Introduction

This book uses an institutional approach to analyse the distinctive phases of Korea's economic transition across roughly four decades. It traces national economic development from a state-led system across three decades of miraculous economic success to the 1997 crisis, and the shift this crisis inspired to a market-oriented system with sluggish economic development in the post-crisis period. The transition of the Korean economy has not been analysed comprehensively in the context of the institutions that influence economic performance, particularly during the globalization era. This book seeks to help fill the void by providing critical analysis of the dynamics of institutional evolution and the operations of important economic sectors as well as the overall Korean economy in the recent past.

Korea's economic success is well documented. It stands as proof that a nation can leap from being one of the poorest in the world to one of the richest in just one generation. Over the period from 1963 to 1996, the economy recorded an annual growth rate of 8.7 per cent, per capita income increased more than 100-fold from \$100 to \$10 548, and GDP rose from \$2.3 billion to \$520 billion (KNSO various years). In 1996, Korea became the 29th member of the OECD. The Korean economy had become a textbook example of successful economic development. As the vast literature on this subject attests (Kwon 1997), Korea's economic success story has stimulated broad international discussion regarding the Korean development model, the sustainability of the development momentum, and the applicability of this model to other developing countries.

The financial crisis in November 1997 that engulfed much of East Asia temporarily crippled the Korean economy and closed the curtains on three decades of 'economic miracle'. In 1998 negative growth of 6.7 per cent was recorded and unemployment soared to 7 per cent from 2.6 per cent in 1997. Inflation increased from 4.4 to 7.5 per cent, and the US dollar value of the Korean won plummeted from 951 to 1415 (KNSO various years). However, unlike all of the other crisis-afflicted economies in East Asia, the Korean economy recovered swiftly, recording 10.7 per cent growth in 1999 and 8.8 per cent growth in 2000, and establishing Korea as the world's 11th-largest economy by 2003. The Korean economy once again stimulated broad international discussion, this time regarding the diagnosis of, remedies for

and recovery from financial crisis, the institutional and structural changes that were implemented in response, and the implications of the Korean example for other countries.

Although it recovered rapidly from the crisis over the ensuing two years, the Korean economy has since shown clear signs of sluggish performance. Over the six years 2001–08, the economy achieved an annual growth rate of 4.4 per cent, which is far below the average over the previous three decades. A number of studies estimate that Korea has entered a low potential-growth phase with a rate of 4–5 per cent over the next ten years up to the mid-2010s, and per capita income remaining one-third below the OECD average (Park and Huh 2004; J.G. Park 2003; Bank of Korea 2005; OECD 2007). This assessment has raised concerns among people in all walks of life in Korea about the consequences of a stagnant national economy and the prospect of failing to cross the threshold to advanced-economy status.

External factors do not explain the Korean economic slowdown, as the global economy and the economies of Korea's major economic partners including the United States, China, and even Japan, performed reasonably well at least up to the 2008 global economic crisis. Soon after the 1997 financial crisis, a consensus formed among analysts that outdated economic policies and institutions and the corresponding economic structure were the primary causes of the crisis in Korea (Kwon 1998; J.M. Lee 2003; Harvie and Lee 2004).¹ Hence, soon after the crisis, sweeping institutional and structural reforms were undertaken to rebuild and fortify the Korean economy. How then should one explain both the sudden economic slowdown early in the new century and the unpropitious prospects of the Korean economy for the decade ahead? What should be done to reinvigorate the national economy for the well-being of the Korean people and to achieve their aspirations for Korea to be one of the world's advanced economies? This book attempts to address these critical questions from an institutional perspective.

The Korean economy has been in transition in many respects from the early 1990s, and in particular since the 1997 crisis. International geopolitical environments have figuratively – and literally – changed the ground on which Korea's economic spectacle is played out. The close of the Cold War has ended the advantage Korea enjoyed as a Western ally from its geostrategic location. The world economy has moved unrelentingly toward globalization, heralding intense global competition and the weakening of national economic boundaries. As a signatory of the WTO and a member of the OECD, Korea has firmly embraced its position on the path of globalization. The Korean economy, which depends on international trade and capital mobility for its own survival, is now maturing such that Korea is

no longer a developing country. Indeed, commensurate with its size and stage of development, the Korean economy has become a vital cog in the wheel of the global economy.

The global trading system is in transition. In 2001 the Doha Development Agenda (DDA), a new round of multilateral trade negotiations, was launched in the WTO. However, the negotiations have been in deadlock since 2006, and the prospect of WTO-based multilateralism for trade liberalization looks dim. In contrast, regional trade agreements have been multiplying particularly since the mid-1990s, thereby deepening regionalization within the global trading system.

Climate change is now recognized as one of the critical issues faced by all of humankind wherever they live. As a result, carbon emissions trading has emerged as one more vital issue in international trade, compelling all countries to pay proper heed to the impact of economic operations on all aspects of climate and the geophysical environments. In recent years, the world has witnessed instability of energy supply and a sharp rise in energy prices, intensifying competition for energy. Securitization of energy resources has become a vital national concern. Rising anxiety about climate change internationally, greater growth in demand for energy, and acute concern over the supply of energy resources in unstable global markets will exert pressure on national governments to reduce fossil fuel use through carbon markets.

International financial markets have expanded dramatically since the mid-1990s. Cross-border flows of financial assets globally tripled during the past decade to \$6.4 trillion, reaching about 14.5 per cent of world GDP by 2005 (Pazarbasioglu et al. 2007). Dramatic growth of international capital flows can be attributed to the increased importance of new financial instruments and the globalization of international financial markets. These new financial instruments include hedge funds, private equity funds and sovereign wealth funds, each of which has expanded greatly in recent years. Global capital markets are becoming more integrated, thereby enhancing linkages between national financial systems. The internationalization of financial markets and growing links between national financial systems have led to the highly unpredictable world of global financial systems and capital markets, which in turn have increased the volatility and subsequent contagion in financial markets. The global financial crisis in the wake of the US financial crisis in September 2008 bears witness. Hence, national policymakers must be vigilant in taking into account developments in global financial markets as well as in the national context when planning and implementing policy.

Another epochal change in the international economic environment looms on the horizon for Korea. North-South Korean relations, political and

economic, have been changing dramatically since the historic summit between the two national leaders in June 2000, followed by another in October 2007. In 2002, North Korea began economic reform through market liberalization, and a number of signs suggested the possibility of further opening to the world outside. However, in 2006 and 2009 North Korea conducted nuclear tests, which provoked UN sanctions, to which North Korea responded with further expansion of its uranium enrichment programme. These developments have important bearings not only on South Korea, its economy and its relations with North Korea, but also on geostrategic and thus economic developments right across the Pacific Rim.

Domestically, too, Korea has experienced a period of transition. The Korean political system has been transformed since 1988 from a series of authoritarian regimes to a vibrant and fully fledged pluralistic democracy headed by a civilian president. Stakeholders in the new political system are not just the president, the bureaucracy, politicians and *chaebol* conglomerates that dominated national economic development strategy and politics through the high-growth period until the 1997 financial crisis. Now workers, consumers, interest groups and other members of the general public are recognized as political stakeholders and they participate actively in the nation's political economy. Korean society and culture have inevitably changed in tandem with the economic and political transformation. As in most nations that have moved towards a more neoliberal system, patriotism and loyalty toward authority have faded, individualistic pursuit has changed the nature of group-oriented society, and the work ethic of the Korean people has weakened. Demographically, as in most industrialized nations, the population is ageing quickly and its growth rate is declining.

Another major transition driven by technological innovation is shifting the Korean economy from industrial to knowledge-based at a time when the global economic paradigm is making a similar shift. In recent years, Korea has been increasingly squeezed between Japan and China in economic competition due to China's exponential improvement in technology as well as its industrial and manufacturing prowess. Thus, international as well as domestic circumstances propel this shift within Korea to a knowledge-based economy.

Importantly for this study, Korea's response to the 1997 financial crisis and to the subsequent shifts in both domestic and international environments has brought metamorphosis to the nation's economic institutions. In compliance with the conditions attached to the IMF rescue package, the Korean government has relentlessly undertaken institutional and structural reforms to liberalize and internationalize the national economy. These major systemic reforms of the nation's institutions have in turn been the main driver of the transition in the Korean economy since the crisis. Liberalization has

induced transition from a state-led to a market-oriented economy. Opening the economy to foreign competition has undergirded the transition to a competition-based market economy. Consequently, Korea presents a fascinating case for enquiry into the evolution of a national economy. The Korean case shows progression from a heavily controlled, protected and remarkably successful economy, to a liberalized, internationalized, knowledge-based economy anchored in market principles.

The national economic drama unfolding particularly since the 1997 crisis begs critical interpretation. This requires re-evaluating the earlier literature on the Korean economy since it reports on studies undertaken before the recent developments in domestic and external policy environments. In particular, there is a paucity of in-depth and comprehensive analysis of the Korean economy in the twenty-first century when economic sluggishness became evident. The sudden and unexpected nature of the downturn that followed the brief interlude of strong recovery in the final years of the 1990s means that knowledge of Korea's institutional and structural reforms, and concomitant economic transition in the longer term, are still in the early stages of development. A few analyses such as Kwon (2005, 2007), Harvie and Lee (2004) and OECD (2004, 2005, 2007) have attempted to explore some aspects of this rich analytical terrain. However, no study has comprehensively drawn together detailed information to capture the 'big picture' of Korea's economic transition and future prospects. One important aspect to which the existing literature has paid little attention is the dynamics of the institutional environments and economic operations of Korea under globalization. The comprehensive nature of topics addressed in this book is a direct response to these information needs.

The institutional approach taken up in this study is an integrated and conceptually comprehensive tool for economic analysis (Olson and Kahkonen 2000). This book uses the concept of institutions proposed by North (1990), Williamson (2000) and others, which sees institutions as the 'rules of the game' in society and includes unwritten informal rules or culture, formal written rules, and enforcement mechanisms. Institutions play critical roles within an economy, as they profoundly influence the behavioural patterns of its actors: individuals, the business sector and government. In particular, institutions determine the level of transaction costs through processes of negotiation between economic agents, the valuation of goods and services to be exchanged, and enforcement of contracts.² For instance, as the world witnessed through the collapse of socialism, institutions help determine economic performance by governing the level of property rights protection and characteristics of the market. Olson (2000) argues convincingly that differences in per capita income across countries are due mainly to differences in the quality of institutions and economic policies.

All this indicates that economic operations are clearly sensitive to changes in institutions.

The institutional approach is openly interdisciplinary, recognizing insights from political science, sociology and anthropology as well as economics. It is also evolutionary rather than attempting to generate all-embracing general theories. Hodgson (1998) points out that the institutional approach enables one to delineate the transition of social, political and economic institutions and to focus on the impacts of institutional transformation on the economy. Understanding the importance of institutions and the appropriateness of the institutional approach to its task, the present study focuses on institutions as one essential factor that helps to determine the overall performance and prospects of the Korean economy.³ Here the logical loop of the influences of economic operations on institutions is not ignored. Nevertheless, the focus is on the flow of causality from institutional changes to the transition and operations of the Korean economy, to keep the task of analysis manageable.

As North (1990: 110) argues, economic systems are specific to particular constellations of institutional frameworks that vary both over time and across countries. In other words, institutional differences result in differences between economic systems. The Korean economy maintains its *sui generis* characteristics largely because of the nation's idiosyncratic institutional framework. North (1990: 7) also argues that persistence of relative inefficiency in institutions is the source of long-run stagnation of an economy. This book therefore examines the Korean institutional context through the multiple lenses of history, society, culture and politics, and analyses aspects of the Korean economy in this light. In particular the book seeks to explore the primary causes of the current sluggish state of the Korean economy through the dysfunction of institutions.

An extensive survey of English- and Korean-language literature has inspired a set of nine propositions concerning the dynamics of institutional changes and their impacts upon the Korean economy.

1. The external context of the Korean economy has changed remarkably in the recent past, including emergence of the globalization and information era, liberalization of the international financial market and changes in international geopolitics. Profound institutional reforms responding to these external changes and to domestic circumstances from the 1997 financial crisis have become the main force for determining the transition path of the Korean economy.
2. In conjunction with institutional reforms, Korea's economic policy paradigm has been shifted from a state-led industrial economy toward a market-oriented and knowledge-based economy.

3. The shock of the financial crisis and institutional reforms implemented in response in the late 1990s, alongside the process of globalization, has generated changes in Korean society and culture consistent with the neoliberal economic paradigm. Patriotism and loyalty toward authority have faded, individualism has risen at the expense of collectivism, and the work ethic has weakened.
4. Fully fledged, pluralistic political democratization has been developed along with and through institutional reforms in Korea. This has increased the range and extent of activity by political stakeholders, making the political process more complex.
5. Liberalization and internationalization of the Korean economy resulting from institutional reforms have provided a more level playing field for foreign competitors in the Korean market, enhancing the attractiveness of Korea's international business environment to foreign businesses. This has facilitated not only trade in goods and services but also inflows and outflows of foreign direct investment (FDI).
6. Even North Korea, with its tightly controlled economy, has undertaken profound institutional and economic reforms in response to changes in both international geopolitics and domestic circumstances. This development has major implications for the South Korean economy.
7. Institutional reforms have been undertaken across the economy and in particular in the business, financial and public sectors. The operations of each of these sectors have been changed remarkably.
8. Labour market reforms and demographic changes have altered the characteristics of the labour market and improved its flexibility.
9. Remarkable changes in Korean society and culture as well as the economic system have transformed society's view on equity, and the need for equity and for an improved welfare system have become more highly valued and actively sought.

These propositions recur across the following 12 chapters where they are explored carefully. A variety of topics of particular relevance to the Korean economy are explored in these chapters, taking the analytical reach of this book beyond that of most conventional analyses of an economy. This book considers not only traditional topics concerning external relations and individual sectors of the economy but also North Korea's 2002 economic reform, inter-Korean economic relations and the impacts of culture and politics upon the economy.

Using an institutional approach for this study gives rise to the question of how to evaluate institutional reforms, a significant issue given the scope of these reforms and the functional changes they have delivered. Choice of the most appropriate institutions and policy paradigm for national economic

policy is predicated on the economic objective that a nation seeks given its perspective of internal and external environments. This study postulates that sustainable and equitable economic development anchored in market principles within a pluralistic political democracy is the Korean people's preferred course for the nation, as reflected by the policies and actions of their fairly elected national government. The question that follows is whether the institutional reforms governments have implemented are adequate and appropriate for achieving such an economic objective. To address this question, the present study undertakes a three-pronged approach.

First, it analyses the internal operations of the organizations that are established to implement institutions. North (1990: 5) observes that organizations are developed in consequence of the institutional framework, and include political, economic, social and educational agencies. He distinguishes between institutions and organizations by using the analogy of the rules of the game and the teams in it, and emphasizes the interaction between institutions and organizations. Certain organizations like regulatory agencies are established to implement and improve institutions. These organizations in turn contain the organizational structure and operational process. Organizational structure includes organizational goals, strategy and governance as well as stakeholders. Operations include processes that enforce and refine institutions through interactions among stakeholders under the prevailing social, political and economic environment. The present study questions whether, in the Korean case, organizational structures are properly constituted in the light of organizational goals and whether these structures function efficiently to meet national policy objectives and the interests and concerns of stakeholders.⁴

Second, the operational outcomes of institutional reforms are evaluated in light of their contributions to achieving reform objectives and other economic policy goals. Even though institutional reforms may be well designed, their implementation may not be effective due to cultural inertia, path-dependence or other unforeseen or poorly appreciated circumstances.

Third, the current state of Korea's institutions is assessed against those of advanced countries. Given that Korea has embraced open market principles under globalization, and seeks to attain advanced economy status, comparative assessment is vital for understanding the Korean institutional framework. To this end, institutional indicators are compared across countries to indicate the performance and relative efficacy of institutions within the Korean economy.

The book has four sections that each take up one of its four interrelated lines of enquiry. The four chapters in Part I explore the evolution of institutions to investigate the impacts of economic policy, culture and politics on macroeconomic development and the economic transition to a knowledge-

based economy. Part II comprises three chapters that examine the reforms of institutions related to Korea's external economic relations, with one chapter assessing recent moves to reform the North Korean economy to understand inter-Korean economic relations better. The three chapters in Part III discuss the evolution of institutions related to three important sectors of the economy: business, finance (banking and securities) and the public sector. Part IV, which contains the last two chapters, examines labour and social welfare issues that are closely related to each other through the national objective of achieving equity for its citizens.

In light of the paramount importance of economic policy for Korean development over the last four decades, Chapter 1 opens discussion of Part I with a critical examination of Korea's economic policy from the 1960s to the present, and consideration of possible future directions. This chapter examines why Korea's economic policy was successful for three decades but ultimately underpinned all the causes of the crisis that struck the national economy in 1997. The chapter then critically examines the transition of the national economic policy paradigm after 1997, and proposes a policy framework consistent with the nation's objective of sustainable and equitable economic growth under the emerging policy environments.

Culture, or informal institutions, has an important bearing on the economy not only by directly affecting the behavioural patterns of individual economic actors but also by influencing formal institutions. Chapter 2 explores the role of Korean culture in national economic development and in particular for future prospects of the economy, by focusing on the impact of culture on individuals' economic behaviour. To this end, this chapter introduces the concepts of transaction costs and creative capacity of all citizens as the intermediary between culture and economic development. It then examines the salient aspects of traditional Korean culture and how it has changed in recent times, to consider possible impacts on transaction costs and the nation's creative capacity. In addition, a variety of Korean cultural facets relevant to economic developments are also analysed comparatively, using social indicators developed by well-known international organizations.

The political system in Korea has transformed remarkably in the recent past from the authoritarian regimes of the 1960s and 1970s to a fully fledged democratic system. Chapter 3 examines the impacts of these political systems on the nation's economic development. To this end, a set of evaluation criteria have been developed which include: the establishment of proper institutions to minimize transaction costs and promote competition; and the implementation of national economic policy with a high degree of deliberation of the nation's aggregate social interests, decisiveness, consistency, credibility and a long-term orientation. Although the formal

structure of the Korean government now differs only minimally from the politically advanced Western models, the Korean political system maintains some distinctive characteristics, many of which are products of history associated with the nation's idiosyncratic Confucian-influenced culture. This chapter discusses the underlying weakness of Korea's political system as it has evolved, including deficiencies in democratic consolidation and civic culture, and the system's inherent instability resulting largely from the factionalism of political parties and single five-year presidential terms. Ways to address these weaknesses are also suggested.

Chapter 4 assesses Korea's transition to a knowledge-based economy (KBE) as an ineluctable development given recent demographic changes and external developments. It uses the analytical framework proposed by Dahlman and Andersson (2000), which recognizes that successful transition to a KBE involves coordinated and complementary development of four pillars: institutions; human resources; information and communication technology (ICT) infrastructure; and innovation system. The Korean government laid out its strategy and programmes in 2000 to promote a KBE more or less in line with this framework, including programmes to address the digital divide that are intrinsic to nationwide KBE development. This chapter assesses Korea's progress across these four pillars by comparing it with world-leader KBEs and emerging economies in East Asia. It identifies substantial progress but also areas of deficiency.

Chapter 5 takes us to Part II to consider Korea's external economic relations. Features of Korea's trade policy such as trade liberalization, the tariff system and free trade agreements are assessed *vis-à-vis* the key policy objective of sustainable and equitable economic development. The chapter then considers specific aspects of trade policy that require further improvement. One is the underdeveloped trade in services, with the service sector characterized by lack of specialization, weak supply capacity and small-scale operations – the result of domestic regulations and barriers that hinder the entry of domestic as well as foreign companies. Assessment in comparison with other countries helps to identify weaknesses and limitations of the Korean trade regime.

Chapter 6 examines and evaluates the systems and institutions involved in Korea's inward and outward FDI, with focus on the former. The 1997 financial crisis forced the Korean government to recognize the value of inward FDI and to pursue a paradigm shift in national FDI policy from 'restriction and control' to 'promotion and assistance'. Nevertheless, inward FDI in Korea has been waning in recent years while outward FDI has been robust. Despite a spurt of FDI soon after the crisis, Korea's capacity to attract FDI is still low by international comparison. This chapter discusses a variety of causes of the sluggish rate of inward FDI, including the impacts of

excessive and opaque regulations, lack of transparency and consistency in FDI policy, labour market inflexibility and turbulent labour-management relations. Global indicators of inward FDI show that Korea ranks relatively poorly *vis-à-vis* emerging East Asian countries. This chapter proposes policy measures to enhance Korea's attractiveness to inward FDI.

Chapter 7 turns to Korea's northern neighbour whose presence as a hostile territory, rather than as part of a unified Korean nation, powerfully influences all aspects of Korean policy and capacity to achieve national goals. This chapter assesses North Korea's economic reform and inter-Korean economic relations. After the bitter experience of economic and social predicaments that resulted largely from institutional failure, the North Korean regime undertook economic reform in 2002 towards decentralizing the tightly planned economy, bringing prices and wages within the market mechanism, establishing private marketplaces, eliminating the rationing system, promoting autonomous enterprise management and pursuing an open-door policy. The regime's reform moves toward co-existence of planned and free market economy are consistent with what the Chinese government calls market socialism, although the North Korean regime disavows this claim. This chapter observes that, although North Korea will encounter serious difficulties in pursuing economic reform and its economy will remain fragile and dysfunctional until nuclear issues are resolved, the regime is highly unlikely to reverse direction back to the pre-2002 system. Further development of North Korea's economic reform and inter-Korean economic relations are mutually intertwined. The high political and economic stakes for both North and South Korea suggest the strong possibility that inter-Korean economic cooperation will expand further. Nevertheless, further nuclear testing in 2009 suggests the North Korean government may continue to surprise and disappoint outsiders whose world-views differ dramatically from those who dominate the North Korean regime.

Chapter 8 opens Part III, which considers individual sectors of the economy. The business sector, which Chapter 8 discusses, has been marked by the dominance of large conglomerates, or *chaebols*, although it has continued to comprise mostly SMEs. In implementing export-led industrialization, successive governments used *chaebols* as a conduit and provided support and protection through incentives and regulations. *Chaebols* expanded and diversified with debt capital to take advantage of these institutionalized privileges, but this practice ultimately led to making them one of the main culprits of the 1997 crisis. In the wake of the crisis, the government has undertaken dramatic reforms of the business sector and eliminated many of the institutionalized privileges previously bestowed on *chaebols*. This chapter evaluates the reform of the corporate sector in terms of corporate governance, financial structure, efficiency and international

competitiveness, and considers the mitigation of economic concentration in *chaebols*. Comparative evaluation of the Korean business sector demonstrates that there is still a long way to go before the reforms are completed. This chapter then explores the causes behind the dismal results of corporate sector reform and their possible consequences in the economy. It also explains the relative underdevelopment of SMEs and the implications of this condition for society and for the economy. Finally, the chapter suggests future directions of the policy paradigm for the business sector and for the SME-*chaebol* relationship.

Chapter 9 examines the transition in the Korean financial sector in the wake of the 1997 crisis and suggests ideas for the sector's future agenda with a focus on the banking sector and securities market. The Korean government used the banking sector as a conduit for financing state-led industrialization throughout the high-growth period. It firmly controlled and protected the banking sector without implementing proper prudential supervision, causing moral hazard and a lack of transparency and of accountability in this sector. These flaws and weaknesses contributed to the 1997 crisis and inspired government to respond with drastic structural reforms to liberalize and internationalize the financial sector and liberalize the capital account. This chapter assesses the banking sector reforms in terms of the reforms' objectives, the operational efficacy of organizations involved, and by comparison with counterpart sectors in other countries.

The Korean securities market played only a minor role in financing economic development through the high-growth period and failed to attract foreign capital. In the wake of the 1997 crisis, however, Korean policy planners have recognized the importance of the securities market and have sought to develop it in line with global standards. Chapter 9 considers and assesses the series of post-crisis reforms to the securities market in terms of financial-market sophistication, efficiency, transparency and openness. Evaluation results suggest failure to transform the financial system toward a market-based model, mostly because of failure in the financial investment services industry, which is the weakest area of the Korean securities market. To boost this industry, the Financial Investment Services and Capital Markets Act (FSCMA) was enacted in 2007 and implemented in February 2009. The FSCMA constitutes a drastic and timely reform of the Korean capital market, aligning the Korean financial investment service industry with counterparts in economically advanced countries. This chapter also suggests ways to improve the efficiency of organizations involved in implementation of the FSCMA.

Chapter 10 turns to the public sector and examines in particular the reforms of public administration undertaken in response to the 1997 crisis. It assesses these reforms, using assessment criteria of effectiveness, efficiency,

predictability and transparency. This chapter also considers the far-reaching regulatory reforms that were introduced to align the nation's regulatory system with WTO and OECD frameworks. Rather than examining individual regulations, it assesses the regulatory reform management in comparison with counterparts in economically advanced countries. It then assesses the operational efficacy of the organizations involved in the reform management. The Kim Dae-jung government established a permanent regulatory reform organization – the Regulatory Reform Committee (RRC) – as well as reform mechanisms such as Regulatory Impact Analysis (RIA) for systematically analysing and communicating the impact of new and existing regulations, and the use of sunset clauses to address ongoing scrutiny and review processes. This chapter identifies strengths and weaknesses in the regulatory management system and proposes suggestions for improvement, particularly in the operational efficacy of the RRC.

Chapter 11 opens Part IV which discusses the two closely related subjects, labour and welfare. This chapter presents a critical examination of the serious challenges that Korea faces in its labour force and industrial relations. The labour force has remained stagnant due to slow growth and the rapid ageing of the Korean population, and there is a significant mismatch between job-seekers' preferences and employment demand. The structural changes entailed in liberalizing the economy have weakened capacity for job creation and signal the emergence of a 'jobless growth' economy. Chapter 11 explores ways to address these issues.

Industrial relations have been dramatically transformed since the 1997 crisis, yet remain one of the most contentious and critical issues in Korea. Internationally, Korea is seen to have one of the world's worst circumstances in both labour regulation and industrial relations, as comparative data attest. The Korean style of industrial relations management produces hostile employment relations, relatively higher wage levels than neighbouring competitor nations, and a duality in the labour market between regular and non-regular workers, all of which raise critical social and economic issues in Korea. This chapter investigates the underlying causes of these issues and proposes ways to address them. These suggestions are by nature socially contentious and controversial, and so require strong political leadership and the skills to build up social consensus. The suggestions include ways to improve the operational efficacy of the nation's three organizations that play important roles in industrial relations management.

Chapter 12, the final chapter, evaluates the Korean social welfare system. Introduced in the wake of the 1997 crisis, the system is intended to mitigate the most pernicious aspects of the market-based economy under globalization: persistent poverty of certain groups of people, and rising income inequality. Successive Korean governments implemented the

'growth-first' strategy up to the 1980s and paid little attention to income distribution and social welfare. Nevertheless, income distribution in Korea was among the most equitable in the developing world, and no serious social concerns were raised about the welfare system until the 1997 crisis. However, the crisis and the reforms that governments implemented in response to it have profoundly transformed income distribution and social welfare issues, rapidly exacerbating income polarization and generating an upsurge in the demand for welfare provision by the state. Korea's social welfare system has been transformed so that its framework and types of welfare programmes now differ little from those of Western advanced countries. Nevertheless, the Korean welfare system today still suffers from serious shortcomings, which are reflected in worsening economic polarization, rising poverty rates and an emerging cycle of transgenerational poverty. If left unchecked, these will adversely affect political and social stability as well as the strength of the national economy. This chapter therefore explores ways to tackle these challenges, including measures to improve the operational efficacy of organizations involved in Korea's welfare system.

Overall, the analysis in this book weaves together a rich array of topics considered across the 12 chapters to present an informative and comprehensive picture of the Korean economy in transition. Its institutional approach for this analysis enables examination of both informal (cultural) and formal institutions, while focusing on the flow of causality from institutional changes to the transition of the national economy. This applies to the treatment of many topics discussed throughout this book. The choice of topics most pertinent to this discussion has been guided by the nature and magnitude of the institutional transformation in the Korean economy in the wake of the 1997 financial crisis. The concerns and themes taken up across the 12 chapters provide the underpinnings for continuity across the volume, although each chapter can also be read independently.

This book is shaped by the author's keen awareness of the unremitting nature of globalization and its impact on national economies worldwide. Some observers may argue that the globalization process will precipitate further changes in the Korean economy that keep it on a path of convergence with other national economies. However, this book maintains that the distinctive nature of Korean culture and institutional frameworks will continue to preserve the *sui generis* characteristics of the Korean economy. Like all nations, Korea has been shaped on all fronts by unique experiences. For Korea's economic performance, these include in recent times the tumultuous financial crisis and swift recovery from it, and sweeping institutional reforms in pursuit of a free market economy. These striking developments make knowledge of the transition of the economy as well as its

miraculous success story particularly valuable for those seeking to understand recent developments in the Korean economy. This knowledge is also valuable for informing policy-making in any country, from a conceptual and a practical basis.

NOTES

1. For a further exposition of this argument, see Chapter 1 of this book.
2. North (1993) cites an empirical study which found that 45 per cent of US gross national product (GNP) in 1970 was devoted to transaction costs.
3. It is of course acknowledged that economic development is a complex phenomenon shaped by multiple factors.
4. This is an analytical approach proposed by Ostrom (2005) who proposes the 'action arena' as a core unit of institutional analysis. The action arena includes 'action situations' and 'participants'. An action situation refers to the social space where participants interact, exchange goods and services and solve problems under circumstances shaped by exogenous variables including attributes of the society, rules and material conditions. Through interactions within the action arena, outcomes are generated, which are in turn evaluated in light of the exogenous variables.

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