secondly, available evidence suggests that even during the 'IMF financial crisis' (as it was often known in Korea), the internal dynamics of governance were a more significant influence on the crisis-management efforts of the Kim Dae Jung administration, than were the Bretton Woods institutions. For instance, interviews with senior officials in the economic bureaucracy suggested that the IMF bail-out in 1998 was not simply a matter of the IMF team insisting on particular structural and policy reforms. Rather, it appears that the overwhelming majority of the IMF package

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<sup>64</sup> Similarly, many respondents interviewed felt that while the DJ government has certainly adopted some western-style policies after the crisis, this does not simply mean that Korea has taken a neo-liberal direction. Rather, they felt that neo-liberalism has had historical and politically specific contexts and situations to which western nations have responded which are different from the context in which Korea has developed. Thus, according to this view, Korea developmental trajectory is unique, as the nation embarks upon its own model of a market economy guided by its own internal dynamics.

<sup>65</sup> A period in which Korea had one of the highest levels of foreign indebtedness in the world. It should be remembered, however, that the IMF was always far more 'lenient' with South Korea than it was with other developing countries in the sense that it never subjected the country to the 'full-force' of neo-liberalism. Part of the reason for this was that South Korea was highly successful in using foreign borrowing for productive (rather than speculative) purposes and consequently had no problems servicing its debt. Additionally, the US government was concerned to build South Korea as a 'bulwark against bolshevism' and consequently was less concerned than might otherwise have been the case, that it was not following neo-liberal orthodoxy 'to the letter' (see Henderson 1993).

(upwards of 90 percent) was actually prepared by Korea's own economic managers.<sup>66</sup> Indeed, as others confirmed at interview, much of the crisis- management strategy was already in place prior to the start of the IMF negotiations. The government had had difficulty implementing these reforms, however, because of resistance in Parliament and from the *chaebol*. In addition to providing the bail-out loans, then, the role of the IMF seems to have been to act largely as a powerful external agency to legitimate the need for the pre-existing reform agenda.<sup>67</sup>

With regard to the World Bank at this time, both informed commentators (eg. Kim YM 2001) and our interview evidence, suggests that the Bank's role was largely to provide a discourse to connect pre-existing Korean ideas for welfare reform to international practices, rather than to press such practices on to the South Korean government. In the pursuit of 'productive welfare', policy directions have deviated, in fact, from World Bank suggestions. Pension reform is a case in point. As Kim (2001) argues, World Bank recommendations for pension reform were very similar to those that had been espoused by the Kim Young Sam administration in the mid 1990s. The Kim Dae Jung administration, however, rejected these reform proposals, choosing instead to launch a plan which preserved the basic framework of the existing pension scheme. As a consequence, few of the neo-liberal elements recommended by the World Bank were ultimately incorporated into the reform package.

Drawing on available evidence and from our own research, we conclude that the progressive social policies pursued after the crisis, while developing in part from high-level economic forums (such as the economic coordination meetings in the Blue House), were not the outcome of progressive orientations from within the institutions of economic governance. Indeed, the majority of economists in the economic bureaucracy, the government economic research institutes, and even the main 'economic' NGOs, appear to have opposed the kinds of social welfare reform advocated by President Kim Dae Jung. Rather, Korea's recent (since 1998) pro-poor initiatives seem to have resulted from Kim Dae Jung's personal interest in expanding social welfare provision after the crisis.<sup>68</sup>

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<sup>66</sup> In total, the Korean government signed nine Letters of Intent with the IMF. The first five Letters (beginning in December 1997) were broadly focussed on macroeconomic policy. At this stage in the crisis, the main focus of the Korean government was on restoring the stability to the foreign exchange markets and increasing foreign reserves. To this effect, the IMF Letters of Intent merely stipulated specific quarterly and annual macroeconomic targets which the government needed to meet. As the foreign reserves reached substantial levels (from less than US\$4 billion in December 1997 to US\$64.0 billion by July 1999), the IMF programme shifted from general principles and macroeconomic targets, to specific recommendations on structural reform. Thus, only by the sixth Letter of Intent (May 1998), were the first detailed restructuring measures - concerning the corporate sector - even mentioned in the IMF package (Wang 1999).

<sup>67</sup> One area in which the IMF may have been the primary progenitor of reforms was in the development of the social dialogue. In seeking a more flexible redundancy system in exchange for economic bail-out, one interviewee confirmed that the Tripartite Commission was an IMF proposal (a view supported by a number of policy experts we interviewed) which the government then advocated in negotiations with labour interests over the Social Accord in early 1998.

<sup>68</sup> Some authors have commented upon a 'triangular alliance' that was formed soon after democratisation in the late 1980s between social policy advocates in the trade unions and NGOs on the one hand, and Kim Dae Jung's then opposition party. (see, for instance, Yang 2000). While these organisations are purported to have helped to bring Kim Dae Jung to power, our research found little to support the idea that there was a concerted 'alliance' between the Kim Dae Jung administration and his Party and the two main NGO proponents of social welfare: the People's Solidarity for Participatory Democracy and the Korea Confederation of Trade Unions.

This analysis leads us to raise some worrying conclusions about the current links between economic governance and poverty in Korea. Given the importance of the economic bureaucracy in affecting the implementation of welfare policies (through budgetary allocations, for instance), a system of economic governance that relies upon the will of the chief executive to inject poverty counter-measures into Korea's macroeconomic strategy, may be both instrumentally problematic and ultimately very fragile. A highly centralised and executive-driven form of economic governance - given Korea's one term Presidential system - is likely to mean that the considerable support required to integrate poverty concerns into the nation's macro-economic management strategy, cannot be sustained against what is now a conservative finance-driven economic bureaucracy. The progressive momentum that Kim Dae Jung has introduced is, in the future, likely to wane. If this does not result from the coming change in the administration (with elections due in late 2002), then it may well result from initiatives within the economic bureaucracy (who will be able to draw on evidence that poverty levels have now fallen to pre-crisis levels), some of whom have always believed that recent increases in expenditure are unnecessary, unsustainable and ultimately detrimental to the Korean economy.

With the demise of the planning functions in the economic bureaucracy and the consequent lack of a 'relative ally' receptive to social welfare concerns in the now finance-dominated economic bureaucracy, coupled with the dependency on Presidential support to place social welfare concerns at the forefront of macro-economic management, Korea is faced with a problematic governing arrangement that may ultimately work to compromise the effectiveness by which poverty counter-measures are formulated and implemented. If the only way to overcome the lack of social welfare support from within the economic bureaucracy is through sheer political will, then initiatives are likely to be rushed through the policy-making process, formulated with insufficient debate and engendered with insufficient institutional capacity to ensure effective implementation. As suggested above, this indeed appears to have been the case with many new programmes aimed at mitigating the social impact of the economic crisis. Thus, while the more immediate problems in implementing anti-poverty measures are clearly related to historical precedent and the country's limited experience with and institutional capacity for social protection, they also appear to be intimately linked to the particular institutional arrangements and policymaking practices that has come to constitute economic governance in Korea.

## **5. CONCLUSIONS**

We began this report by remarking that South Korea, from the 1970s through to the late 1990s, was considered as an exemplary case where poverty reduction had been achieved seemingly as a reflex of economic growth. Investigating a number of issues that lay behind the way in which data on poverty and inequality were calculated in the country, we raised doubts as to whether South Korea's record on these matters was as good as has been claimed. If these doubts are legitimate, then it seems - at the very least - disingenuous to use the South Korean case to bolster what are in effect ideological beliefs about the automatic and positive effects on poverty stemming from economic growth *per se*.

Whatever the reality of South Korea's record on poverty and inequality, however, it is clear that it was able to achieve one of the best performances, on these issues, of any capitalist society, at least prior to the onset of economic crisis in 1997. Among the reasons for this positive performance - and recognising that South Korea was never a welfare state (even in the limited sense of Singapore or Hong Kong) - was the fact that it had an economic governance structure that allowed for coherent and authoritative economic planning that incorporated social welfare considerations.

With democratisation, and particularly during the Kim Young Sam administration (1993-97), the growing flirtation with neo-liberal economics (for various reasons and from various sources) resulted in the abandonment of strategic economic planning, and with it, the marginalisation of concerns with inequality and social welfare within the core economic bureaucracy.

More specifically, the restructuring of the economic bureaucracy over the 1990s—first with the demise of the Economic Planning Board, the disappearance of the social planning department, and the subsumption of some of the EPB functions within the Ministry of Finance and Economy and second with the breakdown of that ministry in 1998—led to a decline in support in the economic bureaucracy for progressive, social welfare ideas. While the issues of inequality and welfare forced their way onto the government's agenda during the economic crisis (as a result of rising unemployment), this effort was politically driven by the President and was not a 'normal' and thus stable feature, of the country's system of economic governance. As a consequence, changes in the direction of social welfare initiated under the Kim Dae Jung administration (1998-2002) may very well change with the election of a new President in late 2002.

As in Korea's authoritarian past, changes in the Presidency may mean that the driving force in economic governance may again revert back to the point where the machinery of government in general, and the economic bureaucracy in particular, take a larger degree of control over policy-making processes. If and when this happens, given the concerns to deepen the alliance with the international financial 'community' and thus its neo-liberal assumptions, the consideration of social welfare in general, and poverty and income inequality in particular, may well revert back (albeit with 'new' neo-liberal legitimations) to the situation in the authoritarian era when economic concerns were given absolute priority over issues of welfare and social protection. In the final analysis, the future direction that Korea takes with regards to economic governance and poverty is likely to revolve around the ability for policy-makers and social welfare advocates to significantly develop the notion of 'productive welfare' (or other 'third way' notions) through a broad based policy dialogue that can achieve consensus and support by all those involved in economic governance.

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## ***Appendix I: Abbreviations***

ALRAA	Agricultural and Land Reform Amendment Act
CCEJ	Citizen's Coalition for Economic Justice
CSS	Committee for Social Security
DMB	Deposit Money Banks
EIS	Employment Insurance System
EPB	Economic Planning Board
FKTU	Federation of Korean Trade Unions
KIHASA	Korea Institute for Health and Social Affairs
KCTU	Korean Confederation of Trade Unions
KDI	Korea Development Institute
KEF	Korean Employer's Federation
IMF	International Monetary Fund
IRRC	Industrial Relations Reform Commission
MCI	Ministry of Commerce and Industry
MCL	Minimum Cost of Living
MITI	Ministry of International Trade and Industry
MOA	Ministry of Agriculture
MOF	Ministry of Finance
MOFE	Ministry of Finance and Economy
MOGAHA	Ministry of Government Administration and Home Affairs
MOL	Ministry of Labor
MPB	Ministry of Planning and Budget
NBFI	Non-Banking Financial Institutions
NBLS	National Basic Livelihood Security
NGO	Non-Governmental Organisation
NSO	National Statistics Office
PSPD	People's Solidarity for Participatory Democracy