

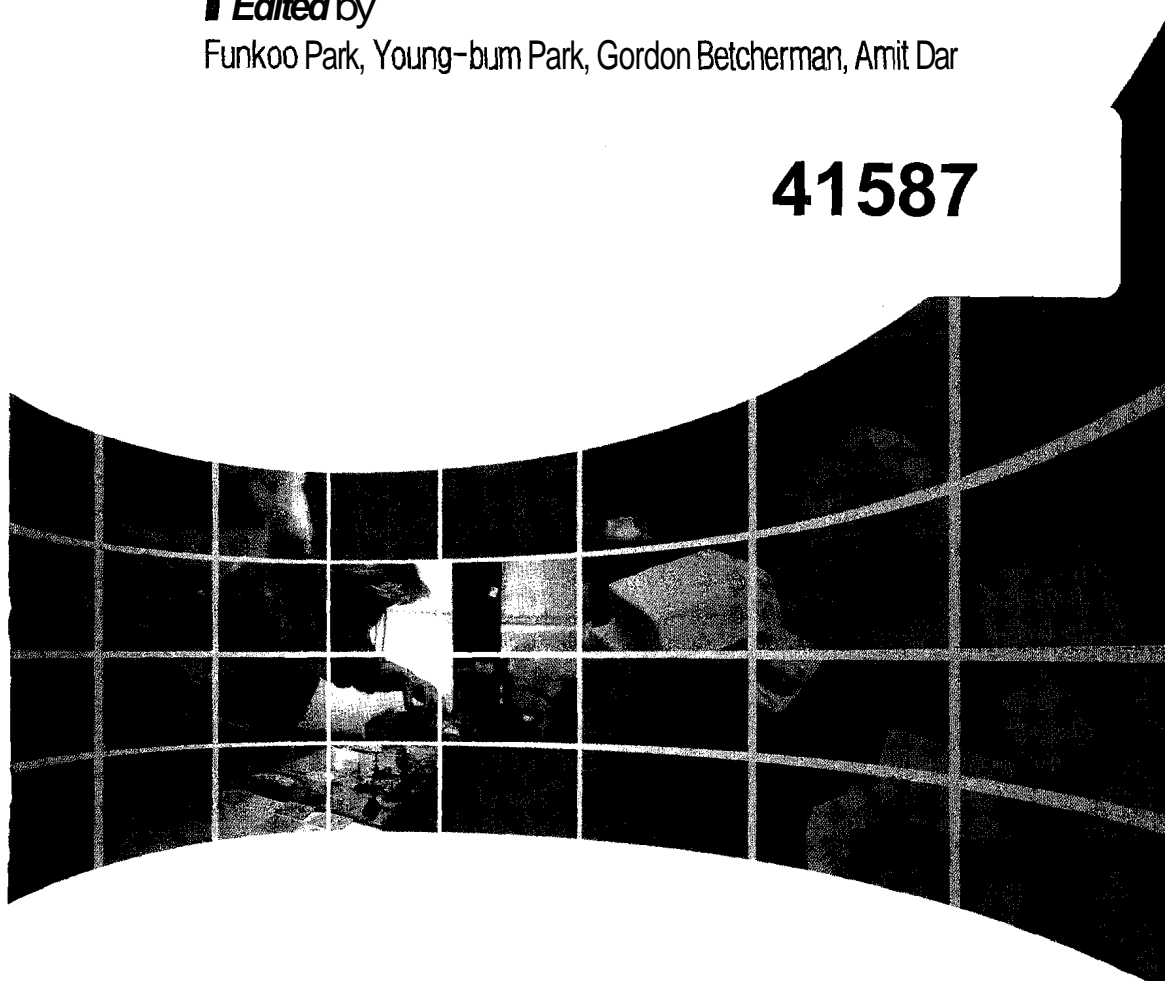
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# Labor Market Reforms in Korea : Policy Options for the Future

■ *Edited by*

Funkoo Park, Young-bum Park, Gordon Betcherman, Amit Dar

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THE WORLD BANK



KOREA LABOR INSTITUTE







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*Edited by*  
**Funkoo Park**  
**Young-bum Park**  
**Gordon Betcherman**  
**Amit Dar**

**The World Bank**  
**Korea Labor Institute**

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**This Book is dedicated to the memory of  
Nicholas Prescott (1953~2000)**





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# Foreword

In the wake of the 1997 financial crisis, Korea experienced unprecedented economic and social disruptions. In the course of combating the crisis, institutionalizing labor market flexibility and building a stronger and more durable safety net stood out as challenging policy issues. The government, employers, labor leaders, and academics devoted themselves to resolving these issues in order to mitigate the painful costs of the crisis and to move forward afterwards.

In this context, the World Bank and the Korean Ministry of Labor launched a project on labor market reforms in Korea. This project was financed through a grant from the ASEM-EU Financial Crisis Fund, with the Korea Labor Institute as the major implementing agency. The project aimed to assess the progress of the Korean labor market reforms after the 1997 financial crisis and provide policy directions for the future so as to respond to challenges created by changing economic and social circumstances.

This book brings together the wide range of studies that were commissioned through this project. It covers income support programs, labor law and labor market regulations, active labor market programs, labor market and gender, and the Korean experience in an international comparative context. Many prominent local and international experts from academia, government and international organizations including the World Bank, OECD and ILO participated in the preparation of these studies. An international conference was held in Seoul in May 2000 to discuss the preliminary outcomes of the project. At this conference, experts from other Asian crisis countries also shared the experiences and lessons of their countries from the crisis.

The ASEM grant facility has played a major role in ensuring the success of this project and I would like this opportunity to thank the EU for their substantial and continuous support for this exercise. Many people also contributed to the successful implementation of the project and the

publication of the book. The main initiator of the project was Nicholas Prescott (World Bank) who tragically passed away before this project could be completed. This project would not have been undertaken without his enthusiasm, knowledge, and efforts and we have chosen to dedicate this book to his memory. I would like to thank Funkoo Park (former President of the Korea Labor Institute), Young-bum Park, and Sri-Ram Aiyer (former Director of Korea Country Office, the World Bank) who were closely involved with this project right from the very beginning. I would also like to gratefully acknowledge the assistance and contribution of many colleagues at the World Bank. Specifically, I am heavily indebted to Tamar Manuelyan Atinc, Gordon Betcherman, Amit Dar and Dalhoe Coue (former staff of Korea Country Office) for their continued collaboration during this project. I would like to express my deepest appreciation for the support provided by the staff of the Korea Labor Institute, including Mr. Chanyoung Park, chief of the publication division.

I sincerely hope this book will contribute to a wider understanding of labor market issues and serve to stimulate a productive dialogue as policymakers map options for the future.

Wonduk Lee  
President  
Korea Labor Institute

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**PART I**  
**INTRODUCTION**





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# Overview

**Funkoo Park\***  
**Young-bum Park\*\***  
**Gordon Betcherman\*\*\***  
**Amit Dar\*\*\***

Korea's financial crisis was as dramatic as it was unexpected. Between October and December 1997, Korea was reduced from the world's 11<sup>th</sup> largest economy to an economy surviving on overnight loans from international financial institutions. Consequently, Korea experienced a devastating economic decline. In 1998 real GDP fell by 5.8 % and the number of unemployed rose by over one million.

The Korean government implemented wide-ranging labor market reforms to accommodate needed structural changes, and was determined to build a stronger and more durable social safety net so as to mitigate the painful social costs of structural adjustment. In order to promote labor market flexibility, in February 1998 the government repealed the two-year suspension in the application of Article 3 of the Labor Standards Act thereby permitting employment adjustment for economic reasons. At the same time, in order to facilitate quick redeployment of labor, it enacted legislation to allow the operation of private manpower leasing services, and relaxed restrictions on the private provision of job placement services.

These developments were controversial. Confrontation between unions and employers concerning the flexibility measures increased as unemployment continued to rise, reaching a record high of 1.8 million in February 1999. Union leaders and workers insisted that layoffs should be averted through wage cuts and work-sharing while management argued that layoffs were necessary for companies to overcome the economic difficulties.

The measures to enhance flexibility were accompanied by interventions to improve labor market functioning. For example, the Korean government

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increased the number and quality of public employment offices while making sure that they would complement rather than crowd out private employment offices. The coverage of labor market information systems was extended to monitor the effects of adjustment on less privileged workers who were employed in establishments with less than five employees.

The government underpinned these labor market reforms with measures to cushion the shock of layoffs as well as to protect vulnerable groups by expanding workers' legal rights. It spent trillions of Korean won on projects to help the unemployed. The coverage of protective articles of the Labor Standards Act was extended to cover employees in establishments with fewer than five workers. Social protection for workers was strengthened by extending coverage of the Employment Insurance Scheme (EIS) to all establishments in October 1998.

Against this background, a grant from the ASEM-EU Financial Crisis Fund was provided to study the labor market impacts of the crisis; to evaluate the experience of interventions designed to alleviate the impact of the crisis; to learn from international experience on the design and implementation of labor policies and interventions; and, based on these diverse set of experiences, to develop policy recommendations for the Korean labor market in the medium and long-term. National and international experts were commissioned to undertake a wide range of studies on these topics. These studies were presented and discussed at an international conference in Seoul in May 2000. Following the conference, they were revised for this volume.

The remainder of this introductory chapter proceeds as follows. First, Korea's labor market developments after the financial crisis are reviewed. Employment, wage and other major labor market indicators as well as industrial relations are discussed. The labor market situation before the crisis is also compared to the post-crisis situation. This is followed by brief summaries of the studies that comprise this volume. These are organized into five areas: income support programs, labor law and labor market regulations, active labor market policies, the labor market and gender, and Korean experiences in a comparative context. Critical assessments of the findings of the papers are also discussed briefly. These assessments are mainly based on comments and discussions made at the conference in Seoul. The chapter concludes with a discussion about emerging policy concerns and areas for further research.

## **Labor Market Developments after the Financial Crisis**

1987 was a turning point for labor in Korea, with the government initiating its withdrawal from its authoritarian approach to become a conciliator within

a legal framework.<sup>1</sup> A revival of the labor movement followed, manifested in dramatic increases in the number of unions, union membership, and disputes. But only minor amendments were made to labor laws, which continued to recognize only the apex union body, the Federation of the Korean Trade Unions (FKTU), and to lock out 'third parties' (i.e. union officials not employed by the enterprise concerned) from collective bargaining. Korean labor laws were not amended substantially until March 1997 when most of the restrictions on union activities were lifted as a result of these amendments. Measures were also taken to increase labor market flexibility. One of the most controversial aspects of this law was the introduction of collective redundancy dismissals. Under the new law, beginning in March 1999, companies would be able to dismiss workers if there were urgent economic reasons.

However, the crisis overtook all these proposed changes. With the IMF's offer of a financing package in 1998 to help alleviate the impacts of the crisis, the Korean government and the IMF agreed that further steps should be taken to improve labor market flexibility. Recognizing that this issue could not be taken solely by the government, on January 15, 1998 President-elect Daejoong Kim established a tripartite committee for labor relations. This included representatives from unions, employers, the ruling political parties, Cabinet members, as well as public organizations. From the start, the committee faced severe opposition from labor over the issue of redundancies. Nonetheless, in February 1998 the committee agreed to allow dismissals in cases where they were absolutely unavoidable or as a consequence of mergers and acquisitions.<sup>2</sup> In addition, under the new agreement, dismissals for collective redundancy were allowed earlier (i.e. starting from April 1998) than had been originally scheduled (March 1999).

Additional agreements reached by the tripartite committee were as follows:

- The government should establish a five trillion won unemployment fund.
- Public servants should be allowed to form a labor consultation body in 1999. Teachers should be allowed to form a labor union in July 1999.
- Labor unions should be allowed to engage in political activities as of the first half of 1998.
- A dispatched worker system should be allowed.<sup>3</sup>

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<sup>1</sup> Protests in the 1980s led by students and union activists against the military government came to a head in June 1987 when the presidential candidate of the ruling party presaged political liberalization. See Park and Leggen for details (1998).

<sup>2</sup> In the earlier 1997 amendment to the labor law, mergers and acquisitions were not considered a justifiable reason for collective dismissals.

<sup>3</sup> This system refers to hiring arrangements whereby an employer employs workers through temporary work agencies instead of hiring them directly.

After this landmark agreement was reached, some members of the more radical Korean Federation of Trade Unions (KCTU) voted against the deal despite their representatives' endorsement of the package. The dissenters claimed the agreement did not fully reflect the interests of labor. However, they did not go ahead with major strikes. Most people hailed the agreement saying that it would contribute greatly to restoring international confidence in Korea.

Following the financial crisis, the Korean economy experienced many difficulties. In real terms, GDP decreased by 5.8% in 1998 (Table 1.1). One of the consequences of the depressed economy was a rapid increase in unemployment. Job losses accelerated through 1998 and the unemployment rate reached 8.6 % in February 1999, the highest it has been since official statistics have been published. This figure represented 1.8 million unemployed Korean workers. Before the financial crisis, less than 500,000 were unemployed.

Job losses were concentrated in certain sectors of the economy. Manufacturing experienced the largest losses, with employment in that sector decreasing by 473,000 between the last quarter of 1997 and the first quarter of 1998. Job losses were also large in the construction sector. On the other hand, employment in the agriculture/forestry/fishery sectors increased during the financial crisis as unemployed workers went back to the rural areas to seek a livelihood.

With mounting job losses, workers and their unions called for guarantees of job security, suspension of unilateral moves by employers to lay off workers in the name of structural reform, and a stronger safety net. Workers felt that government measures did not guarantee a minimum livelihood for the unemployed. As of August 1998, only regular employees working for establishments with five or more employees were entitled to unemployment allowances. Moreover, according to a survey by the Korea Labor Institute (March 1998), two out of five jobless persons had not received severance pay, which is the alternative means of social assistance for the unemployed.

At the workplace level, management was having a hard time introducing labor market flexibility measures. This was especially true in large firms with strong unions. Opposition from workers hardened as there were few re-employment prospects for those who were dismissed. In non-unionized sectors or in smaller firms, on the other hand, downsizing measures were introduced more easily. Thus, a short-term outcome of these developments has been a further polarization of working conditions between large and small firms.<sup>4</sup>

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<sup>4</sup> To some extent, however, institutionalizing a system of collective dismissals for managerial reasons was much easier in the context of the IMF package. Unions as well as workers have had little alternative but to accept the principle of employment adjustment which is required by the IMF and international investors.

**Table 1.1: Selected labor indicators in Korea, 1995-2000**

	1995	1997	1998	1999	1999 Q2	2000 Q2
GDP change rate (%)	8.9	5.0	-5.8	10.7 <sup>1)</sup>	10.8	9.6
Economically active population rate (%)	62	62.2	60.7	61.5	61.0	61.3
Employed (000s)	20,377	21,048	19,926	21,634	20,362	21,268
Unemployed (000s)	419	566	1,463	1,353	1,435	840
Unemployment rate (%)	2.0	2.6	6.8	6.3	6.6	3.8 <sup>1)</sup>
Nominal wage change rate (%)	11.2	7.0	2.4	12.1	10.6	8.7
Real wage change rate (%)	6.4	-2.5	-9.3	11.1	10.0	7.2
Working hours per month	207.0	203.0	199.2	208.1		
Union membership (000s) <sup>1)</sup>	1,615	1,484	1,402			
Number of industrial disputes <sup>2)</sup>	88	78	129	198		
Number of foreign workers in Korea <sup>3)</sup>	128,906	267,546	157,689	227,384		

Notes: 1) Union membership peaked to 1,932,000 in 1989.

2) 7,238 of strike took place from 1987-1989.

3) As of December 31 of each year.

4) From January to September 1999.

Source: Korea Labor Institute (Various Issues), *Quarterly Labor Review*.

Office of Statistics, Korea (Various Issues), Survey Report on *Economically Active Population*.

Industrial disputes increased sharply as job losses mounted. In 1998, 129 strikes were recorded, a 65% increase over 78 recorded in the previous year. Workers who took part in the strikes numbered 146,000, three times as many as the 44,000 who participated a year earlier. The number of lost production days reached 1,452,000 in 1998, compared with 444,000 days a year earlier.

Tension between unions and the government concerning economic restructuring peaked in April 1999. The union representing employees of the Seoul Subway System staged a strike in order to protest the scheduled restructuring plan which would inevitably have led to massive dismissals. However, other unions did not join in a general strike called by the KCTU and the dispute ended unsuccessfully for the union.

The aftermath of the crisis also affected workers' earning through widespread wage cuts or freezes. In the Labor Ministry's survey of wage

deals in June 1998, 87% of the 2,408 firms polled nationwide reported that they had frozen or reduced salaries during the year. After annual wage gains typically greater than 6% until 1996, wage increases were only 0.9% in the fourth quarter of 1997. In 1998, they decreased by 9.3%. Cuts in bonus payments were particularly substantial.

There has been some improvement in the situation over the past two years as the economy has started to grow quite rapidly again. Since February 1999, the unemployment rate has been decreasing - by late 1999, the unemployment rate has dropped to below 5% from a high of close to 7% in 1998. The unemployment rates of the first and second quarter of 2000 were 5.1% and 3.8%, respectively.<sup>5</sup> The improved labor market conditions mirror the marked improvements in Korea's economic conditions since mid-1999. This also confirms that the primary problems concerning unemployment during the financial crisis was deficient aggregate demand (Fields, 1999). Reduced unemployment rates were also partially attributed to income support measures to cushion the shock of layoffs put in place by the Korean government after the financial crisis began. The negative impacts (in terms of jobs) of the flexibility measures introduced during the crisis were to some extent mitigated by these income support programs.

Youth unemployment was a labor market policy concern even before the crisis. In November 1997, the unemployment rate among the 15-24 age cohort was 7.7% (5.7% for the 15-29 age cohort) when the economy-wide unemployment rate was just 2.6%. With the crisis, these youth rates jumped to 19.7% and 14.6% in December 1998 for the 15-24 and 15-29 age cohorts, respectively. While the youth unemployment rate also decreased with the improved economic situation, it is still very high.<sup>6</sup>

However, the improvements in the overall unemployment picture do not mean that the social protection for workers is no longer a problem. The employment situation of the most marginal unemployed workers who do not qualify for unemployment benefits has not improved. While Korea's Employment Insurance System, which was set up in 1995 to cover establishments with 30 workers or more, and then progressively expanded during the crisis (finally covering all enterprises regardless of size by October 1998) provides assistance through three components - employment subsidies, vocational training, and unemployment benefits - only a small proportion of workers remain insured and benefits are very modest by international standards. Furthermore, young people tend not to receive unemployment benefits since many of them have just entered the labor force. Or, if they do receive benefits, their eligibility period is shorter.

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<sup>5</sup> Another problem is that the proportion of long-term unemployed (those unemployed for more than six months) is high. It was about 20 % of total unemployed in 1999. However, it had decreased to 13.6 % in the first quarter of 2000.

<sup>6</sup> The unemployment rate of the 15 to 19 age cohort was 13.9 % and 10.0 % in 1999 and November 2000, respectively.

Since the crisis, there seems to have been a shift towards temporary employment and away from regular forms of work. For example, the number of daily workers, who are not covered by the unemployment insurance scheme, has increased substantially. The proportion of daily employees with less than a one-month employment contract period reached over 18.0% of total employment in 2000, an increase from 13.8% in 1996.

Korean labor market conditions had been very tight up until the financial crisis, with many industries suffering from a shortage of unskilled workers. The rate of unfilled vacancies for unskilled workers was 13.5% in 1996. This situation had drawn foreign workers to Korea in increasing numbers, growing from a few thousand in the early 1980s to almost 300,000 in late 1997 (Table 1.1). While, current immigration laws do not allow unskilled foreign labor to enter Korea, they are, however, allowed to enter as 'trainees'. Nevertheless, a large number of unskilled foreign workers entered Korea for the purpose of employment and undocumented foreign workers comprised 55.3% of the total foreign labor force in Korea in December 1997.<sup>7</sup>

Although the popular view called for the repatriation of foreign workers as the impact of the financial crisis unfolded, many Koreans came to realize that the country still needed unskilled foreign workers. Despite rapidly growing unemployment, not many Korean workers wanted to work in "three-D (difficult, dangerous and demanding) jobs". Small firms in labor-intensive manufacturing sector are still having difficulties in locating Korean nationals who want to work for them. The poor success of government measures to replace foreign labor also confirmed that unemployed Koreans were reluctant to take up 3-D jobs, even under the difficult circumstances.<sup>8</sup>

## Income Support Programs

When the financial crisis began, Korea was not prepared for such high levels of unemployment. An unemployment insurance scheme had been introduced only in 1995 with limited coverage. Only 3% of the total population were protected under social assistance programs. In 1997, the livelihood protection program accounted for the major share of government spending for social safety nets.

With mounting unemployment, the Korean government continuously

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<sup>7</sup> After the financial crisis started, the Korean government offered two amnesty programs to undocumented foreign workers in 1997 and 1999. Some 55,000 undocumented foreign workers left the country under these programs.

<sup>8</sup> The Korean government offered wage subsidies to establishments that replaced their foreign workers with Korean nationals. However, only some companies applied for the subsidy. For example, until September 8, 1999, 16.6% of the targeted replacements were accomplished. As a result, the government has doubled the wage subsidy amounts.

expanded the coverage of the Employment Insurance System and benefits. The total amount of the unemployment allowances increased from 79 billion won (\$64 million) in 1997 to 850 billion won (\$708 million) in 1998, then to 1.5 trillion won (\$1.3 billion) in 1999 (Table 1.2).<sup>9</sup> With employment prospects improving, overall unemployment payments decreased in 2000. During the first six months of 2000, unemployment allowances of 227 billion won (\$189 million) were paid, which represented a decrease of 31.3% as compared to the same period in 1999. The Korean government has also put greater resources into livelihood protection programs. Temporary public assistance programs have been introduced. Around 5 trillion won were (and will be) spent in order to create short-term jobs, mostly through public works projects. Special programs targeting particular groups such as the homeless were launched. In addition, various kinds of training programs were offered for the unemployed. Government expenditures on social assistance have more than doubled since 1997.

Despite all these efforts, only a limited number of the unemployed has benefited from these programs. Just 20% of the unemployed received some kind of social protection from the government in 1998 and 1999. Clearly, income support for unemployed workers remains a critical policy area and the first section of this volume includes five chapters on this issue.

In Chapter two (*Expanding the Coverage of Korea's Unemployment Insurance System*), Jai-joon Hur (Korean Labor Institute) proposes a measure to expand Korea's unemployment insurance system. In June 1999, only 10% of the unemployed workers enjoyed access to unemployment benefits even after the system had expanded<sup>10</sup>. Recognizing the incomplete coverage of Korea's Unemployment Insurance Scheme, Hur proposes that the system be expanded to include daily workers whose employment contract period is shorter than one month. About 20% of paid employees are daily workers. Another 30% are temporary workers and the distinction between the daily and temporary workers is often blurred.

The author proposes a Refined Employment Record-keeping System (RERS). Under the new system, employers will be obliged to report the affiliation of all of their employees to the labor authorities. The introduction of an Employment Record Form (ERF) or Smart Cards is also suggested in order to support employees in keeping track of their employment records. The ERF is a written form of employment record which employers have a responsibility to fill out and give to employees, as well as to submit to the authorities.

Although the RERS proposal addresses one obvious concern with the coverage of the existing unemployment system, various issues need to be

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The exchange rate of Korean won with respect to the US dollar has fluctuated between 900 and 2,000 in the aftermath of the crisis. This paper uses 1,200 Korean won to one US dollar which is close to the rate after the Korean won had more or less stabilized.

<sup>10</sup> This ratio even decreased to 7.9% during the first half of 2000.



**Table 1.2: Expenditures of social protection for the unemployed in Korea<sup>1</sup>, 1997-2000**

	1997	1998	1999	2000 <sup>2</sup>
	(won in billions)			
Unemployment allowances	78.7	850	1,522.7	1,013.6
Livelihood protection program	1,121.0	1,634.9	2,314.7	2,313.6
Regular program		1,379.1	1,488.4	1,709.0
Temporary program		255.8	826.3	604.6
Supplementary social safety net	0.0	2,262.7	4,132.3	2,553.0
Short-term job creation		1,170.4	2,671.8	1,210
Public loans for the unemployed		772	1,179.2	515.2
Provision of lunches and school fee to middle and high school students		107.4	281.6	82.8
Payments for wages in arrears		190.0	0.0	0.0
Training for the unemployed		754.1	583.2	350.9
Employment stabilization scheme		122.4	483.2	366.3
Job placement services		66.0	103.6	79.6
Total	1,199.7	5,667.2	9,140.0	5,922.0

Notes: 1) The figures of 1998 are from the Prime Minister Office and the Ministry of Labor (1999).  
The figures of 1999 and 2000 are from Ministry of Finance and Economy and other government ministries (2000).

2) The figures of 2000 are as of January 11, 2000.

Source: Prime Minister Office and the Ministry of Labor, Korea (1999).

Ministry of Finance and Economy and Other Government Ministries, Korea (2000).

resolved before such a program can be implemented. One issue involves the potential financing burden, especially because of the seasonal nature of much daily work. Depending on the numbers of daily workers included in the Unemployment Insurance Scheme, funding requirements might need to be substantial to cover the high levels of unemployment among daily workers during the winter. Moreover, the RERS would likely only be applicable to daily workers who have a sort of guaranteed employment period as found in construction. Hence, many daily workers in manufacturing and services would still be excluded from unemployment insurance, even with the RERS. Finally, the new system would likely encounter enforcement problems.

In Chapter three (The Potential Role of an Employment Guarantee Scheme in Korea's Social Safety Net System), Gary Fields (Cornell University) proposes a second pillar of the Employment Insurance System which he labels as the Employment Guarantee Scheme (EGS). The EGS would consist of public works jobs, offered on a daily basis to all who wanted them. The EGS would differ from the existing public works system in several respects. First, it would be open to everyone except for persons currently receiving UI benefits. Second, it would be a guarantee scheme

which offers social assistance to those who need help. Third, jobs would be offered for a period as short as a day. Finally, the benefits would be below the minimum wage level.

However, designing social usefully public works jobs on a large scale raises several questions. Particularly, given the EGS proposal that participants receive wages below the minimum wage level, and duration of participation can be as little as a day, is it reasonable to expect that meaningful tasks will be performed? Furthermore, financing the system might be a problem particularly if the country runs a deficit in national financing.

In Chapter four (*The Feasibility of Introducing Noncontributory Cash Benefit Systems for the Unemployed in Korea*), Young-bum Park (Hansung University) considers the feasibility of introducing a non-contributory cash benefit system for the unemployed with special reference to the one put forward by the government under the National Basic Livelihood Guarantee Act. Park recognizes the need to enhance social assistance for the unemployed. However, he argues that efficiently and fairly implementing a non-contributory cash benefit system, such as the one proposed by the government, would be difficult until conditions for means and work tests for the unemployed reach a reasonable level. Therefore, Park proposes that a public works scheme should be maintained as a short-term social safety net even after the financial crisis is over.

Park also argues against the extension of the UI system to small employers unless an appropriate system to solve enforcement problems is developed. This view is quite different from the one proposed in chapter two and, of course, runs counter to what the government has done. The author does suggest, however, that the coverage of UI should be expanded by providing benefits to voluntary job quitters after a certain period. The chapter argues that the complete disqualification of voluntary job quitters is relatively harsh compared to international standards. While some countries do disqualify voluntary quitters, others do not.

In Chapter five (*Unemployment Assistance: Policy Implications from the Crisis of 1997*), Alan Abrahart examines Korea's experience during the financial crisis in operating the UI system and compares it with Australia which offers only non-contributory unemployment assistance. The author draws a number of observations about Korea's UI system during the crisis, concluding that it offered little protection to those workers who were most vulnerable. First, its short-term viability was ensured through generating contributions from employees who were unlikely to make significant claims for unemployment compensation. The people who actually contributed to unemployment insurance were less than 25% of the labor force in 1999, and were those who were least likely to be unemployed. This implies that a relatively small proportion of the labor force is allowed to get access to the system compared to other countries. Second, daily workers were excluded from the system, limiting its scope. Third, the risk of unemployment continues to be highest among those who are uninsured. Finally, and

relatedly, the greatest problem during the financial crisis turned out to be providing social protection to those who were not excluded from the unemployment insurance scheme. The Livelihood Protection Program (LPP) and public works, the two significant instruments for assisting these workers, fell far short of the potential level of demand, leaving many people to rely on family and community support while unemployed.

Recognizing that the government has chosen to supplement the UI system with a non-contributory scheme of assistance, Abrahart argues that Korea should decide the extent to which the UI system and the social assistance scheme are to be considered in one administrative framework. Australian experience suggests that welfare dependency can emerge among people who would not have UI entitlements in a typical contributory system. These are precisely the sort of marginal workers, often working in the informal sector, who suffered most during Korea's financial crisis. The author claims that a crucial issue to consider is the level of assistance to be provided under the two schemes.

In Chapter six (*Assessing the Coverage and Efficiency of the Wage Guarantee System in Korea*), Taigi Kim (Dankook University), Kang-shik Choi (Myungji University), and Joyup Ahn (Korean Labor Institute) describe the Wage Claim Guarantee System which was introduced after the crisis for insuring payment of severance allowance and wage arrears. Based on data collected from the beneficiaries of the system, their study shows that 90% of the surveyed employees found the system helpful in maintaining their livelihood. The authors suggest that the benefits and contributions should be differentiated depending on company size as well as type of industry. They also argue that a standardized manual for judging company insolvency should be developed and that there should be efforts to publicize the Wage Claim Guarantee System.

Some reservations have been expressed in the study's conclusion that that the Wage Claim Guarantee System has been implemented successfully and effectively. These are mainly based on the fact that the survey only covered people who had received benefits. More research needs to be done to include people who qualified for the benefits, but did not receive them (presumably because they were not aware of the system). The effectiveness of the system in terms of costs and benefits should be also reviewed.

## **Labor Law and Labor Market Regulations**

As we have described, Korea's labor laws have undergone revisions to allow for more flexible layoff provisions and for temporary worker agencies (dispatch workers). While it is too early to judge the impact of these regulations, there has been considerable discussion about their impact on labor market flexibility and how these regulatory changes should be linked

to the safety net system. Section 11 of this volume includes two chapters addressing these questions.

In Chapter seven (*Assessment of Labor Market Responses to the Labor Law Changes Introduced in 1998*), Duck Jay Park (Korea National Open University), Jong Hee Park (Korea University), and Gyu-Chang Yu (Sookmyung Women's University) analyze the effects of the legislation legalizing collective dismissals for managerial reasons. Their study, based on an enterprise survey, concludes that even after the Labor Standards Act was amended, the major mode of employment adjustment was not dismissal. Most separations were 'honorable retirements', spin-offs, early retirement, or attrition. This has led employers to claim that greater reliance on these forms of separation, particularly honorary retirement which is a costly mode of employment adjustment, proved that Korea's labor market still lacks flexibility despite the concerned labor law amendment. However, it cannot be denied that the labor law change helped troubled companies reduce their workforces. It has contributed to workers' become more accepting of employment adjustment in such companies. However, the authors expect that collective dismissals for managerial reasons are not going to be the dominant mode of employment adjustment in the near future considering that a sentiment of strong egalitarianism exists in the Korean society.

The authors argue that Korea's social safety net needs to be expanded to enhance labor market flexibility and they feel that this will be necessary for workers to accept dismissal more easily. They also suggest that, in addition, policies to upgrade workforce skills need to be developed and government-private sector training partnerships should be established.

In Chapter eight (*Labor Market Flexibility and Employment Agencies in the UK, Japan and Korea*), Barry Wilkinson (University of Bath) addresses key policy issues relating to the new worker dispatching law. His analysis considers evidence from the U.K. which has longer and more extensive experience with employment agencies. Wilkinson argues that Korea needs to further study the potential costs and benefits of the new worker dispatching law and makes the point that the implementation of the new law was accelerated under crisis conditions.

Based on evidence from the U.K., the chapter raises some issues about the use of temporary worker agencies. First, the contribution of labor market flexibility, including temporary work agencies, to long term employment creation remains unknown. Second, there is a negative relationship between employment agency activity and skills formation except for a small minority of highly qualified agency labor. Third, employment status is highly ambiguous and many temporary agency workers are unclear even as to who their employer is. The author stresses that policy makers have to find a way to achieve a balance between employer and employee needs. He states that this is urgent in Korea since many employment agency activities are illegal despite the recent labor law change and work done by dispatched workers is much wider than the allowed scope of temporary work agency activities.

## OVERVIEW

### Active Labor Market Programs (ALMPs)

Unlike most OECD countries, Korea does not have a strong tradition of Active Labor Market Programs (ALMPs). One of the main reasons has been the low rates of unemployment prior to the crisis. However, the crisis has led to a significant expansion of these programs as the increases in unemployment, the difficulties facing many laid-off workers in reentering the ranks of the employed, and the obstacles facing young people trying to enter the labor force have all underscored the need for policy-makers to consider new options. Section III of this volume includes five chapters on ALMPs.

In Chapter nine (Income Assistance and Employment Creation through Public Works in Korea), Johee Lee (Korean Labor Institute) evaluates the impact of the public works programs during the crisis using the results of surveys of program participants and administrators.<sup>11</sup> The author argues that, although these programs were officially classified as an active labor market measure by the government, the major role of the public works scheme was as a source of complementary income. The program especially benefited women, older, and less skilled workers who were mostly excluded from other income support measures. According to the survey results, participants were mostly satisfied with the scheme and wanted it to continue. Lee also claims that deadweight losses were relatively small as a large majority of the participants were atypical workers who had difficulty in finding jobs during the financial crisis.

This claim is arguable. Even during the financial crisis, many small businesses experienced labor shortages. It seems likely that many individuals who would otherwise have looked for a job participated in the public works especially given that wage rates were much higher than the minimum wage. Hence, critics contend that such schemes deepened the welfare dependency of the participants. On the other hand, supporters of these schemes, including the author, argue that these schemes were critical during the crisis as they assisted the poor to maintain incomes during a difficult period.

Lee makes several recommendations regarding the future direction of Korea's public works programs. First, rather than drastically reducing the projects, he suggests that they should be retooled to cater to the demands of the disadvantaged groups in the private sector which may not be able to benefit from social assistance but can avail of public works. Second, close interactions between public works projects and other unemployment measures including social welfare programs should be established. In particular, with the development of the new social assistance scheme under

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<sup>11</sup> Conclusions drawn from this study are tentative since the study does not include a comparison group of individuals (who were unemployed but did not participate in public works project).

the Basic Livelihood Guarantee System, the role of public works should be redefined. Lee suggests that public works projects could be used as a work test, which would allow many of the unemployed poor to remain attached to the labor force. Third, Lee argues that the wage rates of public works participants should not be lowered considering that they are usually the major breadwinners of their families.

In Chapter ten (Public Works Program in Korea: A Comparison to Active Labor Market Policies and *Workfare* in Europe and the US.), Ivar Lodemel and Espen Dahl compare Korea's public works programs with workfare and other active labor market programs in Western countries. They note that the scale and the nature of the problems experienced in Korea during the financial crisis are more similar to the experiences in the West in the 1930s rather than under present circumstances. They point out that while the Korean scheme offered an effective buffer against the immediate effects of large scale unemployment, it fell short in developing the skills of the work force needed for a changing economy. According to them, Korea's challenge is to transform public works into a modern active labor market program and to reform the livelihood protection program into a modern social assistance program. The enactment of the Basic Livelihood Guarantee Law to replace the livelihood protection program suggests that Korea may be now ready to move in this direction. The authors observe that culturally Korea appears to have more in common with Western European countries rather than the U.S., even though there is a dominance of U.S. style policies which are based on an individualized view of people, their behavior and their aspirations. They caution that when options for reform are considered, careful consideration should be given to the fact that Korea is a cohesive and close knit society, rather than an individualistic one.

In Chapter eleven (Review of *the* Effectiveness of Korean Public Employment Services), Jaeho Keum (Korean Labor Institute) looks at the Korean public employment service (PES) which expanded substantially during the financial crisis. The share of the unemployed who registered with public employment offices increased during the crisis partly because they were able to claim their unemployment benefits as well as receive job search assistance at the PES offices. The author argues that there still remains much room for the expansion of the PES in Korea as the number of public employment agencies, counselors, and beneficiaries assisted by each agency or counselor fall far short of the norms established in OECD countries. However, Korea has yet to reach a consensus about the extent to which the PES should be expanded and what the role of private employment agencies should be. Some argue that the role of the PES should be minimal - such as providing services to the most vulnerable - and that private employment agencies should play a greater role than at present. However, this does not seem to reflect the current view of the Korean Labor Ministry. Some also observe that the Korean PES enjoys monopoly power in the employment services market which is not the case any longer in most OECD countries.

Based on his survey of PES beneficiaries as well as service providers, the author argues that the Korean public employment service still needs to improve the quality of its service and suggests some possible means to do so. First, the PES should be restructured to strengthen areas such as in-depth counseling, career guidance and in-depth occupational information as its job matching services will be increasingly carried out via Work-Net on the internet. Second, the PES should strengthen services to vulnerable groups such as elderly or female household heads, and low-skilled workers. Currently, PES customers mostly comprise of young or highly educated workers. Third, there should be measures to increase the competence and morale of counselors. The survey also showed that counselors had complaints about their status as contract employees, about their pay and promotion prospects, and about working conditions.

The next two chapters look at evidence from evaluations of training programs. In Chapter twelve (Evaluating *the Training for the Unemployed in Korea*), Soon-Hie Kang and Byung Hee Lee (Korean Labor Institute) present results from an evaluation of Korea's training programs for the unemployed. Training has played an important role in Korea's active labor market policy during the crisis, with participation expanding eight-fold between 1997 and 1998. However, the evaluation shows that re-employment rates after participation in training have been no higher than employment rates for the non-participating unemployed. This has been widely interpreted in Korea as proof of the failure of the training programs.

The authors' study is Korea's first scientific evaluation of training programs. It compares employment-related outcomes nine to fifteen months after training among 1,000 unemployed workers who had participated in a training course targeted at the insured unemployed workers in 1998. The comparison group is those individuals who had separated from a job during the same period but who did not undertake training during 1998. The analysis shows that in terms of gross outcomes, the Korean training programs have not helped their participants: about 40% of both the trainees and the control group were employed at the end of the observation period. However, when the different observed attributes of the two groups are controlled for, differences emerge. The probability of moving into employment after training was significantly higher for female trainees than for non-participants (though the impact for males remains insignificant). Although some methodological issues remain to be addressed, this study underlines the importance of conducting scientific evaluations when evaluating active labor programs.

Chapter thirteen (Publicly Funded *Training for Unemployed Adults: Germany, the UK and Korea*) by Paul Ryan (Cambridge University) surveys the evaluation evidence available on public training programs for (East) Germany and the U.K.. The results are mixed. The Eastern German training programs do not appear to have generated significant labor market benefits for their participants. The British programs have, in contrast, helped

participants find work and enhance their earnings.

The author observes that Korean training programs during the financial crisis resembled their East German counterparts of the early 1990s in terms of the rapidity of expansion, their initial emphasis on breadth of coverage at the expense of depth of learning, their overwhelming orientation toward classroom training, and the wide range of participants and training provided. However, the implications of the U.K. and German experiences for Korean policy are limited as the impacts vary significantly based on economic conditions and type of training.

## **Labor Market and Gender**

Gender discrimination was a significant issue in Korea even prior to the crisis, and this issue was further highlighted during the crisis period. In Chapter fourteen (*Were Korean Women More Affected by the Asian Crisis*), Kye Woo Lee and Kisuk Cho (Ewha Woman's University) analyze the effect of the financial crisis on women. The authors find it difficult to draw an unequivocal conclusion on whether female workers suffered more during the financial crisis since both sexes were adversely affected. However, they conclude that male and female workers were treated differently in the labor market during the crisis, especially in terms of earnings, involuntary disengagement, and rehiring status. The average earnings of female workers were lower than those of male workers. The incidence of involuntary unemployment was higher among female than male workers. When female unemployed workers were re-employed, they tended to get non-regular or daily jobs more often than male workers. However, their data do not allow them to analyze whether labor market discrimination against females increased during the crisis.

The authors try to identify which gender discrimination theory best explains these differences in the effects of the financial crisis. While there are some methodological problems with their data and test approaches, their survey data do not conclusively support any of the discrimination theories. Nonetheless, they argue that the data render more support for the cultural gender-type theory than the statistical discrimination or labor market risk theory.

## **The Korean Experience in an International Context**

As the government instituted and expanded a range of labor market interventions to alleviate the impact of the crisis, this provided an ideal



opportunity for Korean policymakers to 'learn and benefit from the experiences of more advanced OECD countries. The final three chapters of the volume look at the Korean experience within the international context.

Chapter fifteen (*Labor Adjustment, Non-Standard Work and Employment Program: Korea in an OECD Context*) by Gordon Betcherman, Amit Dar, Amy Luinstra, and Makoto Ogawa (World Bank) focuses on Korea's adjustment to the crisis and two labor market issues of growing importance for the country – ALMPs and non-standard employment. They show that the structure of the Korean workforce is rapidly becoming more similar to other OECD countries, with low and shrinking agricultural employment and growing employment in the service sector. Further, the educational attainment of the labor force now compares with that of high-income OECD countries.

Their review highlights the flexibility of Korean labor market - both in terms of prices and quantities - during the crisis. This raises questions for social policy and labor market segmentation. Their analysis reveals that Korea has an underlying propensity toward non-standard employment. From an international perspective, Korea has a high share of non-standard employees. While this has been key to the country's labor market flexibility, they view this as an issue that rightly concerns policy makers. There is a clear segmentation between relatively well paid regular workers with access to many kinds of social protection and non-standard workers who are in an insecure position. This is at least partly due to labor policies and practices which create incentives for non-standard jobs. Whether recent reform to extend the coverage of labor standards and unemployment insurance to individuals in these forms of employment will alter these incentives or not will have to be seen.

The crisis has led to a significant expansion of ALMPs. The authors do not draw a definitive conclusion as to whether such an expansion has been justified on economic or social grounds although they view the limited evidence on the effectiveness of these programs in Korea as discouraging. However, they strongly suggest that policy-makers in Korea should not avoid developing ALMPs as the country emerges from the financial crisis. But this should be done cautiously and large scale application of these programs should be avoided without piloting and carefully evaluating them. Furthermore, they argue that Korea's transition toward a knowledge-based economy will have implications for active labor programs in terms of institutional capacity building, delivery techniques, increasing reliance on technology, innovations in financing, and monitoring and evaluation of these programs. Korea can benefit from the experiences of some OECD countries where these transformations are already evident at the cutting edge of active labor market programs.

In Chapter sixteen (*Korean Labor Market and Social Safety-Net Reforms: Challenges and Policy Requirements*), John Martin and Raymond Torres (OECD) argue that Korea is still facing key challenges with respect to industrial relations, labor markets and social protection. They set out reform

proposals to tackle these challenges. The authors state that, although the recovery from the financial crisis is well underway, Korea should not reduce the momentum of reforms since further progress may be more difficult than is often thought. Indeed, future improvements in living standards may have to rest on using resources more efficiently, rather than more extensively as was the case before the 1997 crisis. They suggest a more qualitative approach to the development strategy encompassing an increased emphasis on enterprise training, reducing labor-market duality, and the establishment of a well-functioning social safety-net that covers all individuals.

Martin and Torres also argue that these measures need to be adopted in a context of full respect for basic workers' rights and, in this sense, resolving remaining industrial relations' issues should rank high on the policy agenda. They argue that in a modern and productive economy, it is important that all social actors be involved in the reform process in a climate of mutual respect and trust.

In Chapter seventeen (*The Challenge of Labor Reform in Korea: A Review of Contrasting Approach to Market Enhancement and Experience from Chile and Denmark*), Louise Haagh (Oxford University) points to the importance of an individual-centered approach to labor flexibility issues. Haagh argues that issues of labor market flexibility and social sector reform should not be regarded as separate concerns in an environment where human capital has become central to economic growth. She emphasizes an approach focused on individual welfare to labor market flexibility issues and a strong link between labor institutions and welfare reform.

According to the Haagh, Danish labor reforms in the past decade have succeeded because they have followed such an approach. Reforms have been geared toward supporting the mobility of the individual workers and of the development of human capital. According to Haagh, the Danish experience shows that it is possible to enhance the labor market in the sense of making it easier for individual workers to move in labor markets without necessarily reducing the flexibility of firms. Haagh argues that this can be seen in the high levels of intra and inter firm labor mobility that characterized the labor market throughout the 1990s.

## **Emerging Policy Concerns and Areas for Further Research**

During the financial crisis, the Korean government implemented many temporary measures in order to provide income support to displaced workers and their families, in addition to expanding the coverage of the Employment Insurance Scheme. However, only a small portion of the Korean labor force actually benefited from these programs. Many Koreans in hardship had to fall back on informal safety nets especially family support. Although these

traditional forms of support should not be discounted, Korea's public safety net needs to be further developed in order to assist the most disadvantaged.

One of the fundamental problems for the expansion of Korea's social safety net is the dualistic nature of labor market. Korea has one of the most flexible labor markets in the OECD and this flexibility has been demonstrated throughout the crisis. However, this flexibility is derived at least in part by the large share of non-standard (including temporary) employees who are entitled to very limited unemployment insurance or social protection benefits. The Korean labor market seems to have a propensity toward the creation of these forms of employment that can not be fully explained by the crisis nor by the country's stage of development. Recent government policy measures to extend social insurance and labor regulations to all firms and more categories of workers might decrease the incentives toward non-standard employment. However, the government's capacity to enforce these measures effectively is open to question. On the other hand, the loosening of restrictions on temporary worker agencies is likely to lead to increases in non-standard jobs.

In this respect, there is a view that strengthening labor and social protection for workers in non-standard jobs will decrease labor market flexibility. Whether it will or not deserves further research. What is clear, however, is that a challenge emerging for Korea is to improve social protection for all workers, to create incentives for access to secure work, and to support workers in transition without constraining job creation.

The impact of legislative changes concerning dismissals for economic reasons during the crisis, although not insignificant, was not as significant as expected. There is a school of thought that argues that this proves the lack of flexibility in the labor market. This may be true for some part of the Korean labor market – especially for workers in large sectors protected by strong unions - but it is most likely not true of workers in small enterprises. Hence, a short-term outcome of the crisis and the implementation of the reform package have been the further polarization of working conditions between large and small firms. On the other hand, it is possible that enlarging the social safety net could promote labor market flexibility as workers might be expected to accept dismissals more easily. This is clearly an area that will have to be studied in greater detail in the future.

Labor force participation rates among women are low by OECD standards. Further, the incidence of non-standard work is high among females. During the financial crisis, women were more often subject to dismissals than were men. All these facts imply that policy initiatives should be developed to boost women's participation and upgrade their status in the Korean labor market. This is also an area that needs to receive further attention.

Many of the unemployed was not insured by the unemployment insurance scheme at the beginning of the crisis. While the scheme was gradually extended to smaller private sector companies over the crisis period, less than 20% of the unemployed have benefited from the scheme. This is mainly due

to the fact that those who contributed to the scheme were the least likely to become unemployed and that temporary workers were excluded from participating in the scheme. Policymakers need to examine in greater detail how the coverage of the system can be extended while maintaining its financial sustainability. While the public works scheme contributed to reducing the hardship of the unemployed, especially those who were not entitled to unemployment benefits, critics argue that this scheme was poorly designed as the wages offered were significantly higher than the minimum wage which may have hindered employment generation in the private sector. A challenge for policymakers in Korea will be to design public works programs that are targeted to the most disadvantaged. The government has recently introduced a more extensive livelihood scheme under the National Basic Livelihood Guarantee Act. However, this new livelihood program is likely to face significant enforcement problems, especially given the dualistic nature of the labor market. Ensuring that the livelihood program is effective in meeting the needs of the target groups is an area that needs to be explored in greater detail.

The relative scarcity of rigorous evidence on the effectiveness of ALMPs in Korea does not allow a definitive conclusion as to whether such interventions have been justified on economic or social grounds. However, it is likely that the importance of ALMPs will increase in the future as Korea's labor market structure more and more resembles that of other OECD countries. It is important that further scientific evaluations be conducted in order to identify the impacts of the active labor market programs that were implemented during the financial crisis. As Korea continues the transition towards a knowledge-based economy, it can learn from other OECD countries, especially in relation to the design of ALMPs and their implementation.

Korea's economic progress over the past three decades and its apparent rapid resurgence from the economic crisis have been quite remarkable. This pace of development and change has been accompanied by pressures in the labor market – e.g. high levels of non-standard employment, inadequate levels of social protection, gender discrimination – creating formidable challenges for policy makers. However, Korea's responsiveness to problems over the last few decades gives us confidence about its future prospects as it begins to tackle these labor market challenges.

**PAR II**

**INCOME SUPPORT PROGRAMS**



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# Expanding the Coverage of Korea's Unemployment Insurance

Jai-Joon Hur\*

## Problems with the Existing Unemployment Insurance System

### *Objectives*

On July 1 1995, before the financial crisis, Korea had put into place an ambitious employment insurance system. The three components of this system are traditional unemployment insurance, job training, and employment maintenance/promotion subsidies. Other elements of Korea's social safety net system include a livelihood protection program for the poor, a livelihood stabilization fund for the unemployed whose assets fall below a certain level, a public works program for the unemployed and for the spouses of low-wage workers, and many other smaller programs.

The Korean Employment Insurance System (EIS) is of a compulsory social insurance type. Thus all the employers and employees in the covered firms should be insured and they are entitled to receive grants or unemployment benefits from the Employment Insurance Fund. As elsewhere, the unemployment insurance (UI) component of Korea's EIS protects against the risk of income loss due to unemployment. The UIS provides people with a temporary income after they have been completely unemployed for two weeks.

When the UIS started in 1995, only employees in large firms (hiring more than 30 workers) were entitled to the UI benefit. After the financial crisis, the coverage was rapidly expanded to all firms regardless of their size. The compliance rate, however, is low and UIS covers only 65% of the employees who are supposed to be covered. The objective of this paper is to assess why the coverage of Korea's UIS is incomplete and how the coverage

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can be extended.

Before proceeding, it is important to adopt a guiding framework with which to assess the UIS and around which to make proposals for change. One possible model is social insurance. Under this model, in so far as possible, every employee in society contributes and all of the insured that become unemployed can collect. Under the social insurance model, the financial resources of the system are funded based on pay-as-you-go principle.

A second model is the individual account model. Individual accounts can be publicly-run or publicly-mandated. In either case, the individual builds up the balance in his or her own account while working. In the event of unemployment, the account balance can be drawn upon to provide an income to the unemployed person. Otherwise, the money belongs to the individual, to be used in some other way, e.g., for spending in their old age, home-buying, or medical expenses. Under this model, UI is a type of compulsory savings with self-insurance against unemployment.

The third model is social assistance. Here, the nation taxes itself in order to provide benefits for the needy members of society. Under this model, benefits are means-tested – that is, in order to collect UI benefits beneficiaries must prove not just that they are unemployed but also that they are poor. Such means-testing is not necessarily carried out through declarations or administrative verification of low income or assets; self-declaration through self-targeting is also possible, as is the case with the public works program.

Korea's system has been set up on the social insurance model. Our recommendation will be set forth in the context that this model is continued.

### *The Labor Market Context and Incomplete Coverage of the Existing System*

Beginning in November 1997, the Republic of Korea underwent a devastating economic crisis. Declining macroeconomic conditions brought about major labor market disruptions in 1998: a quadrupling of unemployment, a fall of 9% in real wages, informalization of the remaining jobs, increased job insecurity, and rising poverty and inequality. Disadvantaged groups suffered a disproportionate impact. The result was not only economic misery but also social pain: increased homelessness, rising crime, heightened school dropouts, an accelerating divorce rate, and an overwhelming sense of social malaise.

1999 marked a major turnaround for Korea. GDP grew by more than 10.7%, and real wages increased apace. The unemployment rate is now less than half of its peak level. Women are again returning to the labor force and are finding employment. A sense of guarded optimism is returning to Korean society. Nonetheless, important labor market and social problems remain.

The unemployment rate is now twice as high as it was before the crisis,



and temporary and daily workers are much more vulnerable to unemployment than before. They account for 82.1% of unemployed wage workers, while only 52.9% of the total number of employees. They experience unemployment recurrently to the extent that 77.5% of those who experience unemployment more than twice during given 18 months are temporary and daily workers (Lee, 2000). In sum, they are principal group of workers suffering unemployment.

Even if Korea has expanded coverage of UIS to all firms regardless of their size from Oct. 1998, the UIS fails to cover most of temporary and daily workers who are supposed to be covered. Therefore, one major issue for the UIS in Korea is that as coverage is incomplete what measures can be taken to expand coverage so that more wage workers are insured against income losses due to unemployment.

Before proceeding, we should point out that financing is apparently not an issue. The UIS is running a large surplus – that is, it has a sound financial footing even after the Financial Crisis (Hur, 2000). This allows, without any further increase of contribution rate, room for extending the current UI structure by adding temporary and daily workers who frequently experience unemployment.

## Expanding the Coverage of the Unemployment Insurance System

### *Coverage of UIS*

In 1999, there were 12.5 million wage workers in the Korean labor market. Of these, only 6.1 million employees were working in insured employment – that is, in jobs that would qualify them for UI benefits in the event of unemployment. The gap in coverage comes from two sources: employees who are supposed to be covered but are not, and employees who are not now meant to be covered.

As of Dec. 1999, the estimated number of employees to be covered amounts to 9.2 million, but only 6.1 million are registered at public employment office. These and earlier figures are presented in Table 2.1. About 35 % of the employees that should be covered by the UIS are not actually registered on the EI database.

Even if all the employees, except in some designated cases<sup>1</sup>, are now officially entitled to UIS coverage by law, many employees are still not protected by UIS. Table 2.2 contrasts the number of regular and temporary employees, which can be regarded as a proxy for the number of employees who are supposed to be covered with actual number of insured employees by firm size. The uncovered employees are concentrated among small firms

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<sup>1</sup> Among them are employees working less than a month in a **firm**, government employees and private school teachers, etc. See Yoo (1999) for more details.

**Table 2.1: Number of Insured employees and estimated number of employees to be covered by the Korean UIS, December 1995 to December 1999**

	Dec. 31, 1995	Jun. 30, 1998	Dec. 31, 1999
Scope of coverage (firm size)	30 employees or more	5 employees or more	1 employee or more <sup>3)</sup>
Estimated number of employees to be covered <sup>1)</sup> (A)	4,280	5,710	9,243
Actual number of insured employees <sup>2)</sup> (B)	4,204	4,797	6,054
Coverage ratio (=B/A)(%)	98.2	84.0	65.5

Notes: 1) Estimated numbers of employees to be covered as of Dec. 1995 and Jun. 1998 are cited from Yoo (1999) and that of Dec. 1999 was estimated based on National Statistics Office's Economically Active Population Survey database, Government Employees Pension data and Private School Teachers' Pension data.

2) Actual number of registered employees on the Central Employment Information Office's EI database.

3) Including part-time employees working 80 hours or more in a month.

**Table 2.2: The number of regular and temporary employees and actual number of insured employees of the Korean UIS by firm size, December 1999**

	1-9	10-49	50-299	300-	Total
Regular and temporary employees (A)	3,442	3,385	2,249	1,523	10,598
Actual number of insured employees (B)	1,329	1,356	1,498	1,871	6,054
B/A(%)	38.6	40.1	66.6	122.8	57.1

Source: National Statistical Office, Korea, Economically Active Population Survey database. Central Employment Information Center, Korea, Employment Insurance database.

with less than 50 employees.'

Although it is the employers' duty to declare their employees to the public employment office and pay UI premiums, many small business employers neglect to do this. Informal characteristics in the employment relationship, the loose attitude of economic agents vis-a-vis legal regulations, together with the insufficient capacity of the EI administration underlie the

<sup>2</sup> For employees belonging to firms with equal to or more than 300, the actual number of insured employees exceeds the number of regular and temporary employees. The discrepancy seems to result from the inherent limit of employment statistics by firm size in the EAPS which is a household survey. However, we continue the comparison as there is no better alternative and this does not seriously harm our discussion

incomplete coverage of the UIS in small business firms. Therefore, how the labor administration can effectively identify small business firms and their employees has been an important issue in implementing the UIS since coverage was expanded to smaller firms.

The coverage ratio by industry is given in Table 2.3. Coverage rates are very low in the primary sectors, the wholesale and retail trade sector, the hotel and restaurant sector, and community, social and personal services sector.<sup>3</sup> These are industries with large proportions of temporary and daily employees.

**Table 2.3: Number of regular and temporary employees and actual number of insured employees of the Korean UIS by industry, December 1999**

	Regular and temporary employees (A)	Actual number of insured employees (B)	BIA (%)
Agriculture, hunting and forestry	24,706	10,689	43.3
Fishing	24,869	7,314	29.4
Mining	16,729	17,856	106.7
Manufacturing	2,998,105	2,470,361	82.4
Electricity, gas and water supply	58,620	55,170	94.1
Construction	539,388	467,226	86.6
Wholesale & retail trade, repairing consumer goods	1,559,951	637,669	40.9
Hotel and restaurant	639,730	150,405	23.5
Transport, storage and communications	814,038	552,243	67.8
Bank, insurance and other financial intermediation	660,306	385,299	58.4
Real estate, renting and corporate services	910,868	751,283	82.5
Public administration, defense and compulsory social security	632,839	0	n.d.
Education	847,896	96,408	11.4
Health and social works	314,610	247,929	78.8
Other community, social and personal services	436,493	182,980	41.9
Private households with employed persons	104,178	0	n.d.
Extra-territorial organization and bodies	15,097	0	n.d.
Others in EI database	n.d.	21,647	n.d.
Whole industry	10,598,423	6,054,479	57.1

Note : n.d. means not defined.

Sources : National Statistical Office, Korea, Economically Active Population Survey database.  
Central Employment Information Center, Korea, Employment Insurance database.

<sup>3</sup> The coverage ratio in Education is low as private school teachers are not entitled to UIS coverage.

As of Dec 1999, the 6.1 million registered employees account for 46.5% of total employees. This means that the UIS coverage is too low to be considered as a primary safety net for employees. Also, this is one of the reasons why only 10.7% of the unemployed, on average, received UB in 1999. In Dec. 1999, UB recipients accounted for 9.8% of the total number of unemployed and 15.5% of unemployed wage workers (Table 2.4).

Table 2.4: Ratio of UB recipients with respect to each category of the unemployed, December 1999

	Person ('000s)	Proportion of UB recipients with respect to each category of the unemployed (%)
UB recipients	102	
Unemployed	1,040	9.8
Unemployed who had work experience	947	10.8
Unemployed who lost their job within a year	770	13.2
Unemployed employees who lost their job within a year	660	15.5

Sources : National Statistical Office, Korea, *Economically Active Population Survey* database.  
Central Employment Information Center, Korea, *Employment Insurance* database.

When we look at the composition of employees and that of unemployed employees, temporary and daily employees turn out to be principal group experiencing unemployment (Table 2.5). Daily employees account for 18.6% of total number of employees while daily employees account for 46.4% of the unemployed. Table 2.6 shows that unemployment span of daily employees amounts, on average, to 1.2 month a year, suggesting that they are more in need of a safety net even though the EIS fails to cover them now.

Table 2.5: Employees and unemployed employees by employment status, December 1999

	Employees ('000s)	Unemployed employees ('000s)
Total	13,024 (100.0%)	660 (100.0%)
Regular	6,131 (47.1%)	118 (17.9%)
Temporary	4,468 (34.3%)	236 (35.8%)
Daily	2,426 (18.6%)	306 (46.4%)

Note : The unemployed employees are those who lost their job within a year.

Source : National Statistical Office, Korea, *Economically Active Population Survey* database.

**Table 2.6: Tenure period, employed period, employment period and unemployment period for workers by employment status, June 1999**

	Tenure period <sup>1)</sup> (months)	Employed period <sup>2)</sup> (months)	Employment period <sup>3)</sup> (months)	Unemployment period <sup>4)</sup> (months)	Non-employment period <sup>5)</sup> (months)
Regular	10.5	11.6	11.7	0.1	0.3
Temporary	7.5	9.7	10.1	0.6	1.9
Daily	4.3	7.4	8.3	1.2	3.7

Notes : 1) Tenure period = Employed period as wage and salary workers in a firm

2) Employed period = Employed period as wage and salary workers

3) Employment period = Employed period + Employed period as self-employed or non-paid family workers

4) Unemployment period = Unemployed period while searching a job

5) Non-employment period = Unemployment period + Period as out-of-labor-force

Source : Panel constituted from Economically Active Population Survey database for the period of June 1998 to May 1999.

Table 2.7 shows that daily employees are intensively distributed in firms with less than 10 employees. Among industrial sectors, manufacturing, construction, wholesale and retail trade, and hotel & restaurant are the four dominant sectors with large numbers of daily employees (Table 2.8). In general, where the proportion of temporary employees is important, so is the proportion of daily employees. The construction sector, however, is an exception. In the construction industry the proportion of daily employees is much more important than that of temporary employees.

The distinction between "temporary employee" and "daily employee" in Korea depends on whether employment is scheduled to last more than one

**Table 2.7: Temporary and daily employees by firm size in Korea, December 1999**

Number of employees	All sizes	1-9	10-49	50-299	300-
	('000s)				
Temporary and Daily	6,893 (100.0%)	4,154 (60.3%)	1,938 (28.1%)	603 (8.8%)	198 (2.9%)
Temporary	4,468 (100.0%)	2,565 (57.4%)	1,319 (29.5%)	451 (10.1%)	132 (3.0%)
Daily	2,426 (100.0%)	1,589 (65.5%)	619 (25.5%)	152 (6.3%)	65 (2.7%)

Source : National Statistical Office, Korea, Economically Active Population Survey database.

**Table 2.8: Temporary and daily employees by industry in Korea, December 1999**

	Temporary and daily employees		Temporary employees		Daily employees
	(persons)				
Whole industry	6,893,371	(100.0%)	4,467,646	(100.0%)	2,425,725 (100.0%)
Agriculture, hunting and forestry	100,981	(1.5%)	12,285	(0.3%)	88,696 (3.7%)
Fishing	30,076	(0.4%)	17,500	(0.4%)	12,576 (0.5%)
Mining	3,075	(0.0%)	1,550	(0.0%)	1,525 (0.1%)
Manufacturing	1,547,494	(22.4%)	1,045,992	(23.4%)	501,502 (20.7%)
Electricity, gas and water supply	17,744	(0.3%)	11,374	(0.3%)	6,370 (0.3%)
Construction	904,686	(13.1%)	226,975	(5.1%)	677,711 (27.9%)
Wholesale & retail trade, repairing consumer goods	1,247,805	(18.1%)	988,374	(22.1%)	259,431 (10.7%)
Hotel and restaurant	885,063	(12.8%)	563,456	(12.6%)	321,607 (13.3%)
Transport, storage and communications	230,848	(3.3%)	176,259	(3.9%)	54,589 (2.3%)
Bank, insurance and other financial intermediation	268,460	(3.9%)	244,289	(5.5%)	24,171 (1.0%)
Real estate, renting and corporate services	471,640	(6.8%)	390,394	(8.7%)	81,246 (3.3%)
Public administration, defense and compulsory social security	292,205	(4.2%)	86,016	(1.9%)	206,189 (8.5%)
Education	333,816	(4.8%)	293,843	(6.6%)	39,973 (1.6%)
Health and social works	92,618	(1.3%)	82,420	(1.8%)	10,198 (0.4%)
Other community, social and personal services	302,533	(4.4%)	221,002	(4.9%)	81,531 (3.4%)
Private households with employed persons	161,689	(2.3%)	103,279	(2.3%)	58,410 (2.4%)
Extra-territorial organization and bodies	2,638	(0.0%)	2,638	(0.1%)	0 (0.0%)

Source: National Statistical Office, Korea. *Economically Active Population Survey* database.

month ("temporary") or less than one month ("daily").<sup>4</sup> For policy purposes, the distinction between temporary and daily employees is not important, as both are largely unprotected in the labor market. For this reason, it is often more convenient to integrate them into one labor market category.<sup>5</sup>

<sup>4</sup> For more details, see Box 2. 1.

<sup>5</sup> In this paper, we will use the term non-regular employees in the same meaning as temporary & daily employees.

## Box 2. 1: Classification of employees by status

It is a common tradition in the analysis of the Korean labor market that employees are classified into three categories: regular employees, temporary employees and daily employees. Statistically, regular employees are defined for operational purposes as employees whose employment contract spans, implicitly or explicitly, more than a year or is without any fixed term. Temporary employees are defined as employees who have an employment contract lasting between a month and a year. Daily employees are those employees whose contract period is less than a month.

In reality, however, the usage of those terms has nuances other than just demarcation by contract period. Temporary employees can be fixed term contract workers or project based employees. It is not rare that their employment period exceeds one year or is without any fixed term; as is the case with most of part-time employees and dispatched employees. They are highly substitutable with other workers as their jobs do not require professional skills. Employers can freely dismiss them without offering any severance pay. The employer, regardless of regulations in law, does not contribute a social insurance premium for them as their wage is considered to be inclusive of severance pay, social insurance premium, etc. In many cases, the employer does not keep their employment records so they cannot prove their employment career. Temporary employees are, in the usual sense, equivalent to atypical or non-regular employees.

Daily employees in practical usage can be understood as a subset of temporary employees. They are paid on a daily basis and their employment spans a well-defined project. The employment contract is terminated automatically when the project is completed, even if they remain under the same employer or *Shipjang*.<sup>6</sup> They frequently move from one work place to another. Sometimes it is hard to distinguish them from the self-employed. They conclude a contract as an independent contractor as if they are a self-employed when they have opportunity of getting independent jobs, such as repairing or petty construction.

Regular employees are those whose employment contract period is not fixed. Their employment is stable. Their wage increases on the basis of seniority and they have a predictable promotion path. They fully enjoy the social insurance advantage as regulated by law.

The National Statistics Office takes into consideration these common sense meanings during surveys. When it is difficult to distinguish if an employee is regular or temporary, whether or not he/she is expected to receive severance pay serves as an important criterion during the survey. If an employee is not expected to receive retirement pay from the employer, even if the employment contract is without fixed term, he/she is classified as a temporary employee. If an employee is paid on daily basis and his/her employment contract is terminated automatically when the project is completed, he/she is classified as a daily employee even when he/she is expected to work more than a month in a workplace.

<sup>6</sup> *Shipjang* is an informal organizer of the manpower pool in *the* construction industry. He is not an officially permitted employer or business owner but concludes a contract with the construction company as an independent contractor to perform a process of construction. Traditionally, any experienced worker who is able to organize a group of craftsmen and workers in the construction industry has played a role as a *Shipjang* when he finds a small construction project.

Under the present law, employers are expected to submit an affiliation form to the EI administration of those employees who have worked at least one month. An indispensable condition for affiliating an employee to the EI is that the employers should declare him/her to the EI administration. In the non-regular employees' market where labor turnover is frequent, many employers do not declare their employees due to the exclusion rule of employment for "less than a month". Employers' negligence is not checked afterwards either by employees' claim or inspection by the EI administration. Table 2.9 shows that, between August 1998 and July 1999, 78.2% of daily employees worked more than a month in the same workplace, and 60.1% of them worked more than 6 months as wage workers. But declared daily employees are rare. For example, in the construction industry, the average number of declared daily employees is 3.6 persons per site (Hur and Shim, 1999).

**Table 2.9: Tenure and employed period by employment status in Korea, August 1998 to July 1999**

Months	Tenure period (%)				Employed period (%)			
	Regular employees	Temporary employees	Daily employees	Total	Regular employees	Temporary employees	Daily employees	Total
1	1.9	9.4	21.8	8.0	0.3	2.3	6.4	2.1
2	4.5	12.0	15.8	9.0	0.5	3.0	5.7	2.2
3	1.8	5.2	10.9	4.6	0.5	2.9	6.5	2.4
4	1.8	5.0	12.0	4.8	0.5	3.3	6.8	2.6
5	2.0	6.8	10.6	5.1	1.0	4.3	7.8	3.3
6	1.4	3.2	3.3	2.4	0.8	3.2	6.9	2.7
7	1.9	4.7	4.1	3.2	0.7	3.7	6.1	2.7
8	2.0	4.7	2.6	3.0	0.9	4.1	6.9	3.1
9	2.0	4.0	1.9	2.6	1.2	5.0	8.0	3.7
10	2.1	3.6	2.3	2.6	1.4	6.3	8.1	4.2
11	2.4	4.3	2.9	3.1	2.3	7.6	7.9	5.0
12	76.3	37.1	11.9	51.6	90.0	54.5	23.1	66.0
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Note: The employed period is the period during which the workers were employed as wage and salary workers.

Source: Panel constituted from Economically Active Population Survey database for the period of August 1998 to July 1999. Cited from Hwang (2000).

The duty of declaration is left only to employers and non-regular employees remain without any employment certificate. It is usual in the Korean labor market that employees, whether they are regular or non-regular, move from one workplace to another without any employment certificate or



reference. Employees are not accustomed to asking for an employment certificate when they leave a workplace. Non-regular employees lie, in general, outside of the employers' personnel management system. Those non-regular employees who did not request affiliation do not think of retroactive affiliation afterwards, either because they do not have any employment certificate or because they think of it as irksome task.

Non-regular employees who want to be covered by UIS have to request affiliation to the UIS during their tenure at the workplace. However, these employees do not know about the details of the EI regulations, such as who is excluded from affiliation and who has to be declared. If they do know, they do not have much incentive to request affiliation to an employer as they can hardly satisfy the eligibility condition. This is because on the one hand employers do not declare them properly, and on the other hand they are not entitled to UIS if they work less than a month in a given workplace. Therefore, even if they are affiliated in one workplace it will be practically impossible for them to satisfy the eligibility condition for UI as many work days are not registered in the EI database.

Employers have not felt any obligation to keep employment records, and therefore the EI administration is not capable of judging if an employee in a firm has worked more than a month or not. As a matter of fact, this is one of the reasons why the non-regular employees' market has been, implicitly or explicitly, considered to be an informal sector and the labor administration has until recently placed them outside of the policy area.

Therefore, the remedy for improving the low coverage of employees is to establish an employment reporting system. Such a system will also resolve the irony that the most suffering group is now excluded from the UIS.

### *Informal Employment Relations: the Case of the Construction Industry*

After the financial crisis in Nov. 1997, when how to protect non-regular employees became a critical issue, the term used in the debate was not 'non-regular employees' but 'daily employees'. The reason is that the most conspicuous landmark group who needed a safety net was considered to be former daily employees, in particular those who worked in the construction industry. Diagnosing the possibility and proposing a possible way of covering construction daily employees was the most pressing issue for the UIS in Korea. Therefore, it seems reasonable to concentrate our discussion around the construction daily employees' market.'

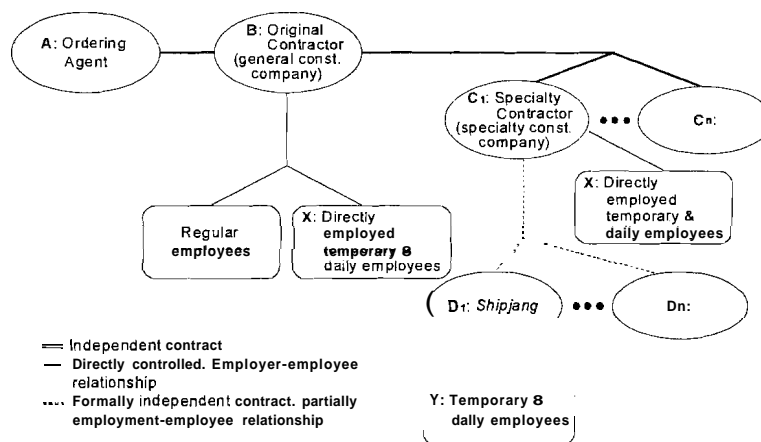
The main obstacle for covering daily employees in Korea's social insurance system is that there does not exist any employment career

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<sup>7</sup> Even if we substitute 'daily employees' with 'non-regular employees', it does not make any difference in the following discussion. The terminology 'daily employees' can be substituted in many places with 'temporary & daily employees' or 'non-regular employees'.

certifying mechanism for daily employees in markets such as construction. Construction daily employees are difficult to cover under an employment insurance system for two reasons. They are hired on a daily basis, generally for cash, and their employers are not accustomed to keeping records. Many of them are employed under vague employment relationships. Employees employed by *Shipjangs* in construction are examples of this category of workers. Figure 2. 1 shows in a simplified form how these *Shipjangs* fit into the employment structure in the construction industry. *Shipjangs* have not had legal status and their identity is unstable. Thus, construction daily employees have not been able to prove their work experience, while regular employees could provide their employment record when it was necessary by submitting the 'employment certificate' issued by the employer.

Figure 2.1: Structure of construction labor



Together with the above reasons, UI coverage of daily workers in the construction industry, where most workers are non-regular, has been hindered by the UIS's current exclusion rule. Many regulations of the current UIS are regular-employee-oriented. According to the current rules, employers are expected to submit an affiliation form within 14 days when they employ workers and also hand in a disaffiliation form within 14 days when their employees quit. Employers don't have to declare to the insurance administration those employees who have worked less than a month.

In the construction industry where labor turnover is frequent and where the predominant number of employees are non-regular, many employers have not declared their employees due to the exclusion rule. A large number of workers come into and out of a construction site following construction process. Many specialty contractor employers who maintain a traditional

management style and share informality with the *Shipjang* have not conformed to the regulations. Frequent employee turnover and employment relation via *Shipjangs* have meant that labor administration control has been difficult.

**Box 2.2:** Some informal characteristics of the daily employees' market

- It is hard to distinguish the employer-employment relationship from an independent contract to the extent that employment is extremely unstable. Daily employees are freely dismissed by simple notice or the employment contract ends automatically when an ongoing project is completed. Not only employers but also daily employees tend to take this for granted.
- Dealing in cash is universal between employees and employers. They do not conclude contracts with written documents. They think that requesting any written contract is a sign of distrust and dishonor.
- Employees think that the cost of litigation is very high (including indirect and implicit costs such as reputation damage, lost time, mental damage, etc.), or that the expected return for litigation is very small.
- People can violate regulations just out of sympathy without any deep consideration about legal responsibility. Many do not distinguish redundant regulations from necessary ones and tend to reject regulations as a whole. Cheating or the false declaration of employment information is, thus, possible and its probability is not negligible.
- Most of employees' time preference rate is so high that they count much present income and count little future income. They prefer not to contribute premiums even if the expected rate of return from their contribution is higher than the market return. Neglect of social insurance such as National Pension and Employment Insurance can prevail because of the high rate of time preference.
- There are still many people of traditional mind who do not have any idea that government can run a contribution-based cash benefit program for them. Therefore, employers' negligence, active or passive, of their duty is not rare and employees fail to ask of the requirements of social insurance.

Non-regular employees have been beyond the scope of the employers' personnel management. Thus, it has not been possible for a non-regular employee who has resigned to request an employment certificate. And, if it is not impossible, there are many daily employees who think that it is a irksome task to request and accumulate employment records for the future possibility of receiving unemployment benefits, given those restrictions on eligibility and low probability of proper record-keeping in most of workplaces.

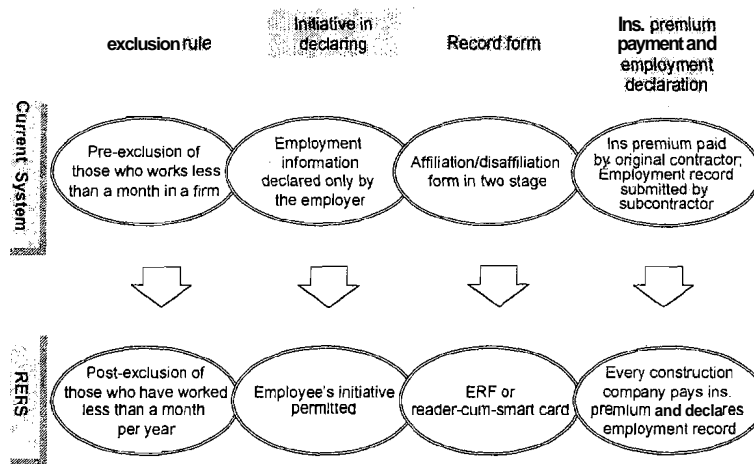
If Korea can find any reasonable way of enhancing the coverage of the UIS for non-regular employees in construction, such a system can be extended without too many difficulties to non-regular employees in other industries.

### Proposal for a Refined Employment Record-keeping System (RERS)

Under the current EI administration process the local labor office collects insurance premiums from the original contractors. They are responsible for paying the insurance premium for the whole workforce involved in the construction project. They submit affiliation/disaffiliation forms when they employ/layoff an employee. Specialty contractor companies are expected to submit affiliation/disaffiliation forms to the labor office and to transmit the withheld insurance premium to the original contractor company. But this process is not undertaken in actuality and neither do temporary & daily employees pay the insurance premium contribution.

Four aspects of the current system can be improved upon. These are summarized in Figure 2.2.

Figure 2.2: Four important aspects of the RERS



#### Exclusion

Every employee should be affiliated as soon as he starts to work and the exclusion should be judged by the EI administration after a certain period of time. Thus, employees who work less than a month in a firm should be declared.

According to the current rule, employers don't have to declare to the EI administration those employees who have worked less than a month. Employees working less than a month in a firm are excluded from coverage.

The EI administration, however, is not capable of judging whether a daily employee at a workplace has worked more than a month or not and construction companies declare only a few of temporary or daily workers at their discretion. The consequence is the average number of declared daily employees is 3.6 persons per site.

The pre-exclusion rule has in fact been adopted for the accommodation of the labor administration. The labor administration has considered that exclusion ex post is too costly. However, this rule encourages the moral hazard of construction companies in declaring employment information to the EI administration.

Naturally a plausible idea to improve the low coverage of the EIS is to apply the exclusion rule differently from the way it is now. Every employee except for self-evident cases (for example, part-time student workers) should be, in principle, affiliated as soon as he starts to work and the exclusion should be judged by the EI administration after a certain period of time, for example one year after. If the total number of days worked by an employee is less than one month during a year, the insurance premium shall be paid back to the employer and the employee.

#### Declaring Work Records

At present, maintaining work records is the responsibility of the employer only. Another modification necessary in the current EI administration is to encourage employees to declare when work has been performed.

In general, in the Korean labor market employees move among workplaces without any employment certificate. Naturally, employees are not accustomed to asking for an employment certificate when they leave a workplace. As for non-regular employees, no records are left in the firm. Non-regular employees, therefore, have to be able to request affiliation to the UIS during their tenure at a workplace or, at the latest, at the moment of quitting. Thus, it is desirable that employees have work records when they leave a workplace.

#### Affiliation and Disaffiliation Records

The EI administration should allow employers to declare employment information for short-term contract workers in a simpler way than now.

According to the current rule, employers are expected to submit an affiliation form within 14 days of the day when they employ a worker and also hand in disaffiliation form within 14 days of the time when their employees quit. The firms' paper workload (in particular, that of small business firms) is not negligible in employee administration due to frequent employment turnover. As a matter of fact even now there are many firms submitting affiliation/disaffiliation form far later than 14 days after the recruit/quit period, respectively.

The labor administration can introduce an Employment Record Form (ERF) so that employers can declare at one time and, if possible, instantaneously short-term contract employees. An ERF is a written form for employment record keeping and declaration for employers who employ workers where there is a high turnover rate, such as in the case of daily employees. An ERF is composed of two parts: one part is written at the beginning of the employment contract and a duplicate is given to the employee. The other part is filled in at the end of employment contract.

The first part of ERF delivered at the beginning of employment substitutes for an employment contract and eases inspection as inspectors check whether or not a daily employee and the employer have filled in the ERF. An ERF is composed of 3 sheets. Those three sheets are shared among the employer, employee and EI administration. Employers complete the reporting process by sending a sheet to the EI office. Employers have the responsibility for keeping the record for a certain period, for example 3 years.

In sum, when an employee starts working, the employer writes the basic conditions of their contract such as the daily wage. When the job is terminated, the employer and the employee fill in an ERF and submit a copy to the labor office. The information written on the sheet is put into the database of the EI office.

Employers could save on paper work by instantaneously declaring employees' record at one time while employees could declare their own employment information on their own initiative. The declaration process could be further simplified by using tools such as a reader-cum-card in order that employers' instantaneous declaration can be possible and the initiative of employees can be systematic.

#### Construction Company's Responsibility

The responsibility of paying the insurance premium and submitting the affiliation/disaffiliation form (under the RERS, it will be ERF) for employees should be given to each company.

At the moment the responsibility for paying the insurance premium for employees is imposed on the original contractors, while the specialty contractor companies have to submit affiliation/disaffiliation forms to the labor office. Specialty contractors may as well pay the insurance premium when reporting their employees.

As for Y-type employees (in Figure 2.1), the responsibility for their affiliation should be imposed on the specialty contractor companies. Specialty contractors can claim that Shipjangs conclude independent contracts with them and that the labor administration should request the employment information of Y-type employees to Shipjangs. But as the Shipjang is an informal employer and *Shipjang*-ship is unstable, it seems reasonable for the labor administration to impose on specialty contractor companies the duty of declaring the employment information for the

## EXPANDING THE COVERAGE OF KOREA'S UI

workers employed by Shipjangs.

### ***Eligibility, Benefit Duration and Other Aspects of the RERS***

The EI, as well as other social insurance systems, can run properly only with a proper employment record-keeping system. Social insurance systems such as Industrial Accident Compensation Insurance can be run simply with employment records. The application of the EI, however, requires some rules in the Employment Insurance Act such as an eligibility condition, criteria for the approval of unemployment, etc. Thus, apart from the record-keeping system, the question of how non-regular workers would be covered by an expanded UI system should be discussed. In principle, it will be desirable for the EI administration to have a single rule that applies to all worker types rather than multiple rules applying to different categories of workers. Finally there are other aspects of the RERS to be discussed.

#### Benefit Eligibility and Benefit Duration

For how long would daily employees have to pay into the system before becoming eligible for benefits? The same rule can be adopted as is applied to other employees. The benefit claimant has to be insured for at least 180 days over last 18 months. For how long could they collect benefits? The same existing benefit duration matrix can be applied to daily employees. The benefit duration ranges from 90 days to 240 days, depending upon the claimant's age and insured employment period.

However, another important aspect should be discussed because daily employees frequently go through a sequence of employment and unemployment spells.<sup>8</sup> It will be important for the EI administration to carefully set rules determining when daily employees are entitled to UI benefits. It does not seem to be consistent with the purpose of the UI to pay unemployment benefits during a short spell of unemployment. In fact, the spirit of the waiting period rule is to prevent the payment, and thus the abuse, of benefits during a short spell of unemployment. The livelihood of the daily employees will not be threatened during a few days of bad weather or during the short interval when daily employees move from one construction site to another.

Some have asserted that the system can be easily abused and the expenditure can be excessive if daily employees are entitled to UI as daily employees frequently repeat employment and unemployment spells. Another difficulty arises from frequent turnover. During the benefit duration after a daily employee started to receive UB, he can soon find a job and can be unemployed again after several days. The rules determining eligibility have to be matched with the contribution formulas so that daily workers do

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<sup>8</sup> According to the Table 2.9, 74.4% of daily employees work less than 6 months and 21.8% of them work less than a month in a workplace.

not become an unreasonable drain on the UI system.

One possible way of coping with this problem is taking fuller advantage of the job search reporting process. According to the current regulations a beneficiary must report every two weeks his/her job search activities. The EI administration can prove a daily worker is unemployed if he/she worked, for example, less than 7 days and apply a sliding scale benefit rule following the number of days worked during the previous two weeks. Someone who has worked equal to or more than 7 days out of two weeks will be regarded as employed.

#### Excessive Benefit Frequency

When would they become eligible for benefits a second time? This raises a second issue. As is shown in the Table 2.6, yearly employment span of non-regular employees ranges from 8.3 to 10.1 months a year.

One simple way is imposing the same eligibility condition on claimants independently of their frequency of benefit collection. As can be expected from the employment span of non-regular employees, many of them can then claim unemployment benefits every year. To prevent excessive benefit claims, an experience rating can be introduced. Or alternatively, the EI administration can put a certain limit on the total length of the benefit span during a certain period (for example, during 3 years). Those unemployed daily workers who are not eligible for UB will be able to participate in the Public Works Program.

#### Smart Cards

When the RERS is launched, it would be an ideal opportunity to introduce Smart Cards. All of the processes done by the ERF can be done with reader-cum-card system. The EI administration can distribute mobile card readers to construction companies and Smart Cards to daily employees. At the moment of quitting, or everyday a worker comes to the construction site, he/she inserts his/her card into the reader and records their employment information. This would enable the EI administration to track employment records person by person.

Smart Cards are small cards like credit cards or bank automatic teller machine cards that are embedded with computer chips on which information can be stored. These are used, for example, throughout France as debit cards and throughout much of Europe as telephone cards, where they complement and more often replace coin telephones.

Recording employment information and making wage payments to employees by Smart Card would have a number of advantages. It would get Korean workers accustomed to dealing with Smart Cards. Workers would not be eligible for unemployment benefits unless they could prove through their electronic accounts that contributions had been made and that the



maximum benefit period had not been exceeded. It would ensure that workers who receive unemployment benefits would not simultaneously receive benefits under other programs such as the Basic Livelihood Protection program, which will be implemented from Oct. 2000.

#### The Importance of Withholding Tax

Many have said that the RERS will not function at all because of 'informal' behavior of economic agents in the construction market. If the process is to work, at least either employers or employees should try to conform to the regulations. However, according to them, not only employers but also daily employees will not declare their employment information. Employers will resist by negligence. Daily employees will not be interested in UB at all as the benefit is too trivial and they may run the risk of paying income tax, etc. This implies that the tax administration should cooperate with the EI administration when the ERF is introduced.

Construction employers should withhold the income tax of daily employees to pay it directly to the tax office, while daily employees should properly settle the accounts of their annual income by a declaration process once a year. This directive has been impossible to impose because of false declarations are made possible by implicit or explicit collusion of employers and employees.

The RERS proposed above can provide a monitoring device for the tax administration. Conversely the tax administration can help the smooth and efficient settlement of the RERS by applying general income tax regulations to daily employees. In this way employers will be induced to be faithful to employment record-keeping and daily employees will be interested in their record-keeping.

#### Not Reporting Work

One advantage of the proposed system is that it can prevent frauds: daily workers who have become unemployed becoming eligible to collect UI benefits, but then surreptitiously returning to work.

However, it will not be difficult to work without declaration at least before the RERS is completely settled because of the informalities of the construction labor market. Daily employees can be tempted to receive UB when it is possible to work without declaration. One way of preventing frauds is to operate inspection-cum-penalty rule so that the expected income of a false claim is negative. But, for the moment it is not certain to what extent this can be prevented by the inspection system.

#### The Advantage of the RERS for Other Social Programs

Covering construction daily employees with the EI is a kind of bridgehead

for other social insurance systems such as the National Health Insurance (NHI) and the National Pension (NP). If construction daily employees are not covered by EI, the NHI and the NP will not be able to protect them as wage workers either. The RERS can serve not only the EIS but also other social insurance systems as well.

## **Principal Recommendations**

In this paper, we have identified one of major problems with Korea's unemployment insurance system. Despite the expansion in October 1998 to all firms, coverage remains quite incomplete. The compliance rate is low and the UIS covers only 65% of the employees who are supposed to be covered. The gap in coverage is mainly due to temporary and daily workers. The main obstacle to covering temporary and daily workers with the UIS is that there does not exist any employment career certifying mechanism for them. In order to overcome this, we have suggested a new Refined Employment Record-keeping System (RERS). Four aspects of the current system can be improved upon.

- Under current law, employers have to declare those employees having worked more than a month in their establishment. We recommend that every employee except for self-evident cases (for example, part-time student workers) should be, in principle, affiliated as soon as he/she starts to work and the exclusion should be judged by the EI administration after a certain period of time, for example one year after. If the total number of days worked by an employee is less than one month during a year, the insurance premium shall be paid back to the employer and the employee.
- At present, maintaining work records is the responsibility of the employer only. It is desirable to encourage employees to keep and declare their employment records before their employment contract ends. Temporary and daily employees may not be interested in declaring their employment information and receiving UB at all as the benefit is trivial and they may run the risk of paying income tax. This implies that the tax administration should cooperate with the EI administration by applying general income tax regulations to temporary and daily employees.
- In order to allow employees to maintain their work records and employers to declare the employment information of short-term contract workers in a simpler way than now, we suggest that the labor administration introduce an Employment Record Form (ERF) or Smart Cards.
- Specialty contractors may as well pay the insurance premium when reporting their employees so that daily workers in the construction

industry are correctly declared to the labor office. Declared workers should include those workers employed by Shipjangs.

The proposed RERS will make it possible to extend EIS coverage to temporary and daily workers, which would make major contributions to Korea's UIS. It will provide substantial benefits to the most disadvantaged group in the labor market who face serious risks of unemployment and are not now covered by the EIS.

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# **3 The Potential Role of an Employment Guarantee Scheme in Korea's Social Safety Net\***

**Gary S. Fields\*\***

## **The Current Employment Insurance System**

Beginning in November 1997, the Republic of Korea underwent a devastating economic crisis. Declining macroeconomic conditions brought about major labor market disruptions in 1998: a quadrupling of unemployment, a fall of 9% in real wages, informalization of the remaining jobs, increased job insecurity, and rising poverty and inequality. Disadvantaged groups suffered a disproportionate impact. The result was not only economic misery but also social pain: increased homelessness, rising crime, heightened school dropouts, an accelerating divorce rate, and an overwhelming sense of social malaise.

1999 marked a major turnaround for Korea. GDP grew by 10.7%, and real wages are growing apace. The unemployment rate is now less than half of its peak level. Women are again returning to the labor force and are finding employment. A sense of guarded optimism is returning to the Korean society.

Nonetheless, important labor market problems remain (and social problems as well). The unemployment rate now is twice as high as it was before the crisis. But high unemployment is the tip of the proverbial iceberg. Income inequality is 15% higher and poverty is twice as high as before.

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\* This report is part of a larger study looking at Korea's social safety net and ways of improving it. One component of that larger study is an assessment of how the unemployment insurance (UI) component of the nation's Employment Insurance System (EIS) should be redesigned or supplemented. Official recommendations are contained in a Korea Labor Institute report "Supplementing Korea's Unemployment Insurance System." What follows are additional recommendations reflecting my own personal views and not those of KLI or any other institution.

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What Korea has is not just an "unemployment problem" but a more general "employment problem." (Fields, 1999) The unemployed are not the only ones who are suffering. Those who lost jobs and have become re-employed in less good ones; those who have kept their old jobs and whose real earnings have declined; those who are employed as daily workers and temporary workers and who have fewer work days than before; and those who face precarious employment and earnings prospects – all these are part of Korea's employment problem too.

Before the crisis, Korea had put into place an ambitious employment insurance system (EIS). The three components of this system are traditional unemployment insurance (UI), job training, and a job information service. Other elements of Korea's social safety net system include a Livelihood Protection Program for the poor, a Life Stabilization Fund for those unemployed whose assets fall below a certain level, public works jobs for the unemployed and for the spouses of low-wage workers, employment maintenance subsidies, support for venture enterprises, and many other smaller programs.

Despite all that Korea has done, the nation's social protection system still has more holes than net. In 1999, there were 35.8 million Koreans aged 15 and over. The average number of unemployed in any given month was 1.4 million. Yet, in a typical month, just 0.1 million received unemployment benefits and 0.3 million participated in public works programs. 1.7 million Koreans received Livelihood Protection benefits at some time during 1999. Taken together, about 0.5 million unemployed had been covered by those assistance programs.

It is important to be clear about the risk being faced. Unemployment insurance in Korea, as elsewhere, protects against the risk of income loss because of unemployment. To date, the system has protected against the risk of losing all of one's income because of the complete loss of job. The EIS provides people with a temporary income after they have been completely unemployed for two weeks. The broader risk, not yet covered in Korea, is unemployment because of a less-than-full work week. UI is not intended to be an income supplementation program for people who are working but earning little; rather, it provides those who are not working with a temporary income while they are searching for employment. Thus, the millions of Koreans who have suffered income losses while remaining in a job are excluded from the EIS. Economic growth and other programs are needed to take care of their problems.

It is also important to adopt a guiding framework for the EIS. One possible model is social insurance. Under this model, in so far as possible, everyone in society pays in and all of the insured who become unemployed can collect. Under the social insurance model, benefits are limited only by the overall financial solvency of the system.

A second model is the private account model. Private accounts can be publicly-run or publicly-mandated. In either case, the individual has his or

her own account. In the event of unemployment, the account balance can be drawn down to provide an income to the unemployed. Otherwise, the money belongs to the individual, to be used in some other way, e.g., for old age spending, home-buying, or medical expenses. Under this model, UI is a type of compulsory savings with self-insurance against unemployment.

The third model is social assistance. Here, the nation taxes itself in order to provide benefits for the needy members of society. Under this model, benefits are means-tested – that is, beneficiaries must prove not just that they are unemployed but that they are poor in order to collect UI benefits.

Korea's system has been set up on the social insurance model. I recommend that this model be continued.

The next question is: Keeping the social insurance framework, what are the issues in providing the best unemployment insurance possible for Korea at the present time? Three concerns are central.

The first is incomplete coverage. Only half of wage workers are insured by the UIS. 60% of employed people are wage workers. Therefore, only about 30% of working Koreans are insured by UIS. The first issue, then, is how to expand coverage so that more Koreans are insured against income losses due to unemployment. The paper prepared for this conference by Dr. Hur (2000) details a plan for doing this.

The second concern is inadequacy of benefits. The problem is that in Korea, UI benefits replace only a fraction of workers' prior earnings, and the benefit duration is shorter than the typical spell of unemployment. The issue, then, is how to redesign the benefit formulas in order to provide better social insurance. The KLI report already mentioned (Korea Labor Institute, 2000) recommends doing this by extending the maximum benefit duration to 49 weeks.

The third concern is weaving a social safety net. The problem is that the employment insurance system, the livelihood protection program, and the other programs in Korea, taken together, still leave major gaps. Gaping holes would remain even if the Refined Employment Record-Keeping System recommended by Dr. Hur were to be enacted, permitting UI benefits to be paid to non-regular workers in the construction sector. Accordingly, the next section of this report proposes that the gaps be filled further by creating an Employment Guarantee Scheme as a second pillar of the unemployment insurance component of the EIS.

Before proceeding, let it be noted that financing is apparently not an issue. KLI studies conclude that the EIS is on sound financial footing, even after the IMF Crisis. Alternative financing arrangements are not likely to be enacted any time soon, and so that issue is not addressed in this report.

## A Proposed Employment Guarantee Scheme for Korea

### *Key Features*

In order for the nation to provide all workers with social insurance against the risk of income loss due to unemployment, I propose a second pillar of the Employment Insurance System. This new pillar is an Employment Guarantee Scheme for Korea (EGS). This new scheme would be a formal part of the EIS and would work alongside traditional unemployment insurance as follows.

As its name implies, an Employment Guarantee Scheme would consist of public works jobs, offered on a daily basis to all who want them. Under this proposal, anybody who is unemployed and wants to receive a day's benefit in exchange for doing a day's work would be eligible for an EGS job. There would be no requirement of having worked previously, no prior contributory period, and no limitation on the duration of benefits. All who are unemployed – including daily workers, temporary workers, new entrants, re-entrants and anybody else who might be interested – would be eligible, with one important exception: because the EGS would be Pillar 2 of the EIS, no worker currently receiving UI benefits under Pillar 1 would be eligible for EGS benefits under Pillar 2.

Under such a scheme, establishing eligibility is not an issue. Doing a day's work would qualify the participant to receive a benefit at the end of the day. In other words, the work performed is itself prima facie evidence that the worker is deserving of benefits.

What would be an appropriate wage to set? International experience has shown that guaranteed jobs cannot be too remunerative, otherwise workers will prefer the EGS jobs over private sector jobs. High EGS wages would result either in a very large and expensive system, or else the employment guarantee feature of the system would have to be sacrificed in order to maintain financial solvency. The solution that has been found to work in other countries is to set the wage for the EGS at below-market-levels – in the case of Korea, the national minimum wage might be an appropriate amount – so that only those who cannot find more attractive jobs elsewhere in the economy would opt for the guaranteed jobs. In this way, the EGS would be self-targeting, so that those with poor market opportunities, and only those people, would participate in the EGS.

The jobs themselves should be designed so that EGS participants will perform socially useful tasks. The work sites would have to be dispersed throughout the country, otherwise the guarantee aspect of the job does not have much meaning. Still, in the best of circumstances, it may be necessary

for workers to have to travel considerable distances in order to get to where the jobs are.

The EGS would replace Korea's current system of public works. Public works were the largest single expenditure item for social protection for the unemployed in Korea in 1999, covering an average of 300,000 participants per month.

The new EGS would differ from the existing public works system in several respects. First, it would be open to everyone except for persons currently receiving UI benefits; the present system, by contrast, has a detailed selection process. Second, it would be a guarantee scheme; the present system is not. Third, jobs would be offered for a period as short as a day; the present system provides continuing, ongoing jobs lasting as long as several months. And finally, the benefits would be below the minimum wage level; the current system pays benefits at or above the minimum wage. (This last feature would have to be carefully explained as a way of enabling the country to afford to offer guaranteed employment on even a daily basis.)

Because the EGS will be a central part of the nation's system of social insurance and will have to be regarded as such, the benefits will need to be paid for by the larger society. Participants would make their contributions in kind by contributing a day's work in exchange for a day's wage, which will have to come from other sources. One possibility would be to levy a tax on "regular" employers; the justification for this would be that is their failure to create full employment that is creating the need for an EGS in the first place. Another possibility is to pay for the benefits out of general revenues, on the grounds that it is society's responsibility to assure earning opportunities to all of its citizens.

### *Lessons from International Experience with Public Works Programs*

As the details are worked out, the Korean authorities will be able to draw on much relevant international experience. Such public works programs to create employment for the poor have been established in the Maharashtra state of India, the principal city of which is Mumbai (formerly Bombay), as well as in Argentina, Bangladesh, Bolivia, Chile, Honduras, Cape Verde, and Botswana.

Lipton (1998) has conducted a thorough review of these programs and recommended the following design features: design employment for low opportunity cost individuals; seek alternatives to direct targeting; use scheme rules and conditions to discriminate for the poor; allow for poor workers' frequent physical difficulties; minimize poor participants' transactions costs; reduce covariate stresses on public works resources; use retailer, employer, and public works competition 'for the poor'; before starting, check that low demand for labor causes poverty; subsidize coverage,



sustainability, and graduation; encourage grassroots pressure groups to improve the scheme; seek complementarities among employment schemes; build up capacity of schemes and workers before works begin; and use performance incentives for officials and participants.

Another source of guidance is the World Bank's forthcoming *World Development Report 2000/2001*, which reaches the following conclusions.

- The wage rate should be determined by the local market wage for unskilled labor, not by the program's budget.
- Using additional eligibility criteria for screening is to be avoided.
- Wage schedules should be gender neutral.
- Labor intensity should be higher than the local norm for similar projects.
- Communities should be involved in project selection to derive maximum benefit from the infrastructure created.
- To maximize risk mitigation effects, the program should be available at all times, expanding automatically during crises, as demand increases.

A final aspect, not touched upon in either of these reviews, is a technological one. When this new system is created, it would be an ideal opportunity to introduce Smart Cards. Smart Cards are small cards like credit cards or bank automatic teller machine cards which are embedded with computer chips that can be written on. These are used, for example, throughout France as debit cards and throughout much of Europe as telephone cards, where they complement and more often replace coin telephones. The bus card used in the Seoul metropolitan area is similar to a Smart Card.

Making EGS payments to Korean workers by Smart Card would have a number of advantages. It would get Korean workers accustomed to dealing with Smart Cards. It would assure that workers who receive benefits under Pillar 2 would not simultaneously receive benefits under Pillar 1 – these benefits would also be paid by Smart Card. It would enable the Ministry of Labor to track usage of EGS jobs person by person. And it would reduce the scope for misappropriation of funds by local EGS administrators.

## **Diagnosis and Principal Recommendations**

In my view, Korea's unemployment insurance system has three major problems. First, despite recent extensions, coverage remains quite incomplete. Second, even if all wage workers were to be brought into the system, a large proportion of Koreans would remain without social protection. And third, the maximum duration of benefits is shorter than the typical spell of unemployment.

This diagnosis leads to three major policy suggestions. First, because temporary and daily workers face serious risks of unemployment and are not now covered by the current UIS, coverage should be extended to this group. In order to be able to do this, a new Refined Employment Record-Keeping System (RERS) has been recommended.

Second, even if the UIS were extended to include temporary and daily workers, there would still be important groups who would be left out of the social protection system. These include some regular workers (government workers and teachers), the self-employed, new entrants and reentrants to the labor force, and those out of the labor force. In order to include those now excluded, it has been recommended that Korea create an Employment Guarantee Scheme (EGS) that offers an assured job to all who wish to work.

And third, because UI benefits do not last long enough to cover a typical spell of unemployment, benefit duration should be extended. It has been estimated that with current financing rates and coverage ratios, the system could afford benefits lasting as long as 49 weeks (Korea Labor Institute, 2000).

However, I would not recommend that benefits be extended to this length for two reasons. First, the EIS needs to protect itself against a serious future adverse shock, such as occurred in the 1997/198 financial crisis. Second, part of the current surplus would be better used, I think, to extend benefits to those who do not now receive them rather than lengthening benefits for those now covered. Accordingly, I recommend that the surplus funds in the EIS be used in part to extend the maximum benefit duration and in part to finance an Employment Guarantee Scheme.

This combination of measures – extension of EIS coverage to temporary and daily workers, a second pillar guaranteeing public works jobs to all who want them, and longer benefit duration for the insured unemployed – would make major contributions to Korea's social insurance system. In addition to providing more substantial benefits to workers now insured who become involuntarily unemployed, the expanded UIS would also cover daily and temporary workers, the self-employed, new entrants and re-entrants to the labor force, and the re-unemployed.

Still left out would be the old, the sick, and the infirm. For them, what is needed is an expanded livelihood protection program, guaranteeing an escape from poverty. Such a program has already been promised for October 2000 and is now being implemented.

If this proposal were enacted, Korea would have a social insurance scheme with three major components: the current unemployment insurance system, extended to cover more wage and salary workers; an employment guarantee scheme for all who are capable of working; and an anti-poverty program for all, whether capable of working or not. The result would be a true social safety net for the first time in Korea's history. This would be a great national achievement.

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# **/// Feasibility of Introducing a Non-contributory Cash Benefits System for the Unemployed in Korea**

**Young-bum Park\***

## **Introduction**

Korea's financial crisis put great strains on employment as Korea underwent a painful structural adjustment. The unemployment rate jumped from 2.1 % in October 1997 to 8.6 % in 1999. This left 1.8 million people without jobs. Korea was not prepared for such a high unemployment.

In order to mitigate the painful social costs of the structural adjustment, the Korean government has built a stronger and durable social safety net. It expanded the coverage of the unemployment insurance scheme to all sizes of establishments and it also increased the benefits amount. Also, temporary public assistance programs have been introduced. Trillions of (millions of US dollars) have been spent to create short-term jobs, mostly through public works projects. Special programs targeting particular groups such as the homeless and various training schemes were provided to the unemployed. However, despite all of the government programs, it turned out that only a small fraction of the unemployed workers actually benefited.

Since mid 1999, economic conditions have improved markedly. For instance, the GDP growth rate recovered to 9.0 % for the 3<sup>rd</sup> quarter of 1999. Also, the unemployment rate fell below 5% beginning in September 1999. This confirms that the primary problem concerning unemployment was deficient aggregate demand (Fields, 1999, p.15). This also proves that the government's position relying more on temporary or supplementary schemes of social safety net during the financial crisis was right (Y.-b. Park, 1999).

However, despite reduced unemployment with improved economic conditions, providing proper social protection for the unemployed is still a

serious policy concern. For instance, the unemployment rate is still twice as high as before the crisis (4.6 % in October 1999 versus 2.1 % in October 1997). The unemployment rate of young workers is still high even though it has been decreasing slowly (13.2 % in December 1999 for 15 to 24 age group). The proportion of the long-term unemployed in the total of unemployed also remains high (19.4 % in September 1999 for those unemployed more than six months). Furthermore, regular jobs decreased to less than 50%. And, inequality of urban household income increased after crisis (the Gini coefficient rose from 0.301 in the 3<sup>rd</sup> quarter of 1999 to 0.322 a year later). An increasing number of people now lives under the poverty (KLI and KIHASA, 1999; D.-s. Hwang *et al.*, 2000).

Recognizing these problems, the government plans to introduce a new social assistance scheme in October 2000. Under the new National Basic Livelihood Guarantee Act, without contributions, unemployed workers will be entitled to cash benefits if they pass means test and work test. This paper studies the feasibility of introducing a non-contributory cash benefits system for the unemployed with special reference to the one put forward by the government under the National Basic Livelihood Guarantee Act. Particularly, this report focuses on the institutional arrangement for accommodating the new scheme. This report also investigates to what extent social protection for the unemployed can be strengthened through reforms of Korea's current unemployment insurance scheme.

## **Current Social Protection Schemes for Unemployed Workers: Contents and Limitations**

### *Coverage of the Social Protection Programs for the Unemployed*

With mounting unemployment, the Korean government continuously expanded the coverage of the unemployment insurance scheme and strengthened the benefits amount. The total amounts of the unemployment insurance allowances increased from 79 billion (US\$ 64,000,000) in 1997 to 850 billion won (US\$ 708,000,000) in 1998, then 1.5 trillion won (US\$ 1,300,000,000) in 1999<sup>1</sup>. With employment improving, the unemployment allowance payment is expected to decrease in 2000. The Korean government has also put increasing resources on livelihood protection programs. Temporary public assistance programs have been introduced. In two years the government expenditures on social assistance more than doubled. Since the new social assistance scheme will be introduced in late 2000, the budget

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<sup>1</sup> The exchange rate of Won with respect to US dollar fluctuated between 900 and 2,000. This paper used 1,200 Won versus one US dollar which was closed to the rate after the Won became more or less stabilized.

of the social assistance of the year 2000 increased. Around 5 trillions of won were spent (and will be) in order to create short-term jobs mostly through public works projects. The government's outlay for the public works of 2000 will decrease more than 50 % since unemployment is on decline<sup>2</sup>. Various kinds of training programs have also been offered for the unemployed<sup>3</sup>.

Despite all the government efforts, however, only a limited number of the unemployed persons turned out to benefit from the government programs.

KIHASA–KLI (1999)<sup>4</sup> showed that only 18.7 % of the unemployed persons benefited from government social protection programs; 16.2 % participated in only one program; 2.3 % received two kinds of benefits; and 0.2 % received three kinds of benefits. A detailed breakdown showed that 7.5 % of the unemployed received unemployment allowances; 7.7 % participated in public works projects; 4.2 % received training for the unemployed; 1.6 % received a loan for the unemployed; and 0.8 % benefited from a temporary public assistance program. Government anti-unemployment measures helped 6.9 % of current wage earners that once experienced unemployment.

The same study also showed that the role played by social support for unemployed households was small. The main sources of their earnings included wage earnings of other household members (54.5 %), savings (33.7 %) and borrowings (21.9 %: 21.9 % (private borrowing) + 2.3 % (government loan)).

D.-s. Hwang *et al.* (2000) which was based on a survey taken from during the second half of 1999 also showed similar results. 22.6 % of the unemployed households benefited from the government anti-unemployment program including job placement services<sup>5</sup>. On the other hand, 16.6 % of the

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<sup>2</sup> The unemployment rate of January 2000 turned out to surpass 5 %. The government is likely to spend more money than it **planned**. In that case, more government budget will be allocated to the public works projects.

<sup>3</sup> Other social protection programs are as follows.

- 1) special public loan for the low-income unemployed;
- 2) agriculture start-up loans for urban people that wish to go to rural areas to start farming;
- 3) provision of lunch to middle and high school students;
- 4) free shelters and meals for the homeless;
- 5) public compensation fund for guaranteeing severance payment and wages of the employees of the bankrupt firms.

The Korea Labor Institute and the Korea Institute of Health and Social Affairs jointly conducted a survey to investigate how the lives of unemployed workers and their families changed after being unemployed and what **they wanted** the government to do. The survey was conducted and analyzed based on households as well as individuals. A total of 4,339 households as well as a total of 5,357 individuals were **surveyed** in depth from September 14, 1998 to October 3, 1998. The **unemployed households** numbered 2,771 with the unemployed persons of 3,230. Meanwhile, the number of **non-unemployed households** turned out to be 1,561. See **KLI** and **KIHASA** (1999) for details.

It includes the job placement services, but excludes the temporary livelihood protection

households that once experienced unemployment since 1988 had help from the government programs.

### *Unemployment insurance scheme as a social safety net*

An insured unemployed worker can claim the job seeking allowance or the employment promotion benefits if he or she meets the eligibility requirements for the benefits.

However, only a small portion of the unemployed workers enjoys access to the unemployment benefits. In June 1999, only 144,773 unemployed persons (10.6 % of the unemployed persons of the labor force survey) received the benefits, while the number of the unemployed workers was 1,356,000.

The limited coverage of Korea's unemployment benefit scheme is attributed to the following factors. First, as of the end of June 1999, only 46.3 % (5,844,018) of the total paid employees is insured. This proportion dropped to 28.3 % if the insured are compared to total employment.

The coverage of Korea's unemployment benefits scheme is limited compared to other countries (OECD, 1991, Table 7.1). Only some countries do not cover established civil servants since generally they do not run risk of redundancy (Austria, Ireland, Japan, Netherlands and Spain). There is also regional and occupational variation in unemployment insurance scheme in some countries (Belgium, Canada, Denmark, Finland, Sweden and United States), which is due to that earlier systems in many countries which were run by unions on a voluntary and commercial basis. However, in Korea, the excluded employment types and/or workers are excluded because the nature of the concerned jobs is temporary or seasonal or it is difficult to obtain correct information on employment record, except civil servants and private school teachers,

The problem of temporary worker, part-time workers and daily workers pose big challenge for policy makers. Their number is not negligible and it has been increasing since the financial crisis took place, as shown above. The exclusion of the daily worker also contributes to not including many temporary workers since the distinction between the daily workers and temporary workers (whose employment contract period is between one month and one year) is often blurred.

Second, small employers often neglect to register at the public employment office and pay their premium. But, the public employment offices find it difficult to enforce the law on small employers.

As of May 31, 1999, 8,342,000 employees in 664,000 establishments were supposed to be covered by the law according to estimations based on a survey data of the National Bureau of Statistics and enterprise data of the National Tax Office (K.-s. Yoo, 1999, p.24). However, only 70 % of the concerned employees in 84 % of the concerned establishments paid the

insurance premiums. As of December 31, 1995, when establishments with more than or equal to 30 employees were required to register, 98 % of the supposed-to-be-covered employees were insured. The Employment Insurance Act is the only labor law applied to all establishments<sup>6</sup>.

Third, all insured workers do not receive the unemployment benefits. The law says that only qualified, insured workers can receive the job-seeking allowance (JSA) that is the main type of unemployment benefits<sup>7</sup>. During the first half of 1999, 1,776,637 insured workers were separated from their jobs. Out of these workers only 30.5 % met the qualification (4), i.e. they were separated against their will (Table 4.1). However, only 189,582 (52.8% of the involuntary separators) applied for the benefits. Many of them (29.1% of the involuntary separators) did not meet the insured period requirement

**Table 4.1: Unemployment benefits claimants in Korea, 1997-1999**

	Disqualified employees from the insurance scheme			Total number (B)	Claimant		B/A <sup>3</sup> (%)
	Total number(A)	Prop I <sup>1</sup> (%)	Prop II <sup>2</sup> (%)		Recognized	Unrecognized	
1/2 1997	730,915	-	-	20,390(100.0%)	20,039(98.3%)	351(1.7%)	2.8
2/2 1997	661,627	14.1	-	30,627(100.0%)	30,273(98.8%)	354(1.2%)	4.6
1/2 1998	1,016,431	32.7	27.2	199,092(100.0%)	197,299(99.1%)	1,793(0.9%)	19.6
2/2 1998	967,257	30.5	28.9	239,373(100.0%)	236,900(99.0%)	2,773(1.0%)	24.8
1/2 1999	1,176,637	30.5	22.1	189,582(100.0%)	187,994(99.2%)	1,588(0.8%)	16.1
Jan. 1999	167,702	36.6	28.4	41,290(100.0%)	41,054(99.4%)	236(0.6%)	24.6
Feb. 1999	132,457	28.1	19.6	33,848(100.0%)	33,601(99.3%)	247(0.7%)	25.6
Mar. 1999	244,850	27.4	18.0	30,924(100.0%)	30,579(98.9%)	327(1.1%)	12.6
April 1999	211,742	29.9	23.0	29,355(100.0%)	29,058(99.0%)	297(1.0%)	13.9
May 1999	192,221	25.6	19.4	28,377(100.0%)	28,102(99.0%)	275(1.0%)	14.8
June 1999	227,665	35.1	23.4	25,788(100.0%)	25,582(99.2%)	206(0.8%)	11.3

Notes: 1) Proportion of the involuntary dismissed

2) Proportion of (the sum of the involuntary dismissed and ones who paid enough insurance premiums to qualify for the unemployment benefits)

3) This ratio needs to be understood with caution. There is a two-week of waiting period and the claimants can choose when they receive the benefits since they can be eligible for the benefits during the next ten months after being unemployed.

Source: Ministry of Labor, Korea (calculated from the unpublished data).

<sup>6</sup> The Labor Standards Act was enacted in 1953, however, most clauses in the law are still applied only to establishments with five or more than employees.

<sup>7</sup> During the first half of 1999, 97.5 % of the unemployment benefits were job-seeking allowance. Employment promotion benefits and sickness benefits constituted the rest.

or some of them found a job before the waiting period (14 days after separation) expired or they did not know of the benefits scheme. As a result, many of the insured separated workers do not received the benefits. During the 1<sup>st</sup> half of 1999, only 16.1 % of the insured separated workers received their benefits<sup>8</sup>. This ratio has dropped substantially since March 1999, reflecting the coverage of the UIS expanded to all sizes of the establishments in October 1998.

Nearly all of the insured unemployed workers who applied for the benefits received the benefits. Which means that the activity test is not rigorously enforced.

Fourth, the duration of JSA varies depending on the insured employment period and the age of the claimant, ranging between a minimum of 90 days and a maximum of 240 days<sup>9</sup>. The average duration of JSA during the first half of 1999 was 118.2 days. It was 98.1 days in 1998. The increased duration of JSA reflects the 60 days' special benefits that was effective from July 15, 1998 to December 31, 1999.

For a majority of the UI beneficiaries, their entitlement period expires without their gaining employment. Among the UI beneficiaries whose unemployment was first recognized during the second half of 1998, only 24.6 % left the UI benefits with a job. Another 7.4 %<sup>10</sup> found a job after the entitlement period expired".

Finally, the rise in the number of daily workers and the high incidence of unemployment among the long-term unemployed and young people are also contributing factors to Korea's limited UI coverage, as discussed above.

### *Social Assistance System for the Unemployed*

Korea has a national social assistance system with clear legal codification (which is implemented under the Livelihood Protection Law) and an unemployed person is eligible for the low-income care if he or she meets certain requirements (Table 4.2).

Since financial crisis took place, a temporary social assistance program has been implemented. Under the temporary scheme, as the assets test requirement has been lowered more low-income people have benefited. In

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<sup>8</sup> This ratio needs to be understood with caution. There is a two-week of waiting period and the claimants can choose when they receive the benefits since they can be eligible for the benefits for the next ten months after being unemployed.

<sup>9</sup> It was a **minimum** of 60 days and a maximum of 210 days until 1999. Since the unemployment insurance benefits scheme was only introduced on July 1, 1995, the actual duration of the JSA is 90 to 180 days until June 30, 2000.

<sup>10</sup> This only included worker who had a job in establishments that were covered by the unemployment insurance scheme.

<sup>11</sup> The insured workers are supposed to claim their benefits within the next ten months (twelve months from April 2000) after their separation from the jobs. Some unemployed workers become not-entitled to benefits with some unclaimed benefits due to this requirement.



1999, a cash livelihood benefit was also given to the low-income care recipients during the winter period and about 50 % of them received the benefits.

Korea's social assistance scheme has been criticized for its limited coverage and/or its inappropriate benefit levels. 1,920,000 people, who are 4.2% of the total population, received social assistance under the livelihood protection scheme in 1999. However, among the livelihood protection program recipients, only 60.4% received the regular protection. This means that only 2.5 % of the total population received a regular social assistance.

In terms of the beneficiary coverage, this ratio is very low compared to some OECD countries (in 1992)<sup>12</sup>. Among the compared 23 countries,

**Table 4.2: Comparison between Livelihood Protection Act and National Basic Livelihood Guarantee Act in Korea**

	Livelihood Protection Act (in 1999)				National Basic Livelihood Guarantee Act
	Home care recipient		LOW-income care recipient		
	Regular	Temporary	Regular	Temporary	
Eligibility criteria	<i>Age etc.</i> Older than 64 or Younger than 18 or Pregnant or Lost ability to work due Illness or accident or People living with those meeting the above criteria and caring them & Assets Less than 28 million won per household & Incomes Less than 23,000 won per month per person & No persons legally responsible for supporting the claimant	Same as the regular one except assets criteria (less than 44 million won per household)	Assets Less than 28 million won per household & Incomes Less than 23,000 won per month per person & No persons legally responsible for supporting the claimant	Same as the regular one except assets criteria (less than 44 million won per household)	Recipient's income appropriation amount should be less than minimum living expenses; Until 2002, the asset and incomes of the livelihood protection scheme will be used.
Type of aids	Livelihood; education; maternity; medical; funeral Regular livelihood aid amounts are larger than temporary one		Education; maternity; medical; self-supporting Cash benefits equivalent to those of 50% of low-income care recipients for six months		Housing aid and emergent payment added
Work test					Yes

<sup>12</sup> Only the Livelihood Aid is considered a cash benefit.

Korea's ratio is ranked almost the bottom with Japan (Eardley *et al.* 1996a; Table 2.6). The coverage of Korea's social assistance is very limited, considering that the livelihood protection scheme is the only public assistance program available to low-income individuals, the national pension is not yet available for most people, and the national medical insurance scheme is also a contribution-based program.

### *Public Works Projects*

The public works scheme is the program on which the government spent the largest amount of money during the high unemployment period of 1998 and 1999. The government spent about 3.8 trillion won (US\$ 3,100,000,000) in two years.

In 1998 and 1999, according to the government estimation a monthly average of 175,000 and 390,000 jobs were created, respectively. Without the public works, the unemployment rate of 1998 and 1999 would have gone up to a maximum of 7.6 % and 8.1 %, respectively<sup>13</sup>.

A survey (J.-h. Lee, 2000) shows that the participants seem to be pleased with the role of the public works as a social safety net. However, public works scheme was not much help for them to get a job. Only 31% answered that the public works helped them to get a job.

On the other hand, the government officials involved with the public works had the negative evaluation about the public works scheme (J.-h. Lee, 2000)<sup>14</sup>. Except for 'helping living of the low-income people', they did not appreciate the contribution that the public works made. They believed that the public works are poorly related to employment opportunities. 90 % of the government officials answered that the public works should be abolished (58.8%) or reduced (29.2%).

### *Training Programs for the Unemployed*

If an unemployed person undergoes a training program offered or authorized by the government, the trainees could have the maximum of 350,000 won (US\$ 292) per month as the allowance. The types of allowance available to the unemployed tell us that the training program for the unemployed has some role as a form of social assistance. Low-income people receive a higher training allowance.

However, B.-h. Lee, (2000) showed that the trainees found the allowances

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<sup>13</sup> We assume that all of the public works were created as planned and all of the participants would had looked for a job without the public works. Thus, these estimated rates are the ones with the possible maximum impact.

<sup>14</sup> The study is based on a sample survey on 585 government officials involved with the administration of the public works scheme. The survey was taken from May 31 to June 5, 1999.

not that helpful for their living. The trainees from the UIS-covered establishments received the monthly average of 228,000 won (US\$ 183) and 45.4 % ('very much' for 8.6%; 'some' for 36.8%) found that the allowances were helpful for their living. On the other hand, the UIS-not-covered trainees received only the monthly average of 58,000 won (US\$ 48) and only 19.6 % ('very much' for 2.8%; 'some' for 16.8%) found that the allowances were helpful for their living.

### **Promoting Social Protection for the Unemployed through Reforms of the Unemployment Insurance Scheme**

The proportion of the unemployed<sup>1</sup> Korean persons who receive the unemployment insurance benefits is about 10% as shown above. This figure is small compared to other OECD countries such as Japan (36% in 1990) or the USA (34% in 1990)(OECD, 1994, Table 8.4)<sup>15</sup>. Like Korea, Japan and the USA have a relatively short duration of unemployment insurance benefits payment and disqualify or postpone the benefits for a long period following a worker voluntarily leaving a job. Consequently, there is need to consider expanding the UIS beneficiaries, through expanding the benefit, or the scope and coverage for which, and to whom, the benefit is paid, as a way to promote the social protection of the unemployed workers.

#### *Expanding the Coverage of the UIS to Daily Workers*

When Korea introduced the UIS, the government excluded some sectors. The government gave the following reasons for the limited coverage of the UIS (Fields, 1993). It was very difficult to collect contributions from small business or some type of workers. And, other social insurance benefits and labor laws also excluded the small business sector. Other countries also introduced the system gradually. It was also argued that the gradual implementation would enable the Korean authorities to learn from the experience.

The Korean government had expanded the system to include firms of all size of firms during the financial crisis. However, some workers are still excluded even though they are those worse-off. It has been argued that daily workers are those who need to be included in the system. The number of daily workers is large and many of them are to some extent those who should be protected, more so than some others who currently received unemployment insurance benefits (J-h. Lee and J.-y. Jang, 1999).

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<sup>15</sup> The low ratios of these countries reflect short duration of unemployment insurance benefits, disqualification or postponement of benefits following voluntary job leaving and limited entitlement to assistance benefits (OECD 1994; 189).

The exclusion of daily workers from the unemployment insurance scheme is closely related to the enforcement problem in the small business sector. 69.3 % of the daily workers are employed in establishments with less than 10 employees. Also, 63.4% of temporary employees work for establishments with less than 10 employees. The distinction between these two types of employment contracts is generally difficult, particularly for the small business sector. Only 20.2 % of the workers in establishments with less than 10 employees have a regular employment status.

There is no doubt that the UIS should be expanded to include daily workers. However, saying that is much easier than implementing it. This is well reflected in that after the UIS was expanded to small firms, a majority of whose workers are temporary, only 70 % of the supposed-to-be-covered workers were actually covered.

Many, including Fields (1993, p.12), have proposed a contribution book system to overcome this administrative difficulty. Under this system, workers are provided with contribution books, into which the employer is required to put stamps indicating that the required UIS contribution has been paid for that particular worker in the particular period.

Currently, the construction industry, more than 50 % of whose employees are daily workers, has a contribution book system for severance payments on construction projects above a certain size. The employers are required to buy stamps equivalent to the wages and employment period of a particular worker and put the stamps on the contribution book of that particular worker. About 6 % of the daily workers in construction are covered by this scheme (H. Kim and K.-b. Shim, 1999).

However, this contribution book system does not work well. The employers who are required to buy stamps are different from the ones who actually employ workers. In construction, the primary contractors hire subcontractors and the subcontractors at the bottom of the subcontracting chain are unauthorized small enterprises, actually employ the workers. Contribution books are not properly managed on an individual worker basis since the primary contractors usually give stamps to the subcontractors and the stamps are traded as a commodity in a sort of black market. The introduction of a contribution book system for the purpose of the UIS is expected to face a similar problem.

Instead, J.-j. Hur and K.-b. Shim (1999) strongly argued for the introduction of a centralized employment-record keeping system. When employers hire and dismiss a daily worker, they are required to submit an employment certificate for that particular employee to the employment authorities. Under this system, basic subcontractors have the responsibility of reporting the employment certificate. However, this system will also encounter enforcement problem due to the primary-sub contract structure of the construction industry. In addition, practically this employment-record keeping system is only applicable to daily workers whose employment with

an employer is longer than a certain period, i.e., to the ones who have a sort of guaranteed employment period as seen in construction.

Hiring practices of many daily workers is another problem encountered in the inclusion of the daily workers. Many daily workers get a job through private employment agencies. These private employment agencies often give advance payment to the daily workers who want to be paid on a daily basis, while employers still want to pay daily workers on a weekly basis (J.-h. Kuem, 1999). Under this circumstance, it is even more difficult to collect insurance contribution from employees as well as employers.

The current income tax system also poses a problem. Employers do not have to collect income taxes if the daily employee's wages are less than 50,000 won (US\$ 42) per day. This also contributes to the authorities' having difficulties in collecting information on the daily workers' true incomes. Consequently:

There is no doubt that daily workers should be covered by the UIS. However, it is difficult to introduce an appropriate system under the current circumstances. Alternative means for strengthening social protection of the daily workers should be introduced.

#### *Including Family Workers or Small Employers under the UIS*

In 1999, employers and family workers constituted 28.8% and 9.5 % of total employment, respectively. Expanding the UIS coverage to these workers may be one way to boost their social protection.

In Korea, it is well known that small employers do not report true incomes in order to evade taxes. Even medical doctors and lawyers do not reveal their true incomes. This is reflected in the harsh criticism government encountered when it expanded the coverage of the National Pension scheme in 1999, since the government did not have correct information on the incomes of the better-off small employers. If the UIS is expanded to include the employers and family workers, many of the worse-off employees will subsidize the small number of the better-off small employers. Therefore, these workers should not be included.

However, this does not mean that there is no need for the social protection for the small employers and/or family workers. On the contrary, they are more like to belong to the poverty group, which will be discussed. Concurrently:

The coverage of UIS should not be expanded to cover the small employers and/or family workers

#### *Entitlement Conditions for the Unemployment Benefits*

Basically, the insured unemployed worker should meet the following three conditions in order to be eligible for the benefits. (1) That person should look for a job actively and be available for the job. (2) He or she should pay

the insurance contribution for a certain period. (3) And, he or she should be separated with neither by the person's own will nor by his or her own fault. The first entitlement condition is rarely applied in Korea. The second condition was recently relaxed. Therefore, the issue is whether voluntary job quitters should be provided with unemployment benefits.

During the 1<sup>st</sup> half of 1999, 34.0 % of the insured separated workers who paid enough contributions for qualifying for the benefits were deprived of the benefits due to the nature of their job termination reasons. We do not know what proportion of the separated workers were those unemployed. Around 11% of the qualified insured workers who became voluntarily separated from their jobs during the first half of 1999 became economically inactive (due to studies, marriage, housework or military service). If unemployment benefits were paid to voluntary job quitters, a substantial portion of the unemployed workers would be entitled to the benefits.

Considering the expansion of the UIS coverage has limitations, especially concerning daily workers, voluntary job quitters should be provided with unemployment benefits. Korea is one of the few countries that disqualify voluntary job quitters completely from receiving unemployment insurance benefits (OECD, 1994, Table 7.5).

On the other hand, with the relaxed entitlement conditions, the unemployment duration is expected to be longer. Empirical evidence of other countries generally confirms the positive relationship between the generosity of benefits, in terms of level and eligibility, to the length of period unemployed although this effect is not always large (Tzannatos and Roddis, 1998, p.3). A Korean study (H.-m. Pang, D.-u. Kim and Y.-s. Ha, 1999) also revealed that unemployment insurance benefits had the adverse effect on the reemployment of unemployed workers. Then, there is a need to develop active labor market programs to reduce the possible adverse effects of the relaxed entitlement condition. Concurrently:

The complete disqualification of voluntary job quitters is too harsh compared to the international standards. Moreover, relaxation of this entitlement condition seems to be only the practical way to expand the coverage of the UIS beneficiaries under the current circumstances. Therefore, changing the entitlement condition in this direction should be seriously considered.

### *Benefits Duration of Job Seeking Allowance*

The benefits duration will be extended for another 30 days for all types of workers from April 1, 2000. However, this benefits duration period is still low compared to many of the OECD countries.

There is no urgent need to extend the benefits duration period further. The Korean workers need to pay only six months during the previous eighteen months in order to qualify for the insurance benefits, in addition to that

Korea has just extended the benefits duration period. Furthermore, the benefits duration can be extended temporarily under the current system, just as in the case of the crisis years of 1998 and 1999. As more jobs are being created with improved economic conditions, there is a need to wait and see how the new scheme of benefits duration period works under the improved economic conditions before the benefits duration period is extended further.

In addition, under the newly introduced social assistance scheme, qualified long-term unemployed workers will be entitled to another type of unemployment benefits. Concurrently:

The benefits duration should not be extended further.

### **Need for A Non-Contributory Cash Benefit System for the Unemployed**

According to a joint survey of the Korea Institute of Health and Social Affairs and the Korea Labor Institute (KLI and KIHASA, 1999) the earnings of many beneficiaries of government unemployment programs turned out to be much lower than minimum living costs. 39.4 %, 65 % and 54 % were the proportion of the beneficiaries whose earnings were below the minimum living cost among the beneficiaries of unemployment allowances, loans for the unemployed and public works projects, respectively.

D.-s. Hwang *et al.* (2000) estimated poverty groups who required social assistance by using survey results. The 1999 criteria of selecting temporary low-income care recipients (44 million won (US\$ 37,000) per household for assets; 230 thousand won (US\$ 192) per month per person for income) were used as the poverty line. 24.5 % of the households and 23.1 % of the individual persons belonged to the poverty group, respectively. More of urban areas and unemployed household belong to the poverty group. However, as they argued, it should be recognized that the estimation of poverty based on the survey results such as this one tend to overestimate the size of the poverty group<sup>16</sup>.

The same survey also showed that more of the persons belonging to the poverty group had unstable jobs or were unemployed (Table 4.3). Hence, the government needed to help at least 16.4 % of them (the unemployed of 8.7 %; the disappointed unemployed of 1.8%; economically inactive, but wanted to have a job to have a job of 5.9%) to find a job.

Korea is also one of the few OECD countries that does not have a cash benefits social assistance for the unemployed. For many of the OECD countries, the ratio of the number of unemployment beneficiaries to the total

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<sup>16</sup> In further analysis, D.-s. Hwang *et al.* (2000) assumed that 12 % of the households and 10 % of individual persons belonged to poverty group.

**Table 4.3: Poverty and economic activities of survey respondent**

	Below poverty line	Above poverty line
	(%)	(%)
Regular employees	8.5	23.6
Temporary employees	6.2	4.3
Daily employees	5.6	2.8
Employer	14.5	13.0
Family workers	6.2	4.2
Unemployed I <sup>1)</sup>	6.1	3.3
Unemployed II <sup>2)</sup>	2.6	1.5
Once looked for a job, now Economically Inactive	1.8	1.6
Now economically inactive, but want to have a job	5.9	5.2
Economically inactive	42.7	40.4
Total	100.0	100.0

Notes: 1) Unemployed workers who looked for a job for the last one week

2) Unemployed workers who looked for a job for the last two weeks

Source: D-s. Hwang et al. (2000), Table 5.2.

number of the unemployed is close to 100 % if the unemployment assistance benefits are included. Even low-benefit-coverage countries such as Spain, Greece and Portugal have a ratio of more than 30% (OECD, 1994, Table 8.4).

Furthermore, Enlarging the coverage of Korea's unemployment insurance beneficiaries by including uncovered sectors such as the daily worker is not practical, as seen above.

Thus, Korea needs to consider a non-contributory cash benefit system for the unemployed, and the Korean government plans to introduce a new social assistance system under National Basic Livelihood Guarantee Act, which will be in effect from October 2000. Under the new social assistance scheme, unemployed workers whose means are below a certain level are paid cash benefits". And, the recipients are supposed to make full use of their personal abilities to become self-supporting, which means that they should actively look for a job and/or they should try to upgrade their skills, if necessary, like the beneficiaries of the UIS are required. Therefore, a task ahead Korea is to have the new social assistance scheme to fit with the needs of the unemployed workers. Concurrently:

There is need to consider a non-contributory cash benefit scheme for the unemployed and the government plans to introduce a scheme from October

<sup>17</sup> Many of the small employers and/or family workers are also expected to receive the social assistance under the new system. 52.7% of the employers and 59.0 % of the family workers fell into the 'poverty group 1', respectively, while only 26.5 % of the employees with regular status fell below the 'poverty group I' (D.-s. Hwang *et al.* (2000), Table 5.2).



2000. Hence, a major take ahead Korea is to make the new social assistance scheme fit with the needs of unemployed workers.

### **Proposed Non-Contributory Cash Benefit Scheme of National Basic Livelihood Guarantee Act**

In October 2000, the Livelihood Protection Act will be replaced with the National Basic Livelihood Guarantee Act. Under the new framework social assistance will be available to all citizens who can not maintain the minimum standard of living subject to a means test and the beneficiaries are obliged to seek work unless they have no ability to work (Table 4.2).

This means that the former low-income care recipients will be entitled to the cash benefits which would remedy one of the most serious deficiencies of the old scheme. Under the livelihood protection scheme criteria of the assets and income tests between the two recipient types are inadequate as their differences are too small (only one million won (US\$ 833) for the assets and ten thousand won (US\$ 8) for the income), while the difference in the benefits between them is substantial. In addition, many of the low-income care recipients turned out to have no ability to work. M.-k. Kim (1998) showed that 47.5 % of the low-income care recipients (in 1996) did not have any individual with ability to work in their households.

Under the new scheme, double requirements of incomes and assets will be integrated into one criterion which is called 'the income appropriation amount'.

There will be seven kinds of allowances; Livelihood Allowance, Education Allowance, Maternity Allowance, Medical Allowance, Self-supporting Allowance, Funeral Allowance and Housing Allowance.

The Livelihood Allowances will be calculated by taking the minimum living expenses and subtracting the Medical Allowance, Housing Allowance, Education Allowance, income appropriation amount and other social payments.

The minimum living expenses will be calculated by a similar method to that used under the current livelihood protection program.

In assessing the income appropriation amount, the incomes and assets will be considered together. However, until 2002, the current means test of the livelihood protection scheme will be used instead of the income appropriation amount.

Housing Allowance will cover key money<sup>18</sup> for housing rental and rent for renters up to a predetermined maximum period. Housing repair costs will

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<sup>18</sup> Key money is the lump sum amount of the bond money that renters pay. If a renter pays the key money, he or she does not pay periodic rents and the key money is returned to the renter when the rental contract expires.

also be given to owner occupiers. The entitlement conditions for other allowances are the same as under the current livelihood protection scheme

Recipients will be required to make full use of their personal abilities to become self-supporting. Those with ability to work (generally ones whose age is between 17 and 61) who are called conditional recipients will be paid the Livelihood Allowance under the condition that they will participate in programs to promote their self-supporting capability.

Urgent payments will be also introduced for exceptional or urgent needs falling outside which is expected to be met from regular allowances. This allowance will be made at the discretion of local social welfare officers.

### ***Criterion Concerning Resource Unit of Claimants***

Under the new scheme, the social assistance claimants will be still expected to seek support from those legally responsible for supporting him or her in addition to their spouses, which is rare among OECD countries (Eardley et al., 1996a, p.65).

This criterion has been criticized for being too tight (M.-k. Kim, 1999). Claimants seek support from siblings belonging to different households and these siblings often refuse to support them. The social welfare workers are supposed not to apply this criterion if the legally responsible family members, who do not belong to the same household, refuse to support the claimants. However, it is known that the social welfare workers often do not exercise their discretionary power since they are afraid of their decisions being questioned during the audit and inspection.

Discussed below is the often-mentioned criticism that the government lacks the capacity to assess the resources of claimants. Particularly, local governments do not have the proper capacity to check the supporting capability of the legally responsible family members of the claimants who do not belong to the same household. Currently, local authorities do not apply this criterion to low-income care recipients. This means that this problem will be more serious with the new scheme since former low-income care recipients will also receive cash benefits under the new scheme. J.-h. Lee (2000) showed that among the public work program participants who received the livelihood protection only 35 % got help from the legally responsible siblings.

It is reasonable that the resource units go beyond the duty of spouses or of parents and children when Korea's strong tradition of family responsibility and obligation is taken into account. This strong family bond also proved to be an important informal social safety net for many Koreans during the financial crisis. But, as Korean society moves toward individualism and as government lacks the capacity to assess the resources (which will be discussed below in detail), social welfare officers tend to apply the resource unit criterion very strictly. It has been suggested that they should be encouraged to exercise their discretionary power of approving more of the

claimants who have legally responsible family members, but can not get support from them. The government should also consider narrowing the scope of family members legally responsible for social assistance claimants as Korea becomes a society based more on the nuclear family. Concurrently:

There is no need to narrow the scope of resource unit at the present time. However, social workers should be encouraged to use their granted discretionary power for favoring claimants when necessary. In the longer terms, narrowing the scope of family members when assessing the resource unit also should be considered as Korea moves further toward individualism.

### *Resources of Claimants for Benefits*

In calculating the income appropriation amount, virtually all kinds of income and resources of all members of the household are taken into account. The same household members include persons registered as the same household with the citizen register of local governments. The spouse and not-married children of the household head as well as the spouses of the children and grandchildren of the household heads (if the children and grandchildren are registered as the same household) are also considered as the same household members.

All assets, including fixed assets, will be counted as resources in the means test. They will be considered to generate income that is assessed by using a formula. All liabilities and a basic amount of assets (that is determined by the Minister of Health and Social Welfare) will be subtracted<sup>19</sup>.

The recipients will be allowed to retain some of their earnings. Higher disregards will apply to earnings made through rehabilitation centers for handicapped persons as well as student earning<sup>20</sup>.

Despite that the Korean system has the features necessary for preventing the possible negative effect of the social assistance scheme, such as earning regards, to some extent it is meaningless to discuss the institutional features of the Korean system concerning the treatment of resource. As seen above, the size of the informal labor market is substantial. Small independent businesses in general do not report their true incomes. Many claimants are likely to claim a payment while still working in the cash economy. However, the government does not have the proper administrative capacity to check the reported income/assets of the low-income claimants. In other words, due

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<sup>19</sup> Korea is one of the few OECD countries that take assets into consideration in assessing resources. Korea also has wider family base as the resource unit as seen above. Therefore, adult children might be expected to sell their properties before their parents have recourse to social assistance, which seems unreasonable. Less strict rules have to be applied to assets in assessing the resources of the legally responsible family members who are beyond the nuclear family.

<sup>20</sup> It was also proposed that higher earning disregards should be applied to earning made through public works and participation in group/community cooperative enterprises. However, this proposal was abandoned due to the opposition of the budget office.

to the same reason why Korea can not include daily workers and/or small employers in the coverage of the unemployment insurance scheme, Korea's system of assessing the resources will not work well. The fact that the government decided to postpone the implementation of the income appropriation amount method until 2002 itself proves that the government is not ready for using the new resource treatment measure.

Currently, in selecting the livelihood protection recipients, the government uses an 'estimated income method' in order to remedy this problem. Based on the discretion of the social welfare workers concerning possible working days and daily incomes, the recipients are given an estimated income. However, the estimation income method has many deficiencies. It is often pointed out that social welfare officers have too much discretion in assessing the estimated income and their power is not exercised properly. Often, an estimated income is allocated to persons who are not capable to work or do not have a job. Not-married children who are registered as the same household, but do not live with the claimant, are also given an estimated income.

Under the new scheme, it is very likely that social welfare workers will also have same discretion power to determine the estimated incomes used for assessing the amount of the Livelihood Allowance. Particularly, concerning conditional recipients who seem to have some incomes, the authorities will decide their income based on the average income of relevant occupations or industries and with the assumption that they work two days a week.

Many suggest that the estimated income method should be abandoned and more scientific ways to assess the claimants' resource should be developed (D.-s. Hwang *et al.*, 2000; M.-k. Kim, 1999). However, due to the peculiar structure of the Korean labor market such as the large size of informal sector and poor income tax collection system as discussed above, the scientific method alone does not guarantee the effective and fair assessment of resources of claimants. This problem will also be more serious under the new basic livelihood guarantee system since about one million of former low-income care recipients have cash benefits based on estimated incomes.

Developing a data-matching system, which matches data held by the local government authorities with data held by other agencies such as the National Tax Office, the National Pension Authorities and the National Medical Insurance Authorities to identify possible discrepancies is the most prominent mechanism to reduce possible incorrect payments. However, in Korea, establishing a data-matching network of this sort takes some time considering that even a nationwide data network connecting different local governments has not been established.

The Korean government plans to finish the installation of the nationwide public administration data network of local governments and a data-matching scheme of different government ministries/agencies by September

2000 (Ministry of Health and Social Affairs, 1999, p.114). But there is still some doubt about the government capacity in finishing these installations on time. Concurrently:

A data-matching network for controlling incorrect payment and fraud should be established. However, establishing this system alone does not guarantee the effective and fair assessment of resources since the government's lack of capacity to control cash economy is evident.

*Government's Capacity to Refer Proper Activities to Promote Self-Supporting Ability of Conditional Recipients*

Under the current livelihood protection scheme, generally claimants initiate their claims in person by visiting their local government offices. Then, social welfare officers review their claims and decide their eligibility and the amounts of aids. Claims should be reviewed at least once a year. In principle, the allowances are paid monthly and the payment should be made directly to claimants' bank account

This procedure of making a claim and receiving the payment will be the same under the new scheme. But, as the new system is introduced, a thorough examination of claims based on the new entitlement conditions will be conducted during May to July of 2000. Once the recipients are determined, in case of conditional recipients their claims should be reviewed every three months.

The government is expecting substantial extra burdens to be placed on social welfare officers, as the-recipients of cash benefits will rise from 540,000 in 1999 to 1,540,000 in 2000. In order to encounter this situation, staff numbers will increase gradually from the current number of 4,200 to 7,200 by 2001 (government estimation; Ministry of Health and Social Affairs, 1999a). In 2000, 600 more of social workers will be hired. The government claims that even with 7,200 of staff the ratio of the social welfare officers to all recipient households will be still low compared to those of advanced countries (Ministry of Health and Social Affairs, 2000).

However, increasing the number of social welfare staff is not sufficient. Under the new scheme conditional recipients are supposed to participate in activities to promote their self-supporting capabilities and social welfare officers are supposed to refer recipients to self-supporting programs that fit a particular conditional recipient to a particular program. Programs for promoting a recipient's self-supporting capability include education/training, job placement services, public works and support programs for self-employment. But, social welfare officers do not have experiences of or expertise in matching recipients to appropriate programs and many social workers will be newly employed.

Since registration with public employment offices is considered an activity to promote the self-supporting capabilities, some sort of partnership is to be established between local governments and public employment

offices, the details of which will have to be worked out among concerned government ministries. But, it is often pointed out that Korea's public employment services are still incompetent (J.-h. Keum, 1999; S.-h. Kim, 1999; Korea Labor Institute, 1999a).

The number of job seekers registered with public employment services increased substantially during the crisis years. This is due, in part, to being mandatory for job seekers to register with the public employment services in order to participate in government unemployment programs. But, the penetration rate (the fraction of job placements that are filled through the public employment offices) is still low (9.1 % according to KLI and KIHASA, 1999). Seeking information is the main reason for using public employment services for 76.9 % of the unemployed who used public employment services. The same study showed that most customers of the public employment services are not satisfied with the services provided by the public employment offices. Another study done a year later also showed that the quality of the services of the public employment offices did not improve much (J.-h. Keum, 1999). The majority of the staff in public employment offices have little on the job experiences and their turnover rate is very high (Korea Labor Institute, 1999a, p.30).

Some (Korea Labor Institute, 1999a; J.-h. Keum, 1999) argue that the public employment services should be enlarged. The size of the public employment services is still very low compared to other OECD countries such as Germany and USA (S.-h. Kim, 1999, Table 4.3). However, expanding the public employment service needs more thorough consideration. Fields (1993) argued that it would be justified if job seekers had poor information regarding job vacancies and had difficulty becoming employed due to lack of information about where the jobs were. He claimed that this was not the case in Korea before the crisis. He also argued in another study (1999, p.16) that job placement services was criticized in Korea during the crisis because Korea's unemployment problem was not frictional, hence placement services did not work due to that they focused on the wrong problem.

Public works need to be a big component of the programs that conditional recipients are required to participate in. Public works is a responsibility of the Ministry of Home Affairs and local governments, while social assistance is that of the Ministry of Health and Social Affairs. However, coordination among relevant government agencies seems to be poor. In 2000 the government plans to spend 64.5 % of the public works budget in the first three months based on the assumption that unemployment rate will be high during this period. There will be little of the budget left for public works related to the new social scheme, which will be implemented in October of this year, unless the government allocates more budget later this year.

Also, training will not absorb a large number of the conditional recipients. In 1999 about 60,000 unemployed low-income people went through a

government-supported training program. This is very small compared to the number of the conditional recipients that are expected to be around one million people.

The government plans to encourage the development of group/community cooperative enterprises. The concerned budget will increase from 1.2 billion won (US\$ 1,000,000) in 1999 to 2.7 billion won (US\$ 2,300,000) in 2000, and the designated enterprises will also rise from 20 to 70. S.-h. Kim (1999) argued that the budget for group/community cooperative enterprises should be at least 500 billion won (US\$ 416,000,000) in 2001. However, this much of the sudden rise of the budget can not be expected.

All of these discussions mean that the government is not ready for implementing a work test scheme through which claimants are required to meet the new entitlement conditions. The government should consider a way of operating the work test that requires only some competence of the authorities until a further institutional framework is developed to accommodate the new entitlement conditions to reasonable level. Concurrently:

Korea is not ready for implementing a thorough and reasonable work test. Thus, the government should operate a work test scheme that requires only some competence of the authorities until a further institutional framework is developed to accommodate the new entitlement conditions more thoroughly.

#### *Benefit Level of Allowances for Conditional Recipients*

In 2000, a home care recipient of a regular program receives a monthly average of 188,000 won (US\$ 156) of aids (135,000 won of livelihood aid; 6,000 won of education aid; 49,000 won of medical aid) (Ministry of Health and Social Affairs, 1999a, p.21). The actual amount of aids he or she receives is dependent on the amount of the incomes of his or her household and the number of household members. A home-care recipient of single-member household on a temporary program receives a maximum 79,000 won of livelihood aid (US\$ 66) in a month. The actual amount of livelihood aid of temporary program also depends on the recipient's income and the number of household members. A low-income care recipient of single-member household on temporary program receives a maximum 79,000 won (US\$ 66) in a month, but the aid is paid only for three months.

It is difficult to estimate the exact amount of additional cash benefits for each recipient with the new scheme. But, it may be inferred from the allocation of the government budget for the years 2000 and 2001.

Additional benefits will not be that large for former home-care recipients. According to the government's budget plan for the year 2000, a monthly average allowance of home care recipients of the current livelihood program will be increased by 9.0 % from October 2000 (Ministry of Health and Social Affairs, 1999a, p.113).

According to the Ministry of Health and Social Affairs, the additional budget that it will need for the year 2001 is a maximum 900 billion won

(US\$ 750,000,000) or a minimum 500 billion won (US\$ 417,000,000) (Ministry of Health and Social Affairs, 1999b)<sup>21</sup>. If the government decides to spend 500 billion won, and this additional 500 billion won is spent only for the cash benefits of additional recipients, each additional recipient will have additional 500 thousand won for the whole year. The annual additional amount of 500 thousand won is divided by nine months since the additional cash benefits recipients already receive the livelihood allowances for the three months in 2000. This means that amount of their monthly allowance for the first nine months will be a maximum 56,000 won (US\$ 47) per person<sup>22</sup>. Or, if the government decides to spend 900 billion won, the benefit amount of a month per person will be 100,000 won (US\$ 83).

Three-member household, which consists of one adult and two children, for livelihood aid, would receive a maximum 300,000 won (US\$ 250) to a minimum 168,000 won (US\$ 140) per month. If education allowance of 6,000 won and medical allowance of 49,000 won are included, this household will receive a maximum 465,000 won (US\$ 387) to a minimum 333,000 won (US\$ 278). This is not low compared to Korea's other social benefits. The monthly minimum wage of between September 1999 and August 2000 is 361,600 won (US\$ 301). The monthly allowance of this household will be a minimum 92.2% of the minimum wage. The minimum amount of 333,000 won is 77.4 % of the minimum monthly allowance of 430,000 won (19,000 won times 24 days) that a participant of public works would receive. Also, it is not low compared to the benefits levels of social assistance of other OECD countries (Eardley *et al.*, 1996a, Table 5.1 & Table 5.2). This means that the government has to make every effort for conditional recipients to be referred to appropriate activities to promote their self-supporting activities<sup>23</sup>. Concurrently:

Conditional recipients of the new basic livelihood guarantee scheme will have reasonable amounts of allowances. This makes the government's need to deliver the new social assistance system with a proper arrangement of work and means tests more compelling.

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<sup>21</sup> It also includes budget for hiring more social welfare workers and the amounts equal to providing 9% increase of allowances to former home care recipients for the first nine months compared to year of 2000.

<sup>22</sup> It is also assumed that the number of recipients and the amounts of the cash benefits per recipient remain the same.

<sup>23</sup> If a reasonable amount of budget is not allocated to the new scheme, it is very likely that many conditional recipients will be only those with distinct labor market handicaps. It is due to social workers will have much discretion with the government lack of capacity in work and means tests. It can be inferred from types of households receiving social assistance in Japan, the system of which Korea is now mimicking. In Japan, the largest proportion of social assistance recipients is older, sick or disabled people (Eardley *et al.* (1996b), Table 14.4).



*Public Works Scheme: Alternative Means of Social Protection for the Unemployed*

Among active labor market programs such as training, retraining or support for self-employment, which the authorities are supposed to refer to conditional recipients, public works often act as a temporary safety net by providing current cash benefits to unemployed people.

In Korea, public works scheme has been extensively used since the crisis began. It took the largest fraction (25.9%) of government expenditures concerning unemployment during the crisis years of 1998 and 1999. It will be phased out as the country overcomes the crisis. In 2000, public works budget decreased by 54.7%. It was 49.7% of the total cut of unemployment program budget in 2000.

But, maintaining public works scheme to a certain level, even after the crisis is over, should continue to be a major alternative social protection means to a public assistance such as the basic livelihood guarantee scheme or an unemployment insurance system in the delivery of social welfare. It is even more so since Korea is not yet ready for imposing reasonable work and means tests to many of unemployed workers who will receive social assistance, as seen above. Public works should be maintained as an a major means of social protection of permanent nature in the sense of maintaining the scheme until necessary conditions for imposing work and means tests fairly and efficiently are met to a satisfactory level without regard to how long it will take.

Public works, unemployment assistance (cash benefits without contribution) and unemployment insurance schemes should be managed as an integrated system as, in Korea, the informal labor market is large and flexible. Many of unemployed workers who need social assistance will have to have the option of choosing public aids or public works. However, the current features of public works scheme (and the perception of government officials about the public works) will have to be changed somewhat. Like other public works schemes, Korea's current program is to provide temporary employment, in addition to its other role as a short-term social safety net. As seen above, government officials as well as the participants were positive about the role of public works program as a social safety net, while the government officials were skeptical about its role of helping re-integrating or increasing labor force attachment of the unemployed. These contrasting evaluations between the participants and government officials are expected as the experiences of other countries have shown similar results (Dar and Tzannatos 1999, p.18).

As a part of the integrated system of social protection for unemployed workers, public works' role of a social safety network for unemployed persons, who otherwise need social assistance, should be emphasized more than the role of an active labor market program. And, the system needs to be

perceived and managed that way by all the concerned parties including the government officials. In this context, relationship between the basic livelihood protection scheme and public works programs including disregards concerning public works earning<sup>24</sup> in the assessment of resources of social assistance claimants should be re-examined. More detailed proposals of the public works scheme go beyond the scope of this study. Concurrently:

Public works scheme will have to be a major means of social protection for the unemployed, even after the crisis is over, until necessary conditions for reasonable means and work tests are achieved to satisfactory level. Also, by providing public works to a large number of conditional recipients, the authorities will be able to manage the work test scheme only with some competence. But, the relationship between the basic livelihood protections scheme and public works program should be re-examined. Public works' role of a social safety net should be emphasized more.

## **Concluding Remarks**

There is a need to enhance social assistance for the unemployed. However, implementing a non-contributory cash benefit system efficiently and fairly for them will be difficult until conditions for means and work tests for the unemployed recipients of the cash benefits reach a reasonable level. In the meantime, therefore public works should continue to be maintained as a short-term social safety net even after the financial crisis is over.

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<sup>24</sup> Under the basic livelihood protection scheme, recipients will be allowed to retain 50 % of earning made through public works.

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# 5 Unemployment Assistance: Policy Implications from the Crisis of 1997

Alan Abraham\*<sup>\*</sup>

In 1997, Korea, which had set about introducing an unemployment insurance scheme (UIS) at a measured pace, was suddenly faced with the need to adjust the scheme in a very short time. Action was necessary to ensure the viability of the scheme in the short-term and the government needed to re-think its views about the longer-term sustainability of the scheme. Questions arose that touched on options for supporting the most vulnerable groups in the economy, especially given the correlation between the lack of employment and poverty, and the role that unemployment insurance might or might not be expected to play.

The events of this time offer a case study into the operation of unemployment insurance schemes during a crisis. They have raised issues about the extent to which such schemes need to be supplemented schemes to assist those who are not covered by insurance, that is, by forms of non-contributory unemployment assistance, particularly. This paper looks at the experience of Korea and compares it with circumstances in Australia, a country that offers only non-contributory unemployment assistance. The paper then draws some implications for the future of unemployment assistance in Korea.

The experience of Korea also offers lessons for developing countries that may have reached a point where, with a growing formal sector of the economy, they, too, need to consider the type of social protection to be offered those who become unemployed.

## **The Impact of the Unemployment Insurance Scheme during the Crisis**

The Korean Unemployment Insurance Scheme (UIS) was instituted in 1995,

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\* The World Bank.

at a time of rapid economic growth. For a short while after that, the growth continued, the unemployment rate remaining at only 2% or less. As to be expected, greater job opportunities meant declining poverty, the poverty rate falling from about 40% to less than 10% in the decade before the crisis. The UIS was initially introduced to protect workers in larger private sector enterprises, that is, those with at least 100 employees. Insurance premiums were paid 50:50 by employers and employees at an overall rate of 0.6% of wages. Compensation was set at a wage replacement rate of 50%. The duration of entitlement, shown in the following table, was related to age and years of contribution.

**Table 5.1: Months of entitlement to unemployment benefit in Korea**

Years of contribution	Age in years		
	Less than 30	30 to 50	50 and over
1-3 years	2 months	3 months	4 months
3-5 years	3	4	5
5-10 years	4	5	6
10 years or more	5	6	7

Given the state of the labour market at the time, the different durations of entitlement seemed more than adequate; unemployment was low and periods of unemployment were relatively short. Prior to the crisis, less than 1 in 10 of the relatively few unemployed had been looking for work for over 6 months. The scheme was therefore consistent with a steady state unemployment rate of no more than 2% and with a prognosis of continuing growth.

The impact of the crisis, however, put these design parameters under severe test. In the first 12 months of the crisis, employment fell by over 5%. Taking into account the total turnaround, the effective loss of jobs amounted to more like 7%. This loss was comprised of increased unemployment of about one million and by labour force withdrawal of about another half million. Almost 70% of the additional unemployed was for males and by mid-1998, two thirds of unemployment was for males, one third for females.

**Table 5.2: Working age population in Korea**

	October 1997	October 1998
	(persons in millions)	
Population	34.90	35.37
Labor force	21.8 (62.5%) <sup>1)</sup>	21.7 (61.4%) <sup>1)</sup>
Employed	21.3	20.2
Unemployed	0.5 (2.1%) <sup>2)</sup>	1.5 (7.1%) <sup>2)</sup>

Notes: 1) The numbers in parenthesis are labor force participation rates

2) The numbers in parenthesis are unemployment rates.

Source: Korea Labor Institute (January 1999).

Following the onset of the crisis, the government came under pressure on four fronts:

- 1) The premiums could no longer cover the insurance payouts;
- 2) The duration of entitlements were considered too short given the increasing periods of unemployment and given that the scheme had been in operation too briefly for anyone to have built up long entitlements;
- 3) The levels of benefit were perceived to be too low; and
- 4) Many of the unemployed had no insurance cover.

To address the first of these issues, the government increased premiums to 1% of wages, still equally shared by employers and employees. To address the second concern, it increased all of the respective durations of entitlement shown in Table 5.1 by two months. To address the third concern, it increased the wage replacement ratio to at least 70% of the national minimum wage.

To address the last of the concerns, UIS was gradually extended to smaller private sector companies: to those with more than 30 employees in December 1997; with 10-30 employees in January 1998; with 5-10 employees in March 1998; and with less than 5 employees in October 1998. Although the government intended to extend the scheme to part-time and temporary workers this has so far proved impractical (as of March 2000).

The extension of UIS to smaller companies, increased its nominal coverage to about 8.5 million, about 45% of the 19.5 million workers in the private sector. By the end of 1998, however, there were actually only 4.9 million contributors. The MOL estimated that compliance among small employers (5 employees or less) was only about 25%.

The relatively fast extension of the UIS was hardly in accordance with the government's original intentions and it took place under economic, social and political stress. But it turned out to be a critical move in ensuring at least the short-term viability of the scheme.

The low rate of compliance in the newly covered sectors was not the issue. The key to bridging the crisis period, which turned out to be briefer than most commentators had expected, was the increased revenue brought about by the wider coverage, despite the overall fall in compliance. At the same time, expenditure was constrained because of the low or zero level of entitlements that had accrued to most of those who had become unemployed. The following tables show the extent to which unemployment was heavily biased towards people with either no insurance cover or limited entitlements.

The data show that people who had been unemployed for less than year, in effect, those displaced or unable to find first jobs during the first stage of the crisis, were mostly workers in Korea's secondary labor market: people who were uninsured and whose work was marginal. Less than a quarter of them had been in permanent jobs, and perhaps less than 1 in 10 had been in companies with more than 100 employees.

Table 5.3: Unemployment in Korea, July 1998

Category	Number	
	('000s)	(%)
<i>All unemployed</i>	1,529	100.0
<b>Non- family heads</b>	818	53.5
<b>Family heads</b>	711	46.5
<b>Family heads - no employed members</b>	297	19.4
<i>Education</i>		
<b>Middle school education or lower</b>	424	27.7
<b>High school graduates</b>	790	51.7
<b>College education or higher</b>	316	20.7
<i>People unemployed for less than 1 year</i>	1,297	100.0
<b>Previously a temporary worker</b>	429	33.1
<b>Daily workers</b>	364	28.1
<b>Permanent workers</b>	292	22.5
<b>Self-employed</b>	194	15.0
<b>Unpaid family workers</b>	20	1.5
<i>Disengaged from firm with: &lt; 10 employees</i>	797	61.4
<b>10-19 employees</b>	165	12.7
<b>20-49 employees</b>	120	9.3
<b>50-299 employees</b>	148	11.4
<b>300 or more employees</b>	67	5.2

Source: Korea Labor Institute (December 1998). Based on data from the Monthly Review on the Economically Population.

In addition, Table 5.4 shows that the impact of the decline in employment during 1998 was concentrated on either younger or older workers.

Older workers may have had the option of early retirement, while the young, many seeking their first job, would have had few if any UI entitlements. In neither case would the call on unemployment insurance compensation have been as high as it would have been among employees aged 30 to 50 years, few of whom lost their jobs. As well, the major declines occurred among lesser skilled workers, in manufacturing and in construction, that is, among the lower paid. On the other a hand, employment actually *increased* among professional and managerial employees and in the service sector.

During 1999, less than 25% of the labour force was actually contributing to unemployment insurance and only about 10% of the unemployed (or 1% of the labour force) were receiving benefits. In broad terms, throughout 1999, the distribution of the working age population was as shown in Table 5.5.

Table 5.4: Employment declines (job losses) in Korea, December 1997 to December 1998

	Age classification ('000s)						Total
	15-19	20-29	30-39	40-49	50-59	60 plus	
1997	347	4,671	5,890	4,856	3,101	1,818	20,683
1998	321	3,956	5,856	4,811	2,835	1,741	19,520
Loss	26	714	34	45	266	77	1,162
Loss (%)	7.5%	15.3%	0.6%	0.9%	8.6%	4.2%	5.6%
Proportion	2.2%	61.5%	2.9%	3.9%	22.9%	6.6%	100.0%
	Industry classification ('000s)						Total
	Agriculture /fishing	Manuf'g/ mining	Constr'n	Retail/ wholesale	Utilities	Services	
1997	1,917	4,433	1,966	5,863	2,030	4,474	20,683
1998	1,882	3,878	1,428	5,637	1,985	4,711	19,521
Loss	35	555	538	226	45	-237	1,162
LOSS (%)	1.8%	12.5%	27.4%	3.9%	2.2%	-5.3%	5.6%
Prop'n (ex services)	2.5%	39.7%	38.5%	16.2%	3.2%		100%
	(Proportions are expressed as excluding services)						
	Occupational classification ('000s)						Total
	Professional /managerial	Clerical	Service/ sales	Skilled agriculture	Unskilled1 prod'n workers		
1997		3,713	2,551	4,947	1,825	7,647	20,683
1998		3,828	2,283	4,770	1,789	6,851	19,521
Loss		-115	268	177	36	796	1,162
Loss (%)		-3.1%	10.5%	3.6%	2.0%	10.4%	5.6%
Prop'n (ex prof/man'l)		-	21.0%	13.9%	2.8%	62.3%	100%
	(Proportions are expressed as excluding professional and managerial occupations)						

Source: Korea Labor Institute (December 1998).

Table 5.5: Labor force in Korea, 1999

Classification	Number ('000s)	% Proportions of:	
		Population	Labor force
Working age population	35,000	100	
Labor force	21,500	61.4	100
Employed	19,850	56.7	92.3
Nominally covered by UI	8,800	25.1	40.9
Actually contributing to UI	5,300	15.1	24.7
Unemployed	1,650	4.7	7.7
Receiving benefits	175	0.5	0.8

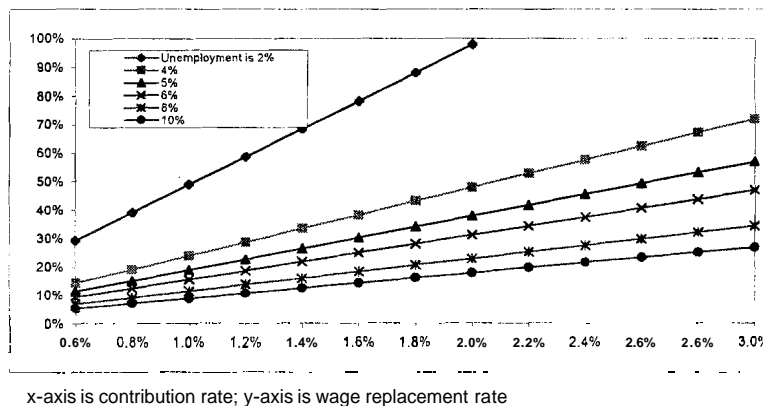
Source: Author's calculations based on government budget figures (January 1999).

The ratio of beneficiaries to unemployed was thus about 1:10.

- (a) Many of the unemployed were not insured to begin with. The Government expects effective coverage to increase with time to reach closer to the nominal target. But plans to include daily workers (largely building and construction workers) and part-time workers have stalled. However, any longer-term industry restructuring that takes place in Korea should increase the proportion of the unemployed that does come from the covered sector.
- (b) Others had exhausted their limited entitlements. It is difficult to be precise from the data available here, but perhaps two thirds of those who became unemployed were aged less than 30 years and therefore probably had no more than 3 months entitlement (subsequently increased by two months). In any case, the scheme had been in operation for only about 3 years at the onset of the crisis and consequently the maximum entitlement (see Table 5.1) that anyone could have accrued was only four months (subsequently increased by legislation to six months).
- (c) Still others would not have accumulated any entitlements. This would have include all those employees who were newly covered by the extensions to the UIS but who were required to contribute for at least six months before becoming entitled to any compensation in the event of becoming unemployed.

In effect, the scheme was able to maintain its reserves during 1998 and 1999 only because the total impact of the full benefit structure had not really been felt. In the meantime, the GOK expected economic growth to resume, which it has done. However, there is still some expectation that unemployment will not come down to its former levels; anymore than it did in many OECD countries in earlier decades.

**Figure 5.1: Replacement and contribution rates for different unemployment scenarios in Australia (100% takeup)**





The question therefore arises as to the longer-term adequacy and sustainability of the scheme. In the absence of administrative complexities, there is a relatively simple relationship balancing a given replacement rate of UI compensation and the level of contribution needed to sustain it. The following graphs demonstrate this.

For example:

- to achieve average wage replacement of 50% under a steady unemployment level of 2%, would require a 1% contribution level.
- on the other hand, if unemployment were to be 5%, a 1% contribution would enable a wage replacement rate of less than 20%;
- to continue paying a wage replacement rate of 50% in the face of 8% unemployment would require the contribution to rise to about 4.3%.

The simplistic approach assumes that all contributors would be entitled to receive benefits, which is never the case in any insurance-based scheme. All schemes set limits on entitlements. These may be limits on the duration of compensation, which imposes a brake on expenditure at times of higher than usual unemployment when the length of unemployment tends to increase. Waiting periods can also be introduced, as they are in Korea, the impact of this being noticeable no matter the level of unemployment.

As we have seen in the case of Korea, the ratio of beneficiaries to unemployed was about 1:10. It is not possible to say just what sort of beneficiary to unemployed ratio might be considered more appropriate, or even whether there is such a thing as an "appropriate" level. It is all a matter of the design parameters. But a ratio of 1:10 is surely low and perhaps a figure of 1:3 would be more typical. In the case of Korea, the nominal coverage of the scheme is now far wider and compliance rates may well improve with greater enforcement of the legislation. The likelihood of an unemployed person having some entitlement to UI compensation should therefore increase significantly.

Under a scenario in which the beneficiary to unemployed ratio was 1:3, the current contribution rate of 1% of wages could support a wage replacement of 50% for unemployment levels up to 5%. The current UIS parameters would therefore be adequate provided unemployment does stay around 5% or less; but if the government wishes to continue with a wage replacement level of 70% the premium will need to rise closer to 1.5 or even 2%.

In summary, then, a number of conclusions about the UIS can be drawn from the crisis.

- The system was immature at the onset of the crisis
  - No insurance business could be expected to handle such an event so soon after its introduction. Plans for its **development** over time and for the building up of reserves were seriously disrupted.
- The short-term viability of the UIS was ensured only by an expansion of revenues through generating contributions in respect of employees who were unlikely to make significant claims for unemployment

compensation

- Although claims for compensation did exceed contributions during 1998-1999, the growth in contributions through expansion of the scheme was sufficient for the UIS to retain positive reserves.
- The UIS was limited in scope to people who were unlikely, for a variety of reasons including the impact of labour legislation, to become unemployed.
  - Labour legislation restricted hiring and firing practices among the very enterprises also covered by the UIS; and
  - Changes to labour legislation are addressing this but questions concerning the portability of insurance contribution will remain.
- The risk of unemployment continues to be higher among those who were uninsured
  - Korea still has a significant informal sector and it has so far proved impracticable to devise a system to cover workers in marginal jobs; and
  - Youth unemployment presents an especially difficult case.
- The government changed the rules of the scheme the moment it was called on to respond to the crisis
  - These changes were beneficial only to those who were insured to begin with and had no impact on the majority of unemployed.
- Compliance with the UIS legislation is lower among smaller enterprises where the likelihood of labour turnover, and therefore intermittent unemployment, is highest
  - The total wage-based levies under the so-called the Employment Insurance Scheme (the EIS, of which the UIS is just one component) is now 1.5% of payroll for small firms and yet they are probably less likely to receive assistance under the various components of the scheme (see the next section).

The UIS, of course, offers a guarantee of compensation under certain conditions. Contributors are *entitled* to compensation, under UIS guidelines, irrespective of their circumstances. It was not, and is not, a poverty-related measure. Government decisions to extend the duration of compensation, for example, had to be made universally, without consideration of contributors' individual circumstances. The greater problem during the financial crisis therefore turned out to be providing social protection to those who were not insured, particularly those who had fallen into poverty.

### **Other Form of Social Protection During the Crisis**

The weaknesses that the UIS exhibited during the crisis will certainly be eased with time but they will not be eliminated entirely. Many people will continue to be uninsured. Others, although nominally covered, will still lack

entitlements or have exhausted what little they had. This will especially be the case for young people at a time when youth unemployment is likely to be greater than before. And within the sectors that are supposedly covered by insurance, compliance with the UIS legislation cannot be totally enforceable. UI reserves stood at only a little over W 1 trillion by the end of 1997. Table 5.6 below shows that by 1999 the government budget for unemployment insurance compensation alone was W 15 trillion, with the total budget for social protection being almost W 77 trillion. The budget for UI compensation was thus only 20% of the budget for social protection. The budget can be considered in two parts: expenditure on labour market programs; and expenditure on social safety nets, including UI compensation.

The budget allocation for labour market programs (excluding UI compensation) was about W 20 trillion. 40% of this was spent on vocational training through a program known as the Vocational Ability Development (VAD) scheme. VAD was financed by a further levy on employers only, averaging about 0.4% of wages, although it varied according to the size of the enterprise. Subsidies were also made available to employers to avoid dismissals. They were applied through a program called the Employment Support (ES) scheme, financed by third levy on employers, equivalent to 0.7% of wages.

Table 5.6: Government budget allocations on social protection in Korea, 1999

	Budget allocation (won in millions)	Size of program (persons)
Total Labour Market Programs	2,069,300	
Vocational training	795,700	320,000
Loans to the unemployed	638,200	70,000
Support to avoid dismissal	491,500	1,020,000
Expansion of placement network	63,600	
Support for highly educated unemployed	60,000	25,000
Training/job placement for women	20,300	6,400
Total Social Safety Net	5,621,800	
Livelihood Program (long-term and Temporary)	1,950,400	1,730,000
Public works	1,600,000	370,000
Unemployment insurance compensation	1,501,200	530,000
Other expenses (support to children, Living costs, rural start ups, reserves)	570,200	
Total Budget	7,691,100	

Source: Ministry of Finance (January 1999).

Both of these schemes, VAD and ES are components, together with UIS, of the Employment Insurance Scheme (EIS). The total levy on wages to finance all elements of EIS therefore averaged about 1.7%, rising to 2.1% during 1998.

The sizes of the respective programs shown in Table 5. 6 represent the total *flow* of people who were be assisted in 1999. A typical stock situation during the year could be expected to look something like the following table.

Table 5.7: Social protection in Korea, 1999

Unemployment assistance		
Number of unemployed receiving:		
Training and job placement	160,000	22%
Unemployment compensation	170,000	23%
Loans to unemployed	70,000	10%
Total	400,000	55%
Poverty alleviation		
Number of people benefiting from:		
Public works	190,000	26%
Livelihood Program	135,000	19%
Total	325,000	45%
Total	725,000	100%

Source: Author's calculations based on KLI (December 1998)

This stocktaking is against a background of an underlying stock of 1.6 million unemployed. In addition, another 1 million people were to be supported during the year by subsidies to employers designed to avoid dismissals. Since, the budget allocation for that was equivalent to about one third of the allocation for UI compensation, the monthly stock Figure 5. would have presumably been in the order of another 100,000 workers.

The table shows that the social safety net budget contained three big-ticket items, which between them accounted for 90% of the social safety net budget:

- ☐ Cash assistance through the Livelihood Protection Program (LPP), providing both long-term and temporary protection, and costing W 20 trillion for an estimated 940,000 participants
- ☐ A public works program costing W 16 trillion for an estimated 370,000 people.
- ☐ Unemployment insurance compensation costing W 15 trillion for an estimated 530,000 people.

The two significant areas of unemployment assistance other than unemployment insurance were thus LPP and public works. The LPP was designed originally to provide long-term assistance to the chronically, rather than to the intermittently or occasionally poor or to the unemployed as such.

The Program was designed as a safety net for what was seen as a diminishing number of poor families, diminishing because economic growth was bringing about continuing reductions in the poverty rate. The Ministry of Health and Welfare reported that 87% of Livelihood registrants before the crisis were located **outside** Seoul. They attributed this to the impact of the assets test which value property at much higher levels in Seoul, disqualifying many people in the city.

However, the number of Livelihood recipients did not markedly increase during the crisis. It essentially remained a program to deal with chronic poverty. The greater crisis response came from the expansion of public works programs. Public works had already been in place but they were driven largely at the local government level using local government finance. Because of this, the main take up of places was in Seoul, the only local government area with sufficient financial backing to put in place a reasonable scheme. Some 80% of places under the existing scheme were **within** Seoul, virtually the mirror image of the LPP. Work was said to be cleaning, laboring, housekeeping, house maintenance, and so on.

Under the impetus of the crisis, the expansion of the program was nationwide, providing public works for the first time in many rural areas. Even so, as the 1999 budget showed, the expansion was still limited. In addition, the function of public works was not always clear and it became somewhat contentious in the legislature. Many considered that public works should provide long-term work opportunities. Public works funds were provided, for example, to the Ministry of Information and Communication for the IT projects such as work associated with the Y2K problem. In addition, the extended public works program during 1999 established priorities for selection as follows: (a) "highly" skilled workers; (b) people aged 30-55; and (c) heads of households. The first category seems unexpected and undeserved in a poverty-related program.

The end result of all of this was that the Livelihood Protection Program and Public Works fell far short of the potential level of demand, leaving many people to rely on **family** and community support while unemployed. In discussion with the World Bank leading towards structural adjustment loans, mainly during 1998, Korean authorities made clear their reluctance to undertake any sweeping expansion of safety net programs so as to avoid any growing welfare dependency. However, as Professor YB Park's paper in this conference discusses, the government does now intend to expand the Livelihood Protection Program. In October 2000, the National Basic Livelihood Act will introduce a program to provide assistance based on the administration of work tests and means tests. In effect, the government intends to expand non-contributory assistance to the unemployed.

## Observations from Another System

The development of an enhanced Livelihood Protection Program will add to the array of government instruments an expanded poverty-related program that complements the system of entitlements under UIS. But a program of this type has its own complexities. Benefits are provided on the basis of need rather than entitlement and that, of course, raises one fundamental issue: how to assess need. Two methods may be used: categorical testing and financial assessments. Whether these two can be easily mixed is open to question.

We may consider the example of Australia<sup>1</sup>, which was looked at more closely in the context of examining the feasibility of introducing a non-contributory scheme of unemployment assistance. Australia is one of only a handful of countries that has no system of unemployment insurance, and consequently, no system of *entitlements* for the unemployed. The Australian system is designed to provide an adequate level of income for all Australians irrespective of any circumstances, other than their financial situation. The essential feature is therefore meant to be an income and assets test (a "means" test).

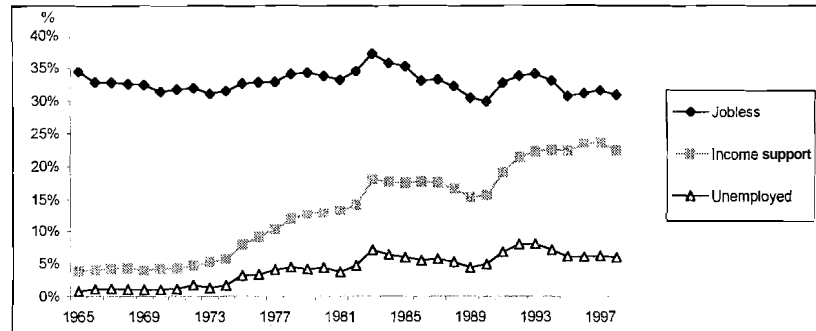
Spending on welfare payments generally increased from around 3% of GDP in the 1960s to over 7% at present, although OECD data indicate that spending on social security is only about 64% of the OECD average. Even so, the Australian Department of Family and Community Services (FaCS) reports that during the 1990s, growing welfare dependency has been a problem for Australia. The proportion of children living in families without any members in work was high in comparison to other OECD members and a significant problem of inter-generational welfare dependency has arisen. FaCS has reported that "young people from income support recipient families were more likely to leave school early, to experience unemployment and long-term unemployment, to have children by the age of 19 years, to receive income support themselves and/or to be classified as homeless for income support purposes"<sup>2</sup>. The extent of welfare dependency within Australia can be seen from the following graph.

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<sup>1</sup> The following draws substantially on the Technical and Other Appendices to the Interim Report of the Reference Group on Welfare Reform: Participation Support for a More Equitable Society, Department of Family and Community Services, March 2000. Copies of the Technical and Other Appendices can be obtained through the Australia Government web site or directly from <http://www,facs.gov.au/>

<sup>2</sup> Australian Department of Family and Community Services (1999)

**Figure 5.2: Proportions of working-age population (15-64) who were jobless, receiving income support and/or unemployed in Australia, 1965 - 1998**



The term 'jobless' is used here to refer to all people without work, whether or not they are in the labour force. One in four people of working age are now in receipt of some form of income support, although it should be understood that this includes support to students in education. As the graph shows, joblessness has actually fallen over the years, even as recorded unemployment may have grown. Part of the increases in the proportion of people receiving income support comes about because of the changing distribution of work among families. There have been increases in the proportion of couples with *no* paid work, at the same time as there have been increases in the proportion of couples with *two* incomes. The proportion of couple-families in which there is only *one* income has declined. In effect, there is a tendency for husbands and wives to be either jobless together, or both earning incomes. In addition, there has been a sustained increase in the rate of single-parent families, which are much more likely than couple-families to be receiving income support.

Another part of the increase in the numbers receiving support comes about because of the way the income support schemes actually operate. To reduce any tendency towards welfare dependency, the system encourages recipients to earn income (including from investments) while still retaining some income support payment. The level of income support provided depends on family structure and the income earned.

Naturally, income support is reduced as other income is earned. Nevertheless, almost 20% of working age income support recipients now receive only part-payments through income support because they have separate earnings, even though the total earnings and income support payments are taxable.

The level of income support provided depends on the exact structure of the means test, which is meant to ensure that payments are targeted to those most in need. The test has two components: an assets test and an income test.

The assets test takes into account assets such as investments, motor vehicles, bank accounts and so on, but excludes the primary (family) home.

The income test is comprised of:

- a *free* area – the amount of private income a person can receive from earnings or other sources before their income support payment is reduced;
- a taper rate – the rate at which income support payments are withdrawn or 'tapered away' over the range of private income between the free area and the final cut-out point; and
- a cut-outpoint – the amount of private income at which a person ceases to receive any income support payment.

A tight income test (some combination of a low free area, a steep taper and a low cut-out point) ensures more accurate targeting of assistance to those with little or no income. But it can reduce the financial rewards from increasing private income (such as through earnings) through the interaction of the income test and increased tax liability. On the other hand, a generous income test (some combination of a high free area, a low taper rate and high cut-out point) will reduce the extent to which assistance is targeted to those with the lowest incomes while increasing financial rewards from working.

The best measure of the proportion of income that is lost through the dual application of taxation and an income test is the effective marginal tax rate (EMTR). High EMTRs reduce the incentive to work since people get to keep only a small amount of the additional income they earn. In some cases, the EMTR may become greater than 100 %, offering little or no incentive to undertake any work.

An increase in the EMTR may bring about two opposite effects:

- An 'income effect': whereby increases in the tax rate reduce the amount of disposable income from a given amount of work and therefore act to encourage greater work effort to make up for this loss; and
- A 'substitution effect': whereby the return for giving up an extra hour of 'leisure' in order to work has been reduced by the increase in the EMTR and therefore encourages people to work fewer hours.

The net effect on work incentives will depend on individual's preferences and their circumstances. Judging from what the FaCS has written, it appears inclined to consider that mothers who are only second income earners in a family are more influenced by the substitution effect; while primary earners are more influenced by the income effect.

EMTRs are not easy to calculate and although individuals may be aware of the general impact that any change to the system will have on the level of their income support payments, they are unlikely to know accurately what EMTR they face. However, a household survey by Australian Bureau of Statistics in 1998 showed that the way schemes are constructed and the effect that earnings may have on pensions and benefits is not necessarily the individual's major consideration in deciding whether or not to participate in the labour force. Non-financial factors are also important, such as self-



esteem, social contacts and work ethic. In addition, income support recipients may be influenced by the availability of other benefits. For example, the prospect of losing a concession card, which allow recipients access to cheaper public transport or health services: may be a greater disincentive to go off income support entirely than a high EMTR.

Although non-contributory schemes do not have specified wage replacement rates as an insurance scheme would have, it is still possible to assess the generosity of a scheme by using effective replacement rates, based, say, on average earnings as a proxy measure.

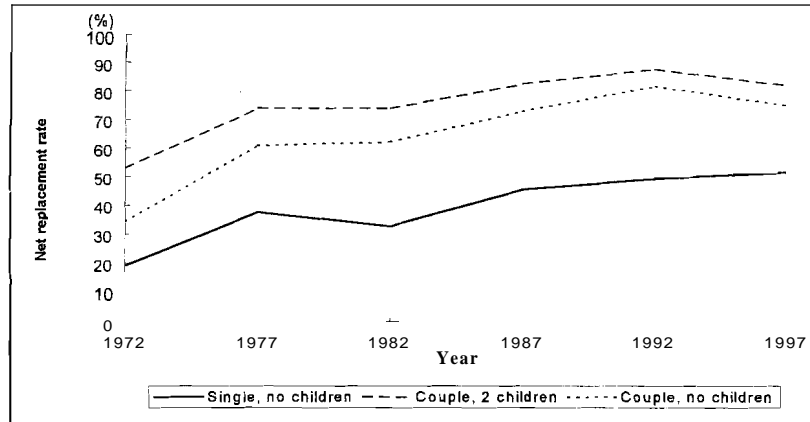
Until the 1970s, income support for those of working age in Australia was generally paid at a relatively low rate and there were few incentives to stay on unemployment benefits: During the 1970s, there were large increases in payment levels effectively pushing replacement rates much higher. Some of the increases took place in the early part of the decade when it was thought that the economy could afford to be more helpful to the poor. A national poverty inquiry in 1973 assessed the benchmark income required to support the basic needs of a family of two adults and two dependent children. Equivalence scales were devised for other types of family and government policy was designed to increase income support levels gradually, to the point where family income at least reached these levels.

Because of supplements payable for spouses and children, the higher replacement rates that began operating in the 1970s had their greatest impact on families that might have otherwise had only a single income earner. For larger families in these circumstances, total income support could often exceed the likely earnings from that person. In addition, supplementary benefits available to people who were renting privately could push the effective replacement rates even higher.

The introduction of means-tested family payments increased the attractiveness of lower-paid work to those with children although at the same time real income support payment rates continued to rise gradually, which offset the effect of the new family payments on replacement rates for families. As the following figure shows, typical replacement rates for families with children did rise during the 1980s, due largely to increases for people who were renting privately. Although the increases were more discernable for single people, again especially for those renting privately, they were from a low base.

It is evident from the figure that replacement rates are considerably higher for couples and families with children than for single people. This is inevitable given that the system is based on family need. However, it also means that welfare dependency is more likely to occur among larger families as they may face little net return from one low-paid full-time job and, if the costs of working are high (for example, transport or clothing costs), they may be no better off at all.

**Figure 5.3: Net replacement rates of income support versus minimum wage, various non-renter income unit types in Australia, 1972 - 1997**



Despite all of this, FaCS reports that Australia's net replacement rates (taking account of both taxation and other benefits) is actually comparatively low among OECD countries. For short spells of unemployment, Australia had the fourth lowest gross replacement rate for single people out of twenty-one OECD countries (1996) while replacement rates for couples were consistent with the OECD average. FaCS states that the "income floor set by income support payments in Australia is sufficiently low, relative to wages, to have had little impact on the supply of full-time workers (compared to other countries)".

Finally, it should be pointed out that although the Australian system is essentially needs-based, it still retains many features of a categorical system. The three most important categories to be considered here are the unemployed, the disabled and youth.

As with any system of unemployment insurance or unemployment assistance, the unemployed must face activity tests, that is, they must be available for work and, under various conditions, be willing to accept work that is offered to them. Immediate problems arise. Should a person be required to take work that is distant from their home and how is the term 'distant' to be defined? Should a person be required to undertake work that is not related to their experience or is at a low wage rate? Should they be expected to take up a 3-D jobs (difficult, dangerous, demanding)? The issue becomes especially relevant when considering how to deal with public works programs. In Australia, public works programs have come and gone in fashion (but are generally very poorly regarded) but they have never been treated as poverty programs per se. Wages have been set according to market standards for the work being undertaken. This has meant that public works programs could be used to administer activity tests. It would not be possible

to administer a pure poverty-related public works program in this way.

Activity tests in Australia have been increasingly tightened over the years and are now increasingly enshrined in the phrase "mutual obligation". Recently (March 2000) the Australian government announced its intention to further tighten the tests, making it obligatory for unemployment beneficiaries to accept *any* jobs offered to them. This new hardening of policy is taking place against a background of relatively strong economic growth. However, during periods of economic weakness and of slackness in the labour market, administering activity tests has special problems. The number of unemployed registered for work may be many multiples of the number of jobs notified to the national employment service. It is impossible under these circumstances to administer a tight test. The end result is that activity tests become most rigorously applied only at the same time as unemployment falls anyway as a result of economic growth. In effect, they mop up the least job ready, those who are probably the most welfare dependent.

The requirements faced by applicants for disability pensions involve medical tests designed to measure a person's impairment for work. Their conceptual basis is therefore quite different to that of activity tests. The following table shows the relative movements in the numbers of disability pensioners and unemployment beneficiaries over the years.

**Table 5.8: Number of recipients of income support in Australia, 1965-1998**

	1965	1970	1975	1980	1985	1990	1995	1997	1998
Disability pensioners									
Number	107,500	134,500	171,500	236,800	271,500	328,200	464,400	527,500	553,300
Annual rate of change		4.6%	5.0%	6.7%	2.8%	3.9%	7.2%	6.6%	4.9%
Unemployment beneficiaries									
Number	12,700	13,000	160,700	311,200	561,400	419,800	795,500	801,800	790,300
Annual rate of change		0.5%	65.4%	14.1%	12.5%	-5.6%	13.6%	0.4%	-1.4%
Ratio of DP/UB	8.46	10.35	1.07	0.76	0.48	0.78	0.58	0.66	0.70

The impact of the recession in the mid-1970s on unemployment beneficiaries is clear. Prior to that, unemployment was low, perhaps 1% or less, and the number of people with disabilities far outnumbered unemployment beneficiaries. Since then, the number of unemployment beneficiaries has fluctuated somewhat, partly to do with economic cycles and partly to do with changing rules on eligibility. But the number of people on disability pension has steadily increased, by a factor of 4.3 in the 30 years to 1995. Disability pensioners are heavily biased, virtually 2:1, in favour of males. The most common conditions of disability are musculo-skeletal and psychological/psychiatric, which between them make up just over 50% of all disabilities. 38% of all new approvals are in respect of people who are transferring from unemployment benefit.

On the face of it, then, the evidence suggests that the growth in disability pensions is one example of increasing welfare dependency, and one that is related to the underlying growth of unemployment in the last quarter century. FaCS now estimates that by 2006 over 750,000 people will be in receipt of a disability pension and that they will once again outnumber unemployment beneficiaries. Unlike unemployment benefits, however, changes to the regulations on disability pensions are not so easily implemented. Appendix 3 to the Interim Report on Welfare Reform in Australia highlights two patterns of income support receipt. One pattern *"is found among (mainly older) people who come onto payment and remain there until age pension or death. Payments that show this pattern includes Disability Support Pension... There is little turnover in the populations on these payments"*. Another pattern *"is found among people on (unemployment assistance). These payments have high population turnover, implying significant proportions of short-term receipt. It is common for people on these payments to intersperse periods on income support with periods of self-reliance"*.

The last category to be considered is young people. The impact of various income support measures on the activities of young people has long been debated. Because unemployment benefits were not insurance-based, people as young as 16 were eligible for benefits immediately they left school. This did not become a problem until youth unemployment rose as a result of circumstances in the mid-1970s but thereafter the policy came under heavy criticism for being a significant contributor to unemployment. Leaving aside the merits of the long debate that ensued, the consequence in the 1980s was a sharp improvement in allowances for students and a reduction in allowances for unemployed young people, especially those under the age of 18 years.

In the 1990s, youth unemployment rates remained high although the absolute number of young unemployed did decline because of dramatic increases in student retention. Youth have therefore been separated out in terms of income support. Student allowances and unemployment benefits have been brought together under a Youth Allowance, applying to people under the age of 21 years. The Youth Allowance is subject to an activity test, which requires beneficiaries to undergo a work test if they are unemployed or maintain full-time attendance in studies if they are students. In addition, the Allowance is subject to a parental means test as well as a personal means test. Exceptions apply, of course, for young people who must be considered as independent, such as those who are married or those, including single parents, who have dependents of their own.

## **Issues for Unemployment Assistance in Korea**

The main policy issue for Korea, unlike many other OECD member

countries, is not how to overcome the well-established problems that have developed in social protection systems for the unemployed but how to avoid them in the first place.

Those well-established problems faced in varying degrees by OECD members are:

- Persistent long-term unemployment;
- Increased reliance on income support;
- The polarisation of households into work-rich and work-poor;
- High levels of welfare expenditure;
- Financial disincentives to work;
- The impact of increasing part-time and temporary work in the labour market; and
- Changes to family structures, especially the growth in single parent families.

In effect, *development* in Korea and *reform* elsewhere should end up at similar points. Korea has already chosen to continue developing its unemployment insurance scheme, UIS, and to supplement it with a non-contributory scheme of assistance based on its existing Livelihood Protection Program. It has not chosen to avoid welfare dependency, clearly one of its major concerns, by avoiding or minimising welfare altogether; but it will still be necessary to proceed with caution.

The future of the UIS is perhaps more certain but even here issues of administration and management need to be considered. The first question to consider the extent to which the UIS and LPP are to be considered in the one administrative framework. The UIS, notwithstanding its 'insurance' tag, is really a first tier of social protection, a system of entitlements generated from contributions that enable a person to claim benefits not available to others. Controls are placed over the way that entitlements are established, much as they are now, for example by being limited in size and duration. In addition, there may therefore need to be tighter controls over the number and type of occasion on which compensation may be claimed; especially as Korea is increasing its labour market flexibility, one consequence of which could be higher labour turnover among the insured labour force. This will become important if the effective coverage of UIS does increase among smaller firms and if ways are found to extend UIS to day workers or part-timers. There would need to be restrictions on how many times compensation can be claimed, perhaps over some specified timeframe, or longer waiting periods may be needed.

It is also important to decide on the extent to which UIS should be self-contained and self-financing. Total monthly payouts exceeded total monthly contributions for a time during the crisis, but the reserves remained in surplus. They were, nevertheless, run down and had the crisis continued, or even if the level of unemployment had risen again, it would probably have proved impossible to protect them. If the UIS were to be regarded solely as an insurance scheme, it would not be possible to run an operational deficit,

or even allow the reserves to be exhausted, for anything other than short periods.

Strictly speaking, allowing long-term deficits to develop runs the risk of undermining the whole insurance of the scheme. However, unemployment insurance does not have the same operational basis as, say, health insurance where the risks are more easily spread over time. It is probably inevitable with unemployment insurance that a government would want to provide financial support to the system during economic downturns; and even more obviously during periods of crisis or sharp economic adjustments. Nevertheless, it is still important, especially when government comes to consider changes in guidelines, to know how-self-contained the UIS should be. Short-term changes that are inconsistent with the longer-term sustainability of the system would not seem desirable.

If the system is not to be self-contained, there will be a disconnection between the guidelines governing contributions and the guidelines governing compensation, the one not really governing the financial viability of the other. In this case, the contributions, no matter how separately accounted for, are really another form of taxation and could just as easily be paid into consolidated government revenues, with the system operating more closely akin to a partly-funded system of unemployment assistance.

This raises questions about the conjunction of the two schemes, UIS and LPP. The Australian experience, and probably the wider OECD experience as well, suggests that welfare dependency becomes generated among people who would not have UIS entitlements to begin with. They are precisely the sort of marginal workers, often working in the informal sector, who suffered most during the 1997-99 crisis in Korea.

The threshold issue to consider is the level of assistance to be provided under the two schemes. In 1998, the estimated monthly cost of a minimum consumption basket for an average household was about W 800,000. This was about 50% of average earnings, which were about W 1.5 million during that year. The average payment to UI beneficiaries throughout the year was W 578,000 per month; about 40% of average wages.

However, there were substantial differences in earnings across different employer groups:

- Monthly earnings in larger companies were W 1.7 million; 115% of average wages;
- Monthly earnings in smaller companies (10-29 employees) they were W 1.2 million; 80% of average wages;
- For companies with fewer than 5 employees, the average monthly wage was only W 600,000; 40% of average earnings.
- The national public works program introduced during the crisis allowed 20 days work a month at 23,000 won per day giving a maximum of 460,000 won a month; 30% of average wages.
- The original (pre-crisis, local government-based) public works program restricted work to 15 days a month at a going rate of about 17,000 won

per day giving a maximum of 205,000 won a month; 15% of average wages;

These figures are meant to give broad comparisons only and can hardly be considered precise. But they suggest some sort of floor to the level of assistance that may be provided. Ideally, that might be one of the possible measures of poverty that could be derived but whether that would be affordable, let alone desirable, is doubtful. An expansion of the LPP at an effective replacement rate of 25% of average earnings would have a noticeable budgetary impact and yet still provide support at a relatively low level compared to the minimum consumption basket.

At present, the priority would seem to be an extension in the coverage of the scheme rather than an improvement in benefits to those already receiving assistance. As we noted previously, the basic LPP is biased towards areas outside Seoul, while the established public works program is biased towards Seoul. The essential difference here is not the nature of the two schemes but their different sources of financing, national and local government. Local governments do have a role in the delivery of social protection, perhaps even more so than national agencies, but they cannot finance it to any significant extent. An extension of national policies and the financing of national programs would seem to be called for.

The relative levels of earnings and benefits also suggest that replacement rates of 50% for UIS are reasonable and affordable provided the 1% contribution rate remains unchanged. But they are probably as high as they should be. At these replacement rates, higher income earners, for example, would be receiving amounts sufficiently in excess of minimum consumption costs; and even lower income earners could be receiving significant, though not necessarily adequate, contributions to household incomes during periods of unemployment. Even if there were an effective replacement rate for LLP of 25% of average earnings, there would therefore be a significant difference between the two, a forceful incentive to take out insurance; in effect an incentive to join the formal sector of the economy.

Finally, we should consider the use of categories, or target groups, to define eligibility for assistance. Even when governments establish poverty-related programs, they usually find it expedient to define target groups rather than rely solely on means test to determine the most needy. In fact, avoiding the use of categories entirely is really impossible. The question becomes whether the categories do identify groups more likely than others to be in need. Even when they do, of course, there will still be a leakage of assistance to those who are not in need. The example of the 1999 guidelines for the extended public works program, in which the highly skilled were established as the preferred target group, is a good example of a misplaced target group in this respect. Whether there is a substantial political or social significance to be attached to a target group is, of course, another question.

Of the categories that could be of concern youth may be the most important. This has not been the case so far in Korea where the emphasis has

been on supporting skilled workers first and adult heads of households second; and whether youth unemployment does become a problem in Korea remains to be seen. But there is little doubt from international experience that the incentives between work and education and the relative roles of the individual and parents are of great importance. Unless this experience is to be entirely dismissed, youth issues will grow in importance in the coming years.

We should conclude by observing that the relevance to Korea of any international experience has to be considered very closely indeed. Developments in Korea are not moving in the same direction as much of the OECD. This not because it is pursuing different objectives but because it is coming at them from a different starting point. Fortunately for Korea, its starting point in policy terms is better placed.



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# 6 Assessing the Coverage and Effectiveness of the Wage Claim Guarantee System in Korea

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## Introduction

The financial crisis that emerged in late 1997 directly led to the rapid deterioration of the labor market in Korea. During the ensuing period of turmoil, a substantial number of workers were laid off without receiving wage arrears and retirement allowances, as their employers suddenly found themselves bankrupt and unable to pay.

The need for a social mechanism that protects the livelihood of laid-off workers and their families has, in fact, been long-standing in Korea. Prior to 1998, employees were not able to receive wage arrears and retirement allowances in cases where companies were found insolvent and financially incapable of paying their debts, even though there is a procedure to sell certain assets possessed by bankrupt companies through various channels.

For this reason, on July 1, 1998, the Korean government introduced the wage claim guarantee system and set up the Public Compensation Fund for insuring payment of retirement allowances and wage arrears. The major objective of the wage claim guarantee system is to provide basic livelihood stability for workers laid off from bankrupt companies. Under the system, workers laid off without pay can claim wage arrears and retirement allowances within a fixed limit from the government, which acts on behalf of financially insolvent employers.

The purpose of this study is to assess the effectiveness of the wage claim guarantee system and to propose directions for further improvements by examining any implementation problems. This paper is organized as follows.

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The next section describes the background of the introduction of the wage claim guarantee system by briefly reviewing the preferential reimbursement for wage claims in the Labor Standards Act as well as its content, nature, and relationship with the employment insurance system. Then, the paper evaluates the wage claim guarantee system by analyzing the data on employees who have received wage arrears and retirement allowances through the system. The final section summarizes the results and proposes policy directions.

## **The Wage Claim Guarantee System in Korea**

### *Background of the Wage **Claim** Guarantee Fund*

There are various reasons for the preferential treatment of workers' claims when an enterprise becomes insolvent.<sup>1</sup> First, workers' claims are likely to be the only source of family income for laid-off workers. Second, workers' claims can often lack an institutional shield because workers are in a less favorable position than the other external creditors. And finally, there is no possibility of shared liability for workers' claims since the employer is the only debtor for these claims.

The preferential or privileged treatment scheme ranks wage claims and other claims ahead of the claims of certain other creditors in the insolvency proceedings according to general preference, special preference, and super-preference. The wage guarantee institution scheme, which seeks to offset any shortcomings of the preferential treatment scheme, guarantees workers' claims by operating a guarantee institution according to the methods applied in social insurance schemes.

In Korea, workers' claims generally had been protected by a Labor Standards Act provision, which stipulates that "wages, retirement allowances, accident compensation and other claims arising from employment shall be paid in preference to other claims as to the total property of an employer except for pledges, mortgages, taxes, and public levies" (Presidential Emergency Measure No. 3, Article 19; on January 14, 1974). On December 24, 1974, the Labor Standards Act was revised with the insertion of Article 30-2, stipulating that "workers with wage claims and other labor-related claims have prior claim to employers' assets. However, these claims do not precede the right of pledges, mortgages, taxes, public levies and other equivalent claims." The special preference of workers' claims was amended further on four later occasions (Dec. 31, 1980; Nov. 28, 1987; Mar. 29,

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<sup>1</sup> Edward Yemin and Arturo S. Bronstein (eds.), *The Protection of Workers' Claims in the Event of the Employer's Insolvency*, Labour-Management Relations Series, International Labour Office, Geneva, 1991.

1989; and Dec. 24, 1997). Finally, the workers' claims that fall under the special preference category are wages for the final three months of employment, retirement allowances for the final three years of service, and accident compensation. These claims take precedence over any obligations, taxes, public levies and other claims secured by pledges and mortgages.

As a measure to cope with the economic crisis that erupted at the end of 1997, the Tripartite Commission was set up on January 15, 1998. The Commission adopted the "Tripartite Joint Statement on Fair Burden Sharing in the Process of Overcoming the Economic Crisis" on January 20, 1998. It also announced "The Social Agreement for Overcoming the Economic Crisis" on February 6, in which the wage claim guarantee system was conceived. The process for legally institutionalizing the wage claim guarantee system transpired as follows. Enactment of the Wage Claim Guarantee Act (Law No. 5,513) occurred on February 20, 1998, and the Enforcement Decree of the Act (Presidential Decree No. 15,804) was promulgated on May 26 of the same year. The Enforcement Regulations of the Act (Ministry of Labor Regulation No. 131) was enacted on June 15, and the wage claim guarantee system entered force on July 1, 1998.

### *Characteristics and Contents of the Wage Claim Guarantee System<sup>2</sup>*

The wage claim guarantee system, based on the Wage Claim Guarantee Act, is a subrogated payment system. In the case of bankruptcy of a business or insolvency of an employer, a worker's deferred wages and retirement allowance are reimbursed up to a fixed ceiling amount by the Wage Claim Guarantee Fund in lieu of payment by the employer in order "to contribute to the stabilization of workers' livelihood by seeking measures which guarantee the wage payment for the workers who retired with their wages unpaid because the company is not able to continue its business or its management is unstable due to fluctuations of the economy and changes in industrial structure, etc. (Article I of the Act)."

There are two types of insolvency subject to subrogated payments (Article 6, Paragraph 1 of the Act): judicial insolvency as per a court decision according to the pertinent law and actual insolvency due to closure following deterioration of business activities. Judicial insolvency providing legitimate cause for subrogated payments refers to: (1) an adjudicated bankruptcy according to the Bankruptcy Act; (2) a decision on the start of composition according to the Composition Act; and (3) a decision on the start of reorganization according to the Company Reorganization Act. As such, the reasons for subrogated payments cease to exist when the procedures are completed, i.e., (1) when a judgment of composition is finalized (Article 58 of the Composition Act) and (2) when the procedure of

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<sup>2</sup> This section refers to Lee, Jeongjo, *The Introduction of the Wage Claim Guarantee System*, Jooangkyungje, Seoul, 1999 (in Korean).

reorganization is completed (Article 271 of the Company Reorganization Act).

Actual insolvency, which is usually not judicial insolvency but rather virtual insolvency depending on the state of insolvency in practice, is confirmed by the head of a local labor administration. Its real conditions (Article 8 of the Enforcement Decree of the Act) are that there is no ongoing business activity, there is no prospect for the resumption of business, and the employer has little or no financial capability of paying wages or retirement allowances.

The government takes full charge of the wage claim guarantee system, but administrative work is entrusted to the local labor administration and the Korea Labor Welfare Corporation (Article 24 of the Enforcement Decree of the Wage Claim Guarantee Act). The local labor administration is responsible for issuing the certification of bankruptcy, examining whether those companies applying for bankruptcy status meet the requirements for subrogated payments, receiving the necessary documents submitted by the company owners, and supervising these companies. The Korea Labor Welfare Corporation (1) collects contributions from employers, (2) provides subrogated payments for workers who satisfy the conditions for deferred payments, (3) exercises the right to claim wages and retirement allowances from employers within the limit of subrogated payments already made to the workers, and (4) reclaims any payments made to those who submit false applications by ordering repayment.

In general, the payment of debts by a third party as prescribed by Article 469 of the Civil Code depends on the types and the nature of the debts and, when the debtor expresses an objection, the third party may not pay the debt on behalf of the debtor. The government's subrogated payment to workers is based on a political measure to protect the livelihood of workers. Article 6 of the Wage Claim Guarantee Act authorizes the government to pay a fixed amount of wage claims regardless of the opinion of the employer, overriding Article 469 of the Civil Code. When the government pays deferred payments to workers, the employer is released from his/her duty to pay workers and instead the government obtains the right of indemnity against the employer. Thus, the government then has claims against the employer within the amount of subrogated payments made to workers.

The Wage Claim Guarantee Act applies to the same category of businesses or business establishments as prescribed in Article 5 of the Industrial Accident Compensation Insurance Act (Article 3 of the Wage Claim Guarantee Act). Article 2 of the Wage Claim Guarantee Act defines workers as prescribed in Article 14 of the Labor Standards Act, which stipulates, "... a person engaged in whatever occupation offering work to a business or workplace for the purpose of earning wages." The determination and administrative interpretation of the definition of a worker in the Labor Standards Act depends on whether the labor is actually provided to employers at businesses or workplaces in exchange for wages, and whether

the work is conducted under a subordinate relationship, regardless of the form of the employment contract. In other words, determination does not look to whether it was an employment contract or a work contract under the Civil Code.

Conditions for subrogated payment are that a worker should have retired or should retire from the pertinent company within one month before or within one year after the bankruptcy of the company and that the petition for the confirmation of insolvency was filed (Article 7 of the Enforcement Decree of the Act). The range of workers' claims protected under the guarantee system has been a matter of legislative policymaking. The amount of wage claims guaranteed under the Act is identical to the amount guaranteed in the Labor Standards Act, i.e., "the amount of wages for the last three months and the retirement allowance for the last three years"(Article 37, Paragraph 2). As in most countries, Article 6, Paragraph 1 of the Enforcement Decree defines the ceilings of the subrogated payment both for one month's wage and for one year's retirement allowance according to age groups.<sup>3</sup>

Article 15 of the Act allows the Minister of Labor to establish the Wage Claim Guarantee Fund to fill up the subrogated payment as prescribed in Article 6. Article 16, Paragraph 1 of the Act defines the financing of the Wage Claim Guarantee Fund.<sup>4</sup> Also, Article 4 of the Act defines the defrayal from the State Treasury as follows: "that the State shall, within the budget of every fiscal year, provide some parts of the expenses, which are required in enforcing the activities for guaranteeing the wage claims under the Act, from general accounting."

According to Article 8 of the Act, the Minister of Labor collects defrayal from the employer equivalent to two-thousandths of the total wage in order to compensate for the expenses required in paying the deferred wages and retirement allowances as prescribed in Article 6. The Act enforces the defrayal by the employer of the concerned business without any compensation to the employer, which makes it different from insurance premiums. In other words, the defrayal is collected from employers at a fixed rate regardless of the possibility of insolvency, while the insurance premium is calculated at varying rates depending on the extent of risk-bearing.

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<sup>3</sup> 800,000 Korean won for retired workers less than 30-years of age, 1 million won for retired workers 30-years of age or older but less than 45, and 1.2 million won for retired workers 45-years of age or older.

<sup>4</sup> The money redeemed by employers as provided by Article 7 (acquisition of the request right to deferred wages); charges paid by employers as provided by Article 8 (defrayal by employer); loans from special financial accounting, financial organizations or other funds on the security of the Wage Claim Guarantee Fund provided by Paragraph 2 of Article 16; revenue accrued from operation of the fund; and other revenues.

Article 9 of this Act states that the Minister of Labor may lighten the charges, as stipulated in Article 8, for an employer under retirement insurance, etc., under Article 34, Paragraph 4 of the Labor Standards Act. The purpose is to promote equality with regards to the defrayal by the employer considering the possible and stable payment of the retirement allowance through the financial system when the employer participates in retirement insurance, etc. It is a measure to emphasize the role of the government in promoting the operation and development of the wage claim guarantee system. The employers who implemented a policy of retirement insurance, etc. for all employees as beneficiaries as of the end of the previous year, as prescribed in the Labor Standards Act, qualify for a reduction in defrayal. This provision aims to provide balanced consideration for employers, for in this case external financial institutions pay retirement allowances to their employees on their behalf.

### *Other Systems Related to the Wage Claim Guarantee System*

The wage claim guarantee system mainly focuses on the social protection of workers' livelihood. The retirement allowance system, the employment insurance system, and the national pension fund system have a similar purpose. The retirement allowance system maintains the stability of retired workers, the employment insurance system guarantees the security of the unemployed, and the national pension fund system secures workers' livelihood during the post-retirement period.

The retirement allowance and employment insurance systems are of direct relevance to the wage claim guarantee system. Retirement allowances are monetary payments made to a worker by an employer when a practical labor relationship is terminated. The payments cover not only deferred wages but also social security and rewards for meritorious service. The retirement allowance system was introduced through a provision in the Labor Standards Act of 1953 in order to guarantee the income level of retiring workers. Article 34 of the Labor Standards Act stipulates that "an employer shall establish a retirement allowance system whereby an average wage of more than 30 days shall be paid to a retired worker as a retirement allowance for each year of the number of consecutive years employed; however, if the worker was employed for less than one year, this shall not apply."

The retirement allowance system in Korea has unique features that are not prominent in other countries. It has the characteristics not only of a private welfare system but also of a public welfare system. The Korean system seeks to meet the need levels of household expenditures at each stage of the lifecycle beyond a simple guarantee of income security during the post-retirement period. Nonetheless, it bears an aspect of inequity in the sense that some workers benefit from the progressive accumulation of retirement allowances while many others are left out of the system. There have been

arguments that the legal retirement allowance system should be changed into a voluntary system when the national pension fund system and the employment insurance system were introduced. In practice, the retirement allowance system and the national pension fund system are closely related to each other. Revisions will inevitably need to be made to the current retirement allowance system as some deposits of the retirement allowance are transferred to the national pension fund system.

Another role of the retirement allowance system to ensure livelihood of the unemployed using a mid-term settlement scheme of retirement allowance was undertaken by the employment insurance system. The first government-level discussion on the introduction of employment insurance took place when the unemployment rate began to rise in late 1979 and 1980 due to political instability and economic recession. In the process of preparing for the 5<sup>th</sup> Five-Year Economic and Social Development Plan in the early 1980s, the unemployment insurance system underwent the beginnings of an official examination, but this was put off indefinitely because of the possibility of negative side effects.

The introduction of employment insurance went through a full discussion during the 7<sup>th</sup> Five-Year Economic and Social Development Plan in the early 1990s. The Employment Insurance Act was enacted in 1993 and went into force on July 1, 1995. It was amended in December 1998 to increase the minimum amount and the minimum benefit period for unemployment benefits. Further revision took place in September 1999 in order to extend the coverage of employment insurance. At the time of the first revision, it applied to business establishments with 30 employees or more, but it began to cover all workplaces from October 1998.

The employment insurance system in Korea consists of the Employment Stabilization Program, Job Skills Development Program and Unemployment Benefits. It is a preventive and active policy scheme for the stabilization and restructuring of the labor market and the enhancement of vocational training. Recent economic crisis and high unemployment rates have proven its importance as an active labor market policy. Despite its role as an ALMP measure, the employment insurance fund is raised and maintained with contributions from employers and employees.

The coverage of the employment insurance system in Korea has expanded rapidly. In particular, coverage was extended to cope with the ever-rising mass of unemployment after the economic recession and nationwide restructuring. The number of work places covered was increased from 43 in 1995, the first year it was introduced, to 664 in October 1998. Also, the number of workers covered increased from 4,280,000 to 8,342,000. 89 % of companies were covered by employment insurance as of September 30, 1999. Of the entire qualifying workforce, 71 % is currently covered by employment insurance. Despite the rapid expansion of the employment insurance system, the number of beneficiaries of unemployment benefits stood at 147,000 as of June 1999, a mere 12.8 % out of 1,356,000 unemployed. The re-employment

rate for the recipients of unemployment benefits is lower than that of non-recipients.

## Empirical Analysis

### *Basic Statistics*<sup>5</sup>

Between the time the Wage Claim Guarantee Act was promulgated (July 1, 1998) and December 1999, a total of 54.9 billion won was paid out to 17,727 workers laid off from 460 bankrupt companies.<sup>6 7</sup> On average, laid-off workers received 3.2 million won each, whereas the average work place received 119.4 million won (Table 6.1). For the year 1999, 12,588 workers displaced from 360 insolvent companies received wage arrears and retirement allowances totaling 38.8 billion won. On average, this translated into 107.8 million won per work place and 3.1 million won per worker.

Table 6.1: Amount and accumulated records of subrogated payments in Korea, 1998 and 1999

Period		Number of workplaces surveyed	Number of beneficiaries (persons)	Amount (won in millions)
1998	3 <sup>rd</sup> qtr	15 (3%)	378 (2%)	1,148 (2%)
	4 <sup>th</sup> qtr	85 (19%)	4,261 (25%)	14,974 (27%)
	Subtotal	100 (22%)	4,639 (27%)	16,122 (29%)
1999	1 <sup>st</sup> qtr	82 (18%)	3,314 (19%)	10,754 (20%)
	2 <sup>nd</sup> qtr	96 (21%)	4,257 (25%)	12,603 (23%)
	3 <sup>rd</sup> qtr	98 (21%)	2,707 (16%)	8,436 (15%)
	4 <sup>th</sup> qtr	84 (18%)	2,310 (13%)	7,020 (13%)
	Subtotal	360 (78%)	12,588 (73%)	38,813 (71%)
Total		460 (100%)	17,227 (100%)	54,935 (100%)

Source: Korea Labor Welfare Corporation.

<sup>5</sup> The population used in the analysis includes all workers who benefited from the wage claim guarantee system during the period between the time of implementation and December 1999.

<sup>6</sup> Korea Labor Welfare Corporation, "Performance Report of the Wage Claim Guarantee Act, 1999" (Press Release), January 2000.

<sup>7</sup> Subrogated payment is a legal term that refers to the third-party payment of debts on the condition that the debtor will make reimbursement at a future date. In the case of the wage claim guarantee system, the government pays a portion of deferred payments (a maximum of 3 months wages and 3 years retirement allowances) to workers in advance, which later will be collected from the employer.



According to this data on about 14,031 workers who received deferred wages through the system (the Korea Labor Welfare Corporation)<sup>8</sup>, the total amount of deferred payments was 53.6 billion won, or 3.8 million won per worker (Table 6.2).<sup>9</sup> Deferred payments are largely divided into two categories: for deferred wages, a total of 22.2 billion won (41.3 % of the total amount paid) were distributed to 11,787 workers, or 1.9 million won per worker; for deferred retirement allowances, 10,553 workers received a total of 31.5 billion won (3.0 million won per worker).

**Table 6.2: Subrogated payments made by type (wages and retirement allowances)**

	Number of workers (persons)	Total amount (won in millions)	Average amount (won in thousands)
Subrogated payment	14,031	53,614 (100%)	3,821
Wages	11,787	22,156 (41%)	1,880
Retirement allowances	10,553	31,457 (59%)	2,981

Source: Calculation of the data from Korea Labor Welfare Corporation

The workers that benefited from the system break down to 10,033 male workers (71.5 % of the total) and 3,998 female workers (Table 6.3). In terms of amount, male workers received 4.4 million won on average, accounting for 81.9 % of the total payment, while each female worker received 2.4 million won. This difference is mostly due to the fact that male workers on average served longer years and thus received higher wages than their female counterparts under the same conditions, and also, the average age of the former is higher than that of the latter.

**Table 6.3: Subrogated payments by gender**

Gender	Number of workers (persons)	Total amount (won in millions)	Average amount (won in thousands)
Male	10,033	43,919	4,378
Female	3,998	9,694	2,425
Total	14,031	53,613	3,821

Source: Calculation of the data from Korea Labor Welfare Corporation.

<sup>8</sup> The analysis results in this paper based on the personal information data differ from the data published by the Korea Labor Welfare Corporation, mostly due to differences in reference periods for data collection. Other reasons for data discrepancies may be that duplicate observations were eliminated and that the provided data did not cover all the workers that benefited from the system. However, these discrepancies are not considered critical in the analysis of workers' characteristics.

<sup>9</sup> This is a significant amount in comparison to 2,278,000 won, the average amount of unemployment benefits paid to the workers (approx. 306,000 workers) whose unemployment benefits ended in 1998.

The 24 and under age bracket accounted for 11.0 % of the total beneficiaries while those between 25 and 29-years of age accounted for 17.8 %, proportionately higher than the other age groups. (Table 6.4) The average amount of deferred payment received increases with each age bracket up to 55, after which it drops. This is due to the fact that wages (and retirement allowances) are in proportion to age. The drop in the deferred payment received by the over 55 age group also agrees with the typical age-earnings profile. Workers up to the age of 55 received wage arrears and retirement allowances in a proportion reasonable to their age.

**Table 6.4: Subrogated payments by age group**

Age group	Number of workers (persons)	Total amount (won in millions)	Average amount (won in thousands)
15-19	180	227	1,261
20-24	1,367	3,024	2,212
25-29	2,500	6,845	2,738
30-54	8,700	39,499	4,540
Over 55	1,284	4,019	3,130
Total	14,031	53,614	3,821

Source: Calculation of the data from Korea Labor Welfare Corporation

By type of insolvency, 6,317 workers (or 45 % of the total) were able to claim their deferred pay on the basis of judicial insolvency, while the remaining 7,714 received it on the basis of the confirmation of insolvency from relevant authorities (Table 6.5). In terms of the amount of deferred payment, judicial insolvency cases accounted for 51.6 % of the total. Therefore, the average amount of deferred payment (4,379,000 won) was higher than that of other cases (3,361,000 won). The main reason for this may be that the latter case applied mostly to small- and medium-sized companies, where wages are relatively low compared to large corporations.

**Table 6.5: Subrogated payments by type of insolvency**

Type of insolvency	Number of workers (person)	Total amount (won in millions)	Average amount (won in thousands)
Judicial insolvency	6,317 (45%)	27,663 (51.6%)	4,379
Confirmation of insolvency	7,714 (55%)	25,951 (48.4%)	3,364

Source: Calculation of the data from Korea Labor Welfare Corporation.

In cases where laid-off workers received deferred payments based on the confirmation of insolvency and others, their personal data also provide the type and size of their employer companies. As this confirmation system was designed for small- and medium-sized companies, thus inapplicable to large

corporations, most companies studied had 300 employees or less. According to Table 6.6, the largest proportion of companies (40.1 %) had 30-99 employees (accounting for 39.7 % in terms of the amount of deferred payments), followed by those with 100-299 employees (21.6 %). Companies with 4 employees or less accounted for 9.0 %. The average amount of deferred payment received does not show any evident pattern depending on company size. The highest average amount was 3.5 million won for those with 10-29 employees.

**Table 6.6: Subrogated payments by firm size (confirmation of insolvency)**

Firm size	Number of workers	Total amount	Average amount
	(persons)	(won in thousands)	
4 or less	694 (9.0%)	2,154 (8.3%)	3,105
5-9	286 (3.7%)	996 (3.8%)	3,481
10-29	1,963 (25.4%)	6,947 (26.8%)	3,539
30-99	3,090 (40.1%)	10,309 (39.7%)	3,336
100-299	1,665 (21.6%)	5,504 (21.2%)	3,305
300-499	16 (0.2%)	41 (0.2%)	2,551

Note: Numbers in parenthesis are % of the total.

Source: Calculation of the data from Korea Labor Welfare Corporation.

### *Descriptive Analysis of the Survey*

In order to further study the effectiveness of the wage claim guarantee system, a survey was given to 423 workers from 47 business companies who had benefited from the system.<sup>10</sup> The survey includes 288 male workers (68.1 %) and 135 females, which is quite comparable to that of the population who received deferred payments through the wage claim guarantee system (71.5 % male). By age, those between 15 and 19-years old accounted for 3.3 % of the survey group; those between 20 and 24-years old, 8.7 %; and those between 25 and 55-years old, 85.1 %. This distribution breakdown is also quite similar to the age distribution of the entire group of workers who benefited from the wage claim guarantee system. Respondents to this survey consist of 83 workers (19.6 %) with elementary or middle school education, 162 (38.3 %) with high school education, and 165 (39 %)

<sup>10</sup> The survey took place between Feb. 14 through Feb. 25, 2000. The survey questionnaire for workers includes: information on workers, their families and employers; the size of deferred wages and retirement allowances; the actual amount of wage arrears and retirement allowances received through the system; difficulties experienced in the course of claiming deferred payments through the system; the general assessment of the wage claim guarantee system; and others. The survey questionnaire for employers includes: the details of the company; main causes for insolvency and the type of insolvency; the amount of deferred wages and retirement allowances; efforts made to sustain business; whether a retirement allowance fund was set up; and the assessment of the current wage claim guarantee system.

with junior college or higher education." The proportion of those with junior college or higher education is greater than that of the educational distribution of the economically active population of Korea in 1999. This indicates that the majority of the beneficiaries of the wage claim guarantee system were not workers with lower-level education.

By occupation, executives and professionals accounted for 11.8 %; technicians and semi-professionals, 26.7 %; office and service workers, 27.9 %; skilled workers, 10.6 %; and machine operators and simple manual workers, 16.8 %. This indicates that a larger proportion of workers with higher education, such as executives, professionals and technicians, have benefited from the wage claim guarantee system compared to the occupation distribution of the entire economically active population. By type of employment status, 373 (88.2 %) were regular workers while temporary and daily workers accounted for a very small number. Since more than half of paid workers in Korea are temporary or daily workers, these figures also represent a much higher proportion of regular workers.<sup>12</sup>

The sample in the survey can be broken down by job tenure. Those with tenure of less than a year accounted for 25.1 %; those with between 1 year and 3 years of tenure, 32.2 %; and those with tenure of between 3 and 5 years, 22.0 %. Approximately 80 % of the workers worked for less than 5 years. However, those who worked 10 years or longer accounted for a considerable 6.6 %.

In terms of work hours, those who worked 18 hours or less per week accounted for 12.8 %. The majority (86.1 %) of the survey group worked 36 hours or more per week. This is another indicator that the majority of the survey group worked full time, as shown in the case of previous work types, and hence it appears that the number of temporary workers is very small.

As one of the main objectives of the wage claim guarantee system is to protect the livelihood of low-wage workers, it is necessary to look at information about their household as well. First, 70.2 % of the survey group were married and living with a spouse, while 29.8 % were either married but not living with a spouse, or single. Also, 18.0 % of the workers in the survey group had four persons or more to support; 31.0 %, three persons; and 18.7 %, two persons. These figures all illustrate the need to take a closer look at workers' households when studying how the wage claim guarantee system affects worker livelihood.

The survey did investigate whether the worker was the head of household or not; and whether any other member of the household was engaged in economic activities and if so, how much they were paid. For the first

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<sup>11</sup> The remaining 3.1 % answered "Others" to this question or did not respond.

<sup>12</sup> One reason for this might be found in the common practice whereby an employment relationship is terminated in the case of temporary or daily work if the wage is deferred continuously.

question, 60.0 % of the workers in the survey group were the head of their household while the remaining 40.0 % were not. (Table 6.7)

**Table 6.7: Characteristic data of workers and their households**

	<i>Total</i>	<i>Head of household</i>	<i>Non-head of household</i>
<i>Total</i>	423 (100.0%)	254 (60.0%)	169 (40.0%)
<i>Individual income: over 1.5 million won</i>	42 (9.9%)	36 (8.5%)	6 (1.4%)
<i>Income of other family members</i>			
<i>Over 1.5 million won</i>	4 (0.9%)	1 (0.2%)	3 (0.7%)
<i>Less than 1.5 million</i>	7 (1.7%)	5 (1.2%)	2 (0.5%)
<i>No income</i>	31 (7.3%)	30 (7.1%)	1 (0.2%)
<i>Individual income: less than 1.5 million</i>	156 (36.9%)	95 (22.5%)	61 (14.4%)
<i>Income of other family members</i>			
<i>Over 1.5 million won</i>	14 (3.3%)	3 (0.7%)	11 (2.6%)
<i>Less than 1.5 million</i>	47 (11.1%)	23 (5.4%)	24 (5.7%)
<i>No income</i>	95 (22.5%)	69 (16.3%)	26 (6.1%)
<i>Individual income: None</i>	225 (53.2%)	123 (29.1%)	102 (24.1%)
<i>Income of other family members</i>			
<i>Over 1.5 million won</i>	46 (10.9%)	13 (3.1%)	33 (7.8%)
<i>Less than 1.5 million</i>	70 (16.5%)	31 (7.3%)	39 (9.2%)
<i>No income</i>	109 (25.8%)	79 (18.7%)	30 (7.1%)

In the following part of this section, the surveyed workers will be divided into several categories depending on the employment of the workers and that of their household members as well as the amount of monthly income. The distribution of these categories will also be examined.

First, those who were the head of household and were currently employed with a new employer accounted for 31.0 % of the survey group. The remainder of the survey group were either still unemployed or economically inactive. However, out of this 31.1 %, a mere 8.5 % were employed with monthly pay exceeding 1.5 million won. The remaining 22.5 % received less than 1.5 million won per month.<sup>13</sup> This is not regarded as a sufficient amount to sustain the normal living of a household.

Although they received less than 1.5 million won, 6.1 % of the survey group (among the 22.5 % with monthly pay of less than 1.5 million won) had other income sources, since other members of their household were employed. However, the remaining 16.3 %, out of the 22.5 % had no other

<sup>13</sup> The caveat against the income report is that it is highly likely that the amount of wages reported through the household survey tends to be underreported.

income source. In this case, their income was the sole income source for the entire household and clearly insufficient to maintain the livelihood of the household.

Second, those who were heads of household and unemployed accounted for 29.1 % of the survey group. This breaks down to unemployed heads of household with no employed family members (18.7 %) and unemployed heads of household with other employed family members (10.4 %). However, even in the latter case, 7.3 % of the survey group fell into the category where the collective income of other family members was short of 1.5 million won.

Third, those who were not heads of household and who were currently employed accounted for 15.8 % of the survey group. However, 6.2 % of the survey group were those with monthly wages of less than 1.5 million won and with no other employed family members. So these also constitute cases where there is insufficient income to maintain the livelihood of the household.

Fourth, those who were not heads of household and unemployed accounted for 24.1 % of the survey group. Specifically, those workers whose family members were also unemployed accounted for 7.1 %. Even when other family members were employed, 9.2 % of the survey group lived on a monthly income of less than 1.5 million won.

In conclusion, households with no income source accounted for 25.8 %, and households with one employed family member (either the interviewed worker or another member), but with a monthly income of less than 1.5 million won, accounted for 39.0 %. These households, which collectively amount to 64.8 % of the survey group, clearly fall below the subsistence level. A significant proportion of the beneficiaries of the wage claim guarantee system are professionals or skilled workers with relatively higher education in comparison to the distribution of the entire economically active population. However, the income of these households was very low (at the time of survey), and thus in urgent need of other measures or other sources of income.

Deferred payment refers to the total sum of wage arrears and retirement allowances that has not been provided on time. For 21.8 % of the survey group, the total amount in arrears was less than 1 million won; for 24.2 %, it was less than 2 million won (but more than 1 million won); and for 15.9 %, it was less than 3 million won. However, those who had not received deferred wages exceeding 5 million won accounted for 15.3 % of the survey group, indicating that a substantial number of workers were laid off without receiving a sizeable amount of wage arrears. In terms of the number of months during which wages are deferred, the highest proportion, 33.1 % of the survey group, had three months of wages in arrears; followed by 24.5 % with one month of wages in arrears; and 10.8 % with two months in arrears. Also, those with four months of wages in arrears accounted for 31.7 %. Since the maximum amount of deferred wages that is provided under the

wage claim guarantee system is 3 months of wages, these people cannot expect to receive the full amount. In terms of the amount of deferred retirement allowances, those with less than 1 million won accounted for 14.5 % of the survey group; less than 2 million won (but more than 1 million won), 20.2 %; and less than 3 million won, 22.2 %. Furthermore, 12.5 % of the surveyed workers had deferred retirement allowances exceeding 5 million won. The total amount of deferred payments, which is the sum of deferred wages and deferred retirement allowances, varied between less than 1 million won (13.9 %), less than 2 million won (13.9 %), and less than 3 million won (13.2 %). In particular, surveyed workers with a total deferred payment exceeding 5 million won amounted to 38.3 % of the survey group.

The average per capita amount of the combined deferred payments was 4.4 million won (based on a sample group of 423 workers). The average amount of deferred wages was 2.6 million (a sample group of 372), while the average amount of deferred retirement allowances was 3.0 million (a sample group of 297). The number of workers who had not received retirement allowances was smaller than that of those who had not received wage arrears, but the average amount of deferred wages was higher than that of deferred retirement allowances. (Table 6.8)

**Table 6.8: Deferred payment per person**

	Number of workers	Total amount	Average amount
	(persons)		(won)
Total	423	1,852,936	4,380
Deferred wages	372	972,361	2,614
Deferred retirement allowances	297	880,575	2,965

Moreover, the Wage Claim Guarantee Act sets the ceiling of the monthly amount of deferred payments depending on the age of the beneficiaries. This is in addition to limiting the amount of deferred wages (up to 3 months) and deferred retirement allowances (up to 3 years).<sup>14</sup> Because of these limiting conditions, 200 (53.8 %) out of 372 workers with deferred wages did not receive the full amount. On average, 1,735,000 won remained unpaid. The workers who have benefited from the wage claim guarantee system, yet did not receive the full amount, can be divided into three groups. The average unpaid amount is 1.3 million won for workers under the age of 30 (25.0 %), 1.8 million won for workers aged between 30 and 45 (54.0 %), and 2.0 million won for workers aged 45 and older (21.0 %). In the case of deferred retirement allowances, 188 (63.3 %) of 297 workers who qualified to receive retirement allowances under the wage claim guarantee system failed to receive 1.7 million won, on average, due to the ceiling amount set by the Act.

<sup>14</sup> Refer to the description of the wage claim guarantee system in the previous section

The average amount unpaid is 0.8 million won for workers under the age of 30 (25.5 %), 2.1 million won for workers aged between 30 and 45 (32.7 %), and 2.0 million won for workers aged 45 and older (14.5 %).

In order to assess how the wage claim guarantee system has benefited workers, those surveyed were asked how useful the wage claim guarantee system was. Overall, an absolute majority or 89.4 % of the sample survey group considered the wage claim guarantee system to be helpful. However, 5 % answered that it made no difference to them, and 3.3 % responded that it was not helpful. This result comes as no surprise given that the survey group did receive deferred payments through the system.

To make a fair judgement, a comparison group made up of those who did not receive deferred payments is needed. The comparison between the survey group (target group) and the comparison group could reveal the true usefulness of the wage claim guarantee system. However, it takes enormous time and expense to construct a comparison group in a household survey. Therefore, in lieu of creating a comparison group, the surveyed workers were asked how the subrogated payment they had received was spent. Out of the respondents, 84.4 % answered that the money was spent on maintaining the livelihood of their family after their retirement. (See Figure 3.22.) 5 % of them spent the payment on the startup of their own business, and 3.3 % spent it for vocational training. There were few respondents who placed the money into savings or other financial investments. This result indirectly suggests that the wage claim guarantee system has been of great help to laid-off workers for maintaining their livelihood, which is one of the objectives of the system.

In order to investigate problems arising from the implementation of the wage claim guarantee system, the surveyed workers were asked how long it took between the time they left their job and the time they received subrogated payments. For deferred wages (deferred retirement allowances), it took less than 1 month for 6.2 % (8.4 %); longer than 1 month but less than 2 months for 17.5 % (17.2 %); and less than 3 months for 33.6 % (35.7 %). Approximately 87.9 % (84.2 %) waited for less than 6 months while 4.8 % (6.4 %) waited for more than one year.

In order to receive subrogated payments based on the confirmation of insolvency, one must obtain confirmation from the local labor authorities. To the question of "whether it is difficult to meet requirements for the confirmation of insolvency," 11.1 % replied "very difficult" and 32.6 % responded "difficult." In total, 43.7 % of the sample group wanted the requirements to be moderated. In contrast, 8.5 % replied "not so difficult" and 1.7 % answered "not difficult at all."

To the question of when they became aware of the wage claim guarantee system, most workers answered around or after their retirement. The survey results showed that 20.6 % of the surveyed workers were aware of this system before they left the company, 22.9 % at the time of leaving, and 46.6 % after leaving. Moreover, 46.6 % of the surveyed workers learned of



the existence of the system through colleagues. 26.2 % heard about the system through "government-related organizations, local labor offices or labor inspectors," and 11.3 % through mass media. In contrast, a mere 2.4 % were informed of the system by their employer company. Therefore, it is necessary to educate employers about the system, and furthermore, to make it compulsory for employers to inform their employees of the system in case they become unable to pay wages in time.

The survey for employers showed a rather poor response rate as it was difficult to get in contact with them. Thus, one must bear in mind that the analysis of the survey results in the following section is somewhat lacking with regard to rigorous statistical significance. The surveyed employers were asked "whether they had applied for the subsidy for sustaining employment provided under the Employment Insurance Act or applied for other corporate loans." This question sought to investigate how much of an effort they had made to save themselves before going insolvent. Only 10.9 % of the surveyed employers (5 companies) gave an affirmative answer. The remaining 89.1 % answered no, indicating that few employers make use of the programs designed to help them.

Out of the five companies which applied for any form of financial support, two applied for corporate loans, two applied for loans for living expenses, and one applied for the subsidy for sustaining employment. In Korea, companies are obliged to set aside part of their total employee retirement allowance as a contingency in case the employees leave the company all at once. Interestingly, most companies did not reply to the question of whether they had a sufficient fund for employee retirement allowances. Only 11 companies responded to the question about the reserve retirement allowance fund. Of these, 63.6 % chose an internal reserve system and the others, an external reserve system. To the question as to whether the retirement allowance fund was ever used as operating money for the company, 3 replied "yes" and 10 replied "no." Four companies used the fund as collateral for bank loans. Of the four, two had paid back the loans in full. These results suggest that business companies are quite reluctant to reserve a retirement allowance fund, and even when they do, they often use the fund as operating capital.

The wage claim guarantee fund is financed with the employers' defrayal, the reimbursement from employers, and loans and profits from the fund operation. The amount of the employers' defrayal is determined by multiplying the total wage with a fixed rate. Currently, this rate is fixed regardless of business type and size. As shown in the previous sections, the amount and extent of deferred wages vary across industries. Those who answered that "the current fixed rate is fine" accounted for 21.3 % of the surveyed employers; those who answered that "the rate should be re-adjusted for different business sectors" amounted to 27.7 %; and furthermore, those who answered that "the rate should be readjusted not only for different business sectors but also according to the credit rating of the

company or employer" accounted for 10.6 %. Taken together, almost 60 % of the employers expressed a negative opinion on the fixed rate for contributions.

Most of the surveyed employers, that is, 89.4 % of the survey group, considered the wage claim guarantee system to be helpful. Only 4.3 % (2 companies) replied that it was not very helpful. Thus, the majority of employers responded positively to the wage claim guarantee system. On the other hand, 42.6 % of the surveyed employers considered it unfair that the government exercises the right of indemnity against them, even though they pay a defrayal for the fund. A considerable 29.8 % also answered that the current system is acceptable.

Multiple answers were allowed to the question about any future improvements to the system. The most frequent answer was the abolition of criminal punishment (33.3 %), followed by the long-term or installment repayment (24.4 %) of the subrogated payment when the government exercises the right of indemnity. Those who proposed an elimination of the employers' dual obligations, along with their contributions to the fund and repayments of the subrogated payment, accounted for 20.0 %. Lastly, 15.6 % answered that a grace period be allowed for employers to repay the subrogated payment made by the government.

### *Determinants of Deferred Payments and Severity of the System*

The size of deferred wages and retirement allowances depends on the average wage of the concerned worker and the length of deferment." The average wage depends on the level of human capital as well as the nature of work and the characteristics of the business establishment. Although the deferment length is generally determined by the characteristics of the business establishment, its current situation, and the overall economic situation, it is also affected by an employer's deliberate deferment. In other words, employers may intentionally abuse the wage claim guarantee system by deferring payment even when they have sufficient financial means to pay wages. In response to the survey question regarding the presumed presence of such intention, 20.3 % of the surveyed workers answered that "the employers did not pay wages and retirement allowances deliberately despite their financial capability."

Therefore, it is important to examine those factors determining the size of deferred payments using a regression analysis with the total amount of deferred wages, i.e., the worker's wage multiplied by the length of deferment, as a dependent variable. The explanatory variables can be divided into two: the worker's wage and other factors. The other factors

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<sup>15</sup> The Labor Standards Act in Korea stipulates that employers of business establishments with 5 employees or more should pay retirement allowances equivalent to a minimum of 30 days of pay for each year of service to retiring employees whose tenure exceeds 1 year.

include those describing the characteristics of the business establishment, such as industrial classification, company size, location, presence of a labor union, company type, existence of subcontractors, and type of insolvency. Also included is the response of the surveyed employees regarding the moral hazard of employers.

Most independent variables that reflect the characteristics of the business establishment influence not only the worker's wage but also the size of the deferred wage. This brings up a consistency issue with estimation in the sense that the wage variable is an endogenous variable and is correlated with the error term in the regression equation. For this reason, the two stage least-square method was used in the estimation. At the first stage, the worker's wage was estimated using only the exogenous variables and then, at the second stage, the estimated wage instead of the actual wage was used as an explanatory variable in estimation of the deferred wage.

The typical Mincer type earnings equation was estimated first.<sup>16</sup> The explanatory variables used in the earnings equation include the properties of human capital, such as educational background, gender and age, characteristics of the occupation, and characteristics of the concerned business establishment. The results of the second regression, which estimates the size of the deferred wage using the estimated wage and other variables as explanatory variables, are shown in Table 6.9. One can see that the worker's wage is a significant factor in determining the size of deferred wages (the coefficient of the (estimated) wage variable is 0.487).

Another factor that affects the size of deferred wages is the size of the business establishment. The coefficient of the dummy variable representing business establishments with 500 employees or more is not significantly different from zero and, thus, these establishments and those with 4 employees or less appeared to register a larger amount of deferred wages.<sup>17</sup> Roughly speaking, medium-sized companies tend not to defer wages in comparison to small companies (4 employees or less).

In addition, different industries showed varying trends in deferred wages. In the service sector, the deferment of wages was less observed than in the manufacturing sector. The coefficients of the dummy variable for the service sectors were all negative and significantly different from zero. In comparison, the coefficients were positive for the construction industry and the agriculture, forestry and fishing industries, but they are statistically insignificant. Thus, the size of deferred wages in the service industry was smaller than in the manufacturing and construction industries. The sizes of the deferred wages did not significantly vary across different types of business establishments.

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<sup>16</sup> The results of the first regression analysis (estimation of the earnings equation) are available from the authors.

<sup>17</sup> The reason why the dummy coefficient for large establishments with 500 employees or more is insignificant may be that these establishments accounted for only 1.9% of the sample group.

**Table 6.9: Determinants of the size of deferred wages: 2SLS method**

Variables	Coefficients	Standard error
Intercept	5.433	(1.000)**
Log wage (estimated)	0.487	(0.162)**
Seoul (=1)	0.483	(0.311)
Big cities excluding Seoul (=1)	0.303	(0.300)
Establishment size (compared to less than 5 workers)		
5-9 workers	-0.966	(0.830)
10-49 workers	-1.267	(0.782)
50-99 workers	-1.071	(0.793)
100-299 workers	-2.788	(0.835)**
300-500 workers	-0.622	(0.919)
500 or more workers	0.397	(1.167)
Union (=1)	0.581	(0.331)*
Industry (compared to manufacturing)		
Agriculture	1.317	(1.477)
Construction	0.051	(0.329)
Electricity, gas, wholesale, retail, restaurant, etc.	-1.075	(0.556)*
Financial, social and personal services	-0.833	(0.483)*
Type of company (compared to corporation)		
Non-corporation	0.328	(0.285)
Others	0.613	(2.109)
Subcontractor (=1)	-0.082	(0.279)
Judicial insolvency (=1)	-0.034	(0.336)
Moral hazard (=1)	-0.378	(0.297)
Cause for Insolvency (compared to transitory financial problem)		
Chronic financial problem	-0.557	(0.313)*
Decrease in sales	-0.275	(0.299)
Insolvency of the contractor	-0.443	(0.455)
Number of observations	371	
R <sup>2</sup> (Adjusted R <sup>2</sup> )	0.117	(0.0609)
F-Statistics	2.09**	

Note: \*\*\*, \*\* and \* stand for 0.01, 0.05 and 0.10 significance levels, respectively.

The amount of deferred wages varied little with the type of insolvency, but it did vary with the cause of insolvency. For insolvency due to a transitory financial strain, the amount of deferred wages was smaller than that due to chronic financial strains. In the former case, the dummy variable has a negative value and was significantly different from zero. When the employer was declared insolvent due to sluggish sales or due to the insolvency of their contractor who placed a contract order, the amount of deferred wages was small, but the coefficients were not significantly different from zero.

Table 6.10: Severity for the confirmation of insolvency: **logit** analysis

Variable	Coefficient	Standard error
Constant	-0.443	(0.380)
Seoul	-0.227	(0.163)
Firm size (compared to less than 5)		
5-9	-0.501	(0.392)
10-49	-0.070	(0.334)
50-99	-0.338	(0.349)
100-299	-0.385	(0.387)
300-500	-1.142	(0.431) ***
Total amount of deferred payments	0.000	(0.000) ***
Period to receive deferred payments	0.043	(0.015) ***
Cause of insolvency (compared to <i>temporary problem</i> in finance)		
Perpetual problem in finance	0.200	(0.168)
Decrease in sales	-0.061	(0.174)
Insolvency of the contractor	-0.575	(0.305) *
Union (=1)	0.070	(0.190)
Industry (compared to manufacturing)		
Construction	0.092	(0.191)
Electricity, gas, wholesale, retail, restaurant, etc.	-0.055	(0.321)
Financial, social and personal services	0.010	(0.291)
Occupation (compared to clerical workers)		
Manager, specialist, technician	0.229	(0.162)
Service	1.438	(0.494) ***
Operator	0.037	(0.227)
Unskilled labor	-0.044	(0.224)
Number of observations	415	
'Eligibility is stringent'	185	
'Eligibility is not so stringent'	230	
- (log likelihood)	255.90	

Note: \*\*, \*\* and \* stand for 0.01, 0.05, 0.10 significance levels, respectively

For the presence of moral hazard, there is no reliable evidence that supports the surveyed employees' affirmative response with regard to companies having failed to pay a larger amount of deferred wages. The coefficient of the dummy variable related to this question was not significantly different from zero.

The labor inspector at the local labor office with jurisdiction over the concerned company determines whether or not to confirm the insolvency. At this stage, the labor inspector's personal judgement may come into play, and thus, depending on the inspector, the standards and requirements may vary significantly. The results in Table 6.10 show that compared to respondents in other cases (e.g., transitory financial strains or chronic financial strains), the respondents from companies that became insolvent following the insolvency of their contractor company were more likely to find the requirements as not so difficult to meet. From the standpoint of the labor inspector, it is easier not only to determine the insolvent state of contractor companies, which are generally large corporations, but also to secure wage claims for exercising the right of indemnity in the future. Thus, such cases give rise to fewer complications with regard to obtaining the confirmation of insolvency. However, in the remaining cases, it is not so easy to determine whether the concerned company is really insolvent or not, and it is even less easy to secure wage claims. For these reasons, workers from companies that become insolvent due to the insolvency of the contractor company find it easier to obtain confirmation of insolvency. Also, in the case of service sector companies, the labor supervisor finds it rather difficult to confirm insolvency. Naturally, workers from these companies will consider it complicated to obtain confirmation of insolvency.

## **Summary and Policy Suggestions**

On the surface, workers who benefited from the wage claim guarantee system do not appear to be the underprivileged in the Korean labor market. Their educational background was on average higher than that of the entire economically active population. Also, a larger proportion of them, as compared to the national average, were positioned at a managerial post before leaving the job. However, although a relatively larger proportion of workers benefiting from the wage claim guarantee system had higher education and held professional and skilled positions, their household income was so low at the time the survey was taken that an urgent call for additional policy measures is needed. The result of the survey indicates that both employees and employers find the wage claim guarantee system to be positively effective. Although those who benefited from the system were not

considered as vulnerable groups in the Korean labor market, they found it difficult to maintain their livelihood after their employer became insolvent.

There still are several improvements to be made when the wage claim guarantee system goes through a redesign process in the near future. First, it is necessary to differentiate the benefits of the workers as well as the rate of the employers' defrayal depending on the size of the company and the type of industry. Among the results found in this paper with regard to differentiation, of particular note is the parallel decrease in the remaining amount of deferred payments (= the total amount of deferred payments – the subrogated payments from the wage claim guarantee fund – any additional amount provided by the employer at a later date) with the company size. In light of this, more consideration should be given to the needs of employees at small-sized companies when improvements are made to the system. In the case of retirement allowances, consideration should be given to the trend whereby workers in the manufacturing and construction sectors show a larger amount of deferred retirement allowances in arrears than those in the service sector. Furthermore, different regulations should apply to different industries.

Second, it is imperative that a standard manual for the confirmation of insolvency be developed. At present, labor inspectors at the relevant local labor office examine and determine the state of insolvency. Any decisions made regarding insolvency may reflect their personal opinion, and thus vary on a case-by-case basis. Moreover, labor inspectors also face intrinsic limitations in judgement as they have insufficient information regarding the concerned business establishment. Therefore, a manual that provides objective yardsticks to determine the state of insolvency is urgently required in order to prevent arbitrary judgements by labor inspectors.

Third, the wage claim guarantee system is not widely known yet. Thus, employers should be obliged to inform their employees of the wage claim guarantee system, especially when they become insolvent and cannot pay wages and retirement allowances.

Fourth, employers' contributions (defrayal) to the wage claim guarantee fund should be readjusted. When the government provides subrogated payments from the fund to laid-off employees, the government later exercises the right of indemnity against employers, even though they already paid their contributions to the fund. So employers are facing dual burdens. In order to alleviate the problem of duplicate burdens, the amount of reimbursement employers are to pay the government should be adjusted depending on the amount of contributions they already made to the fund. Also, further considerations in the form of long-term or installment repayments should be given to employers when the government exercises the right of indemnity.

Lastly, it is necessary to improve the current retirement allowance system. The average amount of deferred wages received through the wage claim system is less than that of deferred retirement allowances. Nonetheless,

business establishments are reluctant to reserve a retirement allowance fund, or if they have set aside a reserve, they are likely to use the fund for other purposes. Under these circumstances where companies themselves make very little effort, the subrogated payment of retirement allowances would impose serious financial strains on the operation of the fund in the long run. Also, the payment of retirement allowances might be overlapped by other systems, such as the national pension or the unemployment benefits system. However, this is not a matter that requires improvements within the wage claim guarantee system itself and is beyond the scope of this paper. Therefore, a separate study is needed to improve the legal retirement allowance system in Korea.



# **PART III**

## **LABOR LAW AND LABOR MARKET REGULATIONS**



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# 7 Assessment of Labor Market Response to the Labor Law Changes Introduced in 1998\*

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## Introduction

In early 1998, Korea changed its labor law in the aftermath of the severe economic crisis that occurred late 1997. There are two main changes: legal permission is granted for dismissal for 'managerial reasons', and legal permission is granted to temporary work and temporary work agencies. The aims of these changes were to help firms overcome their predicament and to boost Korea's economy by making the labor market in Korea more flexible.

The main purpose of this paper is to analyze the effects of the legislative changes on the employment adjustment system and labor market flexibility in Korea. We had three main research objectives. First, we tried to analyze the impacts of the employment adjustment system and temporary work services on the labor market and human resource management. Second, we tried to identify the causes of labor-management conflict that occurred in the process of employment adjustment and the adoption of temporary work services. Third, we tried to find out policy implications for the employment adjustment system and the temporary work services for the future.

For the study, we employed multiple methodological approaches. First, we conducted in-depth interviews with human resource managers and union officials in eleven firms and the representatives from two temporary work agencies.

Second, we conducted a survey on enterprises. The survey was conducted during November and December 1999 by a professional survey team. Two

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sets of questionnaires were developed: one for management, and the other for trade unions. The items included in the questionnaires were the general situations of firms, opinions about dismissal provisions, opinions about legislation on temporary work services, experience of employment adjustment and related human resource management practices, and experience of using temporary work services.

The population of the survey was 6,691 business firms with more than 150 employees, which are obliged to be inspected by external audit institution. Small firms with less than 150 employees were excluded as most of them are non-unionized enterprises in Korea. We used a simple random sampling method. A final sample universe was 638. The number of firms that responded to the survey was 483 (response rate of 76 %). The distribution of the firms by industry was: 226 in heavy and chemical manufacturing, 104 in light manufacturing, 47 in construction, 29 in wholesale & retail, restaurants & hotels, 21 in transport, storage & communication, 25 in finance and insurance, 31 in business, personal, public service & others. Among the 483 firms, 173 were unionized firms and the rest were non-unionized.

This chapter is organized as follows. In the following section, we analyze the effects of the legalization on dismissal on the employment adjustment practices of firms. Then, we analyze the effects of the legislation on temporary work and the temporary work agencies, and we look at the causes of the labor-management disputes in the process of employment adjustment. In the last section, we conclude with policy proposals.<sup>1</sup>

## **The Effects of Legal Permission to Dismiss**

In Korea, lifetime employment used to be considered as a normal system. This was mainly because, during the past era of rapid economic growth, firms expanded their organizations continuously, and therefore, employment relations could continue throughout the lifetime of workers. In this era, this system seemed efficient for employers. As companies have traditionally hired new employees without job experience and developed most of them through firm-specific education and training, long-term employment relations had been regarded rational.

In these circumstances, the concept of employment in Korea was regarded as a more concrete relation than that based on a contract between boss and worker. Lifetime employment also fitted well with the Korean sentiments of egalitarianism and communitarian consciousness. These sentiments are well

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<sup>1</sup> Owing to the limit of space, we omitted the theoretical aspect of employment adjustment and temporary work. Some articles explaining the theoretical aspect are presented in the references.

expressed by the employee's phrase 'our company', meaning the company he works in.

However, the economic crisis that occurred at the end of **1997** brought about a drastic change in the employment practices of Korean companies. During the time of crisis, many big companies collapsed or were downsized. In this situation, the practice of lifetime employment initiated by big companies also began to diminish.

It was in **1989** that a precedent first presented detailed conditions for justified dismissal in Korea. The decision of the Supreme Court requested fulfillment of the following four conditions to justify dismissal of employees. First, there had to be urgent managerial needs. Second, all possible alternatives had to have been studied. Third, even if dismissal was unavoidable, employees subject to dismissal had to be selected by reasonable and just standards. Fourth, the employer had to consult with the labor union or employees on the measures for avoiding dismissal and setting fair standards for selecting employees to be dismissed.-

In late **1996**, the precedents governing dismissal were first legislated. However, as it was opposed by trade unions and was immediately substituted with amended law on March 13, **1997**. Then the provisions for dismissal set forth in the Labor Standards Act revised in March **1997** were suspended for two years in accordance with addenda.

The laws of **1998** were made to fulfill the condition that called for greater flexibility of the labor market in return for receiving emergency relief funds from the IMF. Current regulations were legislated at the temporary meeting of the National Assembly on February 20, **1998**, based on the direction agreed at the Tripartite Commission composed with trade unions, business, and the government.

The provisions for dismissal in the Labor Standards Act were in line with the precedents. In other words, the law demands urgent managerial needs, employer's efforts to avoid dismissal, and reasonable and just standards to select employees for dismissal as the preconditions for dismissals.

In this section, we will analyze the effects of the change of law on the employment adjustment system of Korea.

### *Employment Adjustment after the Enactment of the Law concerning Collective Dismissals*

#### Change of Employment and Major Devices of Employment Adjustment

What was the effect of the change of law on employment adjustment in Korean firms? Table 7.1 shows the impact of law amendment on regular employees after the change of law.<sup>2</sup> This reveals that dismissal was carried out

<sup>2</sup> Employment adjustment was actively carried out mainly in 1998. Korea's rate of GDP growth was 8.9% during the early three quarters 1999, drastically increased from -5.8% in

only by 15 % of firms, 75 out of 483, during 10 months just after the change of law in 1998. The average number of dismissals per firm was about 46.

**Table 7.1: Impacts of the enactment of act concerning collective dismissals on regular employees**

year	Number of employees affected by the act	Attrition		'Honorable' retirement		Dismissal		Others <sup>4</sup>	
		(No. of firms)	(%)	(No. of firms)	(%)	(No. of firms)	(%)	(No. of firms)	(%)
1998 <sup>1)</sup>	Less than 10 employees	57	11.8	18	3.7	22	4.6	17	3.5
	10-19	61	12.6	22	4.6	11	2.3	8	1.7
	20-29	47	9.7	15	2.9	10	2.1	2	0.4
	30-39	40	8.3	0	0.0	2	0.4	5	1.0
	40-49	33	6.8	15	2.9	13	2.7	7	1.4
	50 or more	142	27.1	101	20.9	17	3.5	25	5.2
	None	103	21.3	312	64.6	408	84.5	419	86.7
	Total	483	100	483	100	483	100	483	100
Average <sup>3)</sup>	103	-	231	-	46	-	252	-	
1999 <sup>2)</sup>	Less than 10 employee	89	18.4	20	4.1	25	5.2	13	2.7
	10-19	78	16.1	15	3.1	8	1.7	8	1.7
	20-29	36	7.5	8	1.7	2	0.4	9	1.9
	30-39	24	5.0	7	1.4	0	0.0	3	0.6
	40-49	24	5.0	12	2.5	6	1.2	7	1.4
	50 or more	84	17.4	22	4.6	3	0.6	15	3.1
	None	148	30.6	399	82.6	439	90.9	428	88.6
	Total	483	-	483	-	483	-	483	-
Average <sup>3)</sup>	64	-	95	-	15	-	107	-	

Notes: 1) 1998 means the period from March to December of 1998;

2) 1999 means the period from January to the end of July;

3) Average means average number of the employees per firms that carried out the program;

4) Others mean spin-off, early retirement, etc.

The percent of firms that used 'honorable' retirement as a means of shedding labor was 35 %, much higher than that of firms using dismissals. The average number of workers per firm who quit by this method was 231, also much higher than the numbers being dismissed. Others, the last column in Table 7.1, include spin-off<sup>3</sup>, sub-contracting, early retirement, etc. These were used by about 13 % of the firms. The average number of workers per firm affected by these methods was 252.

1998. So the need for employment adjustment decreased drastically in 1999

<sup>3</sup> Spin-off means a process of a corporate restructuring whereby the capital stock of a division or subsidiary of a corporation is transferred to a separate firm, which generally is established by employees buy-out or management buy-out of the employees (management) of the division or subsidiary. In this case, mother corporation generally guarantees work by subcontracting.

Attrition was used most widely in reducing employment. About 80 % and 70 % of the firms reduced employment by way of attrition in 1998 and 1999, respectively. The average numbers of employees per firm reduced by attrition was 103 and 64 in those years, respectively. At the time of the survey, the average numbers of employees of the 380 and 335 firms that reduced employees by attrition were 1,368 and 1,627, respectively. Hence, the annual attrition rates were very high at 9 % and 8 % respectively.

Why did firms carry out employment adjustment? As shown in Table 7.2, as many as 57 % of the firms replied 'overcoming the crisis of the firm' as the main reason for employment adjustment. This indicates that many firms were in deep crisis when they were trying to adjust employment.

**Table 7.2: Main reason of employment adjustment**

	(firms)	(%)
To make vacancy for promotion	7	2.9
To reduce excess of employees generated by automation	13	5.4
Corporate restructuring and downsizing	39	16.3
To reduce wage costs	31	12.9
To overcome crisis of the company	136	56.7
Merger and acquisition with other company	3	1.3
Others	11	4.6
<b>Total</b>	<b>240</b>	<b>100.0</b>

The fact that so many firms were in deep crisis gives us a general picture of employment adjustment at the time. Confronted with a severe business downturn, with decreasing orders and slack work, and some firms on the brink of insolvency, employees could not help but quit their job. By doing this, they thought they could, at least, retrieve some retirement allowances in addition to the severance pay. In these circumstances, legal permission for dismissal by the change of labor law gave employers the upper hand in the process of persuasion to quit. Many workers were worried that, however strongly they opposed dismissal programs, employers would be able to dismiss them anyway, paying only little or no compensation.

In this context, a large number of voluntary or 'honorable' retirees surged. We can see this in an airline company. At first, the employer had planned 'honorable' retirement of about 200 employees in 1998. After the firm's announcement of 'honorable' retirement program, more than 700 out of 16,000 employees applied, and in the end, 695 employees retired by the program. Seeing rampant vacant seat owing to the decrease of passengers and frequent cancellation of flights, many employees were worried about the possibility of bankruptcy of the firm. That was the major reason why so many of them rushed to apply for 'honorable' retirement.

We can see the same phenomenon in the banking industry, too. In this sector nine major banks cut huge numbers of staff by October 1998 through

'honorable' retirement. Even though 9,000 staff cuts were planned at first, an extra 1,000 took 'honorable' retirement as they worried they would lose any chance of retrieving a retirement allowance if they stayed. Chohung bank was to cut 2,222, but an extra 200 took the 'honorable' retirement. Those to go were primarily young females in low-level jobs. After that, banks rehired some retirees on a temporary basis (The Chosunilbo, October 9, 1998).

As a result of this kind of employment adjustment, there were large-scale job cuts in the commercial banking sector. After the end of 1997, the banking sector cut the number of regular employees drastically. As shown in Table 7.3, the total number of employees in this sector was 113,994 at the end of 1997. At the end of 1998, however, 75,677 remained, a 34 % cut. At the end of June 1999, this number was further reduced to 74,851.<sup>4</sup>

**Table 7.3: Change of regular employees of commercial banking sector in Korea, 1997-1998**

	End of 1997		End of 1998		End of June 1999	
	(persons)	(%)	(persons)	(%)	(Persons)	(%)
National banks	94,065	100.0	64,830	68.9	65,187	69.3
Regional banks	19,929	100.0	10,847	54.4	9,664	48.5
Total	113,994	100.0	75,677	66.4	74,851	65.7

Source: Financial Supervisory Commission.

In 1999, firms that cut regular employees by attrition or any other intentional devices decreased compared with 1998. As will be explained shortly, some of this reduction may be the result of the speedy recovery of Korea's economy in 1999. In 1999, however, the order of employment adjustment devices used by firms and the number of employees affected by them were the same as in 1998.

### *Detailed Analysis of Employment Adjustment*

What kind of firms carried out which employment adjustment programs? Let's look at the firms which carried out dismissals. Table 7.4 shows that, dismissal was most common in small firms with employment of less than 300.<sup>5</sup> Big firms with employment of 1,000 or more were far less likely to

In terms of employment adjustment, the banking sector was in a peculiar position after the economic crisis. While the major reason for Korea's economic crisis was the bankruptcy of several heavily indebted business groups, their problems left the banking system in tatters, necessitating a large-scale rescue financing by the government.

<sup>5</sup> The relative briskness of dismissal in small firms is also ascertained in other survey of the Korea Labor Institute. This shows that 87 out of 355 firms that carried out dismissals from April to October 1999, 32 firms (37 %) were firms with less than 100 employees (Korea Labor Institute, 1999b, p.28).



carry out dismissal. Non-unionized firms were more active in dismissal compared with unionized firms. The low percentage of dismissals in big or unionized firms might be related to the opposition from trade unions or large number of employees to dismissals (see Table 7.4).

**Table 7.4: Characteristics of the firms that carried out dismissal**

	Industry			Number of employees			Union	
	Mfg1 <sup>1)</sup>	Mfg2 <sup>2)</sup>	Others <sup>3)</sup>	Less than 299	300 to 999	More than 999	U <sup>4)</sup>	Nu <sup>5)</sup>
<b>1998</b>								
Co. <sup>6)</sup>	34 (15.0%)	19 (18.3%)	22 (14.7%)	39 (23.5%)	26 (14.9%)	10 (7.0%)	41 (13.2%)	34 (19.7%)
Workers <sup>7)</sup>	50	46	57	30	62	107	52	49
No. <sup>8)</sup>	226	104	153	166	175	142	310	173
<b>1999</b>								
Co.	17 (7.5%)	13 (12.5%)	14 (9.2%)	24 (14.5%)	13 (7.4%)	7 (4.9%)	22 (7.1%)	22 (12.7%)
Workers	6	17	27	6	35	7	11	21
No.	226	104	153	166	175	142	310	173

Notes: 1) Manufacturing sectors such as metal and mechanical products, transport equipment (including cars), chemicals, medicines, plants, etc. (so-called heavy) and chemical industry;

2) Manufacturing sectors such as food products, textile and garments, printing and publishing, medical equipment, etc. (so-called light industry);

3) All industries except manufacturing;

4) Unionized firms;

5) Non-unionized firms;

6) Number of firms that carried out dismissal;

7) Average number of workers dismissed per firm that carried out dismissal;

8) Number of firms that responded to the question; Numbers in the parenthesis are the % of the total respondents

Table 7.5 shows that firms in heavy and chemical industry and non-manufacturing industry rather than firms in light industry carried out 'honorable' retirement more often. Big firms with 1,000 or more employees and unionized firms were more active in carrying out 'honorable' retirement. Unionized firms were a bit more active in 'honorable' retirement compared with those without a union. 'Honorable retirement' seemed to function as a substitute for dismissal for the big unionized firms.

In the case of spin-off or early retirement (others), firms in heavy and chemical industries were more active compared to those in light industry or those of non-manufacturing industries. Big firms with 1,000 or more employees were also more active rather than small-and-medium size firms in adjusting employment by these programs. Non-unionized firms were more active in utilizing these programs compared with unionized firms (see Table 7.6).

**Table 7.5: Characteristics of firms that carried out 'honorable' retirement**

	Industry			Number of employees			Union	
	Mfg1 <sup>1)</sup>	Mfg2 <sup>2)</sup>	Others <sup>3)</sup>	Less than 300	300 to 999	More than 999	U <sup>4)</sup>	Nu <sup>5)</sup>
<b>1998</b>								
Co. <sup>6)</sup>	88 (38.9%)	23 (22.1%)	60 (39.2%)	42 (25.3%)	56 (32.0%)	73 (51.4%)	128 (41.3%)	43 (24.9%)
Workers <sup>7)</sup>	290	207	151	39	73	473	261	143
No. <sup>8)</sup>	226	104	153	166	175	142	310	173
<b>1999</b>								
Co.	40 (17.7%)	17 (16.3%)	27 (17.6%)	17 (10.2%)	29 (16.6%)	38 (26.8%)	61 (19.7%)	23 (13.3%)
Workers	148	24	56	13	25	188	114	32
No.	226	104	153	166	175	142	310	173

Note: same as Table 7.1 and Table 7.4

**Table 7.6: Characteristics of firms that carried out spin-off or early retirement**

	Industry			Number of employees			Union	
	Mfg1 <sup>1)</sup>	Mfg2 <sup>2)</sup>	Others <sup>3)</sup>	Less than 300	300 to 999	More than 999	U <sup>4)</sup>	Nu <sup>5)</sup>
<b>1998</b>								
Co. <sup>6)</sup>	34 (15.0%)	11 (10.6%)	19 (12.4%)	18 (10.8%)	20 (11.4%)	26 (18.3%)	37 (11.9%)	27 (15.6%)
Workers <sup>7)</sup>	317	193	161	35	119	517	235	280
No. <sup>8)</sup>	226	104	153	166	175	142	310	173
<b>1999</b>								
Co.	26 (11.5%)	13 (12.5%)	16 (10.5%)	9 (5.4%)	18 (10.3%)	28 (19.7%)	32 (10.3%)	23 (13.3%)
Workers	162	54	57	9	31	188	141	46
No.	226	104	153	166	175	142	310	173

Note: same as Table 7.5.

Lastly, firms that reduced employees by attrition were prevalent regardless of industry, number of employment, unionized or not.

#### 'Honorable' Retirement: Characteristic Features of Employment Adjustment System in Korea

'Honorable' retirement appears to be a system of employment adjustment

peculiar to Korea. Here, we will analyze it in more detail.

In general, its process proceeds as follows. When an employer finds out that he has an excess number of employees in relation to current and anticipated demand, he sets a target of job cuts, in accordance with the business strategy. When the workplace is unionized, he consults with the union and seeks its consent. Then, he invites employees to apply for 'honorable' retirement, promising to pay some compensation to the retiree until the number of applicants reaches the target. If the number does not reach the target, they sometimes persuade, induce, or coerce certain employees to apply. The expression of 'honorable' here is meant to give impression of praising applicants for the sacrifices they make for the sake of colleagues and the company.

In general, they have a target group who they wish to release. The specific features of the target group depend on the employment structure of the firm. They are generally employees of low ranking in performance appraisals, old workers anticipating retirement in the near future and female or young workers who do not have a large family to support.

As it is based on the application of individual employee, there is a risk of adverse selection. That is, competent employees, who the employer did not wish to lose, may apply. Especially in circumstances of bleak business prospects, the risk escalates. In a normal firm, however, the employer is able to reduce the size of the workforce through persuading incompetent employees to retire, paying some compensation.

Employers paid more money in compensation to the workers who took 'honorable' retirement than to those to be dismissed. The amount of compensation for individual applicants depends on factors such as seniority, remaining work year, rank and position, etc. As Table 7.7 shows, 95 % of the firms paid retirement allowances. The average amount was about 7 months' wages of the retiree.

**Table 7.7: Payment of compensation for 'honorable' retirement**

	(firms)	(%)
Paid	180	94.7
Did not pay	10	5.2
Total	190	100
The average amount of payment	Wages of 7 months	

By adopting this method of employment adjustment system, which requires some compensation, employers in Korea could weaken the opposition against employment adjustment from the workers and the union. In these firms, many workers appreciate 'honorable' retirees as martyrs sacrificing themselves for the company and the co-workers. So, it was helpful for improving employees' morale in times of hardship.

Furthermore, it could be a convenient bypass for the leaders of trade

unions. They may understand the inevitability of employment adjustment of the firm in due course. However, it is taboo to attend a meeting for consultation on dismissal, least of all to agree to it, in Korea. They are liable to be discharged by a no-confidence resolution by the agitation of militant sections of the union. However, as 'honorable' retirement is carried out based on *de jure* application, although not necessarily a *defacto* one, of the employees, trade union leaders could be excused for not being militant enough to block the employment adjustment.

An example of an 'honorable' retirement program of a TV maker, one of our case studies, will help in understanding the system. Because of the excess supply of TVs in the world market, its profits plummeted since 1991, with a huge loss in 1998. Accordingly, its employment decreased to 1,400 in 1997, mainly through attrition, from the peak of 2,500 in 1991.

In 1998, the firm adopted three devices for further cuts. Firstly, by spin-off it reduced employment, mainly in sectors of automatic inserting and packing materials, by 130. Secondly, by subcontracting operations previously done by its own employees in sectors like transport and logistics, it reduced employment by 70. Lastly, by 'honorable' retirement program it reduced employment by 94. Any employees who were in service more than 5 years could apply for it. The amount of compensation promised by the firm for the 'honorable' retirees was about 1,600,000 – 1,800,000 won (US\$ 14,000-15,600) per person depending on seniority and the rank of the retiree.

The first 'honorable' retirement program was in February 1998. At this time there were 46 retirees, all of them *de facto* applicants and most of them manual workers. As the first cuts were small compared to the firm's plan, there was a second 'honorable' retirement program in August 1998. At this time the employer eagerly tried to invite mainly non-manual workers to apply for the program. In particular, the employees in the bottom order of the performance appraisal were the main target of the persuasion. At this time, the firm cut by 48.

As trade union leaders and employees had been watching slack orders and idle factory lines for years, they did not oppose to the program. As the employer coerced the non-manual workers to apply, union leaders were not so eager to block it, either. The main target of the employer's invitation was non-manual workers, who were not members of the trade union. Instead of opposing it, the union leaders demanded increased compensation, to which the firm agreed. In addition to the comparatively generous compensation, the support program for the retirees which helped retirees find new jobs probably made it proceed more smoothly.

As employers utilized devices like 'honorable' retirement, they had more discretion in recruiting new employees. We could find that many firms recruited new employees in the process of the adjustment. Table 7.8 shows that about half of the firms that carried out dismissals or 'honorable' retirement recruited regular employees in 1998. In the same period, about 34 % of them recruited non-regular employees, too. In 1999, the number of

firms that recruited regular or non-regular employees increased. The fact that so many firms were recruiting new employees in the midst of employment adjustment seems to indicate that Korea's employers have strong authority in recruitment, with no strong intervention from the union, unlike in the US.<sup>6</sup> According to Table 7.8, the percentage of the firms with newly recruited employees is higher in non-unionized firms than unionized firms. The gap, however, is not so large. Moreover, the average number of recruitment of regular employees in unionized firms is much larger than that of the non-unionized firms, both in 1998 and 1999.

Under the seniority wage system in Korea, old worker's wages are higher than those of the young in the same job. Most of the programs for 'honorable'

**Table 7.8: Number of firms having new recruitment among the firms that carried out dismissal or 'honorable' retirement**

year	Number of workers recruited	Regular workers			Non-regular workers		
		union	Non-union	Total	Union	Total	
1998	Less than 10 workers	28	11	39	24	14	38
	10-19	13	8	21	16	2	18
	20-29	9	5	14	2	2	4
	30-39	7	8	15	4	0	4
	40-49	2	2	4	1	0	1
	50 or more	21	6	27	6	8	14
	Did not recruit	89	27	116	115	41	156
	Total	169	67	236	168	67	235
	Average number of workers recruited in the firms that recruited	79	46	68	34	8	14
1999	Less than 10 employees	35	19	54	36	18	54
	10-19	22	11	33	9	5	14
	20-29	12	6	18	11	2	13
	30-39	10	3	13	3	2	5
	40-49	3	6	9	1	1	2
	50 or more	26	9	35	16	9	25
	Did not recruit	61	13	74	92	30	122
	Total	169	67	236	168	67	235
	Average number of workers recruited in the firms that recruited	54	37	49	35	45	38

Notes: 1) Respondents are employers of the firms that conducted dismissal or 'honorable' retirement programs.

2) Average means average number of the newly recruited employees per firm that responded to have recruited

<sup>6</sup> In the US, most collective agreements provide for recall of employees after layoff. These provisions usually specify that employees be rehired in order of seniority (Holley and Jennings, 1997, p. 459)

'honorable' retirement, therefore, target primarily old workers. If there are not enough applicants to reduce wage costs, employers sometimes coerce old employees to apply. By replacing young workers for old ones, they could succeed in reducing substantive wage costs.

## **Temporary Work Services**

### ***Introduction***

After the financial crisis in late 1997, increasing flexibility of the labor market was one of the important conditions necessary to recover from the economic crisis in Korea. The Tripartite Commission of the Republic of Korea, established on January 15, 1998 to overcome the economic crisis, issued its first joint statement on January 20, 1998, that labor, management and the government would each bear the burden of responsibility for the crisis equally. As one of the means to achieve labor market flexibility, the Tripartite Commission made a critical compromise regarding temporary work agencies. On February 20, 1998, the Act Relating to Protection, etc., for Dispatched Worker was enacted.

The "temporary work" defined in the Temporary Work Act<sup>7</sup> means that the temporary work agency hires employees (dispatched workers), and while maintaining employment relations, leases these employees to a third party (user firms) to work under the service recipient's supervision and direction in accordance with the employment leasing agreement.

The Temporary Work Act places restrictions on the types of business for which temporary work is allowed. These are divided into two categories. One is temporary work in areas that require special knowledge, technique, or experience, other than manufacturing, falling under the 26 categories set forth in the Presidential Decree. The term for such temporary work shall not exceed one year. The purpose behind such restrictions is to uphold the original purpose of temporary work business, which is to meet the temporary demand for workforce and the demand for specialists who cannot be employed at all times. In other words, by making sure employees are leased for just the appropriate amount of time, the service recipient may not make a common use of dispatched workers for a long-term to replace regular employees. However, if an agreement is reached between the temporary work agency, the company that uses these employees, and the employees dispatched, the term may be extended by one year, limited to one extension.'

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<sup>7</sup> We use "Temporary Work Act" here instead of its full name of "Act relating to Protection etc., for Dispatched Workers" just for convenience. "Temporary work" is more commonly used term in journals written in English in Korea.

<sup>8</sup> If a company uses dispatched workers for an uninterrupted period of more than two years, these workers shall be regarded as regular employees of the company after the two year

The other is dispatched workers to fill a temporary vacancy. When a company needs dispatched workers to fill a temporary vacancy or meet increased need (not for the purpose of replacing regular workers), it may lease workers for a limited time regardless of the type of work, as long as the work is not listed in the Decree. However, even in such a case, the employer must consult in good faith, prior to such leasing, with the labor union or the representative of a majority of workers if there is no such union. The term of lease is restricted even in cases of leasing employees for such temporary and intermittent need. When it is clear that employees are needed to fill a vacancy or a temporary need, the term of lease may be such as to solve the problem. For instance, to fill a vacancy for maternity or sick leave, employees may be leased for the term of such leave. In other cases, the term may not exceed three months, but if an agreement is reached between the three parties, the term may be extended for not more than a three-month period.'

### *The Current Situation of Temporary Work Services in Korea*

#### Temporary Work Agencies and Their Activities

Although temporary work agencies had been illegal in Korea, quite a large number of manpower leasing agencies had actually operated even before the passage of the law under the implicit allowance of the government (Jeong & Yoon, 1993; Jeong, 1999). The precise number of temporary work agencies was not known. However, it was estimated that at least hundreds of agencies operated. After the passage of the law, we can estimate the number and activities of temporary work agencies since the Ministry of Labor of Korea (MOL) announces key statistics for them.

The most recent data available at this time are presented in Table 7.9. In the 4<sup>th</sup> quarter of 1998 (about a half year after the passage of the law), 789 temporary work agencies had obtained legal permission from MOL. The number increased to 968 during the 1<sup>st</sup> quarter of 1999 and again to 1,095 during the 2<sup>nd</sup> quarter of 1999. That is, during a period of 6 months, the number of legally permitted temporary work agencies increased by almost 40 %. However, the number is somewhat exaggerated because not all permitted agencies actually provide services. According to MOL, only 784 firms out of 1,095 are currently in the temporary work business, which is

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term expires, provided that the dispatched employees do not clearly demonstrate a wish to the contrary.

9

There are cases in which temporary work is prohibited even in temporary or intermittent need. These may be categorized as the following: construction work, unloading work related to transportation or circulation business, ship work under the Seamen's law, work harmful to public morals or sanitation, work harmful or dangerous under the Industry Safety and Health Act, driving in the transportation business, and certain work under laws governing the medical business

Table 7.9: Recent trends in temporary work agencies in Korea, 1998 Q4-1999 Q2

	1998 Q4	1999 Q1	1999 Q2
Number of temporary work agencies (TWAs), permitted by MOL	789	968 (22.7%)	1,095 (13.1%)
Number of TWAs, currently in actual operation	564	728 (29.1%)	784 (7.7%)
Number of user firms, received services from TWAs	4,302	4,178 (-2.9%)	4,701 (12.5%)
Number of dispatched workers	41,545	44,665 (7.5%)	46,407 (3.9%)
Average number of workers per agency	73.7	61.4	59.2

Note: The numbers in parenthesis are the rates of increase compared to previous year

71 % of the total agencies.

As of the 2<sup>nd</sup> quarter of 1999, 4,701 employers used dispatched workers, which represents 9 % increase after the passage of the law. On the other hand, over the same period, the number of dispatched workers employed by TWAs increased by 12 %, from 41,545 in 1998 to 46,407 in 1999. Although the increasing rate of dispatched workers is very high compared to that of regular workers, the proportion of dispatched workers out of total employees in Korea is still 0.2 %, which is very small compared to other OECD countries (OECD, 1999).

The average number of user firms per TWA is currently 6 as of the 2<sup>nd</sup> quarter of 1999, a slight increase from 5.7 in the first quarter, but a decrease from 7.6 in 1998. Also, the average number of dispatched workers is currently 59 per TWA, a decrease from 61 in the second quarter of 1999 and 74 in 1998. This indicates that temporary work agency activity is rapidly expanding, but their size is very small, and getting smaller.

Table 7.10 shows more detailed figures of the average number of workers per TWA. As indicated, 311 agencies (28 %) are not currently operating businesses.<sup>10</sup> Also, most agencies (87 % of acting agencies) have less than 100 dispatched workers. Only 101 agencies have more than 100 dispatched workers and 2 % of all have more than 300 dispatched workers. While this figure confirms that most TWAs in Korea are very small, there is also the phenomenon that a few agencies are getting bigger. The president of the Association of TWAs in Korea told us in an interview that a few leading agencies are preparing M&A in response to both the demand of the market and the entry of large international TWAs.

<sup>10</sup> The reason they are not operating after receiving permission for business from MOL is not clear. We hypothesize that they overestimated the market situation in the temporary work industry, but it has turned out to be too competitive for many small agencies to compete profitably



**Table 7.10: Trends in the average number of workers per TWA, 1998 Q4-1999 Q2**

Number of workers	1998 Q4		1999 Q1		1999 Q2	
	(persons)	(%)	(persons)	(%)	(persons)	(%)
0	225	28.5	240	24.8	311	28.4
1 - 49	407	51.6	548	56.6	583	53.2
50 - 99	71	8.9	81	8.4	100	9.1
100 - 299	64	8.1	74	7.6	77	7.0
More than 300	22	2.9	25	2.6	24	2.2
Total	789	100	968	100	1,095	100

### *User Firms*

In our survey, as well as asking questions on dismissal procedures, we also sought to identify the extent to which firms used dispatched workers (See Table 7.11). Thirty-seven % of firms reported that they currently use dispatched workers. During 1998, after passage of the law, 27 % of firms used dispatched workers. However, the usage rate of dispatched workers employed by firms rapidly increased in 1999 from 27 % (129 firms) to 37 % (177 firms). The survey also showed that user firms tend to employ more dispatched workers than in the past. Firms that employed more than 50 dispatched workers increased from 16 % in 1998 to 23 % in 1999 (See Table 7.12). Similar to the worldwide tendency of an expansion of dispatched work, we found strong signs that firms increasingly rely more on TWAs for their human resource management practices in Korea.

We asked firms whether they would expand or discontinue use of dispatched workers if they currently used them or whether they planned to employ dispatched workers in the near future if not currently used by them. Only 33 % of respondents said they would neither expand, nor plan to use, dispatched workers (See Table 7.13).

**Table 7.11: Companies using dispatched workers**

Use		Do not use		Total	
(firms)	(%)	(firms)	(%)	(firms)	(%)
178	37.0	305	63.0	483	100.0

**Table 7.12: Trends in number of dispatched workers used per firm**

	March 1998 - December 1998	January 1999 - November 1999
Less than 10 dispatched workers	59 (45.7%)	76 (42.9%)
10 - 19	19 (14.7%)	25 (14.1%)
20 - 29	12 (9.3%)	21 (11.9%)
30 - 49	19 (14.7%)	14 (7.9%)
More than 50	20 (15.5%)	41 (23.2%)
Total	129 (100.0%)	177 (100.0%)

**Table 7.13: Future plan to use dispatched workers**

	(firms)	(%)
Expand or newly plan to use	211	43.9
Neither expand nor plan to use	161	33.3
Don't know	111	23.0
Total	483	100.0

There were differences in industries regarding the extent to which firms use dispatched workers (See Table 7.14). It was shown that firms in the service sector, such as retail, banking and other services industries, tended to use dispatched workers more frequently than manufacturing firms. Around half of service firms among survey respondents responded to use dispatched workers. We also analyzed size differences regarding the extent to which firms use dispatched workers (See Table 7.15). Larger firms tend to use TWAs more frequently than smaller firms. However, there was little difference regarding future plans to use dispatched workers, in terms of both industry and firm size.

**Table 7.14: Companies using dispatched workers by industry**

	Heavy manu- facturing	Light manu- facturing	Construc- tion	Retail	Transpor- tation	Banking	Other service
Use (%)	38.9	30.8	17.0	44.8	23.8	64.0	51.6
Do not (%)	61.1	69.2	83.0	55.2	76.2	36.0	48.4
Total (%)	100	100	100	100	100	100	100
Total number of firms	226	104	47	29	21	25	31

**Table 7.15: Firms regarding using dispatched workers by firm size**

Number of employees	1 - 299		300 - 1000		More than 1000	
	(firms)	(%)	(firms)	(%)	(firms)	(%)
Use	39	22.0	66	37.3	72	40.7
Do not use	127	42.2	109	36.2	65	21.6
Total	166	34.7	175	36.6	137	28.7

User firms were asked why they resort to dispatched workers. The most frequent answer was to fulfill peripheral work (26 %). Next to that were to obtain employment flexibility (23 %), to reduce labor costs (22 %), to supplement a temporary labor shortage (11 %), due to a temporary high workload (6 %), and due to jobs which require special knowledge and skills not available within the firm (6 %) in that order.

**Table 7.16: Reasons why firms use dispatched workers**

	1 <sup>st</sup> reason	2 <sup>nd</sup> reason	3 <sup>rd</sup> reason
	(firms)		
To supplement a temporary labor shortage	20	12	22
To fulfill a short-term demand increase	11	15	17
To fulfill peripheral works	46	31	23
Due to jobs which require special knowledge and skills	10	6	5
To supplement workers for specific time period	8	8	8
To reduce labor costs	38	35	21
To obtain employment flexibility	41	49	23
To prevent labor-management conflict	2	1	5
Others	0	1	1
Total	176	158	125

### *Impact of the Temporary Work Act on Labor Market in Korea*

We asked questions regarding the impact of the passage of the Act in 1998 on labor markets and the interests of workers to both employers and union officials (Table 7.17). First of all, employers regarded the passage of the Act to have had a positive effect on the growth of temporary work services and also a positive effect on labor market flexibility. About 40 % of employers believed that the Act helped the activation of temporary work services in Korea, while only 11 % of employers disagreed. About 50 % of employers agreed that the Act helped enhance labor market flexibility. Employers did not think that the contents of the law were inappropriate in terms of the protection of dispatched workers. However, employers were concerned about types of jobs permitted and length of employment periods. About 60 % of employers thought that the types of jobs permitted in the law are too limited, whereas 58 % of employers complained that periods of temporary work services are too restrictive. In interviews, employers argued that the maximum two years of contract are too short to fully utilize dispatched workers in terms of the skills and experiences obtained within the firms. Likewise, when we asked an open question regarding improvement of the law in the future, the most frequent answers were types of jobs and lengths of employment periods (Table 7.18).

However, opinions of union officials were very different from those of employers (See Table 7.19). Seventy-seven % of union officials did not agree that the Act includes regulations for appropriate protection of dispatched workers. Also, 61 % of union officials thought that the types of jobs were rather too comprehensive, and 63 % of them disagreed that periods of services were appropriate. Union officials were mostly concerned about protection of dispatched workers. In an open question regarding improvement of the Act, the most frequent answers were, "Need more

protection for workers regarding working conditions" and "Need methods to prevent wage appropriation by temporary work agencies". Some of the union officials even argued that the Act must be abolished because of the possibility of abuse by TWAs and user firms.

**Table 7.17: Employers' opinions regarding the impact of the act concerning temporary work agencies**

	Strongly disagree	Disagree	Neither agree nor disagree	Agree	Strongly agree	Don't know	Total
Helped the growth temporary work services	18 (3.7%)	42 (8.7%)	177 (36.7%)	172 (35.7%)	21 (4.4%)	52 (10.8%)	482
Helped enhance labor market flexibility	6 (1.2%)	43 (8.9%)	151 (31.3%)	217 (45.0%)	19 (3.9%)	46 (9.5%)	482
Due to too much protection of workers, made it more difficult to use dispatched workers	9 (1.9%)	109 (22.6%)	200 (41.5%)	94 (19.5%)	11 (2.3%)	59 (12.2%)	482
Included appropriate protection of workers	9 (1.9%)	66 (13.7%)	175 (36.3%)	154 (32.0%)	9 (1.9%)	69 (14.4%)	482
Types of jobs are too limited	4 (0.8%)	33 (6.8%)	92 (19.1%)	233 (48.3%)	57 (11.8%)	63 (13.1%)	482
Periods of temporary work services are too restrictive	4 (0.8%)	39 (8.1%)	93 (19.3%)	211 (43.8%)	67 (13.9%)	68 (14.1%)	482

**Table 7.18: Employers' opinions regarding the amendment of the act concerning the temporary work agency**

	(firms)
Lift the limitation of types of jobs or diversify further	115
Lift the limitation of periods or expand longer	100
Total	225

**Table 7.19: Unions' opinions regarding the impact of the act concerning temporary work agencies**

	Strongly Disagree	Disagree	Neither Agree nor Disagree	Agree	Strongly Agree	Don't Know	Total
Included appropriate protection of workers	66 (34.6%)	81 (42.4%)	23 (12.0%)	12 (6.3%)	1 (0.5%)	8 (4.2%)	191 (100.0%)
Types of jobs are too comprehensive	11 (5.8%)	33 (17.3%)	15 (7.9%)	95 (50.0%)	21 (11.0%)	16 (8.4%)	191 (100.0%)
Periods of temporary work services are appropriate	38 (19.9%)	83 (43.5%)	19 (9.9%)	21 (1.0%)	1 (0.5%)	29 (15.2%)	191 (100.0%)

**Table 7.20: Unions' opinions regarding amendment of the act concerning temporary work agency**

	(frequencies)
Must provide ways for preventing wage appropriation	8
Types of jobs must be restricted	7
Must abolish the law because of abuse	12
Need more protection for workers regarding working conditions	16
Total	43

## **Labor-Management Relations in the Process of Employment Adjustment**

Wherever they were, workers and trade unions were never insensitive to employment adjustment. Even in the US, where an 'employment at will' doctrine predominates, large non-union firms are reluctant to lay off employees for fear of unionization. In the case of unionized firms in the US, management has obtained union acceptance of layoffs in times of downturns, in return for management's acceptance of seniority as the basis of layoffs (Mills, 1994, p. 487).

As there is not such a systematic compromise between the two sides, the employers in Korea have reasonable grounds to fear employees' opposition to labor adjustment. This is another important reason why so many employers choose 'honorable' retirement rather than dismissal. By adopting 'honorable' retirement, they hope to evade industrial conflict.

As explained above, employers must fulfill 4 preconditions if they are going to dismiss employees due to managerial reasons. During the process of fulfilling these conditions, they are liable to collide with trade unions or representatives of employees. Trade unions representing employees of big corporations were especially militant against the employers' attempts at dismissal. The militancy against employment adjustment is partly connected to the unions' tough bargaining tactics which are used in anticipation of a better pay off.

This was well illustrated by industrial disputes in some of the Korean firms. For instance, in 1998, Hyundai Motor Company was going to dismiss 1,448 employees after domestic car sales plunged by 50 %. Before that, the firm cut 4,858 jobs from a total of 46,000 through 5 separate 'honorable' retirement programs. However, trade union leaders insisted that all dismissals be revoked in exchange for wage cuts and paid leave. As the employer could not accept that, the union went on strike, although it was illegal, for about four weeks. After an acrimonious showdown between the union and the company, the union finally agreed to accept dismissal. The deal between the two sides, with state intervention, appeared to achieve the

union's goal. As the unionists insisted on dismissal of a minimum number, it was reduced to a token 277 from the originally targeted 1,538. Workers who lost jobs received compensation of up to nine months' wages. Another 1,261 workers were to go on 18 months' unpaid leave, with the last six months spent in job retraining schemes (The Korea Herald, August 25, 1998).

There is another example of an industrial dispute on the dismissal issue. The trade union in Mando Machinery Corporation led a strike in August 1998 protesting against the company's plan to dismiss 1,090 workers out of 4,500. After a 17-day-long strike, the police raided the six factories of the company. The police raid, although it ended the strike, touched off strong protest by labor sympathizers nationally, and the Korean Confederation of Trade Unions (KCTU) threatened to stage an anti-government campaign and a sympathy strike (The Korea Herald, September 4, 1998).

In the case of trade unions in small-and-medium firms and those in firms verging on collapse, the opposition against employment adjustment was not so strong as to lead to strikes. Table 7.21 shows this. Even among unionized firms, only 5 % of the firms (9 out of 171) replied there were labor-management disputes. Among non-unionized firms, there were labor-management disputes in 3 % of the firms.

**Table 7.21: Firms that had a labor-management dispute in the process of employment adjustment**

	Had	Did not have	Total
Unionized	9 (5.3%)	162 (94.7%)	171 (100.0%)
Not unionized	2 (2.8%)	69 (97.2%)	71 (100.0%)

Even in the firms that had no labor-management disputes, curtailing employment was not easy. What was most difficult in the process of employment adjustment for the employers? Table 7.22 shows that about half the employers replied that it was to make employees understand the necessity of employment adjustment. Next came 'consultation about the criteria to select who are to lose their jobs', 'consultation about the compensatory package for the workers to be adjusted', and 'consultation about the number to be adjusted', in that order. A higher percentage of employers at unionized workplaces than those of the non-unionized workplaces answered that making employees understand the necessity of employment adjustment was a difficult task.

We can also see the difficulties faced by employers through trade union's responses to the attempt to enact dismissals or 'honorable' retirement. About 45 % stated they were strongly opposed to dismissal, and 32 % were strongly opposed to 'honorable' retirement (see Table 7.23). According to the opinion of employers, paying a redundancy package and allowances for 'honorable' retirement is a way of reducing opposition from workers (Table 7.24). In the case of dismissal, 73 % of the firms paid

redundancy packages in addition to the severance pay required by the law. The average amount was as much as 2.6 months' wages. In the case of 'honorable' retirement, employers generally promised to pay a higher amount of retirement allowances than in the case of dismissal. The difference of the average payments between the two seems to be related to two facts. One is that mainly small-and-medium firms carried out dismissals. The other is that in the case of dismissals, employers cannot soothe workers resistance by the payment of allowances.

**Table 7.22: Most difficult thing to firms in process of employment adjustment**

	Unionized	Non-unionized	Total
Make understand the necessity of employment adjustment	73 (51.8%)	16 (39.0%)	89 (50.9%)
Consultation about the number to be adjusted	16 (11.3%)	5 (12.2%)	21 (12.0%)
Consultation about the criteria to select to be adjusted	28 (19.9%)	14 (34.1%)	42 (24.0%)
Consultation about the compensatory package	18 (12.8%)	4 (9.8%)	22 (12.6%)
Others	6 (4.3%)	2 (4.9%)	1 (0.6%)
Total	141 (100.0%)	41 (100.0%)	175 (100.0%)

**Table 7.23: Union's positions to the attempt of firm's employment adjustment**

	'Honorable' retirement	Dismissal
Support for stable employment of majority of the employees	20 (18.2%)	22 (30.1%)
Reluctantly acquiesce	55 (50.0%)	18 (24.7%)
Strongly oppose	35 (31.8%)	33 (45.2%)
Total	110 (100.0%)	73 (100.0%)

**Table 7.24: Firms behavior concerning redundancy package**

Paid	62 (72.9%)
Did not pay	23 (27.1%)
Total	85 (100%)
Amount of payment	2.6 months' wages

Note: Amount means the average of the firms that responded to have paid.

We can see this by the answers of employers about the reasons of their paying the redundancy package. Table 7.25 shows that most employers thought it reasonable and humane to pay some compensation and show their sympathy to the workers who were going to retire against their wish. On this matter, there was not much difference in the percentage between the firms with trade unions and without unions.

**Table 7.25: Reasons for paying redundancy package**

	Unionized	Non-unionized	Total
Smoothing resistance of retirees	12 (26.7%)	6 (23.1%)	18 (25.4%)
Sympathy, goodwill to the retirees	33 (73.3%)	17 (65.4%)	50 (70.4%)
Others <sup>1]</sup>	0 (0.0%)	3 (11.5%)	3 (4.2%)
Total	45 (100%)	26 (100%)	71 (100.0%)

Note: 1) Others include methods for improving morale of remaining employees, donation of the remaining employees, etc.

This employer attribute may be related to their needs to uphold a community consciousness among their employees. Table 7.26 shows that among the firms that carried out dismissal or 'honorable' retirement, 53 % carried out some activities for enhancing the morale of remaining employees after adjustment. About 33 % of them undertook activities to help outgoing workers find jobs. These activities include providing information on the labor market, supporting business start-ups, providing training for getting jobs, etc. A high proportion of firms was active in helping not only the remaining employees but also the outgoing employees. This indicates that the employer's relation with the employees does not end completely through dismissal or retirement.

**Table 7.26: Firms that acted for outplacement and morale enhancement**

	Did	Did not	Total
Outplacement	80 (32.9%)	163 (67.1%)	243 (100.0%)
Morale enhancing	128 (52.9%)	114 (47.1%)	242 (100.0%)

From the employees' point of view, compensation for 'honorable' retirement allows them to maintain their living standards for the time being. Korea currently has a poorly developed welfare system and has a meager social safety net. Considering this, paying some amount of money in addition to the mandatory severance pay to the retirees must be helpful for smoothing opposition from the unions and boosting the morale of the remaining workers as well.

## **Policy Suggestions and Conclusion**

There was active employment adjustment in Korea after the change of the Labor Standards Act in 1998, though the major method for employment adjustment after the passage of the law was not dismissal but 'honorable' retirement, spin-off, early retirement, and attrition. However, the overall employment adjustment undoubtedly helped by the change of law permitting dismissal due to managerial reasons. As we have seen in above,



the number of temporary work agencies, dispatched workers and user firms has also rapidly expanded in the period after the passage of the Act.

Employment adjustment in 1998 and early 1999 was facilitated not only by legislative change but also by the economic crisis. As so many firms were in deep trouble many employees chose to leave jobs for fear of losing severance pay, or on behalf of the firm they have always worked for and identified with. Furthermore, the unions were weakened by a sharp increase in unemployment and by public opinion unsympathetic to their militancy.

However, in future the need for employment adjustment will not come from business downturns alone. As globalization of the economy progresses, as advanced technology becomes prevalent, and as the lifecycle of products shrink, more flexibility in the labor market is likely to be called for, whatever type it may be. Furthermore, the conditions underpinning long-term employment - strong corporate profitability, easy bank lending terms and a steady supply of graduates committed to one company - are more likely to change as the *chaebols* are driven by the government towards reform.

Recently, with the success of new firms utilizing advanced technology, there has been a collapse of long-term employment in the labor market of university graduates. Nowadays, talented people are less likely to choose long-term employment in search of higher earnings. They change jobs, arrange flexible working hours, and even work from home, which were all unthinkable a few years ago. In this era of rapid change, big corporations, which are not necessarily sufficiently flexible to adapt, are losing hundreds of talented brains. These trends could exert a great influence on employment practices in the 'old' industries.

Nevertheless, considering the sentiments of strong egalitarianism and communitarianism in Korea, employment adjustment by dismissal is not expected to be dominant in the near future. Rather than dismissal, 'honorable' retirement and functional flexibility through job rotation will still be more popular. Further, if firms rely on a harsh approach of downsizing and drastic job cuts, they must take a risk of tearing up their loyalty contracts with their workers, the majority of whom are not of the 'new graduate' category with easily transferable scarce skills.

There are differences of opinion on labor market flexibility. The position taken in this paper is that it is inevitable that employers will be allowed to dismiss employees due to managerial reasons, at least for a considerable time. However, labor flexibility must be pursued without destroying workers' employment stability and living conditions. This is not an easy task in any country, least of all in Korea which is in a vulnerable position with a bailout from the IMF.

So, what should government policy concerning labor market flexibility be? First of all, the government should enlarge the social safety net so that unemployed people can live without a drastic degradation of living conditions. For instance, the employment insurance system in Korea was

initially relevant only to the better-off employees, excluding the daily workers and part-time workers. Because of this, when the crisis broke out and the workers lost jobs *en masses*, it could not adequately cope with the situation. It could provide benefits to only about 99,000 (5.8%) persons among the 1.7 million unemployed. This gave rise to a widespread sense of discontent (Pak *et al.*, 1999, p. 44). By improving the employment insurance system and social safety net the government can enlarge the protection for the unemployed and unskilled workers. In view of the growing income gap in Korea, these policies should have priority." In an upcoming era of the 'digital economy', the inequality between the permanent skilled workers and the temporary unskilled ones is likely to increase further.

Second, there should be a policy to upgrade workforce skills to keep up with changing technology. Up to the present, firms were the most important actors in providing training for workers. As workers' mobility increases and more workers are employed on a temporary basis, the benefits for firms to invest in the training of under-skilled employees diminish. As global competition increases, firms can no longer afford to wait for their employees to develop over many years. In these circumstances, government-private sector 'training partnerships', as have been considered in the UK, could be invaluable.

Third, there should be a legal stipulation which helps identify the legitimate representative of employees. According to the present law, the employer who intends to dismiss employees due to managerial reasons should consult with the representative who stands for more than half of all employees. The trade union representing more than half of the employees in the firm is deemed to be a legitimate representative. However, there can be a problem of misrepresentation if the targets of dismissal are employees in higher positions, because most of the unions in Korea limit their membership to employees below a certain position. As a matter of fact, there was a court verdict in February 2000 judging it illegal to dismiss a worker in a senior position, on grounds that the union, which was the consulting partner then, could not be a legitimate representative. Therefore there should be a stipulation to select the representative of all employees who will consult with the employer on matters such as dismissal or 'honorable' retirement.

Fourth, if we accept the logic that a surge in merger and acquisition (M&A) activity is crucial to Korea's economic prospects, there may be a need for a detailed stipulation or precedent making employment adjustment easier in these cases. In article 31, section 1 of the Labor Standards Act of

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<sup>11</sup> Recently, the relative earnings of low-skilled workers deteriorate in Korea. According to the National Statistical Office, income inequalities between the rich and poor worsened in 1999, despite the overall income increase and a government package of measures to support the middle class and the poor. The Gini coefficient of concentration, a measure of inequality among income brackets, amounted to 0.3204, the highest since 1979 (National Statistical Office, 2000).

Korea, there is a description concerning dismissal in the case of M&A. It says, "the case of M&A for overcoming business crisis is considered to have an 'urgent managerial need' for dismissal". There is no denying that this is a progress in terms of labor market flexibility if we compare the description to the previous precedent that made the employer responsible for maintaining employment in times of business acquisition. However, the meaning of this description is so equivocal that it is likely to cause conflicts between the dismissed workers of acquired firms and the employer of acquirer after the M&A deal. Furthermore, the need for employment adjustment in the case of M&A does not arise by a crisis of the firm alone. As we can see in the recent takeover of the German telecommunications company Mannesmann by Vodafone AirTouch, the British telephone company, deregulation and globalization of financial markets are promoting M&A deals even of the prosperous firms. By jettisoning peripheral or overlapping activities and focusing on a few core businesses, successful M&A accelerate business restructuring and boost profits of the firm. To make this process smooth, there should be a stipulation governing employment adjustment in the case of M&A. In particular, the employer should have some leeway for employment adjustment when there is overlapping activities and redundant workers as the result of M&A.

Fifth, there should be policy for improving the profitability of TWAs. As most temporary work agencies are small and their management abilities are poor, they have far weaker bargaining positions than user firms. Therefore, they often play the role of a placement service firm rather than a temporary work agency. This lack of bargaining power creates several negative effects on temporary work services in the labor market. It leads to excessive competition on price among agencies, which then imposes lower wages on workers. It also leads to a lack of proper protection, such as social insurance and industrial safety, which must be provided to the workers under the law. In the long run this eventually leads to negative effects on user firms as temporary agencies cannot reinvest their profits and provide user firms with quality services such as the training of workers and adequate customer services.

Sixth, there should be policy to reduce the possibility of the misuse of temporary work services by user firms. As we have seen, user firms tend to use dispatched workers for dealing with simple, monotonous, repetitive work and reducing labor costs rather than as temporary substitution due to seasonal and short-term labor shortages. The unions argue that user firms are using dispatched workers to replace regular workers. If this is true, although the introduction of temporary work services in Korea may help expand labor market flexibility, it may also distort the labor market for regular workers. We do not know how many regular workers have been replaced with dispatched workers. Such a misuse of temporary work services may lead dispatched workers to remain as "Temps" in the longer term during their career. A "temporary" work position could be a "permanent" job for

dispatched workers, not an opportunity for getting new skills and job experience. It may hurt the job security of regular workers as well. It could lead to poor productivity and poor morale among workers, which may have a negative effect on firm performance and on the national economy in the long run.

Seventh, there should be a deregulation of the law in terms of number of jobs and the length of temporary work services permitted. Tight regulation can restrict (good-minded) user firms in the expansion of the use of temporary work services. This may lead user firms to disguise their use of dispatched workers as subcontractors. Many firms we interviewed said that although they would prefer to use dispatched workers in many areas, they could not do so because those jobs are not permitted under the current law. For example, human resource officials in one manufacturing company argue that they would like to transform jobs currently performed by subcontractors to temporary work services. They prefer temporary work services as they can directly control work performance, which is difficult when they use subcontractors.

To work properly, the society requires a balance of openness and inclusion. Up to 1997, Korea's labor market indicated the characteristics of excessive inclusion. Under this system, new employees could be continuously recruited, which was helped by rapid economic growth. However, in the forthcoming era of slower growth, which Korea is entering, too much inclusion in the labor market could negatively impact on the profitability of firms and reduce the employment opportunities of new participants in the market. In this era, we need more openness in the labor market.

However, we must be cautious not to swing to the opposite position by eliminating the employment stability of most workers. In the system of employment adjustment, we should try to maintain the balance of power between employers and the unions.

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# **§ Labor Market Flexibility and Employment Agencies in the UK, Japan and Korea\***

**Barry Wilkinson"**

## **Labor Market Flexibility in the UK, Japan and Korea**

It seems ironic that as recently as the 1980s, when the concerns of many economists and sociologists were focussed on flexibility of labor deployment, Japanese and other Asian (and within Europe German and Italian) models were held up as exemplars for the rest of the world (Kern and Schumann, 1987; Kumazawa and Yamada, 1989; Oliver and Wilkinson, 1988; Piore and Sabel, 1984; Piore, 1986). At the turn of the century, in the context of a long period of high unemployment and slowed growth in many European countries, and severe economic problems in Japan and elsewhere in East Asia, it is the US which has come to the forefront as the model for labor flexibility the world over, and within Europe it is frequently the UK which is held to provide the model of a flexible labor force. This shift is clearly related to the apparent economic success of the US and UK in recent years, which has underpinned a resurgence of neo-liberal economic ideology.

This section focuses attention on labor market flexibility at the national level in the UK, Japan and Korea, though developments in the strategies and structures of employing organizations are included as important factors. For each of the three societies, there is discussion of labor market institutions and mechanisms in their economic and political/legislative contexts.

### ***Labor Market Flexibility in the UK***

The election of a Conservative government under the leadership Mrs

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\* This chapter benefits from descriptive and quantitative data provided by Professor Park Duck Jay of the Korea National Open University. The author, however, takes sole responsibility for the arguments put forward.

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Thatcher in 1979 heralded a major change in approach to the management of the UK economy. Neo-liberal rhetoric was used to justify the reduction of subsidies and other forms of assistance to industry, the wholesale privatization of the publicly owned utilities, and the introduction of market mechanisms in the public sector.

The assertion of the primacy of competition and capital markets had implications for labor markets, which were seen by the government as rigid and distorted due to excessive trades union power, and over the next 15 years or so a whole raft of legislation aimed at curbing that power was introduced (see Brown and Wadhvani 1990, and Brown *et al.* 1997 for detailed discussion). Also important were competition policy, the increased exposure of UK (or UK-based) businesses to international competition, and shifting firm strategies. These forces combined with legislation to produce a decentralization of collective bargaining activity, a reduction in the size of the (traditionally highly organized) public sector, and a restructuring of the economy which decimated some of the industries (for instance coal and steel) that were traditional trades union strongholds. Such developments helped pave the way for the extension of the contingent labor market.

The reduced size of the UK's public sector was associated with government encouragement of competition *within* the remaining public sector through 'competitive tendering'. In-house activities were reduced through the contracting out of services that could be provided more cheaply and (it was argued) effectively by private sector organizations, many of which would be less likely to use unionized labor on permanent terms. In cases where the outsourcing company takes over the existing labor force the *Transfer of Undertakings (Protection of Employment) (TUPE) Regulations 1981* comes into play. These specify that the workforce is entitled to the same terms and conditions as offered by the previous employer, though it is possible for the new employer to 'whittle away' any terms and conditions it considers undesirable by making new appointments on new terms and inducing existing employees to voluntarily accept such (see 'Privatizing Personnel', *IRS Employment Review*, no.648, 1999 for a detailed example.)

International exposure to competition in product markets has also had an effect, albeit immeasurable. Manufactured imports increased as a proportion of home demand from 26 % in 1980 to 45 % in 1995 (Brown *et al.*, 1995) forcing business restructuring and cost cutting, which often includes changing employment relations. The increase in foreign investment activity has also had an impact, with companies setting up on green-field sites able to establish new employment practices (often with the cooperation of single unions desperate for membership) which include mechanisms for flexible usage of labor (Bassett, 1986; Oliver and Wilkinson, 1988).

Employing organizations have, then, shifted their employment practices in ways that increase the size of the contingent labor force. These shifts are undoubtedly related to the shift in the political climate, reduced trades union power, competition policy, and increased exposure to international com-

petition. A whole industry of 'strategic human resource management' has grown out of these changes, with 'flexibility models' distinguishing between 'core' and 'peripheral' workers who contribute in different ways to firm competitiveness. Whether HRM in these organizations really is 'strategic', and whether the use of contingent labor really does contribute to firm competitiveness is, however, open to question. According to Purcell (1996, p.19):

In practice this rational, ordered planning and analysis is rarely embarked on. What evidence we have is that firms adopting peripheral policies do so for short-term cost reasons and rarely link this development to core strategies. Contingent working seen in temporary work and the growth of insourcing and outsourcing has been more a reflection of cost reduction exercises in the context of labor market deregulation and continuing high levels of unemployment.

This observation raises serious questions about the real economic and social consequences of extensive use of contingent labor which will be addressed in section three.

We should also comment on what the future might hold. In 1997 a Labor government was elected following 18 years of Conservative rule. The new government has vigorously asserted a continuing commitment to a flexible labor market policy, but has attempted to combine this (or for cynics to legitimize this) with notions of 'fairness at work'. Indeed it was the *Fairness at Work* White Paper that led to the 1999 *Employment Act*. This includes 'family friendly' provision - in particular more generous rules for parental leave on birth or adoption of a child. Overall the Act leaves employer prerogatives over flexible labor deployment intact. However, in the longer term it is possible, particularly since the UK recently signed up to the *Social Chapter*, that pressures from the EU might force the UK to adopt stronger measures that circumscribe employer prerogatives. On the other hand if convergence across Europe is to occur it could be in the form of the rest of Europe moving to the UK model: German employers for instance have been suggesting they might be given freedoms similar to those in the UK, and Murray (1999) suggests a recent ideological shift in the European Commission which is more supportive of extensive use of temporary workers. There is not room in this paper to dwell on this issue, but lively discussions of the prospects can be found in Guest (1997) and Barnard and Deakin (1999).

Significant grey and black elements in the contingent labor market mean there can be no definitive statistics on its size. Different methods of calculation cause problems too. For instance the *Labor Force Survey* relies on self-definitions of worker respondents, while the *Workplace Industrial Survey* (see Cully *et al.*, 1999) relies on responses from employing organizations. Even so, it is possible to get a feel for the characteristics and

types of contingent labor.

A preliminary point is that there is evidence of ethnic and sex biases: it has been reported that eight % of women in the UK are temporary workers compared with six % of men, and 10 % of ethnic minorities are temporary workers compared with seven % of whites. Given what we know about sex and race discrimination in employment generally in the UK such a bias may not be surprising. (In the US too, women and ethnic minorities are over-represented among 'non-traditional' workers (Houseman, 1999; US Department of Labor, 1999).)

The major types of contingent labor used in the UK include home workers (common in manufacturing), labor-only sub-contractors (popular in construction), casual workers (agriculture, hotels, catering, dock work), fixed term contract workers (especially important in the public sector), and agency supplied temporary workers (commonly found in an increasing number of sectors). For discussions see: Beatson (1995); Labor Market Trends (1997); Ministry of Agriculture (1999); Local Government Management Board (1998); *IRS Industrial Relations Law Bulletin* (no.534, 1995); Casey *et al.* (1997); *FRES* (1997:18). Labor Market Trends (1997) estimated that the number of temporary workers in the UK grew from 5.2 % of the working population in the mid 1980s to 7.1 % in 1996 - a modest expansion. However, according to the *Labor Force Survey* the numbers of economically active people in the UK defining themselves as 'self employed' almost doubled between 1979 and 1990 to represent 13 % of the employed workforce. A large, but unquantified, number of these self-defined 'self-employed' are in reality contingent workers in all but name. Hence the real numbers of temporary workers in the UK are almost certainly far greater, and have grown far more rapidly, than official figures suggest.

### *Labor Market Flexibility in Japan*

Japan has taken a different route to labor market flexibility:

There is a flexibility trade off. Concern with labor market flexibility – especially managers' ability to hire and fire at will – is strengthened in the Anglo-Saxon economies by the inflexibility of the financial markets they face. Japanese firms, being more insulated from the short-term demands of shareholders, have hitherto been able to afford more 'rigid' employment systems from which they gain the advantage of employee commitment and cooperative and flexible attitudes to work. (Dore, 1996)

The sovereignty of capital markets and the power of shareholders in the UK and US is today being pushed as a model for the way forward for Japan (and elsewhere in East Asia). The pressure comes from international (especially US) sources but also from within Japan, which is searching for a way out of a recession that has persisted for nearly ten years. The difficulty



in adopting less 'rigid' employment systems and establishing an ability to 'hire and fire at will', as Dore puts it, appears to be not so much a function of trades union power (as arguably was the case in the past in the UK) but of corporate decision making structures. 'Corporate governance' has been a key focus of critics, with many commentators finding problems in 'too' close relationships between the state and business, between businesses inter-locked through shared ownership and shared senior directors, and between businesses and their employees. The proposed solution, well rehearsed in the pages of *Far Eastern Economic Review* and other popular Dow Jones publications, is to loosen the ties that bond businesses to a broader community of interests. and to focus their attention on shareholder demands (usually short-term profits and rising share prices). Boards of directors should be restructured in ways that increase 'transparency' and 'accountability' to shareholders, hence giving control over the direction of companies to capital markets.

Such a transformation of corporate governance in Japan could be as radical as that which was forced on Japan during the post-war US occupation, and those scholars who see Japanese employment practices as rooted in hundreds of years of culture and tradition (Whitley 1992) might rule it out as a possibility. However, there are at least two additional reasons, found in more recent history, for reluctance to change radically. Firstly, Japan has been highly successful for most of the second part of the twentieth century, such that the recession may need to get even deeper and scandals even more outrageous to precipitate a sea change. Second, established obligations – to inter-locked businesses and local communities as well as employees – are not easily broken. In those cases where they have been in recent years, it has generally been a last resort rather than a choice. Obligations to regular employees do not derive, as in Germany for instance, from formal employee representation on boards of directors. Rather, Japanese directors are usually selected from middle management ranks, and are expected to act as leaders of employees who monitor their affairs. Well established life-time employment expectations and 'bottom-up' *ringgi* decision making, combined in some companies with employee stock ownership plans, also contribute to the difficulty of 'downsizing' at will (Yamakawa, 1999; Yasui, 1999).

The mechanisms supporting labor market flexibility in Japan were until recently studied by many foreign observers for the lessons which might be gained. One focus of attention was the internal labor market flexibility of 'core' employees enjoying life time employment and seniority wages within the large corporations: the common observation was that employer benevolence fosters employee loyalty and a willingness to work flexibly in terms of job function and working hours (OECD, 1977; Dore, 1987). Employment security is offered in return for wage restraint, and competitiveness is achieved through skills development and investment rather than treating workers as disposable resources (Sako, 1997).

A second focus was on 'peripheral' workers who work on temporary bases. Official figures show over five million 'temporary' plus over one million 'daily' workers in Japan in 1997. Additionally there were nearly eight million 'self-employed', an unknown number of whom might be temporaries in all but name. Peripheral workers are less likely to be unionised, are paid lower wages, and tend to bear the brunt of the impact of any economic downturn (Oliver and Wilkinson, 1988; Berggren and Nomura, 1997). Japan was considered to benefit from a 'dual' labor market, with core workers providing 'internal' flexibility, and peripheral workers 'external' flexibility. However, the prolonged recession finally began to take its toll towards the end of the 1990s, when the big firm sector saw some major casualties, and many more big firms are looking for downsizing on a scale which could cut into the core workforce.

The main means to cope with over-staffing in most big companies for most of the 1990s have been reducing temporary worker headcounts, hiring freezes, reducing the extent of overtime worked, and extending the use of *shukko* and *tenseki* transfers (Benson and Debroux, 1997; Berggren and Nomura, 1997). *Shukko* refers to temporary transfers of employees to other companies, and *tenseki* refers to permanent transfer to a new employer. This practice typically occurs between companies that are related by capital or business transactions, and often means larger firms sending employees to smaller firms. Several purposes have traditionally been served, including transferring technology and managerial expertise, but increasingly the practice has been used to 'shuffle off' older employees to jobs in other firms with lower status and less favourable terms and conditions (Sato, 1996). However, firms are still reluctant to lay off permanent workers – dismissals remain rare as a means of employment adjustment (Genda, 1999). The famous Yamaichi Securities case may be illustrative of the obligations to permanent employees. Yamaichi had no choice but to dismiss its 7,694 workers soon after its collapse. But the firm set up an in-house working party that managed to obtain 28,000 job offers from 4,000 companies for its dismissed workers. Over 3,000 employees were successfully placed very quickly – older employees were more difficult to place. Yamaichi even helped 241 out of 279 graduates who were due to take employment at Yamaichi to secure positions at other companies (Japan Labor Bulletin, 1 May 1998).

Many firms in Japan still appear to be attached to long-term employment relations, and the reluctance to abandon the Japanese employment system is shared by the Japanese state. The Ministry of Labor's (1999) White Paper on Labor is ambiguous about the wisdom of abandoning long term employment practices, expressing a range of fears including economic de-stabilization, rising unemployment benefit payments, reduced company training provision, industrial relations conflict, and loss of employee morale. The outcome is that while government and employers have been searching for mechanisms that can help labor force adjustments to changing economic structures and

circumstances, so far changes in both corporate approaches and in labor legislation have been limited (Yamakawa, 1998; 1999).

### *Labor Market Flexibility in Korea*

For the bulk of the period from the 1960s, when the country embarked on its ambitious program of export-oriented industrialization, to the latter part of the 1990s, Korea enjoyed a situation of full employment. The giant conglomerates, or *chaebol*, which have led the economy, recruited most of their employees without job experience, and developed their human resources through company based education and training. Long-term employment relations were regarded as rational as the focus was on securing a sufficiently large workforce to meet rapid growth prospects. The ownership and control of *chaebol* differs from the Japanese *keiretsu* - in Korea family owners keep control over their vast conglomerates and have typically been described at the authoritarian end of the paternalist spectrum (Rhee, 1985; Eckert, 1990; Park, 1992), whereas in Japan, as described above, ownership is corporatized and control is more diffuse. However, as in Japan, long-term employment systems have combined with seniority wages and enterprise based trades unions to create a situation where workers' interests became closely aligned to those of the company, making labor adjustments during Korea's late 1990s crisis both painful and controversial (Park *et al.*, 2000).

A great deal has been written and said about the causes of Korea's crisis and many have offered prescriptions to cure the ills. Most importantly of course the IMF has laid down loan conditions focused on corporate governance mechanisms which seek to increase the transparency and responsiveness of *chaebol* to capital markets. (See Il Chong Nam *et al.*, (1999) for detailed characterization of corporate governance in Korea and discussion of measures taken by the Korean government.) The focus here is specifically on the measures taken to ease labor market adjustments with a view to enabling smoother and quicker corporate restructuring.

Following the onset of Korea's economic crisis and under pressure from the IMF, the government of Korea convened a Tripartite Commission consisting of government, employer and labor representatives in February 1998. The Commission signed an agreement on 'Social Compromise to Overcome the Economic Crisis in Korea; which included an article on 'Enhancement of Labor Market Flexibility'. Changes to the Labor Standards Act followed making dismissal for economic reasons much easier, and the National Assembly passed the 'Act Relating to Protection, etc. for Dispatched Workers'. This Act legalized temporary employment agencies and became effective in July 1998 (Park *et al.*, 2000). It is difficult to separate out the effects of these legislative changes from shifts in companies' employment strategies, though at the very least they served an important symbolic function in signaling that employment security could no

longer be taken for granted.

Unemployment rose dramatically from around two % in 1997 to 7.4 % by the end of 1998, but Park *et al's* (2000) research, based on a large sample of companies across a range of sectors, suggests that dismissals were relatively rarely used by firms in their employment adjustment during the 10 months after the change of law. Only 15 % of firms in the sample dismissed workers, while attrition was used to reduce headcounts in 80 %, and sub-contracting, early retirement and outsourcing was used in 13 %. Those firms that did dismiss workers laid off an average of 51 using this method during 1998, whilst averages of over 200 per firm were removed from employment by the other mechanisms. However, 34.2 % of firms used 'honorable retirement' as an adjustment mechanism, and these firms on average shed over 50 staff through this method. It seems that 'honorable retirement' is induced in employees through a mix of retirement incentives, moral persuasion, and sometimes coercion.

While the numbers of workers losing their jobs in 1999 was a little less than in 1998, the popularity of the different mechanisms remained basically the same. Korean employers may have tended to avoid straightforward dismissals on economic grounds because of felt obligations to employees, though it is difficult to distinguish this as a factor from the fear of militant trades union action - several heated industrial disputes over the size and procedures of dismissals occurred during 1998. Either way, while simple dismissals are not expected to become the predominant mechanism for labor adjustment in the near future, employment security can no longer be taken for granted by Korean workers.

While corporate governance structures in Korea are quite different to those in Japan, there are some strong similarities with regard to employment practices, and both societies are going through the painful process of adjusting such practices in the face of economic crisis, global competitive pressure, and international political demands. The UK (and the US) offer a well established alternative labor market paradigm, but so far the evidence suggests there has probably been more lip service than action to implement the espoused mechanisms. We now turn attention specifically to the mechanism of temporary employment agencies, which have been offered a wide role in Japan and Korea only very recently, before focussing in on the potential costs and benefits of labor market transformation in the following section.

## **Employment Agencies: Context and Characteristics**

While employment agencies have a long history in the UK, their activities have grown enormously during the 1990s. In Japan and Korea, employment agency activities were severely restricted until the last couple of years of the

1990s. This section characterizes employment agencies and agency workers in the three countries - and sets them in their economic and institutional contexts.

### *Employment Agencies in the UK*

While employment agencies have been significant in the UK for at least a century, it is only in recent years (with a few exceptions) that serious attempts have been made to document the size and characteristics of the market. The figures available today, however, remain fraught with difficulties, partly related to methods of calculation, and also to what we define as an employment agency.

Labor Force Survey (LFS) data, frequently used by labor economists, may underestimate the significance of employment agencies: for Spring 1998 it found there were 222,000 agency supplied temporary workers – less than one % of the employed population. Figures from a survey conducted by the Federation of Recruitment and Employment Services (FRES, the industry association) on the other hand estimate 879,000 temporary staff on agency payrolls for one sample week in November of the same year (FRES, 1997/198). If accurate this would represent close to four % of the working population. Labor Force Survey data may grossly underestimate the size of the agency labor force because they are based on individuals' self-reporting of their status: many may mis-categorize themselves as employed by the client, or as self-employed. Further, agencies often treat temporary workers as self-employed when the reality may be rather different (Burchell *et al.*, 1999).

The definition of employment agency also makes for difficulty in estimating the size of the agency workforce. For instance as mentioned in section one, labor-only sub-contracting is prevalent in the construction industry, where the 'gang boss' may make the arrangement for his workers to be paid on completion of a job. We might legitimately wish to define the gang boss as an employment agent, yet construction workers hardly figure in data on temporary agency workers. The extent to which inclusion of gang bosses and other intermediaries (often in grey or black market sectors) would affect our calculations of the size of the temporary agency labor force is not known, but it would be to calculate upwards, and it would be significant (Rothwell, 1990).

Exactly where the boundary is drawn around what counts as an 'employment agency' has to be a problematic, if not random affair, but a convenient one here is that used by the industry association FRES, by the market intelligence agency MINTEL, and by the British government in its 1999 consultation document (described below). Since 1995 there has been no requirement for employment agencies to be licensed by the government, so there is no definitive register. However, FRES uses Business Pages listings to make annual estimates of numbers of employment agencies, and

the government's business register is used to gather detailed information on industry structure, turnover, etc. Here the industry is defined by the SIC code 74500, 'Labor Recruitment and the Provision of Personnel'.

FRES data (FRES, 1998) estimates a growth in the number of employment agencies operating in the UK from 7,745 in 1995 to 10,570 in 1998. Those agencies with FRES membership have also grown, from 2,824 in 1994 to over 4,700 in 1998. In 1998 the industry directly employed over 63,000 staff, handling nearly 900,000 temporary placements and nearly 400,000 permanent placements. An industry turnover growth of 325 % in real terms between 1993 and 1998 is recorded.

Focussing on the temporary staff on agency payrolls, the extent of business derived from different industrial sectors is indicated in Table 8. 1.

**Table 8.1: Temporary staff on agency payrolls in the U.K. ,1997-1998**

	Numbers	
	('000)	(%)
Secretarial/clerical	225	29.0
Blue collar	229	26.0
Technical/engineering	91	10.3
Nursing/medical/care	70	8.0
Drivers	62	7.0
Computing/IT	56	6.4
Hotel/catering	26	3.0
Financial	18	2.0
Professional/managerial	12	1.4
Other	62	7.0

Source: FRES Survey (1997-1998)

The high profile of certain client industry sectors in these figures is no great surprise, but it is worth noting the absence of some sectors where we know temporary working is extensive - in local government, education, and construction sectors for instance. This is explained by the predominance of alternative temporary arrangements such as short-term contracts in the public sector and 'lump labor' in the construction industry. However, it is possible that employment agencies may increase their presence in more sectors in the years to come as new opportunities arise associated with, for instance, changing labor market circumstances and changing human resource strategies of client companies, and as agencies themselves work to increase their presence in new markets. Further, while the UK's Employment Service is likely to remain the biggest job broker through its Job Centers for the foreseeable future, public-private partnerships being pushed by the present government could lead to further opportunities for employment agencies. Limited partnership activity between the Employment Service and selected private sector agencies began in 1998, and could expand.

The structure of the UK employment agency industry is characterized by quite extreme fragmentation due in part to low entry barriers and low start up costs. This contrasts with most EU countries where industry concentration is now well established, partly because EU social regulation is much tighter, making it difficult for small players (MINTEL, 1998). The largest player in the UK, Manpower, accounts for 3.7 % of total industry turnover, and only another eight agencies account for more than one % of turnover. However, acquisition activity by (especially US) foreign multinationals has been strong in recent years -they now own a third of the top twenty agencies, and most are seeking to expand their markets. Three additional forces which could encourage industry concentration may be: (i) changes to UK legislation and the adoption of EU legislation which might add to the employment responsibilities of the agencies and therefore raise barriers to entry; (ii) changes in the requirements of many large client companies who are looking to outsource whole 'non-core' functions, or to find 'supranational solutions' to their human resources problems; and (iii) technological advances which are allowing employment agencies to drastically reduce response-to-client times through the use of call centers and computer software which uses large databases to automatically match the C.V.'s of workers with client company specifications. All of these developments could put the bigger employment agencies in a better position to meet client company expectations.

In the UK, employment agencies are set minimum standards of conduct via *The Employment Agencies Act 1973*. The Act makes the distinction between an *employment agency*, which finds employment for workers, or provides client employers with workers, for employment *by them*, and an *employment business*, which supplies *its* own employees to act for, or be under the control of, others. The term 'employment agency' is typically used to cover both types of agency: most agencies in any case undertake both types of activity. Regulations made under the Act in 1976 required employment *businesses* to issue written terms and conditions to recruits; failure to do so could lead to a revoked license. But licensing requirements were repealed in 1994 (IRS Industrial Relations Law Bulletin, 534, December 1995). The 1975 Finance Act obliges all employment agencies to deduct tax and national insurance contributions from the temporary workers they place, which can make the agency the employer for tax purposes but not necessarily for any other purpose. As well being among the most free in Europe, UK regulations are also among the most ambiguous, giving scope for agencies and/or client businesses to enter into relationships with workers on a variety of bases - a favored one is to define the worker as 'independent contractor', which means no employment rights, and may help account for the dramatic rise in the numbers of 'self-employed'.

The DTI does take complaints directly and is willing where it deems necessary to investigate and take action. Since 1996 over 10,000 enquiries per year led to 1,300 formal investigations into actual or alleged breaches of

the standards set out in 1976 regulations (DTI, 1999).

Over the years disputes over employment rights (in relation to home workers, lump labor, trainees and others as well as agency workers) have given rise to four tests which are used in law to determine when a worker might be defined as an 'employee' rather than 'independent contractor' (IRS Industrial Relations Law Bulletin, 533, November 1995). The *control test* examines the extent of the employer's control over how, where and when work is done. The *integration test* asks to what extent the worker or job is an Integral part of the organization. The economic *reality test* questions whether the worker is in business on his or her own account. And the *multiple test* takes all the circumstances of the case into account before making a judgement. Agency workers, however, are often particularly troublesome to define because of the tripartite nature of the relationship - agency, worker, and client business. (For a detailed discussion of the problematic nature of the relationship between the three parties, see Fenton-Jones, 1999).

Two more pieces of legislation of relevance are the recently introduced Minimum Wages Legislation, and the European Working Time Directive which came into force in the UK in October 1988. Minimum wages legislation applies to agency workers in the same way as to all employees - the impact is not clear, though MINTEL (1998) claims most agency workers were already paid above the minimum. The Working Time Directive specifies three weeks annual holiday after a three-month qualification period, and working hours limited to 48 hours per week (though there is provision for employee opt-out). There is also provision on rest breaks and night working. The Directive applies to temporary and contract staff working through agencies, many of who have had to renegotiate contracts with their temporary workers and clients (and indeed their own direct employees!) (MINTEL, 1998).

The biggest legislative impact on the employment agency industry could arise out of the adoption of the European *Social Chapter*, to which the present government is committed to implementing after signing up in June 1999. This puts pressure on the UK to bring its employment agencies in line with mainland European practice by making them liable for the full costs of employment protection, including redundancy. However, before the government signed the agreement, the European Commission had shifted from its previous position that temporary work was a low quality form of employment which should be limited to certain strictly specified circumstances, to one which asserts a 'symmetry of need' for temporary work between employers and workers (Murray, 1999). In other words, EU demands on the UK (and some other European countries) could have been far more extensive and radical in the absence of an ideological shift regarding temporary work. Whether such a shift will be maintained remains to be seen.

Perhaps partly in anticipation of EU pressure, one month before signing the *Social Chapter* the government's Department of Trade and Industry



published a consultation document on *The Regulation of the Private Recruitment Industry* that recognizes legal ambiguities and the scope for abuse of agency workers (and indeed client businesses). This document, which came out of the *Fairness at Work* White Paper, will form the basis for the introduction in early summer 2000 of a new set of regulations to govern the industry as part of *The Employment Relations Act 1999* (the White Paper and the 1999 Act are described briefly in Section one of this report).

Like the *Fairness at Work* White Paper, the consultation documentation on the regulation of employment agencies begins from the premise that 'fairness in the workplace' must go hand in hand with the continued pursuit of labor market flexibility. The document states (p.10)

If the industry is to continue to expand, it needs a modern legislative framework that ensures that the high standards set by reputable bureaux are not undermined by cowboy operators interested only in cutting corners.

Four objectives intended to inform the regulations are laid out as follows: (i) *increasing clarity*: in particular, client businesses should be given unambiguous terms which specify who is engaging whom on what basis, and work seekers should be given clear information about their employment rights; (ii) *promoting labor market flexibility*: outdated regulations which unnecessarily restrict employment agencies' activities should be removed, and agencies should not issue contracts to workers which restrict *their* flexibility; (iii) *proper protection for clients and the general public*: agencies should *themselves* ensure the suitability and qualifications of workers - especially for pilots, doctors, care workers, and other groups who have significant social responsibilities; also for workers being placed in jobs which could be hazardous without the correct training and experience; (iv) *curbing payment abuses*: the regulations must ensure workers are paid fully and on time for their work. In addition, the document makes it clear that under normal circumstances temporary workers supplied to a client by an agency should be treated *as employed by the agency*.

The final regulations are still to be seen, but it seems unlikely the government will stray from the principles established in the consultation document. How far they might go towards curbing malpractices remains to be seen, but it appears that the employment agency industry will have to make significant changes. If 'fairness at work' really could be established at the same time as labor market rigidities are reduced even further, this would be considered quite a feat.

### *Employment Agencies in Japan*

In Japan employment agencies are known as worker dispatching agencies (WDAs). Because of the harsh exploitation of dispatched workers before the Pacific war, WDAs were illegal right up until 1985, when they were

legalized for 26 allowable occupational categories. Legalization followed strong political controversy (Araki, 1994). The number of dispatched workers then grew from 145,000 in 1986 to over 700,000 in 1996, a little over one % of the Japanese working population. The categories allowed meant that most of these dispatched workers were female white collar.

In 1999 restrictions on allowable occupational categories (there were only 26) were abolished through an amendment to the Worker's Dispatching Law – suddenly only a few categories where serious exploitation was feared (notably including construction, security work and port work) were prohibited (Araki, 1999). The extension of allowable WDA activity was the result of government attempts to activate an external labor market which was seen as impeding the flow of workers between businesses during economic restructuring. WDAs were seen **as** a key means of providing the rising ranks of unemployed in the mid to late 1990s with employment opportunities and career development choices. (Around the same time private employment placement services were given legal permission to extend their activities, with the same object of improving labor market flexibility in mind.) As in the UK, the WDA is expected to be the employer of the dispatched worker while they are under the direction of the client company, though (also as in the UK) there are cases where the client company has been held up in law to be the employer (Yamakawa, 1995).

The revisions to Worker Dispatching Law in 1999 were preceded by heated debates in the tripartite Employment Security Council and in the Japanese Diet, the outcome being a compromise whereby WDAs were given **the** go-ahead to extend their activities at the same time **as** regulations governing their operation were tightened. Fears that client firms might use dispatched workers to replace permanent workers were addressed through a one-year limit on their use in the same post at a client company. Further, under the new law client companies are legally obliged to offer dispatched workers the same working environment as their own employees, and dispute resolution and personal information protection mechanisms are made tighter.

The growth of WDA activity is likely to be substantial, but tightened regulations associated with legalization – such as restrictions on renewals of dispatching contracts – could conceivably limit the emergence of a 'hire and fire mentality'. While we await evidence of the impact of **the** new legislation and the response of client firms to the new employment possibilities, we can only speculate on the likely consequences for the Japanese employment system.

### *Employment Agencies in Korea*

Prior to the legalization of temporary work agencies (TWAs) in Korea in 1998, the government had turned a blind eye to grey market TWA activities. Surveys by the Korea Labor Institute prior to legislative change suggested that while employers claimed positive effects on labor market flexibility,

dispatched workers were provided with far poorer wages, social protection and employment terms and conditions than their permanent counterparts. (Park *et al.*, 2000). The number of agencies was not known.

The Act Relating to Protection, etc. for Dispatched Workers became effective in July 1998. This rules out ambiguity over employment status by specifying that the TWA, not the client company, is the legal employer. The TWA must gain approval to operate from the Ministry of Labor, and this approval has to be renewed after three years. There are restrictions on the type of work dispatched workers may be used for, and on the length of contracts (one year renewable for a maximum of one further year), and there is requirement for consultation with the trades union prior to engagement of temporaries under some circumstances. Various legal safeguards to prevent abuse of dispatched workers are included in the Act. and at the same time the Act provides guards against the use of dispatched workers to replace permanent employees.

By the last quarter of 1998, a few months after passage of the Act, 789 TWAs had gained legal permission to operate from the Ministry of Labor, increasing to 1,095 by the second quarter of 2000. (A little over a quarter of these were not currently operating.) The numbers of dispatched workers accounted for by registered agencies grew from 41,545 in the last quarter of 1998 to 46,407 in the second quarter of 1999, representing 0.23 % of Korean employees. While the average size of TWAs is very small, a few agencies have been growing rapidly, and agency industry concentration via mergers and acquisitions is expected.

Park *et al.*'s (2000) survey of 483 firms found 37 % of the sample using dispatched workers, with 43.9 % planning to introduce or extend their use. Larger firms in banking, retail and other services were most likely to use them, though they were commonly found across a range of sectors and firm sizes. Employers were generally positive about the effects of TWAs on labor market flexibility, but felt the periods of temporary work allowed and the limitations on job types were too restrictive. Union officials, on the other hand, felt the regulations provided insufficient protection for agency workers, and that permitted jobs were too comprehensive.

While it is clearly too early to **attempt** to judge the impacts TWAs will have in Korea, it is clear that employers are likely to gradually extend their use. However, as in Japan (but not yet the UK) the adoption of tight regulations under pressure from the labor movement could limit their usefulness to firms wishing to practice 'hire and fire' policies.

### **Flexible Labor Markets and Employment Agencies: Economic and Social Consequences**

Two popular arguments are used to legitimate employment agency activity,

and the promotion of temporary working generally: 'more employment' and 'better employment' (Murray, 1999, p.273). 'More employment' and 'better employment' need to be broken down a little further, and in this section various evidence and argument is examined in order to pass comment on the potential economic and social consequences of the expansion of temporary employment agency activity. In particular we examine the consequences for: (i) overall employment levels and labor adjustment; (ii) skills development, innovation capability and quality; (iii) labor rights and representation; and (iv) worker well being. Evidence is taken primarily from extensive research undertaken in the UK, and this is used to point to the issues which may need to be addressed in Korea (and Japan) as temporary work agencies gradually extend their activities.

### *Employment, Skills, Rights and Well-being*

It is frequently argued that labor market flexibility has beneficial effects on employment by improving the prospects for job creation (and also low inflation and productivity growth) (OECD, 1986). Indeed this was a central tenet of the Conservative administration in the UK which, despite its poor record in the preservation and creation of jobs for most of its tenure, could report a consistent reduction in unemployment whilst maintaining low inflation during its last three years in office in the mid-1990s. Further, it was claimed the UK emerged from recession before many European countries in the 1990s because employment legislation had made labor adjustment easier, so that employers were more willing to take on extra labor (Guest, 1997). Recently the European Community has begun to move from an active labor market intervention stance (Potts, 1999) towards an acceptance of a relationship between flexible labor deployment and the achievement of high employment (Barnard and Deakin, 1999). Employment agencies are seen to play a key role in encouraging and enhancing flexible deployment by matching workers to companies at the same time as handling employment obligations – effectively agencies help reduce the costs and risks of hiring and firing labor to the client firm.

However, there is little direct evidence on the effects of flexibility on employment creation, and what little research has been done often uses dubious proxies such as presence of a trades union or presence of temporary workers as indicators of flexibility within sample firms (Haskel *et al.*, 1997). Further, separating out the effects of flexible employment practices from other variables is a difficult task, such that results of studies, whether positive or negative, are always likely to be open to alternative interpretation.

Haskel *et al.*'s own research suggests that labor input (in terms of hours worked and/or numbers employed) is more responsive to demand change in a flexible labor market. This means that 'whilst flexible firms are more likely to create jobs in upturns they are more likely to destroy them in downturns' (p.375). More flexible firms find it less costly to adjust the size

of the workforce and therefore are more responsive to business cycles, and this may help explain why employment picked up much quicker following the early 1990s recession compared with the early 1980s recession (Beatson, 1995). This research does not tell us, however, about the long-term effects on overall employment levels, which remain subject to debate in the absence of systematic evidence, and the consequences for productivity remain unclear. While Beatson (1995) found some evidence of an association between the extension of flexible working and a better productivity performance in the UK, a European Commission Expert Working Group concluded that 'when employment relationships are more precarious, motivation and willingness to cooperate are likely to be lower, with negative consequences for firms' productivity' (Bosch, 1994, p.26). Nor does it tell us about other potential benefits or costs to national economies, to which we now turn.

Evidence with regard to the relationship between labor force flexibility, skills formation and product and service quality in the UK is mostly negative. Arulampalam and Booth's (1998) study of flexible employment and training concluded that the expansion of flexible forms of employment was negatively related to work-related training. The Institute of Management and Manpower (1996) found that the use of flexible manpower was mostly driven by cost considerations, and one of the costs that could be minimized was training. Casey *et al.* (1999, p.76), in a review of research findings in the area, found that

in many cases managers have sought to employ flexible workers precisely in order to distance themselves and the employing organization from the individual employees and to minimise the organization's obligations and commitments towards that worker.

It also appears to be the case in the UK that temporary work often goes hand in hand with low cost product strategies. Casey *et al.* (1999) use the examples of the hospitality sector and services contracted out from the public sector to make the point. In both cases, temporary labor is chosen *because* it helps cut costs: once chosen, it is difficult to move to higher value offerings because it produces conditions 'that render the sophisticated, developmental people management systems the high performance model demands almost impossible to achieve' (p.76). Not dissimilar findings have applied to UK manufacturing too. A review of the evidence available by Ackroyd and Procter (1998) led them to conclude that large UK manufacturing organizations were not using the high value, high trust flexible firm model as advocated by the EU and OECD. Nor were they developing product market strategies, employment practices and people management systems that would provide for the emergence of such a model. Relatedly, it has been argued that the removal of labor market rigidities in the long run have a detrimental effect on the product and process innovation capabilities

of firms (Kleinknecht, 1998).

There are a few exceptional areas where highly skilled and professional workers such as IT consultants, interim managers and research and development workers carry scarce skills between organizations, often via employment agencies. For these workers temporary work is often taken out of choice rather than necessity: they benefit the client organization with their specialist skills, and they gain a degree of control over their own working time and income.

Flexible work practices do not *have* to be associated with low cost, low value strategies, but the evidence to date suggests this is the route most UK employers have taken. The present Labor government perhaps recognizes it must play some role in guiding employers along desired paths. Tregaskis (1997) is skeptical of the prospects for individual workers taking on responsibility for their own skills development, and suggests the state should extend its 'public-private partnership' ideas more firmly into workforce skills development activities, with 'training partnerships' between employers, individuals and the state. This might help improve individuals' future 'employability', eventually creating a virtuous circle whereby the organization will have to provide learning opportunities for highly skilled candidates. It is also feasible that the forthcoming Employment Agencies legislation could have some impact, at least for those employees who gain temporary jobs through the agencies, though developments here are difficult to foresee. However, in the absence of at least some government intervention, it seems likely that the flexibilization of the UK labor force will continue to 'undermine the national policy objective of securing the upskilling of the UK workforce' (Casey *et al.*, p.76).

Employee representation and contingent labor rights have been found to be problematic issues. Union membership among '*flexible*' workers has been found surprisingly high at around 30 %, though problems with defining 'flexible workers' (see section one) might mean this figure is an overestimate. Probable reasons why unionization is higher than might be expected are that many types of 'flexible worker' are most common in larger workplaces where union density is highest (Labor Market Trends, 1998) and that unions in the UK actually have a reasonable tradition and good experience of recruiting contingent labor – in hospitals, docks and taxi driving for instance (Croucher and Brewster, 1998). For many of the newer types of flexible worker, however, unions face particular difficulties – of recruitment, communication, and provision of cost effective services. Temporary agency workers who occasionally or frequently move clients are particularly difficult to deal with. Their dispersal means unions are rarely in a position to offer them collective bargaining services, and frequently it is not clear whom they should be bargaining with (Croucher and Brewster, 1998). The latter problem might be partially resolved with the changes to employment agency legislation due in summer 2000 (see section two).

At the same time as trying to find ways to extend representation of the

contingent labor force, unions have been vocal politically about the spread of temporary working. A motion supported by the General Council at the Trades Union Congress of 1994 noted that

Agency workers...are continuously denied employment rights as they are moved on to different workplaces. In addition, agency workers are often denied all the pay and conditions benefits provided under collective agreements and opportunities for training provided and/or paid for by their employers. (TUC, 1994)

The motion included a call for the reform of statutory employment law to provide full employment rights. It should be emphasized, however, that the trades union movement is not against temporary working *per se*. TUC Secretary General John Monks has recently commented that workers must be flexible in a 'twenty four hour society' with round the clock services. The point is that employees should have more choice and flexibility themselves to determine times worked: employers must keep their side of the psychological contract (*IRS Employment Review*, no.163, December 1999).

In reviewing research and literature on the implications of contingent working for the psychological and social well-being of workers it quickly becomes apparent that the negative viewpoint is most strongly represented. However, there are those who point out significant potential benefits to workers. The two benefits most commonly cited are contingent working as a means to enhance lifestyle, and as a means to work whilst continuing family care responsibilities (Bronstein, 1991; Osawa and Kingston, 1996). The former benefit is largely restricted to those with scarce skills who can develop more than one 'income stream' which enables them to gain control of their working time (a relatively small but growing proportion of the UK workforce). The latter relates primarily to part-time work, which, it is almost universally agreed, does benefit parents with families by allowing both parents to undertake some paid employment. Of course much part-time work is also *permanent*, and is not necessarily of the precarious kind found in other categories.

The government's view is that temporary working *can and should* be 'family friendly', and Wood (1999) has produced evidence that in certain types of organization 'family friendly management' is being institutionalized. These are large firms that place a high value on employee welfare and see a 'bottom line' in adopting family friendly policies and gaining workforce commitment. The consensus, however, is that such firms are thin on the ground. An Institute of Personnel Development study (Stredwick and Ellis, 1998) describes flexible working as often a euphemism for chronic instability and exploitation: 'the threat of flexible working lies in the increased potential for employee exploitation, unregulated sweated labor and the end of the meaningful long term employment relationship'. And on the

basis of its extensive of handling temporary workers' grievances the independent National Association of Citizens Advice Bureaux (1997) comments that:

For many (employers) flexibility means withdrawal from the responsibilities associated with the employment relationship. From this perspective, basic employment standards such as protection from unfair dismissal and decent rates of pay are seen as constraints on flexibility, and so damaging to the health of the economy.

Purcell *et al.* (1999) found positive benefits for employees where flexibility was 'sensibly managed' and not exploitative, but that the costs of temporary unstructured employment outweigh the benefits unless employees have scarce skills and can be involved in choosing when and where to work.

In sum, if the published evidence provides a reasonably accurate portrayal of worker well being under conditions of temporary work, there is a way to go before 'symmetry of need' between employers and workers comes into existence.

## **Policy Issues**

Among other forms of contingent working, temporary work agencies have been accepted as a legitimate means of enhancing labor market flexibility in furtherance of economic and societal objectives in Korea (and Japan). While it appears unlikely that the principle of temporary work agency activity will be challenged in the foreseeable future, policy issues related to their use will be carefully debated in the light of agency behavior and in the light of the experience of agency activities from the perspectives of the state, employers, labor and trades unions. Following discussion of the consequences of labor market flexibilization and temporary work agencies in the UK, the four key areas which will become the focus of concern are clear.

Firstly, *do temporary work agencies help employment creation?* Evidence from the UK and elsewhere is ambiguous. It is generally accepted that agencies can contribute to the efficient matching up of labor supply and demand. Park *et al.* (2000) found that Korean employers were positive about the effects of TWAs on labor flexibility, effects which they suggested would be even more positive if there were fewer restrictions on the use of dispatched workers. However, the contribution of labor market flexibility generally, let alone specific flexibility mechanisms, to long term employment creation remains unknown as problems of measurement and methodology dog research. Until these problems are resolved, this key policy question will remain the subject of ideological debate in the absence of unambiguous evidence.



Second, *what is the relationship between employment agency activity and skills formation?* Here most of the evidence from the UK (and US) strongly suggests a negative relationship except for a small minority of highly qualified agency labor such as consultants, interim managers and research staffs, who develop and update their portfolio of skills as they move between assignments. So far in Korea, most agency labor has been employed in unskilled jobs which demand relatively little training (Park, 2000) such that the impact on skills formation is likely to be neutral for the employer and negative for the employee. The question then becomes how to establish the conditions whereby a positive relationship can occur. 'Training partnerships' between the state, employers and/or agencies, and labor have been mooted as a way forward in the UK, though we await developments on this front. In the meantime the objective of upskilling the UK workforce may continue to be undermined by short term employment practices and 'hire and fire' policies. Korea needs to avoid such a development.

Third, *what are the employment rights of contingent workers generally and temporary agency labor specifically?* In the UK employment status is highly ambiguous and many agency workers are unclear even as to who their employer is. The current government has recognized this as a serious problem and promises to address the issue in forthcoming legislation. The new legislation on agency work in Korea (and Japan) is rather less ambiguous on this front, though it will be important to monitor the situation carefully to prevent abuses by unscrupulous agencies or employers. Park *et al.* found that Korean employers felt the level of legal protection afforded agency workers was adequate, whereas Korean union representatives felt there was a need for tighter legislation on working conditions and a need for measures to prevent 'wage appropriation' by agencies. Employment rights for temporary workers will undoubtedly be a policy issue for Korea in the years to come.

Fourth, *how can a balance between employer and employee needs be achieved?* Contingent working as a means to enhance lifestyle or combine work with family care responsibilities is frequently argued. But several studies have demonstrated that for the majority of contingent workers in the UK such benefits are imaginary. While 'family friendly' employment policies are now on the UK (and Japanese - see Sato 2000) political agenda, the whole rationale of employers in their use of temporary workers is to do with *their own* flexibility. (It is worth noting here that Korean temporary worker well-being may be less likely to appear on the national political agenda than is the case in the UK because far fewer temporaries are unionized and they have little by way of other means of representation.) Conceivably temporary work agencies could play a role in matching employees' needs for employment flexibility with those of employers, but the evidence suggests that at the moment it is the agency workers who have to make the adjustments. Industry concentration which could enable the emergence of larger and more professional employment agencies could be a

basis for changing this situation (Park *et al.*, 2000), but evidence from the US, where large professional outfits already dominate the agency market, would suggest this development in *itself* would have little impact (Houseman, 1999).

## **Conclusion**

In accepting IMF loans Korea has been pressured into accepting reforms of its systems of economic and corporate governance, entailing among other things significant changes in labor market adjustment mechanisms. In the space of less than two years employment security for core workers has been drastically reduced if not curtailed, and the national labor market has been significantly freed up. The speed of change is reflected in the fact that temporary work agency activity was liberalized sooner than in Japan, which had been debating extensions of the role of dispatched workers under recessionary conditions for several years previously. While consensus among the interested parties was gained for the principle of labor market flexibilization and the adoption of employment agencies through Korea's Tripartite Commission, accelerated implementation of new worker dispatching laws under crisis conditions in Korea meant little time for considered internal debate over its potential costs and benefits, and how these might be dealt with.

As employment agency activity grows, further consideration in the light of solid documentation needs to be given. The experience of the UK could be a good starting point. While the results of research are in some respects inconclusive, and while lessons from one society are not necessarily easily transferred to another, the areas of serious concern and therefore in need of careful monitoring are quite clear. It is hoped this paper has pointed clearly to these areas and thereby might contribute to an important policy research agenda.

**PART IV**

**ACTIVE LABOR MARKET PROGRAM**



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# 9 Income Assistance and Employment Creation through Public Works in Korea

Joohee Lee'

## Instruction

Public expenditure on labor market programs was almost negligible in Korea before the financial crisis in the winter of 1997. Throughout the 1990s, Korea spent less than 0.1 % of GDP on these programs, one of the lowest rates in the OECD. The relatively small amount of spending reflects the low level of unemployment (OECD, 1998, p. 148). Compressed industrial transformation in Korea has constantly created new jobs in the nonagricultural sectors of the economy, and as a result Korea was accustomed to near full employment for several decades. This picture has significantly changed after the crisis. The growth in employment was radically reversed by the severe economic recession in 1998. Due to the recession the unemployment reached 6.8 % in 1998, and 6.2 % in 1999. Although still lower than the average OECD spending, Korean public expenditure on unemployment measures expanded to 1.26 % of GDP in 1998, and to 1.87 % in 1999 (Jeong *et al.*, 2000).

One notable feature of Korean public spending on unemployment measures was that it struck a balance between passive income support and more active measures<sup>1</sup> that were designed to improve access to the labor market for the unemployed and to improve the employment situation. Except for a few countries, the share of spending on passive measures was far larger than that on active measures in most OECD countries. On the one hand, it is a promising sign that Korea is in line with the general principle of

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\* Korea Labor Institute.

<sup>1</sup> For analytical and policy purposes, the OECD splits public spending on labor market programs into 'active' and 'passive' measures. Active measures comprise a wide range of policies aimed at improving labor market access for the unemployed and the employment situation, job-related skills and the functioning of the labor market (Martin 1998).

shifting public resources from income support to active labor market policies, a shift that has been endorsed by many Labor Ministers in developed countries (Martin 1998). On the other hand, however, social assistance programs in Korea are in general underdeveloped, with numerous cut-off levels for eligibility and restrictions in entitlements. As Korea lacked broad based social assistance programs, the situation was quickly reached where Korea had to accommodate a number of the unemployed who were not eligible for unemployment and at the same time not sufficiently poor enough to be covered by livelihood protection programs.

It is in this context that public works projects emerged as a crucial unemployment measure in the overall system of income support and social protection. In 1998, over 1 trillion won was poured into the projects, and in 1999, about 2.5 trillion won (Lee 1999). Although officially classified as an active measure, these schemes mostly played an important role as complementary income support in Korea. Even in developed countries it is a common phenomenon that many active measures tend to become inadvertently 'passive' during periods of high and persistent unemployment as there is more emphasis on the social objectives of the projects than on their efficiency objectives (OECD 1998). This is the reason that Korean public works projects should not be solely evaluated based on the net effects of programs on aggregate employment and unemployment. This research therefore attempts to evaluate the distribution effects of the projects as well as employment effects.

As some projects hastily made by the unprepared municipalities were not always effective or useful to the public, the private sector was increasingly critical of the projects, regarding them as "unnecessary make-work".<sup>2</sup> Actually, most evaluations show that subsidized employment schemes are ineffective due to considerable dead-weight, displacement and substitution effects (OECD 1998). However, the system-wide effects of the public works projects, which were not easily measurable, could be more beneficial than expected. The projects boosted and created effective demand, and provided much needed services to the disabled, the elderly and children of low-income families. Thus whether the projects bear beneficial outcomes, along with unexpected externality effects, is also investigated in this paper.

The remainder of this paper is organized as follows. The next section provides a detailed description of Korean public works projects. It is followed by sections that seek to advance an analytical discussion regarding the various dimensions of project evaluation, and explanations of the research methods utilized to conduct project evaluation. The majority of empirical work in the result section is devoted to the impact of project

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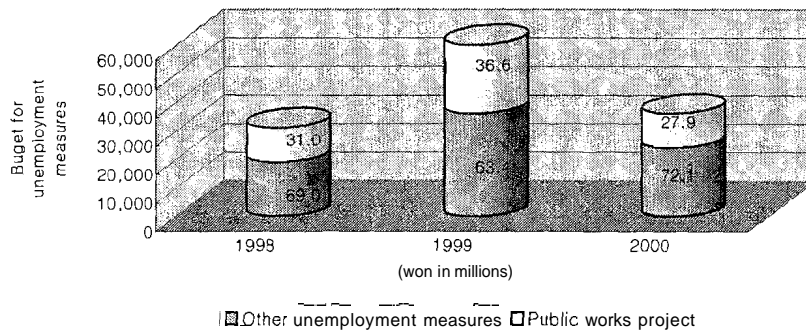
New Deal emergency relief projects were similarly criticized in the U.S. For more information on this issue, see Rose (1994). She argues that inefficiency was built into the public works projects because these projects were mandated to use a maximum of human labor and a minimum of machinery.

participation on individual workers, but it also briefly engages in a broader discussion of project effects on the national economy. In the final Section, we conclude this study by recapitulating the findings and discussing future policy agenda, with special emphasis on their relationship with the Basic Livelihood Security System for the Nation to be enacted in October 2000.

## Project Profile

Public works projects were implemented as a two-stage project in 1998 (Phase I: from May to August; Phase II: from September to December), and as a four-stage project in 1999 (Phase I: from January to March; Phase II: from April to June; Phase III: from July to September; Phase IV: from October to December). As shown in Figure 9. 1, the projects consumed a substantial portion of the entire budget for unemployment measures. The public works projects generated about 400,000 jobs on average during the year 1999.

Figure 9.1: Budget for public works projects in Korea, 1998-2000



In general, the public works projects fell into four broad categories. Infrastructure works (*kongkong saengsansung*) projects involved forestation, new construction of small public facilities such as community parks, and repairing public property. Public service (*kongkong service*) projects provided temporary workers to public organizations and community welfare service centers. These public workers engaged in a variety of activities, which ranged from managing cultural assets in national museums to teaching children from low-income families in after-school classes. Maintenance (*Hwankyung Chit Inghwa*) projects were mainly composed of such activities as garbage collection and lawn maintenance in national parks,

snow removal, and street cleaning. Information Technology (*Chungbohwa*) projects, added to the public works programs in 1999, can be classified as professional or nonmanual projects. Relatively young and educated workers were included in this category, and they mostly constructed database, and provided assistance on resolving the year 2000 computer problems.

In 1998, those who wanted to participate in the programs had to be unemployed persons between 15 to 65 years old. In Phase II of 1999, age restrictions were tightened to include only those between 18 to 60 years old, which brought about wide-spread complaints from the old unemployed about the selection procedure. At last, those between 61 to 65 were allowed to participate as long as they were within the 5 % of the total selected participants in Phase III of 1999. Selection criteria are different depending on the skills and credentials required by the particular projects. But priorities were given to the head of the household, those in their prime working age, i.e., 30 to 55 years old, and the poor unemployed. Since Phase III of 1999, screening decisions have been made based on the aggregated scores given to the following 9 factors: age, householder status, number of dependents, assets, female householder status, handicapped, duration of unemployment, the first-time participant status, and household income.

Changes in wage rates for the public works projects are shown in Table 9. I. There were no differentials in wages by sex or by age. At the end of Phase II 1998, wage rates were highest, paying about 35,000 won per day to those performing professional work, and 25,000 won to low-skilled manual workers. Determination of the wage rates was controversial process as the business sector argued for lower rates. This criticism has led to the reductions of wage rates, once in Phase II of 1998, and again in the beginning of the Phase I 1999. These rates were maintained through Phase I 2000. As wage rates had been reduced, the projects began to attract more and more disadvantaged workers in the regular labor market. Table 9. 2 demonstrates this point. Women, less educated, and older workers dominated the projects by the end of the Phase IV, 1999.

**Table 9.1: Changes in wage rates for public works projects in Korea**

	1998 Phase I	1998 Phase II	Oct. 1, 1998	1999
	(won)			
Low-skilled office work	20,000	22,000	22,000 or less	19,000 or less
Manual labor	25,000	25,000	22,000 or less	19,000 or less
Labor-intensive manual Labor		30,000	27,000 or less	24,000 or less
Professional work		35,000	32,000 or less	29,000 or less



**Table 9.2: Characteristics of the public works project participants in Korea, 1998-1999**

	1998		1999			
	Stage 1	Stage 2	Stage 1	Stage 2	Stage 3	Stage 4
	(% )		(% )			
<b>Sex</b>						
Male	67.7	57.0	58.7	50.5	45.6	44.0
Female	32.3	43.0	41.3	49.5	54.4	56.0
<b>Education</b>						
Primary school or less			37.4	36.0	34.7	40.0
Middle school or dropouts			22.3	23.3	21.3	22.3
High school or dropouts			27.2	27.3	27.1	24.1
2-year college or dropouts			5.0	4.9	6.1	5.1
University dropouts or higher			8.0	8.5	10.7	8.5
<b>Age</b>						
Under 20	1.2	0.7	1.0	0.9	1.3	1.2
20 - 29	12.0	8.8	11.6	13.5	16.0	13.0
30 - 39	20.7	19.6	22.7	21.4	18.8	16.6
40 - 49	26.1	26.9	32.4	30.4	27.2	26.2
50 - 59	27.6	30.6	27.4	22.5	29.0	37.3
60 - 65	12.4	13.4	5.0	11.2	7.8	5.8

## Principle Objectives of the Public Works Projects

Public works projects in Korea have not simply been job creation programs. As in other debt-stricken developing countries, poverty as well as unemployment became a much greater problem. This problem was exacerbated by the fact that Korea lacked a pure income maintenance program for the unemployed. The Korean government expanded the existing livelihood protection programs<sup>3</sup> in order to provide temporary relief for the unemployed that did not qualify for unemployment insurance. In order to be eligible for the original program, one should have income less than 230 thousand won per month, must pass an asset test, and must have no family that can support them. This program was mostly for those who were unable to work, such as the handicapped, elderly, and children. The temporary livelihood protection program eased some of its strict means-test criteria to cover additional people, however, it is still too limited in its coverage and

<sup>3</sup> Korea introduced social assistance long before it introduced programs of universal social insurance. A case in point is the livelihood protection program, created by livelihood protection act in 1961.

generosity to complement unemployment insurance and to substitute for unemployment assistance. Among those covered under the program, more than two-thirds were classified as the "self-supported," for whom cash benefits were not available except during winter.

Thus the expanded public assistance scheme in Korea was not well equipped to function as an ultimate safety net of income support for the newly unemployed. This was the reason that the public works projects had to offer short-term income opportunities to those newly unemployed. Therefore whether the public works projects actually cover the major target groups with high unemployment risks,<sup>4</sup> especially the low skilled, the long-term unemployed, and the poorly unemployed heads of the household is an important indicator that measures the distribution effect of the public works projects. It is also necessary to explore the economic status of women participants, as they were frequently suspected of being economically inactive people who were not eligible for the projects. If these participants turn out to be the actually unemployed, and non-beneficiaries of the other unemployment measures, the distribution effect of the program can be more positively evaluated.

The major goal of the direct employment creation projects was to increase the available number of jobs while satisfying the needs that were not met by the private sector. To put it otherwise, public sector job creation should not compete with or substitute for existing jobs. Although the direct effect on employment creation seemed significant, the literature on labor market policy and evaluation (Forslund and Krueger 1994; Calmfors 1994) has cautioned that the net impact of job creation, that is, gross impact minus deadweight, displacement and substitution effects, could be much less than expected. Furthermore, public sector job creation could produce indirect employment effects that may or may not be favorable for labor market outcomes of project participants. In order to assess such net impact of public works projects on job creation, the following concerns must be fully explored.

First of all, labor market outcomes for participants are not always positive. Participation in the projects may stigmatize them, reducing reemployment opportunities and future earnings. Second, the net employment generated by a public employment program decreases in proportion to the incidence of

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Freedman (1990) explains why public employment programs often fail to meet the eligibility requirements as follows. First, those who suffer the most serious economic and educational disadvantages may be the most difficult to reach for reasons of access to information about and personal attitudes towards the programs. Second, programs and project organizers are often concerned with producing results that look good on paper, and may tend to favor participants who are likely to fare well in the programs. Third, where programs offer employers a subsidy to hire members of the target group, it is likely that "creaming" will occur, i.e., employers will seek to minimize their risks by selecting those participants who appear better qualified.

deadweight losses, or fiscal substitution,' such as when a local administration takes advantage of a federal subsidy to create a job that administration would have created otherwise (Erhel *et al.*, 1996). Such an effect is only indirectly investigated in this study. Programs targeted on the disadvantaged would be less vulnerable to fiscal substitution because these target group workers are seldom qualified to do a job that required regular employees. Third, the employment creation effects of the public works projects diminished if the projects made participants continuously dependent on the projects. This problem is called the locking-in effect. It is therefore necessary to investigate whether participants want to continue their participation and how long the participation would last. Finally, subsidized employment schemes such as public works projects may have a number of objectives other than creating additional jobs. They may enhance effective labor supply by helping individuals to keep in contact with the world of work, thus maintaining their motivation and skills (OECD, 1998). Again, this effect cannot be directly measured, but it is necessary to investigate whether project participation enhances willingness to work by surveying the attitudes of the participants.

## Research Methods

The empirical research reported in the following section was based on a survey of project participants, conducted during September-October 1999. The sample for this survey consists of adults who participated in the public works projects during 1998 and 1999. Respondents were sampled with a multi-stage cluster sampling procedure. The integrated list of those who participated in central government projects in 1998 was not available, so they are excluded. This exclusion should not lead to a serious bias in analyzing the data, as public works projects in general were most extensively implemented in 1999, and a majority of participants worked for local government projects. There were also no compelling reasons to believe that those who participated in 1998 central government projects differ significantly from those participated in 1999 projects.

Those who participated in 1998 local government projects were sampled based on local government participant lists, and those who participated in 1999 central and local government projects were sampled based on the lists obtained from the central employment information institution of the labor ministry. Among 1578 cases selected, a total of 1505 cases were collected

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<sup>5</sup> Schmid (1996) argues that whereas efficiency is always impaired by deadweight effects, displacement and substitution might be intentional. Preferential treatment for one person at the cost of another – promoting women at the cost of men, long-term employed at the cost of short-term employed- can be an explicit social policy.

via personal interviews conducted during the summer of 1999. Regional allocation of the samples are as follows: Seoul (274), Kyungki (289), Inchon (52), Kangwon (84), Pusan (144), Ulsan (33), Southern Kyungsang (107), Taegu (105), Northern Kyungsang (113), Taejon (50), Southern Chungchung (94), Northern Chungchung (45), Kwangju (48), Southern Cholla (80), Northern Cholla (60). Since it was virtually impossible to form a benchmark or control group of individuals who did not participate in the projects, we were not able to directly judge and compare earnings and employment outcomes of the participants against non-participants.

### *Data Description*

Table 9.3 shows that overall, men accounted for 45 %, and women 55 %, of respondents, which closely reflects the characteristics of population reported in Table 9.2. However, younger participants were overrepresented, and older participants were underrepresented in the sample. The mean age of respondents was slightly over 42 years. Similarly, highly educated participants were overrepresented, especially those who were college graduates. Those who held the legal head of the household status were 50 % of respondents. The mean household size was 3.5 persons. For those married only, about 56 % of respondents had unemployed spouses.

Participation in public works projects has grown rapidly since the beginning of 1999. The projects were most extensively implemented during Phase I and Phase II of 1999. During that time, the number of unemployed, employed, and economically inactive respondents was subsequently reduced. A large number of respondents (66.8 %) participated in public works projects run by the local governments, and only 6.4 % of respondents participated in the central government information technology projects in 1999. About 27 % of the respondents participated in other central government projects in 1999. A majority of respondents (78.4%) participated in the projects to support a family. A majority of respondents participated in the projects just once or twice, and when they participated in the projects, they seldom quit the projects.

## **Results**

### *Income Assistance: distribution effects*

Although half of the respondents own houses, the average monthly household income of all respondents was just 950 thousand won (Table 9.4). Considering that the average household size was 3.5 persons, this amount was close to the poverty line. The minimum cost of living for a household with 4 persons was 930 thousand won in 1999.

The public works projects have received a great deal of criticism due to women participants not being considered eligible for the projects. The survey results in Table 9.5 demonstrate that these women came from economically disadvantaged households, where almost half of them (44.3 %) were major breadwinners and half of those married women's husbands were unemployed.

Table 9.3: Descriptive statistics for survey respondents' characteristics  
(total =1505)

Characteristics	(%)
<b>Sex</b>	
Male	45.0
Female	55.0
<i>Age</i>	
Age 20'	1.0
Age 21 to 30	27.2
Age 31 to 40	15.3
Age 41 to 50	23.1
Age 51 to 60	28.2
Age 60*	5.1
Mean age (SD)	42.1(13.2)
<i>Schooling</i>	
Elementary School	32.1
Middle School	16.9
High School	20.9
College or university	30.0
<i>Family status</i>	
Head of the household	50.0
Dependent	50.0
Mean size of household (SD)	3.5(1.4)
<i>Marital status</i>	
Married	54.0
Never married	30.0
Separated, divorced, widowed, etc	16.0
<i>Employment status of spouse (married'only)</i>	
Regular worker	12.0
Atypical worker	22.6
Self-employed	6.1
Non-paid family worker	3.0
Unemployed	56.4

**Table 9.4: Economic status of survey respondents**

Characteristics	(%)
<i>Housing</i>	
Own house	55.0
Chonse <sup>1)</sup>	22.0
Monthly rent	19.6
Other	3.2
<i>Major breadwinner</i>	
Respondent	51.8
Spouse	17.3
Parents	21.9
Child(ren)	5.4
Other family members	3.5
<i>Household income(won)</i>	
Monthly household income	950,000
Monthly household expenses	860,000
<i>Indebted</i>	
Yes	37
No	63
<i>Loan amount and payment (indebted only)(won)</i>	
Total amount	17,500,000
Monthly payment	170,000

Note: 1) A rent system in which the tenant pays a lump sum to the landlord and the tenant gets the money back when s/he leaves

Respondents spent 4.97 months on average participating in public works projects from January 1998 to July 1999. On average, they were employed for 4.04 months, unemployed for 5.31 months, and economically inactive for 4.68 months. Those who were employed for less than a month amounted to 46.7 % of respondents, which reflects the harsh labor market conditions after the financial crisis. Those who were unemployed for less than a month amounted to 40.7 %, and economically inactive for less than a month 54.3 %. These figures imply that a portion of participants might not be the unemployed, and the projects might have activated previously economically inactive population. The proportion of economically inactive population did not significantly differ by sex and residence.

Only 15 % of respondents benefited from unemployment policies other than public works projects. The number of respondents who received NGO's relief activities was even smaller, being just 31 persons out of 1505

**Table 9.5: Economic status of survey respondents by sex**

	Male	Female
	(%)	
<i>Legal householder status</i>		
Head of the household	74.0	30.0
Dependent	26.0	70.0
<i>Major breadwinner</i>		
Respondent	61.0	44.3
Spouse	10.7	22.7
Parents	20.0	23.5
Child(ren)	4.2	6.5
Other family members	4.2	3.0
<i>Employment status of spouse (Married only)</i>		
Regular worker	8.8	15.5
Atypical worker	21.1	24.6
Self-employed/employer	5.1	7.3
Non-paid family worker	5.0	1.2
Unemployed	59.9	51.4

**Table 9.6: Types of benefited unemployment policies (total=248)**

Characteristics	(%)
Livelihood protection program	<b>54</b>
Unemployment insurance	1
Vocational training	43
Loan schemes for the unemployed	1
Tax exemption	0
Others	1

respondents. A majority of the beneficiaries of government unemployment measures have participated in either livelihood protection programs or vocational training programs. Table 9.6 demonstrates that most public works project participants have not been benefited from other unemployment measures. In sum, the public works projects did appear to help those who needed social protection due to a sudden and massive upsurge of unemployment and poverty.

*Job Creation: Labor Market Outcomes*

A large number of project participants were previously atypical workers, such as daily, temporary, or non-paid family workers. By occupation, they were also predominantly unskilled manual workers (Table 9.7). This table also illustrates that the employment structure of those 399 workers who found jobs after the project participation remained surprisingly similar to the employment structure shown before project participation. About 42 % of respondents answered that the compensation and working conditions of their current jobs were worse than their previous jobs, whereas only 18 % experienced improved compensation levels and working conditions in their current jobs. It suggests that the project participants had to face harsher labor market situations as a result of the financial crisis, and they took jobs that were inferior to their previous ones instead of lingering on the public works projects.

Respondents' desired job characteristics, however, were significantly different from respondents' previous job characteristics and the current employment structure of those who were able to find jobs. Almost 80 % of respondents who are searching for employment prefer to have a regular job, whereas only 34 % of respondents who were previously employed had regular jobs. Their desired wage rate (96 thousand won) was much higher than the rate of those who found jobs after the project participation (70 thousand won). The respondents' strong desire to have a regular job is to a certain degree related to the fact that these projects were designed to be implemented for a relatively short period of time, i.e., two and a half months, in order to provide stronger incentives for job search activities.

Logistic regression coefficients for regression of job attainment after public works project participation on several independent variables are reported in Table 9.8. The regression equation for the model reveals that male workers, younger workers and major breadwinners in the households were more likely to attain jobs after participating in the projects. Compared to the manual labor workers, those participated in the DB construction, mainly low-skilled white-collar workers were less likely to find jobs. Workers who were unsatisfied with working conditions, wage rates, labor intensity, and project duration were more likely to find jobs. The table also shows that previous job experience certainly helped most workers to find jobs after participation, with the exception of those workers who had worked in white-collar jobs.



**Table 9.7: Employment structure of those employed before and after PWP participation (total=before:750; after:399)**

Characteristics	Before	After
	(%)	
<i>Employment status I</i>		
Regular worker	34	34
Temporary worker	22	23
Daily worker	31	30
Self-employed	9	8
Non-paid family worker	3	3
Dispatched worker	1	2
<i>Employment status II</i>		
Full-time worker	81	80
Part-time worker	19	20
<i>Occupation</i>		
First job		17
Same as previous job		45
Different from previous job		38
<i>Compensation and working conditions</i>		
Better than previous job		18
Same as previous job		39
Worse than previous job		42
<i>Industry</i>		
Manufacturing	22	17
Construction	16	18
Service	11	17
Hotels and restaurants	12	9
Agriculture, forestry, etc.	9	9
Other	30 <sup>1)</sup>	28 <sup>3)</sup>
<i>Type of worker</i>		
Unskilled manual worker	41	37
White-collar worker	14	18
Skilled manual worker	12	10
Service worker	13	11
Other	20 <sup>2)</sup>	24 <sup>4)</sup>
<i>Monthly wage (won)</i>		
(SD)	870,000 (738,100)	700,000 (374,400)

- Notes: 1) Wholesale/retail repair service (6%), educational service (5%), housekeeping service (4%), public administration (3%), transport distribution and telecommunications (3%), Finance and insurance (3%), social welfare (2%), fishery (1%), public utilities (1%), real estate (1%).
- 2) Technician (7%), skilled worker in agriculture and fishery (5%), expert (3%), machine operator (3%), high ranking manager (2%).
- 3) Educational service (5%), social welfare (5%), wholesale/retail repair service (5%), finance and insurance (3%), public administration (3%), transport, distribution and telecommunications (3%), real estate (2%), fisheries (1%), mining (1%).
- 4) Skilled manual worker (10%), expert (6%), skilled worker in agriculture and fishery (6%), expert, machine operator (2%)

Table 9.8: Logistic regression coefficients for regression of job attainment after PWP participation on selected independent variables

Independent variables	Logistic coefficients (SE)
Gender (male=1)	.340 (.140)*
Age	-.048 (.008)***
Education	.087 (.062)
Breadwinner <sup>1)</sup>	.322 (.146)*
Project types (Manual labor)	
DB construction	- 1.122 (.308)***
Information technology	-.295 (.307)
Administrative assistant	-.204 (.235)
Educational activities	-.547 (.286)
Internship	-.153 (.394)
Welfare client assistant	.653 (.813)
Degree of overall satisfaction on PWP	-.033 (.020)
Degree of satisfaction on project management	-.036 (.016)*
Previous job experience (no experience)	
white-collar worker	.015 (.257)
Service worker	.599 (.245)**
Skilled manual worker	.661 (.259)**
Unskilled manual worker	.704 (.172)***
Other	.683 (.207)***
(Constant)	.317 (.462)
-2log likelihood	1570.576
Chi-square	133.584***
Degree of freedom	17

Note: 1) Breadwinner is a dummy variable coded 1 if the respondent is the major breadwinner in the household.

\*p<0.05, \*\*p<0.01, \*\*\*p<0.001

When respondents searched employment, they frequently relied on personal networks and local newspaper advertisements, instead of using institutionalized services such as local labor offices or public employment centers for daily workers (Table 9.9). Respondents also answered that they had difficulties in finding jobs because there were few job openings, inadequate job information, and age discrimination. Naturally, among 1196 respondents who have not yet been employed or are currently working in the

projects, about 81 % (967 respondents) answered that they wanted to participate in the projects in the future. A majority (60 %) of those respondents who answered positively on this question wanted to participate in the projects until they ceased to exist. Particularly, women, older, and less educated workers were more inclined to participate in the projects instead of searching for jobs. It clearly indicates that those workers who are not easily sellable in the labor market might develop a tendency to depend on the projects for a long time.

Table 9.9: Job search methods of survey respondents

Characteristics	(%)
Personal network	26.8
Newspapers, TV ads., etc	21.4
District (Local) newspapers	14.6
Pay a visit to workplaces	10.3
Internet search	9.7
Local labor office	6.6
Manpower bank	4.2
Public employment center for daily workers	2.8
PWP workplaces	2.1
Private employment service center	1.4

### *Attitude Survey on Project Implementation and Future Direction*

The respondents' evaluation of the projects might not represent that of the whole population, but precisely because of that it could be more accurate. Table 9.10 shows that the project participants gave fairly positive answers to five items evaluating the projects. They rather strongly agreed on the fact that the projects provided "protection for the poor," and gave "opportunities to work for disadvantaged groups". Table 9.11 presents OLS coefficients for the regression of public works projects' evaluation on several independent variables. The dependent variable was calculated by averaging the scores on the items in Table 9.10. In general, women, older, less educated, and poorer workers were more satisfied with the projects. Frequent participants evaluated the projects more positively than one-time participants did. Those workers who had worked in information technology projects and those who had worked as administrative assistants were significantly more satisfied than participants in manual labor projects.

In general, respondents were satisfied with the administration of the projects. They were, however, not satisfied with wage rates and project duration. According to the survey results, 56 % of respondents believed that wage rates should be raised to meet the prevailing market wage for similar

work, whereas only 3 % believed that wage rates should be lowered to increase the number of beneficiaries of the projects. Actually, as it was shown in Table 9.1, wage rates have been reduced twice, mostly due to the business sectors' complaints that high wage rates in public works projects were leading to labor shortages.

As public works projects have been implemented during the severe economic downturn, it was not likely that twice cut wage rates of the projects caused labor shortages or raised wage rates in the labor market. Some small and medium-sized firms with substandard working conditions that are known as 3D sector<sup>6</sup> in Korea suffered from labor shortages, but they have experienced this problem for a long time. Even when these firms offered higher wages than the other firms did for a similar job, workers did not want to be employed in this sector because of their dire and unhealthy working conditions. If wage rates were lower than the current rates, the public works projects might have not been able to attract the unemployed heads of households who were the major target group for the projects. Manual public works project participants earn 500 thousand to 600 thousand won per month on average, which is below the minimum cost of living for a household with 4 persons.

Respondents also complained about the duration of the projects, which last less than 3 months. Although in some cases this period was too short to implement long-term projects, the short project period helped to pressure participants to find more secure jobs in the private sector.

**Table 9.10: Five items measuring respondents' evaluation of public works projects**

<i>For each of the following statements, please tell me if you strongly agree (2), somewhat agree (1), somewhat disagree (-1), or strongly disagree (-2) with it.</i>	Mean values
The public works projects helped the unemployed by Creating jobs	0.44
The public works projects provided welfare service to The community	0.62
The public works projects provided protection for the Poor	1.05
The public works projects encouraged the unemployed To keep in contact with the world of work	0.47
The public works projects provided opportunities to work For disadvantaged groups in the labor market	0.99

<sup>6</sup> Three D sector denotes workplaces where dirty, dangerous, and difficult jobs prevail

**Table 9.11: OLS coefficients for the regression of PWP evaluation on selected independent variables (total number=1505)**

Independent variables	OLS coefficients (SE)
Gender (male=1)	-.932 (.222)***
Age	.058 (.011)***
Education	-.471 (.091)***
Householder <sup>1)</sup>	-.023 (.243)
Working spouse <sup>2)</sup>	.328 (.216)
Monthly household Income	-.004 (.001)***
<i>Total number of program participation</i>	
(1)	
2	.734 (.216)***
3	.733 (.244)**
4	1.236 (.402)**
5	1.100 (.642)
<i>Previous Job Experience</i>	
(no experience)	
white-collar worker	-.369 (.386)
Service worker	.350 (.384)
Skilled manual worker	.567 (.388)
Unskilled manual worker	.332 (.242)
Other	.269 (.315)
<i>Project types</i>	
<i>(manual labor)</i>	
DB construction	.118 (.433)
Information technology	1.210 (.504)**
Administrative assistant	.792 (.360)**
Educational activities	.368 (.575)
Internship	-1.680 (1.391)
Welfare client assistant	.591 (.389)
Drop-out <sup>3)</sup>	-.449 (.236)
(Constant)	2.847 (.707)***
Adjusted R <sup>2</sup>	.200

Notes: 1) Householder is a dummy variable coded 1 if a respondent is the head of a household.

2) Working spouse is a dummy variable coded 1 if a respondent has a working spouse.

3) Drop-out is a dummy variable coded 1 if a respondent quit PWP before a three-month participation period is over.

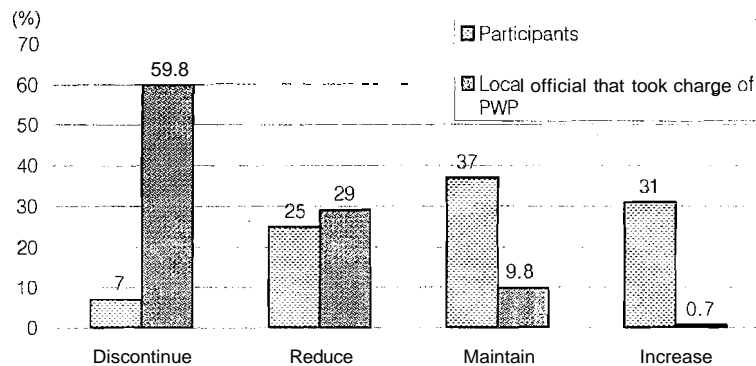
\*p<0.05. \*\*p<0.01, \*\*\*p<0.00

Figure 9.2 demonstrates that respondents did not want the projects to be discontinued. This sharply contrasts with the response of the local officials who took charge of the projects, as 59.8 % of them want the program to be discontinued. In sum, the public works projects in Korea appeared to have

produced two beneficial outcomes: they provided jobs for people who were unemployed or underemployed, and they provided much-needed economic and social services to the general public at both national and local administrative levels.

Although this paper does not aim to evaluate the cost-effectiveness of each project, the public works projects in general seemed to provide many government services that people could not afford before. For example, the information technology projects helped to bring about the digital economy earlier than expected, and substantially improved the efficiency of administrative services by producing major databases for government documents. The two most fundamental principles guiding the implementation of the projects were (a) the labor market is not to be disturbed by the public works projects, (b) the projects should be labor intensive ones, with the budgetary constraint that the projects should use 50 to 70 % of the project funds only for labor costs. Considering that these principles were restraining conditions that naturally prohibit productivity and efficiency of the projects, the criteria that were used to evaluate the projects should not be so much focused on how successful they were in terms of generating profits.

**Figure 9.2: Future direction of PWP**



Note: The data for local officials come from a survey conducted by the KLI, in June 1999. The sample consists of 585 municipal officials who took charge of PWP. Respondents were sampled with a PPS (Probability Proportional to Size).

## Summary and Policy Agenda

As an unemployment measure, whether the public works projects actually helped the unemployed has been the subject of much controversy. The findings of this research suggest that the projects might have activated some

economically inactive population. However, about a half of women participants, who in general were erroneously considered as the economically inactive, turned out to be the major breadwinners in poor households. Furthermore, the average monthly household income of all respondents was close to the poverty line, which implies that the projects should even be considered as a successful poverty measure. Most project participants were also non-beneficiaries of other unemployment measures. All these strongly support the fact that the distribution effects of the projects are fairly positive.

Deadweight losses due to the public works projects were only indirectly inferred. As project participants were mostly low-skilled, less educated, and older workers, these workers were not expected to do jobs that required regular workers.

In addition, respondents spent just less than 5 months on average participating in the projects, brushing away concerns regarding the locking-in effects. A large majority of those participants who are disadvantaged in the labor market, however, responded that they would like to participate in the future, instead of searching for a job. Younger male workers and major breadwinners in the households were more likely to attain jobs after the project participation. A majority of project participants were previously atypical workers, and those workers who found jobs remained surprisingly similar to the employment structure shown before the project participation. Their new wage rates were however substantially lower than the average wage rates of respondents' previous jobs. It partly reflects the worsened labor market situation for these unskilled workers after the financial crisis.

According to the survey results, respondents were quite satisfied with the management and outcomes of the public works projects, except for wage rates and project duration. They strongly agreed with the statement that the projects provided protection for the poor, and gave opportunities to work for disadvantaged groups. Respondents therefore did not want the projects to be discontinued, which sharply contrasted with the response of the local officials, a majority of which wanted the projects to be discontinued. Respondents also preferred the public works projects to unemployment assistance, believing that the projects need to be expanded. The project outcomes bore fundamental limitations because the projects must put priorities in providing income assistance to the unemployed poor and thus in using a maximum of labor. Central government projects were in general more positively evaluated, as they were implemented with more supporting managerial manpower and more carefully prepared proposals. Among the central government projects, the forestation project and the project that ran after-school classes for the children of low-income families were among the most highly evaluated. Since one of the central principles of this public job creation scheme was that the private labor market is not to be disturbed by these projects, there were few externality effects that threatened the functions of the market.

These findings of the paper<sup>7</sup> point to the following three policy recommendations.

First, the public works project should not be discontinued or drastically reduced. The projects have successfully played the role of a social safety net ever since unemployment rates skyrocketed. The projects especially benefited women, older, and less skilled workers who have been excluded from the other institutionalized unemployment measures, such as employment insurance and the loan schemes. Despite decreasing unemployment rates, rapid expansion of atypical employment is degrading the quality of working life, requiring immediate attention. The crucial policy dilemma here is that it has been extremely difficult to simultaneously attain flexibility in the labor market and social protection for workers. The projects need to be retooled to cater to the demands of the disadvantaged groups in the private labor market.

Second, it is vital to pay careful attention to the interactions between the public job creation scheme and other unemployment measures and related social welfare programs. The disadvantaged participants mentioned above have a tendency to be dependent on the projects perennially. This "unemployment trap" is particularly daunting for people whose chance of escaping from unemployment is to be underemployed, which could be worse than participating in the public works projects. In order to facilitate their job search process, the projects should develop a close linkage between them and public employment services and vocational training programs. Moreover, the projects also should be prepared to play a new role of workfare, especially after the enforcement of the Basic Livelihood Security System for the Nation. The System is expected to secure the basic livelihood for the low-income class earning less than the minimum cost of living, and at the same time, to provide self-support aid to those with the ability to work. In this system, the projects can be used as a work test in order to make many unemployed poor remain in contact with the labor market. In doing so, the projects should not degenerate into a vehicle to enable the unemployed to earn living expenses. Eventually, the projects should develop into a two-tiered system in which they can be utilized as both an active labor market policy for the relatively young and more educated unemployed, and as an effective workfare program for poor groups with greater barriers to the labor market.

Third, despite private sector discontent regarding the projects' wage rates, wage rates should not be lowered in order to maintain the participation of the major breadwinner. Further decline in wage rates also exacerbates the distributional effects of the projects. The project duration, which was

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<sup>7</sup> This study only provided evidence on short-run outcomes, covering at best slightly more than 1 year after program participation. Much evaluation literature cautioned that this may well be too short a period for a full assessment of the private and social returns to public investment of many active measures (OECD 1998). Public works projects are still being implemented in Korea, and there is very little evidence on the long-term effects of these projects.



intentionally designed to be very short in order to pressure participants to actively search for jobs, should be more flexible with a shift from one-month duration projects to yearlong duration projects.

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# 10 Public Works Programs in Korea: A Comparison to Active Labor Market Policies and Workfare in Europe and the US

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## Introduction

The aim of this paper is to compare recent changes in the Korean social protection system to ongoing developments in Western Europe and in the US.

After the financial crisis in 1997, Korea introduced a large scale public works program as a measure to provide income maintenance and meaningful activities to the new unemployed. This program has been described, also in World Bank documents, as a "workfare program". The main purpose of the comparison to follow is to provide a framework within which it is possible to position the Korean public works programs.

There is today a large degree of confusion about how to understand and define the different measures which are generically referred to as "active policies". The paper elaborates on the distinction between active labor market policies (ALMP) and Workfare made by Lødemel and Trickey (eds. 2001) and introduces a third form of activation to the comparison; public works<sup>1</sup>.

The paper compares the Korean programs with workfare and other active labor market program in Western countries, with a view to highlight similarities and differences. The paper discusses whether the term "workfare" describes the Korean public works program in a meaningful way. It is suggested that an alternative is to compare it to Western experiences with large scale public works. In the West such programs were last used, on a scale comparable to present day Korean policies, during the recession in the 1930's. The scale and the nature of the problems experienced in Korea

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<sup>1</sup> The first few pages of this chapter contains material from chapter 1 of the forthcoming book "An Offer You Can't Refuse: Workfare in International Perspective" (Policy Press 2001)

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today may be more similar to these early experiences than to modern workfare, which is targeted at groups who are marginal in relation to the labor market, and which focuses more on supply side measures than demand side measures. The rudimentary nature of the Korean welfare state also suggests that it is more fruitful to compare public works to earlier experiences of mass unemployment in Europe and in the US.

### **From Passive to Active Policies**

This section presents, first, the broad area of active policies, second, Active labor market policies (ALMP), third, workfare, and fourth, public works.

Throughout the OECD-area the social consequences of joblessness continue to be a major focus of policy analysts and politicians. A range of difficult issues arises in formulating appropriate policy responses. There is the limited degree to which macroeconomic policy can be expected to improve the situation in the immediate future. There are various constraints that limit the ability of national governments to stimulate demand, and reduce the effectiveness of macro-economic management. Moreover there is general agreement that in many countries labor market rigidities are common, limiting the ability of macro-economic policy to affect the level of employment.

At the same time, there is growing concern about the ways in which benefits provided to the jobless contribute to the rigidities that complicate macroeconomic policy and imply slow adjustment to changing economic realities. A central advisor to the Blair government in the UK describes this as 'moral hazard' (Giddens, 1998); by discouraging initiative and fostering dependence, such policies may actually contribute to the incidence and duration of the problem they are intended to alleviate.

The emergence of a new 'risk society', as described by Beck (1992), involves a 'temporalization' and a 'democratization' of unemployment and poverty. The first refers to a change from permanent situations towards problems which are either short term, permanent or recurrent. Second, 'democratization' means that these situations are no longer confined to members of lower classes; poverty and unemployment are increasingly experienced also by members of the middle classes. More than before, therefore, policies targeted at the unemployed, need to be better tailored to individual needs.

Moreover a high level of unemployment implies a high level of social security spending. It is likely to mean a high level of spending on social assistance, as rights to social insurance are exhausted, and as younger workers and others without contribution records become affected by unemployment. There may therefore be pressure to ensure that budgets are kept in check, and that money is targeted to the individuals most clearly in

need of assistance.

In response to these concerns and new realities, both social policies and labor market policies are changing. In general a shift towards a more 'active' use of funds with the view to further self-help can be observed in all OECD countries. In Western Europe during the last decade, '*activation*' has become a key concept to describe this trend. By contrast, this term is seldom used in the United States, where concepts such as a move towards an 'enabling state' (Gilbert and Gilbert, 1989; Gilbert, 1995) express similar ideals. The present change in Europe is based on an understanding that while the existing welfare states often provide 'soft landings on the side of active society, we need...to build bridges back to work' (Larson in Heikkila ed., 1999).

While 'activation' and the ideas underlying it are long established in areas such as social work and the rehabilitation services (Hvinden, 1999), the present usage is different. Whereas in political rhetoric activation is perceived to guide most of the programs of the welfare state, the policy changes resulting from this new emphasis are mainly targeted at furthering paid employment. The term 'active' is therefore usually understood as *economically* active, and the aim of policies is to further (re-) integration in the labor market. On the other hand, an important aspect of the new activating policies is an extension of the role of labor market policies to go beyond its traditional concern with those closest to the labor market (the insured unemployed) to include other groups such as the disabled and jobless recipients of social assistance.

The rapid *diffusion* of these policies in recent years is partly a result of initiatives made by international organizations. In 1992, the OECD formulated a number of recommendations for member countries to reform social and labor market policies with the view to further integration, in work as well as in other institutions in society (OECD, 1994). Similarly, a meeting of European ministers of social welfare in the preparation of the 1995 United Nations Summit in Copenhagen stressed the importance of active social policies (United Nations, 1995). Finally, the European Union has adopted activation as the cornerstone of their social policies. In 1997 the Luxembourg Jobs Summit of the EU established three quantified objectives: first, to guarantee that after six months out of work, all unemployed people be offered training or other employability measures, second, a repeat of these measures after twelve months if necessary, and, third, an increase in the use of active labor market measures, to include at least 20% of the unemployed (European Commission, 1998)

### *Active Labor Market Policies (ALMP)*

The most important instrument designed to achieve these targets is active labor market policies (ALMP). The term refers to the attempt at transferring passive benefits into active measures with the view to make the unemployed

more attractive on the labor market (Hvinden, 1999). The origin of the present emphasis on ALMP in Europe has been traced to the Scandinavian countries (Wilensky, 1992). In particular Sweden has a long history of using labor market policies as an instrument to stimulate both the demand and the supply of labor in times of economic restructuring.

Both ALMP and workfare are characterized by the use of *incentives* to achieve desired aims. The recent change towards incentives has been described as a 'fundamental shift in policy makers' beliefs about human nature and behavior' (Taylor-Gooby, 1998) and 'the victory of rational choice thinking' (Le Grand, 1997). Incentives can be delivered in the form of either positive or negative sanctions, or, in more colloquial language, as 'carrots' or 'sticks'. While ALMP typically applies a mix of positive and negative sanctions, idealized workfare is distinguished by a greater emphasis on negative sanctions (Hvinden, *ibid.*; Abrahamsen, 1998). Idealized workfare, in this perspective, can therefore best be described as the 'stick' of the new active policies.

Workfare is distinguished from ALMP in three further ways. First, while the use of compulsion may be a part of ALMP, for example where the receipt of unemployment benefits is conditioned upon participation in various activities designed to further labor market integration, the compulsory nature of workfare is compounded by the last resort nature of social assistance. While, in many countries the failure to meet ALMP requirements may result in the loss of unemployment benefits, a lower tier of social assistance is often available. With workfare, however, there is no safety-net below. It is in this situation that the 'offer' of work is one that 'you can't refuse' (Lødemel and Trickey, 2001). Second, unlike most active labor market programs, the required activity in workfare is more often work than training. Training may be one of several options available in the first instance, or the participation in work activities is presented as training in the skills of functioning in a work place. Third, while ALMP is usually organized by the labor market authorities, workfare is typically a part of the social services. In practice, however, the use of the workfare instrument differs across nations, and the extent to which it shares similarities with ALMP, and the extent to which it is integrated with these policies in implementation, are questions that will be addressed in this chapter.

### *Defining Workfare as a Part of the New Active Policies*

At present no consensus exists regarding a single definition of workfare. The use of the term varies over time and between countries (Peck, 1998) and the language of workfare is at least as 'hazy' today as it was a decade ago (Standing, 1990). There are two main reasons for this lack of clarity. First, in comparison to other social policies, 'workfare' policies are not easily defined either in terms of their purpose (e.g. as compared to 'rehabilitation policies') or in terms of their target group (e.g. as compared to 'pension

provision schemes'). Policies variously described as 'workfare' are often associated with different aims and target different groups of people. Second, workfare has always been a politically charged term. When it was originally used during the Nixon administration in 1969 it was marketed as a very positive alternative to the passive provision of income maintenance. Surveys of public opinion suggest that the idea of replacing unconditional benefits with requirements to work receives substantial support across different welfare states. Over the last decade the term has most frequently been used by those who oppose work requirements, which they perceive to be eroding rights-based entitlement to assistance (Shragge, 1997). In Europe the word 'workfare' is often used by policymakers as a foil, to explain what the new policies are *not*. Only the political right in the United States still use the term to describe policies which they advocate.

The lack of clarity about what workfare 'really is', has not prevented it from increasingly penetrating public and academic discourse. In the three largest US newspapers more references were made to workfare in the year 1995 than in the entire period 1971-80 (Peck, 1999a). The academic literature also bears witness to this trend. Of a total of 90 articles describing 'workfare', only 11 were published before 1990 (Social Citation Index). The use of the term in the academic literature reflects its ambiguity and the blurred boundaries between workfare and related policies.

A key distinction can be made between *aims-based* (Evans, 1995; Morel, 1998; Nathan, 1993) and *form-based* definitions (Walker, 1991; Wiseman, 1993; Jordan, 1996; Shragge, 1997; Mead, 1997). Applying a form-based approach, Morel (1998) compares the French 'insertion approach' within social assistance, with a US 'workfare approach'. She suggests that the key difference is that the workfare approach is concerned with a fight against 'dependency', whereas the insertion approach is intended to counteract 'social exclusion'. Nathan (1993) focuses on the aim of policies when he distinguishes between two forms of workfare that can be identified in the US context. He uses the term 'new-style workfare', now commonly used in the United States, to refer to a range of 'strategies which aim to ...facilitate entry into the labour force'. By contrast, '*workfare*', referred to US policies in the 1970's and 1980's, was restrictive and punitive' (Ibid.). According to Nathan, the different aims *are* reflected in the form of the policies; while the former offered little more than work in exchange for benefits, 'new style workfare' encompasses a variety of work and training programs designed to help welfare recipients gain access to regular jobs.

In the first systematic comparison of welfare programs in a large number of countries, Lødemel and Trickey outlined as: *Programmes or schemes which require people to work in return for social assistance benefits*. The definition thus has three elements – that workfare is *compulsory*, that workfare is *primarily about work*, and that workfare is essentially about policies tied to the *lowest tier of public income maintenance* (Lødemel and Trickey eds., 2001)

*Public Works Programs*

Both ALMP and workfare are modern responses to the problems experienced by the matured welfare states within the OECD area. Both represent a reaction to what is increasingly described as "passive policies". By contrast, public works programs are typically associated with the large scale programs implemented in the industrial countries of Europe and North America during the recession in the 1930's. In the absence of support systems for the unemployed outside the Poor Law, work was created by the state and the unemployed were able to earn a living.

It is important to distinguish the purpose and nature of these programs from those of the present day active policies. Commenting on the main US public works programs, organized by the Civil Works Administration, Katz argues that "the CWA was not relief or a dole. Rather, it reflected the administration's highest priority; to put the unemployed back to work" (Katz, 1996). The participants were typically previously full time workers, including both blue- and white color workers. The task performed was designed to serve the interest of the community in a situation where funds for construction and maintenance were depleted: "building and widening roads, clearing sites for recreation workers, schools hospitals, libraries and other public buildings got replastered walls, new coats of paint and even decorative murals" (Ibid.). Public works programs were not only a part of the policies of democratic governments. In Europe, the programs installed by the Nazi government were perhaps the largest. The endorsement of these latter programs as an example to follow in Europe today. is at the core of the recent European isolation of the new right-wing government in Austria.

The public works programs of the 1930's therefore combined the need to rebuild and maintain the nation's infrastructure and to offer non-poor law support to the regular unemployed. In doing so, they also represent a precursor to later demand side oriented Keynesian economic policies. In the words of Katz, the CWA "pumped 1 billion dollars into the stagnant economy" (Ibid.).

In recent academic contributions to the discussion of the upsurge in workfare, references are often made to these programs as precursors to current policies pursued in the mature welfare states (Andenas, 1992; Salonen and Johansson, 2000; Struthers, 1996). The discussion above suggests that these programs differed strongly both from current workfare initiatives for the uninsured and ALMP for the insured unemployed persons.

We have identified and defined three forms of active social- and labor market policies targeted at the unemployed. Although there are considerable overlaps in design and practical implementation, the differences among the three forms can be expressed in an idealized typology as shown in Table 10.1 below.

**Table 10.1: Distinguishing characteristics of three forms of active policies targeted at unemployed people**

	ALMP	Workfare	Public works
Relationship to welfare entitlement	Voluntary or compulsory. For UB-recipients	Compulsory condition for soc. assistance entitlement	Not attached to entitlement program. Only access to aid
Form of regulation	Supply side and demand side	Supply side	Demand side
Main target group	Unemployed, close to labor market	Un. recipients of assistance. Distant from labor market	Unemployed close to labor market
Main activity	Training	Work	Work
Responsible authority	Labor market	Social services	Labor market

## Empirical description

### *Western Europe and the US*

In recent years the emphasis on activating policies has resulted in an increased role of both ALMP and workfare. In this overview the focus is on workfare, because this is the policy form to which Public Works in Korea is most commonly compared. But first a few points about ALMP.

#### ALMP

Sweden is considered the pioneer in applying ALMP (Wilensky, 1992). It is interesting to note that the Swedish programs originated in the economic crisis in the 1930's. Already at that time, the Social Democratic government replaced relief work with "public temporary employment" (Salonen and Johansson, 2000). The change involved a new responsibility by the state in providing suitable and meaningful work for the unemployed. In the 1950's this demand side orientation was complemented by supply side measures. The programs were increasingly used to speed up structural changes in the labor market. By means of job brokerage, job subsidization and training measures, ALMP was designed to improve both labor demand and labor supply (Hvinden in Heikkila ed., 1999).

The Swedish experience has inspired other nations to use ALMP in the



change towards more activating labor market policies. International organizations, most importantly the OECD, have played an instrumental role in promoting such policies in recent years. OECD countries differ, however, considerably in the extent to which they have transferred passive policies (with a focus on income maintenance) into ALMP. In the mid-1990's it was found that the Nordic countries remained "the activist corner" compared to other Western European nations (Hvinden, *Ibid.*). The UK and the US featured the lowest degree of activism in this period (OECD 1996).

### Workfare

Lødemel and Trickey (eds. 2000) have compared the institutional characteristics of workfare in Denmark, France, Germany, the Netherlands, Norway, the UK and the US.<sup>2</sup> On the whole the introduction and extension of workfare programs into Europe is a 1990s phenomenon. However, whilst the United States, is often seen as the originator of workfare policies, having a history of programs going back to the early 1970s, there are important exceptions within Europe. Denmark has taken a pioneering role in European compulsory activation, and in Germany a provision for workfare was included in the 1961 social assistance legislation, though the policy largely lay dormant until the onset of mass unemployment in the 1970s.

Lack of employment ('worklessness') experienced by population sub-groups is a common concern in many western nations despite a range of labor market circumstances. Changes in the size and composition of unemployed and inactive populations; growth in the number of social assistance claimants; and, an associated rise in social assistance expenditure can be everywhere identified as key motivating factors for the introduction of active labor market policies, including workfare (Heikkila, 1999).

Despite common reasons for rise in social assistance claims and common concerns about social assistance expenditure (Ditch and Oldfield, 1999), the relationship between wider macro-economic concerns and program objectives is not straightforward. In addition to economic considerations, the use of workfare is underpinned by common ideological objectives related to

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Programs chosen to represent the six European countries were: Activation (Denmark); RMI based Insertion (France); Help Towards Work (Germany); The Jobseeker's Employment Act (JEA) for Young People (The Netherlands), local authority schemes resulting from the 1991 Norwegian Social Assistance Act (Norway); and, The New Deal for Young People (The UK). In Germany, France and Norway national legislation is reinterpreted locally to such a degree that a different programme might be considered to exist in each locality. To accommodate this, an 'overall' picture of the programme (or set of schemes) is given from a national viewpoint and the extent of intra-national variation is indicated. Three states' programmes for claimants of Temporary Assistance for Needy Families represent the United States (New York, Wisconsin and California). The programmes listed are not representative of the totality of programmes in each country – for example, the three American programmes represent three of the most developed forms of workfare in the US.

changes in the way the relationship between paid work and citizenship is understood and described. These have been made manifest in rhetoric through the concepts of 'social exclusion' and 'dependency' – insofar as they refer to exclusion from the labor market and 'dependency' on social assistance – and to changes in the contract of 'rights and responsibilities' between claimants and the state.

A range of different explanations for worklessness underlies the programs considered here. Whilst architects of all the programs focus to some extent on eliminating 'dependency' – which is the reason for them being compulsory, to different extents they also aim to tackle 'social exclusion' and, in some cases, low labor demand. This is reflected in the extent of focus on external-based as opposed to individual-based problems, and on 'demand-side' as opposed to 'supply-side' issues.

There are very important differences in primary target groups between Europe and the US. Within Europe, the focus is on young unemployed people. Danish Activation stands out as the program most intended to apply to people whose main reason for claiming is not unemployment. Programs differ as to whether they are applied universally or more selectively to their target populations. The most 'universal' programs are the Danish, Dutch and British programs, with the German and Norwegian programs being the most selective.

The extent to which programs diverge from the idealized model of workfare outlined in the definition given above are a reflection of the extent to which their architects define the causes of worklessness differently, and, so, seek to accommodate the varied circumstances of individual clients. Different strategies are a reflection of differences in underlying ideological aims, and in attempts to respond to the heterogeneous needs of target populations.

The programs differ in the extent to which they are integrated with programs for the insured unemployed (ALMP). The most integrated programs are found in the UK, Denmark and the Netherlands. These are also the most "offensive" programs, focussing more than the others on human capital development in the form of training and other measures in addition to work. This suggest that where the social division of training is narrow, the traditionally marginal groups targeted by workfare may benefit from belonging to a wider "risk group" (Baldwin, 1992) which also include the unemployed who are closer to the labor market.<sup>3</sup>

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<sup>3</sup> For a detailed comparison of workfare programs, see chapter 9 of Lodemel and Trickey (eds. 2001). For a discussion of possible explanation to differences among programs, see chapter 10 of the same book.

## PUBLIC WORKS PROGRAMS IN KOREA

### *The Korean Case*

#### Social Welfare in Korea

It is commonly acknowledged that people's welfare stems from three different sources: the public, the market and the family. By western standards the welfare state in Korea is fairly limited and "lean" (Lee, 2000). This applies to budgets, degree of universalism, number of beneficiaries, and benefit levels (Park, 2000). However, it would be a mistake to take the official figures at face value. Still traditional family and caring values prevail in Korea, and many firms, in particular the large corporations, provide fringe benefits and welfare goods which are of great value to their employees. Accurate and reliable estimates are however, difficult to come by. At least up to the crisis in 1997, the Korean labor market provided near-lifetime employment and a seniority system which served as social protection. Non-public welfare is not revealed in the official figures, but should be considered. Needs for welfare goods are also lower in Korea than in most western countries because the number of elderly in Korea is relatively low.

#### The Late 1990 Crisis and Its Background

After nearly three decades of continuous and steady economic growth Korea was in 1997 hit by a sudden and dramatic economic crisis. In a short time, from the fall of 1997 to early 1998, unemployment soared from 2.1 to 8.4 per cent, implying that 1.7 million Koreans were left without jobs almost over the night. No doubt, this is a conservative estimate as more than half a million is perceived to leave the work force completely. Real wages dropped by almost 10 per cent. Unemployment inflicted most groups, but some groups were affected more seriously than others: well educated employees experienced lower unemployment rates than the low educated, and non-professional workers in construction, trade and manufacturing were particularly hard hit (Kang *et al.*, 1999).

In 1998 the GDP dropped by 5.8 per cent which led Korea from being the world's 11<sup>th</sup> largest economy to become dependent on loans from international finance institutions (Park, 2000; Kang *et al.*, 1999). A crisis of such proportions was unprecedented in post-war Korean history although the country went through a recession in the early 1980s. The period from 1962, when the first of a series of five-year development plans were implemented, and onwards may be characterized by four key words: economic growth, industrialization, drastically improved standard of living, and a sustained income equality, by international standards (Choo, 1993). It is generally perceived that Korea still is an egalitarian country, at least what income is concerned (Choo, 1993, p.351). What concern growth and industrialization, as late as in 1961 Korea was still an agricultural society with virtually no

industry and no exports. The Government introduced export incentives, and encouraged private capital to invest in Korea (Kwon, 1993). Several commentators have labeled this transformation an economic miracle. It is argued that investment in human capital and education is one of the key factors in this development (Kwon, 1993). Five years development plans in close co-operation with private business and geared at promoting the private sector were also decisive factors. Among other things a plan for developing a heavy and chemical industry plan was announced in the early 1970s. Following the economic downturn in the early 1980s which was characterized by negative growth and high inflation, the Government turned to liberalization, deregulation and market mechanisms to tackle the problems.

In the period up to the recent crisis real wages increased enormously and doubled several times. The absolute poverty rate decreased from 40 per cent in the mid 60s to about 10 % in 1980 (Leipziger, 1993, p.364). Up to 1990 income inequality (measured by the Gini index) fluctuated between .32 and .39 and did not show any increasing trend, rather the opposite (Choo, 1993). One should keep in mind, however that the statistics suffer from the weakness that the very rich and very poor are excluded, and so are self employed like doctors and lawyers.

The public welfare system in Korea rests on three pillars: social insurance, social assistance, and social welfare services for the disabled, aged etc.

#### Social Insurance

The social security law was enacted in 1963. It first implemented a work injury program in the early sixties (Choo, 1993, p.164). In 1977 a health insurance system was introduced which was made universal in 1989. In 1988 a national Pension system for workers at workplaces with 10 or more was introduced. This was expanded to workers in workplaces with five or more workers in 1992 and made universal after 1997.

Unemployment insurance was introduced in 1995. Less than 50 per cent of Korean workers were covered by unemployment insurance when the crisis hit in 1997. However, since the scheme just had been made operative, many workers were entitled to only a few months of benefit. The crisis also hit marginal workers in small firms much harsher than the core workers in the big firms and corporations. Thus a disproportionately high rate of marginal workers were thrown into unemployment without a social safety net. No more than 11 per cent of the unemployed population received unemployment benefit when the crisis peaked early in 1999 (Park, 2000, p.16).

#### Social Assistance

Korea first introduced social assistance, labeled Livelihood Protection (LP),

in 1961. Just as the economic growth as such was used as a means to eradicate poverty, so was the LP scheme. From the beginning the LP scheme served as a poor relief program. The Ministry of Health and Welfare is responsible for this program (while the Ministry of Labor is responsible for Public Works). A clear division of responsibility is in existence, as the first take care of income maintenance programs, while the latter handles the work related programs. The Ministry of Health and Welfare is essentially concerned with income protection even if their programs contain certain productive work, or activity requirements.

The target group of LP is the poor, marginal workers in the informal sector, for example elderly women who sell food on the street. They are considered as able-bodied. They also should meet the requirements of the assets of 28 million won (23 thousand US dollars) per household in 1999, and income tests of 220 thousand won (183 US dollars) per month per person in 1999.

A strong version of the subsidiarity principle applies to the LP program. Claimants are required to seek assistance from spouses or parents, or the spouses of the parents or grandparents or the spouses of the grandparents, or brother/sister belonging to the same household before having recourse to public assistance. Older claimants are expected to seek assistance from spouses or children, or spouses of the children or grandchildren, or spouses of the grandchildren or sisters/brothers belonging to the same household.

There are six forms of aid: Livelihood Aid, Education Aid, Maternity Aid, Medical Aid, Self-supporting Aid and Funeral Aid. The Livelihood Aid takes the biggest proportion of these. The law describes entitlement to aids as individuals, but the actual unit for whom benefit is payable is household. The social assistance scheme has no limits on duration as long as the recipients meet the requirements.

#### Recent Changes in Korean Welfare: Temporary Livelihood Protection and

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Since the financial crisis in the late 1990s, a temporary Livelihood Protection has been introduced. The means testing (asset and income) in the temporary LP are lower than in LP, and so are the benefits. Under the temporary scheme, as the assets test requirement has been lowered to 44 million won (US\$ 37,000) per household in 1999, more low income people have benefited. 310,000 and 760,000 more of the low income people were targeted for the beneficiaries in 1998 and 1999, respectively. In 1999, a cash livelihood benefit was also given to the low-income care recipients during the winter period and about 50 % of them received the benefits. Public works participants (see below) or the low income care recipients with household's income above 600 thousand won (US\$ 500) per month were excluded from this program.

1.92 million people, or 4.2% of the total population, received social

assistance under the livelihood protection scheme in 1999 including those receiving benefits under the temporary program. However, only 60 % received the regular protection. This means that only 2.5 % of the total population received a regular social assistance. In terms of the beneficiary coverage, this ratio is very low compared to some of other OECD countries. Among the compared 23 countries, Korea's ratio is ranked almost the bottom with Japan (Park, 2000). The coverage of Korea's social assistance is thus very limited, considering that the livelihood protection scheme is the only public assistance program available to low income individuals.

The Public Works program (PW) was launched in 1998 as a direct response to the soaring unemployment among more or less regularly workers. It was expanded in 1999 and contracted in 2000 in conjunction with the business cycle and the fluctuations in the unemployment rates. In 1999 the number of participants on the program peaked by covering some 1.6 million people (Lee, 2000). The PW scheme is the program on which the government spent the largest amount of money during the high unemployment period of 1998 and 1999. The government spent about 3.8 trillion won (US\$ 3,100,000,000) in two years.

There have been several changes in the contents of the public works scheme since its initial implementation. The following does not cover development after May 2000.

### Aim

The aim of the PW program is to carry out work in the interest of the public while at the same time provide a decent income to people who became unemployed "over the night" in the wake of the economic crisis. The program is claimed to be an income protection program as well as an active labor market program (Lee, 2000). Participants carry out a variety of work tasks ranging from high tech computer jobs to manual work like cleaning the parks. The participants receive allowances between 19,000 won (US\$ 16) and 22,000 won (US\$ 18) depending on their work type. Lately the benefits have been reduced in line with arguments put forward by the private sector, and supported by the press. The allowance is paid on daily basis. A public works project period, lasts about three months, and may, after reapplication, be extended by four months. The participants work five days per week and eight hours per day.

### Target Groups

The characteristics of the target groups have been altered, due to criticism that the wrong people participated in the program, e.g. women and the "elderly" i.e. those over 60 years of age. Since the last half of 1999 the selection criteria are based on a sum score of nine characteristics. Among these are age, householder status, number of dependants, assets, female

householder status (Lee, 2000). Unemployment benefits recipients, home care recipients of the Livelihood Protection program, the spouse of the household head with regular income, farmers with certain size of land, and students are not allowed to participate. If more than one member of the household participates in the current period or a person has participated for three consecutive periods (it is possible to participate after one month), that person is also not eligible.

One might ask why a completely new program – Public Works- was invented when the crisis swept over Korea? Why did the government not build on the existing Livelihood Protection (LP) program, which had been in place for decades? One plausible answer is that LP and PW are targeted at different groups. The target groups under The Ministry of Health and Welfare's LP programs are different from the ones under the Ministry of labor and Public Works. Therefore they provide quite different working conditions and benefit levels, the latter being superior in these respects. The first is targeted at the poor, most of them quite distant from the labor market, at least distant from the ordinary labor market. PW on the other hand was initially designed for ordinary workers – often skilled - who suddenly found themselves without work due to the economic crisis. Due to prevailing norms, one simply does not mix regular workers with poor people on a poor relief program like LP. Adding to this, many of the newly unemployed men were closer to the labor market than the recipients of the old LP. This might have facilitated the decision to introduce a new and more appropriate program of better quality than the old LP.

PW is about to be phased out in pace with the business cycle. This characteristic strengthens the image of the extraordinary and temporary nature of this program. This stands in contrast to the Livelihood Protection program which is about to be modernized as a new legislation is currently being implemented (Ministry of Health and Welfare, 2000). The new program, called the Basic Livelihood Security System, became effective from October 1, 2000. Among other things the new law will secure basic livelihood protection for people with low income. Furthermore it will introduce measures to enhance recipient's ability of self-support, and strengthen the rights and responsibility of claimant. Accompanying measures are social services provided by more and better educated social workers.

## **Comparative Analysis**

In this chapter we have identified three forms of activating policies, workfare, ALMP and Public Works. Because the Korean Public Works program is often described as a Workfare program, the empirical description of the Western initiatives focussed on this area of policy.

### *Similarity to ALMP*

The Korean Public Works program exhibits some features of ALMP. They are focussed primarily on unemployed people who are close to the labor market and the programs are organized as part of labor market, rather than social policies. They differ, however, on three important points. First, in contrast to ALMP, they are not tied to entitlement to income maintenance transfer. As such, they exist "instead of" benefits. Second, whereas ALMP typically combine supply-side and demand-side measures, the main objective of the Korean program is to provide work for the jobless. Third, it follows from the demand-side orientation that training, unlike in ALMP's, is not an important part of the Korean program.

### *Similarities to Workfare*

Public Works in Korea also share some features with workfare policies in emphasizing work more than training and other forms of human capital development. They differ, however, both in focussing on demand side- more than supply side measures of regulation; in providing work instead of entitlement to aid, and therefore not as condition for aid.

It has been found that the workfare programs in Western countries also diverged from an idealized model of workfare (Lødemel and Trickey, 2001). In some countries, notably Germany and France, the scale and nature of workfare share many similarities to demand side oriented public works programs. Also, in some of the French programs and recently also in the US, workfare is detached from entitlement to public transfers, and can therefore be described as an "opt in" program, enabling the jobless to receive public support- a distinguishing feature of public works programs. This variation suggests that the Korean program share more similarities to workfare in some countries than in others.

### *Similarities to Public Work*

The ways in which the Korean program differs from ALMP and workfare are similar to the features of public work as expressed in Table 10. 1 above. Providing that our interpretation gives a correct picture of both the featuring characteristics of different active policies and of the nature of the Korean program, it appears to be most fruitful to compare the program to the public works initiatives of the Western countries during the great depression of the 1930's.

There are also two other features which make it more fruitful to compare the Korean programs to these experiences rather than to present day workfare and ALMP in Europe and the US; the scale of the problem addressed, and the nature of the welfare state.



*The Scale of the Problem Addressed*

Workfare and ALMP have recently been introduced by countries which have experienced varying levels of unemployment during the last three decades. By contrast, public works in these countries were introduced as a crisis measure following a sudden economic shock which was accompanied by a steep increase in the level of unemployment. The latter is also the case in Korea. On a scale similar to that found in the West in the 1930's, following the economic crisis in 1997, in less than half a year the country went from near full unemployment to a situation where 1.7 million people were out of work.

*The Nature of the Welfare State*

An important drive for reform in present day Europe is an increasingly shared view that too much entitlement and too generous benefits stifle initiatives among the unemployed by weakening incentives to seek work. The reforms therefore take place within welfare states which have matured to a point where transfers programs provided universal, or close to universal support for the unemployed, regardless of the status of the person or the reason for the lack of income from work. In addition, relative high benefits, as compared to alternative earnings facilitated the "de-commodification" of labor (Esping-Andersen, 1990). Today, the pressure on public budgets and the changing needs of the labor market have contributed to an emphasis on the negative impact on incentives to seek new opportunities in the labor. As a result, the current reforms can be viewed as a "re-commodification" of labor. The level of benefits in Korea today, suggests that incentives may be less of a problem here.

When public works were introduced in the 1930's the Western welfare states were for the most part rudimentary. While coverage in most cases was achieved for industrial injury and retirement, the Poor Law remained the main source of support for the unemployed. The repressive nature of the Poor Laws, and their association with marginal groups in society added to the need for a non-Poor Law alternative for the new masses of unemployed persons.

The situation in Korea today is similar to this. After a rapid development of the welfare states over the last four decades, the first system of Unemployment Insurance was introduced in 1995. By the onset of the crisis two years later, it had not reached a level of maturity that would make it an effective buttress against hardship for the newly unemployed. In a situation similar to that experienced in the West, the Livelihood Protection program represented the only public income alternative. When asked why this was not extended to meet the new needs, the response we received from different Korean officials was that this program was neither designed for, nor suitable

to offer relief to the newly unemployed.

In summary, therefore, both the nature of the Public Works program, the scale and the nature of the need it is designed to meet as well as the nature of the welfare structure into which it is introduced suggests that it is more fruitful to compare this program to the Western public works programs of the 1930's than to ALMP or workfare.

## **Policy Recommendations**

As guests to this country it is not our intention to degrade neither the nature nor the achievements of the Public Works program. Rather, it is our firm belief that when new terms are being spread in our globalized world, often with the aid of international organizations, it is necessary to remain critical and plan future policy developments on the basis of a correct description of the present. From our reading of the literature, as well impressions made during our visit here, we find that the people of Korea have good reason to be proud of its country achievements during the last four decades. When Europe and the US faced their great depression, more than sixty years ago, this took place after a period of industrialization which in many cases dated two centuries back. Moreover, the development of the non-poor law welfare state started with Bismarck's reforms in Germany half a decade prior to the crisis. By contrast, Korea remained an agricultural society until the beginning of the 1960's, only three decades before the crisis. During the interim period, the country not only experienced an impressive economic development. The structure of the welfare state was developed in a far greater speed than that found in the West during its period of industrialization. As in the west, other groups were covered before the turn came to the unemployed. Having experienced much greater problems with fluctuating unemployment, no Western country had achieved coverage of unemployment insurance comparable to Korea today when they faced their first economic shock. These observations should be kept firmly in mind when the current state and future path of the Korean welfare state is commented upon.

We have been asked to conclude this chapter with recommendations for policy changes. Adding to the observations made above, the short period in which we were able to study up on policies and to meet officials and the people participating in the Public Works program calls for a humble approach to this task.

The work sites visited during our mission in March appeared to offer well organized and meaningful work activities for the participants. A site where workers made park benches out of fallen acacia trees gained both the participants; who not only were able to receive economic relief, but also carried out work which was both useful to the community; to the state which was able to get something in exchange for "benefits"; to the local

community which saw its infrastructure improved as well as the environment which benefited from the recycling of resources which otherwise may not have been put to use. This contrasted sharply to the work sites designated for the participants of the Livelihood Protection program, where elderly women (mainly) were set to sort garbage. Therefore, our impression is that a clear "social division" of both welfare and activation is in place in Korea - as in the West. But while this takes place between public works and the work program within poor relief in Korea, the division in the West is mainly between workfare and ALMP. The challenge therefore may be twofold; to develop Public Works into a modern ALMP program and to reform the Livelihood Protection program into a modern social assistance scheme.

The inadequate development of ALMP perhaps represents the greatest shortcoming in Korea's attempt to meet her economic crisis. While Public Works may offer an effective buffer against the immediate effects of large scale unemployment, it falls short in developing the skills of the work force to the needs of the changing economy.

In addition to all the hardship and problems arising, a crisis may also open up new opportunities. Lessons from history tells us that once a national system and local implementing agencies are put in place, this can be changed to meet new needs (Lødemel, 1997). As the crisis appears to be lessening today, this is perhaps the time to take this opportunity to develop new policies which may combine to serve as a buffer in future periods of high unemployment, and to develop the skills of the workfare through training and other measures attached to work.

The good features of Public Works may also offer good examples in the strive to reform the Livelihood Protection (LP) program. Work that requires few formal skills may be both useful to the individual and to the community. While the sorting of garbage may serve the environment, other tasks may be chosen if the desire also is to enhance the position and self-esteem of the most vulnerable groups of the nation.

The reform of the LP program, recently enacted by Parliament, suggests that Korea is ready to reform its last resort service in the direction of a modernized social assistance program, combining the provision of cash with social work intervention. While the cash-care multifunctional nature of social assistance in the West until recently has been perceived as a sign of a lacking departure from previous Poor Law systems, the tendency today is to strengthen the integration of income maintenance and care with the view to achieve integration through a combination of human capital development and control. In the West it remains to be seen if this trend results in a return towards the coercive nature of the Poor Law or towards a new form of assistance offering the recipients more than money alone. Korea is today in the fortunate situation where she might be able to make a transition into a new form of social assistance, without experiencing all the mistakes of the West since the abolition of their Poor Law in the early post World War Two period.

Compared to the other Asian countries suffering from the 1997 crisis, Korea has proved an ability to offer more than economic relief to the unemployed. These are positive signs of a country that continues to meet the needs of its people, as well as those of the economy. The economic and social progress in post-war Korea took place within a traditional cultural heritage which was favorable to the country's development towards modernity. Weber's classical argument that the work ethic based on religious ideals was an indispensable premise for the birth of early Western Capitalism, seems to have a bearing on the Korean case. While protestantism was the decisive factor in Weber's analysis, Confucian ethics appear to play a similar role in Korea. In both cases, religion promoted attitudes which were advantageous towards work, self discipline, desire for education, strong family ties and loyalty to the country.

A lesson which we believe to be universal is that a welfare state is most successful in meeting the needs of its people at large if it is carefully constructed on the foundation of its national culture. Direct imports are seldom successful. Still, we believe that some countries may offer better examples than others. As a cohesive and close knit, if hierarchical society, Korea appears to have more in common with the Continental and Nordic countries than with the US. Today, there is a dominance of US style policies among international organizations giving advice and support giving community. In our assessment, this is particularly the case for the IMF and the World Bank. While the US is an example for Europe in its success in combining sustained economic growth and low levels of unemployment, other aspect of US policy are more negative.

In contrast to Europe, and we believe also Korea, US welfare policies are based on an individualized view of people, their behavior and their aspirations. The "end of entitlement" enacted by the US in 1996 reflects these views. While it builds on a strongly divided society, our fear is that the new legislation will further deepen the divisions.

Also in Europe there is a turn away from an emphasis on entitlement and towards a greater stress on the obligations of those in need, but the new reforms are based on a more structural understanding of the reasons for joblessness. As a result, we find a different balance between rights and obligation in European policies compared to the US. The countries differ, in the extent to which they have succeeded in developing programs for different groups. In the strive to modernize the programs for the young and for other vulnerable groups, the best examples of programs which combine obligations with human capital development are perhaps found in the Netherlands, the United Kingdom and in Denmark.

In the area of ALMP the best examples are perhaps found in Scandinavian countries. When Korea today considers her options for reform, it is perhaps particularly inspiring to note that Sweden's pioneering and leading role in ALMP grew out of the unique way in which this country built on the public works experiences of the 1930's.

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# 11 Review of the Effectiveness of Public Employment Services

Jaeho Keum\*

## Introduction and Background

### *Financial Crisis and Unemployment*

The financial crisis drove the labor market to a situation characterized by rising unemployment and underemployment, with reduced rates of new hiring and declining real wages. The GDP growth rate recorded -5.8 % in 1998. This recession resulted in soaring unemployment as had never been seen before. The unemployment rate, which was 2.6 % in 1997, soared to 6.8 % in 1998. The number of workers dropped from 21,048 thousand in 1997 to 19,926 thousand in 1998. Moreover, a large number of people became economically inactive, as they gave up the search for new jobs in the labor market.

To resolve the problems of rising unemployment, the Korean government has expanded and reinforced public employment offices for job placement and has created a nationwide network for job information.<sup>1</sup> The number of public employment offices managed by the central government has increased from 52 in February 1997 to 157 in December 1999, as shown in Table 11.1. The number of public workers specialized in the job placement services has also increased from 141 to 2,556 during the same period.<sup>2</sup>

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<sup>1</sup> Historically, the government more or less neglected the employment services prior to the financial crisis, with the portion of the government in job matching constituting a mere two % at that time.

<sup>2</sup> Most of the newly hired counselors have civilian status and are involved in not only the job matching service but also other duties such as employment insurance. Thus, it is acknowledged that only a portion of the counselors recruited perform only job matching services and this becomes one reason that lowers civilian counselors' morale, in particular where the counselor had initially expected job matching to be part of their duty.

In 1998, to improve the quality of employment services and to create a user-friendly environment, the government combined the employment insurance section and the employment security section of the local labor offices into a center called the "Employment Security Center (ESC)." These centers are based on the concept of "One-Stop Service" and are designed to provide job seekers with all kinds of information and services; from job vacancy information to vocational training. Right now, the most outstanding advantage of these centers is that an unemployed worker can receive both unemployment benefit and job search assistance at the same place. The "Manpower Bank", which is co-managed by the central government and the provincial government, is specialized on the job-matching service while the "Employment Center for Daily Workers" targets daily workers' job matching. Also, nearly all municipality and local governments, consisting of 253 cities, counties, and districts, have established their own employment services called "Employment Information Center (EIC)". And the size and number of staffs working in the EIC have been expanded as a result of the government's efforts to improve the PES during the crisis. Currently, the EIC offer placement services and counseling and refer clients to training programs and public works. However, they do not pay out unemployment benefits and do not perform eligibility checks.

In addition to dramatically increasing the number of public employment offices and counselors, the government has launched several projects in order to enhance the quality of services.

**Table 11.1: Number of employment service agencies in Korea, February 1997 to December 1999**

	<i>February 1997</i>	<i>December 1999</i>
<i>Central government</i>		
<i>Local labor office</i>	46	-
<i>Manpower bank</i>	3	20
<i>Employment security center</i>	3	122
<i>Employment center for daily worker</i>	-	15
<i>Subtotal</i>	52	157
<i>Number of counselors</i>	141	2,556
<i>Local government</i>		
<i>Employment information center</i>	251	253
<i>Information center</i>	34	28
<i>Subtotal</i>	285	281
<i>Private agencies</i>	1,432	1,756
<i>Total</i>	1,769	2,194

Source: Ministry of Labor, Korea.

### Work-Net

The government formally launched an electronic labor exchange system called "Work-Net" in May 1999, using Canada's "WorkInfoNet" as a standard. The Work-Net, which can be accessed from the Internet at home, provides various information and services such as job vacancies, vocational training, career guidance information, employment policies, employment insurance, labor market statistics: and labor laws. In this way, the Work-Net opens up a way to manage unemployment measures and the labor market more efficiently and effectively. .Almost all job vacancies registered in public employment offices can be searched via the Work-Net unless the employers are reluctant to make public their telephone number and address. As all information on job vacancies and job seekers is channeled into the Work-Net, regardless of the type and place of the public employment office at which employers and job seekers register, overlaps in job vacancy reports and job search registrations can be avoided.

### Occupational Classification

The employment service system is based on the occupational classification, which constitutes the framework that provides structure and coherence to the system. That is, occupational classification not only provides the foundation for the labor market information system, but also forms the basis for the vitalization of job placements. Currently, job placement in Korea is based on the matching of job orders and job seekers coded to the 5-digit level of the Korean Standard Classification of Occupations (KSCO). However, this type of job matching is no longer suitable because it fails to allow for the fact that the skills for jobs and individuals sometimes overlap in different occupations. Also, the current KSCO does not reflect the recent changes in occupational structures and technology.

The Korean government is currently developing an occupational matrix based on a 4-digit level of occupational classification. The new occupational classification will be based on extensive occupational research, analyses and consultations conducted across the nation. This will include the development of skill levels based on the education system, as well as on the types of critical skills. The project, which represents a new structure for the labor market and reflects occupational changes over the last 10 years, will enhance the analytical application of occupational information and should increase the possibility of efficient job matching.

### Worker Profiling System

Reemployment policies for the unemployed can be divided into six categories: unemployment benefits, vocational training, public works, temporary livelihood protection, loans to the unemployed., and job search

assistance. To enhance the effectiveness of these measures and to minimize waste by preventing the unemployed from receiving multiple benefits at the same time, an integrated information system of the unemployed is required. To achieve this, the government has developed a set of databases of the unemployed and introduced a Worker Profiling System, which is a statistical model based on reemployment experiences of past unemployed workers with similar characteristics<sup>3</sup>.

The purpose of profiling is to provide for the early identification and referral services to harder-to-employ unemployment benefit recipients so that they can quickly find jobs. Under this program, claimants receive reemployment services that are adequate to their needs, and they are encouraged to use these services as soon as possible after losing a job. The implementation of the worker profiling program provides one of the significant initiatives to a more fully integrated labor market information system. As a result, barriers between unemployment benefits, employment services, and vocational training programs can be bridged to give job seekers better services and taxpayers a more cost-effective program.

In addition, the government published the 'Occupational Outlook Handbook' in July 1999, as well as various career guidance books, a CD-ROM version of DOT (Dictionary of Occupational Titles), a new Occupational Preference Test, and the Standard Job Manual for Counselors.

### *Improvement in the Public Employment Service*

As a result of the government's efforts to expand public employment services, the number of job seekers using the public employment system has greatly increased from 243,467 in 1997 to 1,702,219 in 1999, as shown in Table 11.2. Also, the number of job vacancies posted has almost tripled during the same period. In addition, 'A Survey on Unemployment and Welfare Needs' conducted in September 1998 reports that the ratio of the unemployed registered with public employment offices had increased to 22.5 % in 1998 from 4.8 % in 1996. Considering the fact that only 9.1 % of the unemployed are using private employment services for job searches<sup>4</sup>, it can be concluded that the role of public employment services has been greatly enlarged after the financial crisis.

This result is confirmed by the "Korea Labor and Income Panel Study (KLIPS)". The 1999 KLIPS shows that 14.1 % of the unemployed use the PES as their job search method, compared to 12.7 % in the 1998 KLIPS and 2.4 % in the "Survey on Urban Unemployment" conducted in 1996 (see Table 11.3 below).

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<sup>3</sup> The worker profiling system developed is similar to that developed by the Australian government and used mainly as an advisory tool in the field. For details, see Eberts & O'Leary (1996) and DEETYA (1998).

<sup>4</sup> Source: A Survey on Unemployment and Welfare Needs, KLI & KIHASA, 1998



**Table 11.2: Records of public employment offices in Korea, 1994-1999**

Year	Vacancies (A)	Job seekers (B)	Job referrals	Employed (C)	(A/B) (%)	(C/B) (%)
1994	225,652	148,597	180,248	28,141	152	18.9
1995	196,319	116,147	175,416	20,938	169	18.0
1996	215,925	150,668	306,501	20,939	143	13.9
1997	245,223	243,467	644,295	36,425	101	15.0
1998	410,005	2,130,687	2,356,881	157,442	19	7.4
1999	697,368	1,702,219	3,128,980	318,904	41	18.7

Source: Ministry of Labor, Korea

**Table 11.3: Job search methods of the unemployed**

Job search method	1999 KLIPS (%)	1998 KLIPS (%)	Survey on urban unemployment in 1996(%)
School and teachers	9.1	10.5	9.6
Friends and relatives	61.7	65.7	39.2
Public employment service agency	14.1	12.7	2.4
Private employment service agency	2.4	5.7	3.5
Newspaper, TV, and etc	49.2	57.2	18.4
Direct employer contact	24.8	35.9	19.3
Internet and other networks	8.9	6.7	0
Others	3.4	2.8	8.7
Total	100.0	100.0	100.0
Number of unemployed	496	1,255	1,054

Note: Multiple answers were allowed for the KLIPS.

### *Challenges in the Public Employment Service*

However, in 1999 the number of job vacancies had increased by almost 70 % while the number of job seekers visiting the public employment offices had decreased by 25 %, as shown in Table 11.2. This reduction in the number of job seekers, in part, reflects the economic recovery. But there remains a lingering question as to whether the PES satisfies user's demand. To evaluate the effectiveness of the Korean PES, the KLI had conducted a field survey in October 1999. From this survey it was found that even though the PES has succeeded in the provision of basic information and services such as job vacancy information, employment insurance and simple job matching, it however failed to provide in areas such as in-depth

counseling, career guidance and in-depth occupational information. Also, it has been found that job searchers using the PES constitute mostly young and highly educated workers. Only a small portion of the low-skilled and/or disadvantaged workers such as the elderly, female, and disabled currently use PES agencies because they think that the PES does not give timely and necessary information and services.

In the past, the most important role of the PES has been merely simple labor exchange, which is the finding of jobs for workers and the finding of workers for jobs. However, as the Internet becomes more widely accessible and able-workers find suitable jobs without the PES, the main focus of the PES should shift to the provision of in-depth counseling for low-skilled and/or disadvantaged workers, as well as the dissemination of labor market information, career development, and active labor market programs.

In Korea, before the financial crisis in 1997, information on job openings was usually sufficient for job seekers. However, with the crisis, characterized by high unemployment and economic depression, job seekers increasingly seek information not only on available job opportunities but also on vocational training, career development, the labor market situation, and occupational prospects. This tendency will continue even after the financial crisis in line with the changing economic environment, such as the accelerated progress in technology, continued globalization, and increased competition. The role of the PES as a core delivery system for employment policies and development of human resources will be enlarged since economic growth and the well-being of people largely depend on knowledge and human capital in the new era of the 21st Century. Especially, as the Korean government has introduced the 'Productive Welfare', the role of the PES as a delivery mechanism of government measures for the low-income families will be expanded.

In this respect, the Korean PES faces two big issues. One is how to improve the quality and quantity of information and services. The other is consensus on the future role of the PES in the Korean labor market. To answer these questions, a field survey was conducted in August 1999. The sample consists of job seekers visiting the public employment offices, counselors working at the PES, and firms using the PES. The results of this survey are presented in the following section. Then, we analyze the issues and challenges faced by the PES. Also, the results of in-depth interviews with experts and counselors as well as reviews of related papers are summarized in this section. The PES in Korea as one of the most important instruments for developing human resources should focus on career guidance and counseling service. It also has to provide coordinated information and services on vocational training, occupational information, labor market trends and so on. Practical ways of improving the PES' services is introduced in the concluding section. Various suggestions and future directions are presented in this section in detail.

## **Analysis of Effectiveness and User Demand for the Public Employment Service**

### *Survey Outline*

To evaluate the effectiveness of the public employment service and to access the user demand, a survey was conducted in 1999 for 7 days, between October 11th and October 21st. The survey interviewers visited Manpower Banks, Employment Security Centers, and local government's Employment Information Centers in the Seoul metropolitan area, including Incheon.

Those surveyed include job seekers visiting public employment offices and enterprises that use public employment offices, as well as counselors working on one of the three types of public employment offices. Specifically, the survey sample consists of the following:

- 500 job-seekers,
- 100 counselors, and
- 200 firms using the PES to recruit new employees.

### *Analysis of Survey Results on Job Searchers*

#### Characteristics of Respondents

The survey result shows that the public employment offices are relatively most active amongst job seekers in their 20's and those with tertiary education. Among the job seekers surveyed, 89.4 % (447 persons) stated that they were 'currently unemployed', while those that were currently employed at the interview time but wanted a change of job consisted only about 10.6 %. Among those currently unemployed, a relatively large proportion of 86.8 % (388 persons) actually did have prior work experience. The average working period of previous experience is 5.84 years. We observe that compared to new entrants to the labor market those having prior work experience are more likely to visit the PES agencies in order to find new job opportunities.

We distinguish between two types of job seeking activities: active and passive. With reference to Table 11.4, the former and more aggressive approach to job search constitute items (1) through (7), and involve contacting 'friends and relatives', 'school and teachers', 'public employment service agency', etc. In contrast, passive job search activities constitute items (8) to (10), where the job seeker either simply collects information, or waits half-heartedly for a job search result.

Without taking the PES agencies into consideration, roughly half of the unemployed preferred the search method of 'see vacancy advertisements and

contact employers'. This method of job search is followed by the method of finding out about possible work opportunities through 'friends and relatives' (40.2 %), 'private employment service agencies' (26.8 %), and 'direct employer contact' (21.4 %).

**Table 11.4: Job search method of respondents**

Search method	Job seeker			Survey in 1998 (%)
	Total (%)	Male (%)	Female (%)	
School and teachers	19.6	17.9	23.0	8.5
Friends and relatives	40.2	39.4	42.8	53.4
Public employment service	100.0	100.0	100.0	14.0
Private employment service	26.8	29.9	20.6	9.1
Direct employer contact	21.4	25.7	12.7	29.8
Job fairs	17.0	19.1	12.7	5.5
See vacancy ads and contact	50.4	52.8	45.5	24.1
Simply see vacancy ads	47.8	48.7	46.1	43.3
Search vacancy ads of the internet	33.6	33.1	34.6	8.2
Others	2.6	2.1	3.6	6.7

Note: Multiple answers were allowed and 'Survey in 1998' indicates 'A Survey on Employment and Welfare Needs' whose sample size was 30,000 households representing the whole nation.

Representing the passive method of job search, 47.8 % of unemployed workers look for job opportunities through 'vacancy advertisements of newspapers and other periodicals'. Also, as the Internet becomes more popular, especially, among the younger generation, a substantial number of job seekers (33.6 %) use the Internet to get information on available job vacancies. The Internet has become increasingly important as a job matching tool.

When asked about the difficulties encountered during job searching, a good number of respondents indicate that 'job opportunities are either insufficient or unavailable' (Table 11.5). Others state that 'low wage offers' have presented added difficulties in the search for work. We rate the responses to questions according to the following 4-point scale: 'strongly agree' 4, 'fairly agree' 3, 'somewhat disagree' 2, 'strongly disagree' 1. The average point calculated is 2.94 to the question whether 'job opportunities are either insufficient or unavailable', and 2.83 to the question whether potential employers presented 'low wage offers'. This shows that roughly half of the job searchers in general faced difficulties in looking for work.

**Table 11.5: Difficulties in job-search activity**

	point average	Strongly agree	Fairly agree	Somewhat disagree	Strongly disagree
		(%)			
Few job vacancies	2.94	18.8	54.4	17.6	3.4
Lack of job information	2.45	6.2	37.2	35.6	9.8
Inadequate education and skills	2.60	10.4	42.6	30.2	8.2
Lack of work experience	2.45	10.4	34.6	31.4	14.8
low wage offer	2.83	13.8	51.2	23.0	3.0
Inadequate working condition/working hours	2.48	7.4	35.0	37.6	7.8
Age discrimination	2.47	14.0	33.2	26.2	18.4
Sexual discrimination (female only)	2.31	9.7	26.7	37.6	17.6
Childcarehouse chores (married female only)	2.96	31.5	29.6	20.4	7.4

*Job Search Activities at the PES*Reason for Visiting PES Agencies

**76.9 %** of respondents indicate that they visit public employment offices specifically to 'gather information on employment opportunities'(Table **11.6**). This is similar to results found in the **1998** 'A Survey on Unemployment and Welfare Needs'. A mere 2.3 % said they visit public employment offices for reason of 'career consultation'. Compared to the **1998** study, those

**Table 11.6: Reason for visiting PES agencies**

Reason	Job searchers (%)				Survey on unemployment & welfare needs (%)
	Manpower bank	ESC	EIC	Sub total	
Gathering vacancy information	84.4	76.5	62.3	76.9	71.0
Career consultation	3.3	2.3	-	2.3	-
Receiving unemployment benefit	4.1	9.4	13.2	8.5	13.1
Participating public works	0.8	1.9	13.2	2.9	6.3
Participating vocational training	5.7	8.4	5.7	7.4	7.0
Receiving loans	-	-	-	0.0	0.0
Others	1.6	1.6	5.7	2.1	1.3
Total	100.0 (122) <sup>1)</sup>	100.0 (310)	100.0 (53)	100.0 (485)	100.0 (3,208)

Notes: 1) The numbers in parenthesis are number of respondents

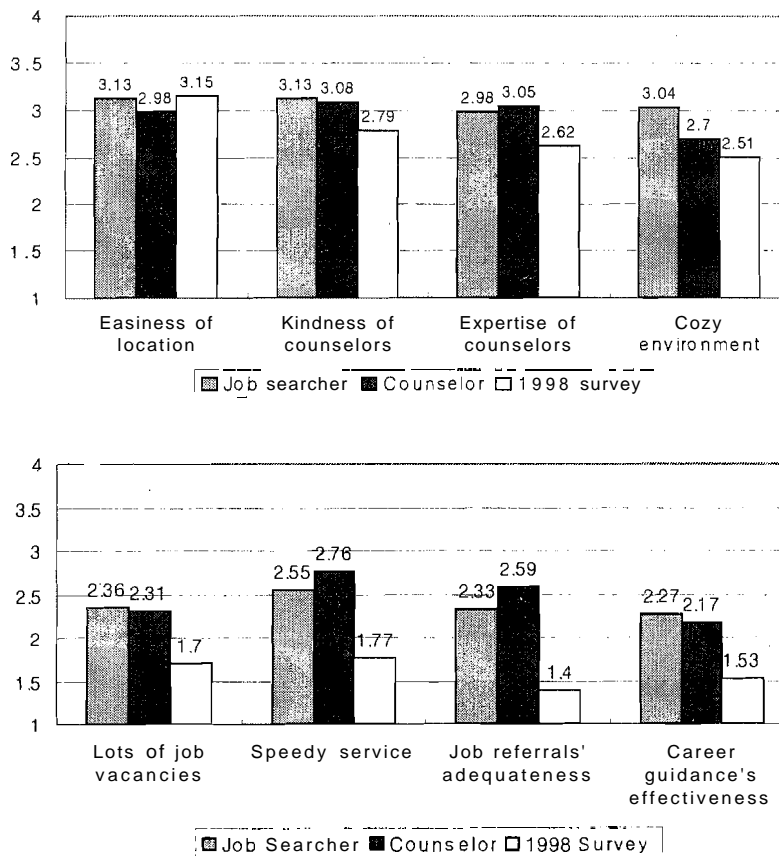
2) ESC and EIC are abbreviations of 'Employment Security Center' and 'Employment Information Center' respectively

receiving unemployment benefits and participating in public works somewhat declined. The primary reason for visiting public employment offices is to look for work.

### *Evaluation of the Public Employment Service*

Compared to the 1998 'A Survey on Unemployment and Welfare Needs' a substantial improvement in the quality of services is reported (see Figure 11.1). Apart from the item 'easy to locate', improvements in other areas are reported, in particular 'abundance of job vacancies', 'promptness of service', 'adequateness of job referral', and 'effectiveness of career guidance', thereby

Figure 11.1: Evaluation of the PES – job searchers, counselors and the survey of 1998



reflecting perceived improvement in the overall employment services. Despite differences in opinions of counselors and job seekers as to whether 'the site's environment is cozy', in general, both tend to display a similar opinion towards the quality of employment services. However, notwithstanding a definite improvement in employment services during the past year, more continued effort must be exerted to provide quality services to job searchers.

When asked if the respondent ever received either interview or career counseling at the **PES** agencies, 58.2 % of job seekers give affirmative answers. The remaining 41.8 % reply that they visit **PES** agencies simply for the purpose of vacancy information or to participate in various unemployment programs such as unemployment benefit, public work, and vocational training. This result suggests that the **PES** agencies and counselors are currently under-utilized.

Interview or counseling time typically ranges between 1 minute to 2 hours. In fact, an average of 17.1 minutes is calculated. Those that fall in a higher age group and/or have lower education level appeared to participate in relatively longer periods of interview or counseling time. In general, 70.5 % of those receiving interview or counseling (205 persons) state that there was 'sufficient time for interview or counseling' and find no need for more in-depth counseling. About two thirds or 62.5 % answer that 'the general environment and mood was suitable towards interview or counseling' while the remaining one third state that the environment was not appropriate and that they could not communicate what they had in mind.

Among job seekers that received interview or career counseling, when asked what types of service and information they wanted or should be supplied, 86.3 % replied that they wished to have access to job vacancy information (Table 11.7). Among those that hoped to know about job vacancy information, over two thirds or 68.5 % reply that they were satisfied with the information they received.

Moreover, job searchers felt the need for 'job search techniques', 'resume and document writing methods', and 'information on self-employment', but found that services and information on these were relatively poor. In particular, 35.1 % of respondents hoped for 'psychological counseling'. However, more than half or 55.9 % state that they had not received any psychological counseling.

Thus, most job seekers who received interview or counseling felt that they did receive requested information on job vacancies and about the work that they wished to know about. But services and information, such as 'psychological counseling' and 'labor market trend and perspective', were felt to be as yet insufficient or shallow even though many job searchers requested these.

**Table 11.7: Type of desired service and degree of satisfaction**

Type of service and information	Ratio of job searchers	4 point average	All of them provided	Most of them provided	Partly provided	Never provided
	(%)					
Information on job vacancies	86.3	2.83	19.9	48.6	25.9	5.6
Resume writing methods	41.9	2.43	18.0	37.7	13.9	30.3
Job search techniques	47.8	2.22	12.2	30.2	25.2	32.4
Psychological counseling	35.1	1.78	8.8	16.7	18.6	55.9
Occupational information	56.4	2.58	17.1	37.2	32.3	13.4
Occupational perspectives	45.7	2.03	7.5	27.8	24.8	39.9
Information on self-employment	39.2	2.12	12.3	31.6	12.3	43.9
Information on college entrance	28.9	1.79	2.4	29.8	11.9	56.0
Labor market trend	36.4	1.94	6.6	22.6	29.3	41.5
Aptitude and other tests	34.4	2.10	11.0	30.0	17.0	42.0
Maintenance of livelihood	37.8	1.69	3.6	20.9	16.4	59.1
Laws and regulations	37.1	1.75	4.6	16.7	27.8	50.9

Note: 'Ratio of job searchers' represents that among those who received counseling the ratio of answered who need respective service and/or information.

### ***Ways of Improvement of the PES***

Respondents answer that the most important improvement required in the PES is 'the expansion of job vacancy information' (40.3 % as the top priority), which overall constitutes 70.3 % of responses (Table 11.8). Next, respondents felt that there were needs for 'improvements in career guidance information' (48.7 % of overall respondents) and 'active and progressive service of counselors' (45.8 % of overall respondents)

The counselors, not unlike job seekers, feel that there is need for 'improvements in job vacancy information' and 'improvements in occupational and career guidance information' (Table 11.9). However, while job searchers stress the need for an 'active and progressive service of counselors', counselors point to 'improvement in the morale of counselors', and as such, an opposing view is observed. This opposing view could be answered by the explanation such that 'a more progressive stance on the part of counselors' may be brought about by better 'counselor's morale'. Additionally, compared to job searchers many counselors understand the importance of 'career guidance counseling' and highly evaluate the importance of 'Work-Net' and other computer network systems.



Table 11.8: Improvement directions of the PES – job searchers

Content	First	Second	Third	Overall
	priority	priority	priority	
	(%)			
Kindness of counselors	17.2	6.2	1.3	24.2
Progressive attitude of counselors	15.4	18.2	15.3	45.8
Enhancement of counselor's expertise	7.0	4.6	8.1	18.3
Expansion of job vacancy information	40.3	14.7	18.7	70.3
Improvement of work-net	4.0	9.3	8.1	19.8
Counseling environment and office layout	0.7	8.5	4.3	12.5
Increase in interview and counseling time	3.3	3.5	5.5	11.4
Improvement in occupational/career information	7.7	27.0	17.9	48.7
Improvement in vocational training information	4.4	8.1	20.9	30.0
Total	100.0	100.0	100.0	
	(273) <sup>1)</sup>	(259)	(235)	

Note: 1) Numbers in parentheses are number of respondents.

Table 11.9: Improvement directions of the PES – counselors

Content	First	Second	Third	Overall
	priority	priority	priority	
	(%)			
Active development of job vacancy information	28.9	9.4	7.3	45.4
Improvement in occupational/career information	16.5	25.0	8.3	49.5
Improvement of work-net	8.3	5.2	10.4	23.7
Progressive attitude of counselors	7.2	1.0	9.4	17.8
Enhancement of counselor's expertise	8.3	12.5	13.5	28.9
Enhancement of counselor's morale	14.4	15.6	20.8	50.5
Providing college entrance information	8.3	22.9	14.6	45.4
Assistance of business start-up	6.2	7.3	13.5	26.8
Others	2.1	10.4	2.1	14.1
Total	100.0	100.0	100.0	

### *Evaluation of 'Work-Net'*

Among job seekers, 38.8 % had used Work-Net at least once while 47.6 % answer that they had never used Work-Net before even though they had knowledge of it. The remaining 13.6 % state that they had never heard of Work-Net.

During the past one month it was observed that a job seeker visited the Work-Net site an average of 8 times. This reflects the relative frequency of visiting the Work-Net site. However, there is mixed reaction among those that have used Work-Net. In general, those that express remorse about the Work-Net find problems in the 'coordination among information flows' and 'the speedy removal of obsolete information and the addition of new information'. In particular, despite the wide variety and abundance of information and the convenience of searching through the database, many users complain that the information is not helpful in finding suitable job.

Not unlike job seekers, counselors agree that there is a wide variety and abundance of information in the Work-Net and that the search mechanism is user friendly in general. That is, the Work-Net received a favorable evaluation from counselors. But counselors also find that there are problems in the 'coordination among information flow' and 'the prompt replacement of old information with new relevant information'. However, 56.7 % of counselors feel that Work-Net is efficient in meeting the demands requested of it and that it increases the effectiveness of the PES.

### *Analysis of Survey Results on Counselors*

#### Characteristics of Respondents

Out of the 100 surveyed counselors, 68.0 % worked for the Employment Security Center, 23.0 % worked for Manpower Banks and 9.0 % worked for Local Employment Information Centers. Among the respondents, up to 70 % of counselors are engaged in job matching service and 27.3 % work mainly at Employment Security Centers taking charge of employment insurance duties (Table I1.10).

Almost all of counselors are private contracts of professionals whose contract term is 1 year. Prior to their present work, counselors with previous experience on the employment and career counseling constitute only 18.2 %. So, in most cases counselors actually have their first experience in employment and career counseling when they begin their work at public employment offices. Moreover, prior to their present work, only 16.3 % underwent vocational training on employment and career counseling; thus a large number of counselors working at public employment offices are either inexperienced or do not have the required skills. In public employment

**Table 11.10: Characteristics of counselors**

Classification	Employment security center	Manpower bank	Local employment information center	Sub total
	(Yo)			
Total	68.0(68)	23.0(23)	9.0( 9)	100.0(100)
<i>Main duty</i>				
Job matching service	58.2(39)	95.7(22)	88.9( 8)	69.7( 69)
Employment insurance	38.8(26)	-	11.1( 1)	27.3( 27)
Other administrative duties	3.0( 2)	4.4( 1)	-	3.0( 3)
Subtotal	100.0(65)	100.0(23)	100.0(9)	100.0(100)
<i>Type of employment</i>				
Civil servant	2.9( 2)	4.4( 1)	22.2( 2)	5.0( 5)
Private professional	94.1(64)	95.7(22)	22.2( 2)	88.0( 88)
Participant of public work	2.9( 2)	-	55.6( 5)	7.0( 7)
Subtotal	100.0(68)	100.0(23)	100(9)	100.0(100)
If had experience on the employment and career counseling	17.7(12)	22.7( 5)	11.1( 1)	18.2( 18)
If received vocational training on the employment and career counseling	13.3( 9)	27.3( 6)	11.1( 1)	16.3( 16)

Note: Numbers in parentheses are number of counselors.

offices, it has been observed that counselors have had their present positions ranging from one to forty months. Counselors reside at their place of work for an average of 10.6 months, that is, for less than a year.

#### Working Hours of Counselors per Week

Counselors work an average of 47.5 hours per week, spending 38.3 % (18.2 hours) of their total working time on attending to visitors. 15.2 % of their work time (7.2 hours) is spent on the telephone and on out-of-office remote counseling (Table 11.11). Combining these two duties, we find that more than half the time is spent on interview and/or counseling and the supply of information to the unemployed. Additionally, a total of 12.4 % of the counselor's working time is spent on developing counseling capacities through vocational training and education (3.4 hours per week) and attending meetings and administrative duties (5.8 hours per week).

With respect to the allocation of duties, only 39.4 % of respondents answer that the allocation of duties is appropriate. That is, more than half the respondents regard the duty allocation as inappropriate. When considering adjustments in the allocation of duties, areas where working times should be extended include 'interview or counseling of visitors', followed by 'contact!

Table 11.11: Counselor's duties and working time per week

Duties	Employment security center	Manpower bank & EIC	Total
	(hours)		
Interview or counseling of visitors	18.2	18.2	18.2
Development of job vacancies information	5.6	7.4	6.2
Preparation of various job match meetings	4.4	3.1	4.0
On-line interview and consultation	7.2	7.2	7.2
Training/education for capacity improvement	3.3	3.5	3.4
Meetings and administrative activities	6.4	5.1	5.9
Others	2.7	3.1	2.8
Total	47.7	47.0	47.5

Table 11.12: Counselor's duties **to** be expanded

Duties	First priority	Second priority	Overall
	(% )		
Interview and/or counseling of visitors	62.7	12.0	72.9
Contact with employers & development of job vacancies	15.3	36.0	45.8
Preparation and participation of meetings for job match	3.40	6.0	8.5
On-line interview and consultation	3.40	6.0	8.5
Training & education for capacity improvement	15.3	36.0	45.8
Meetings and administrative activities	0.0	4.0	3.4
Others	0.0	0.0	0.0
Total	100.0	100.0	-

with employers and development of job opportunities' and 'training & education for capacity enhancement'(Table 11,12). To improve the quality of employment services, interview and/or counseling time should be extended with development of vacancy information and development of counselor's capacity.

As for the duties for which working times should be reduced, counselors chose 'meetings and administrative activities and 'on-line interview and consultation'(Table 11.13). In particular, with respect to the latter, counselors think that specialists should perform as their main duties such as on-line interview or counseling. These results suggest implicitly that the management of the PES agencies overburdens counselors, and that in

general, counselors don't have sufficient time to provide in-depth counseling service to needy job searchers.

Table 11.13: Duties of counselors to be curtailed

Duties	First priority	Second priority	Overall
	(% )		
Interview and/or counseling of visitors	3.7	8.0	7.4
Contact with employers & development of job vacancies	0.0	12.0	5.6
Preparation and participation of meetings for job match	7.4	4.0	9.3
On-line interview and consultation	38.9	24.0	50.0
Training & education for capacity improvement	1.9	0.0	1.9
Meetings and administrative activities	44.4	44.0	64.8
Others	3.7	8.0	7.4
Total	100.0	100.0	

#### Activities of Counselors

Counselors report that among job searchers visiting the PES agencies, 21.1 % needed in-depth counseling as opposed to merely receiving information on job opportunities and employment insurance. Unemployed workers who need in-depth counseling include job seekers 'unemployed for over 9 months' and 'middle aged males (40–55 years)'. Specifically, the ratio of the unemployed who require in-depth counseling is highest among long-term unemployed (more than 9 months of unemployment) and middle aged males, whose figures are 29.7 % and 27.0 %, respectively. In addition, the analysis of the survey indicates that the ratio of the unemployed who need in-depth counseling is higher than average for teenage workers and middle aged female workers.

To the question 'what kinds of in-depth counseling is required', counselors selected 'provide detailed information on work opportunities' (72.5 %), which is followed by 'counseling on career in future' (60.2 %), 'vocational training and education' (60.2 %), and 'psychological counseling' (53.1 %). This result reflects that the PES does not currently provide the necessary services to the job searchers except for information on job placements. Thus, development in career guidance counseling and psychological counseling needs to be emphasized.

The average time of interview and/or counseling for visitors is 15.9 minutes. Interview or counseling time of on-line service average 7.6 minutes, but it is difficult to tell the differences across agencies. In general, counselors state that 88.3 % of interview or counseling time over the telephone last under 10 minutes. Regarding the length of interview or

counseling, a little over a half the counselors (53.6 %) answer that 'interview or counseling time was (extremely) insufficient', contradicting the responses of job seekers as reported above. A substantial portion of job seekers (70.5 %) state that 'counseling time was sufficient'. However, when asked what the appropriate times for interview or counseling sessions should be, counselors respond that for personal visits the average should be 26.1 minutes and 13.1 minutes for counseling over the line.

Over half of the counselors (56.7 %) reply that currently the PES doesn't provide appropriate information and services to job searchers, and also, fails at maintaining their efficiency.

Table 11.14: Reason for ineffectiveness of the PES

Reason	Employment security center	Manpower bank	Total
	(% )		
Low morale of counselors	18.5	25.9	20.7
Overburden of counselors duties	10.8	0.0	7.6
Lack of counselors' expertise and experience	0.0	0.0	0.0
Insufficient information on job vacancies	20.0	18.3	19.6
Insufficient occupational information	10.8	3.7	8.7
Mismatch between job seekers and employers	29.2	18.5	26.1
Low capacity and high expectation of job searchers	7.7	25.9	13.0
Others	3.1	7.4	4.4
Total	100.0	100.0	100.0

The lack of effectiveness of the PES, 26.1 % of counselors answer, is due to 'mismatches between job seekers and job referrers' (Table 11.14). Moreover, the 'low morale of counselors' (20.7 %) is found to be another main cause of the ineffectiveness of the PES. Especially, among counselors working at Manpower Banks, low morale is the main reason for low productivity and the poor quality of services.

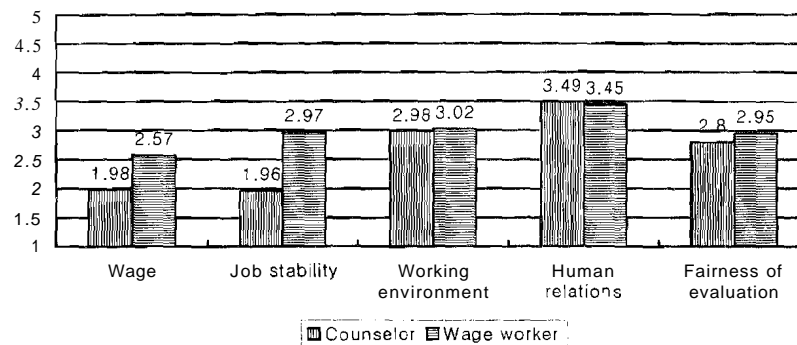
#### Job Satisfaction of Counselors

Most of the counselors are satisfied with regard to 'working hours', 'communication and human relations at work', 'sense of achievement', and so on. However, more than 70 % of counselors express insecurity and dissatisfaction as regards, among others, 'job security' and 'wages' (Table 11.15). The 'working environment' and 'possibility of career development' also constitute counselors' concerns, with 35.7 % and 43.9 % of counselors expressing dissatisfaction respectively.

**Table 11.15: Job satisfaction of counselors**

Items	5 point average	Very satisfied	Satisfied	Middle	Un-satisfied	Strongly un-satisfied
Wage or income	1.98	1.1	2.1	21.9	43.8	31.3
Job security	1.96	2.1	3.1	22.5	33.7	38.8
Sense of achievement at work	3.14	6.2	32.0	36.1	21.7	4.1
Sense of creativeness	2.83	3.1	13.4	55.7	19.6	8.3
Sense of autonomy	2.93	7.1	20.4	41.9	13.4	11.2
Possibility of career development	2.59	4.1	13.3	38.8	25.5	18.4
Working environment	2.98	8.2	24.5	31.6	28.6	7.1
Working hour	3.46	12.4	38.1	35.1	13.4	2.1
Human relation	3.49	15.3	37.8	33.7	7.1	6.1
Fairness of evaluation	2.80	3.1	14.6	56.3	14.6	10.4

Compared to the findings of the Korean Labor and Income Panel Study (KLIPS) of 1998, there are little differences between counselors and wage workers in general as to job satisfaction on 'working environment', 'human relations', 'fairness of evaluation' and so on. (Figure 11.2) However, compared to wage workers in general there is substantial increase in dissatisfaction as regards 'wages' and 'job security'. This dissatisfaction on the part of counselors reflects the fact that almost all of them are civilian specialists with one year contracts and a monthly wage of around 1 million Won. Actually, the low morale of counselors is one of main obstacles preventing the PES from providing effective and efficient services to needy people.

**Figure 11.2: Job satisfaction of counselors and wage workers (1998 KLIPS)**

## Issues and Challenges of the Public Employment Services

### *Issues in the Public Employment Service*

#### Low Share of the PES in Job Matching Service

The quality and quantity of the Korean PES have to reach that of advanced countries as the analysis of this survey showed. The share of PES-induced placements in the economy, most experts believe, is around 10 %, which is far below that of advanced countries, for example, Germany and Japan.<sup>5</sup> Most workers are still looking for new jobs using informal search methods such as 'friends and relatives' and 'direct employer contacts'. These informal search methods eventually jeopardize the efficiency of the labor market. Also, when compared to foreign countries, as can be seen in Table 11.6, the number of agencies, the number of counselors and the number of workers attended to by each agent fall far behind. Thus, there still remains much room for the expansion of the PES in Korea. In this respect, a nationwide consensus is required as regards the future direction of the PES.

**Table 11.16: Public employment service in selected countries**

Country	PES agencies	Counselors	Num. of workers per counselor
Japan	619	15,320	3,401
Germany	842	93,000	364
Sweden	570	11,000	325
U.K.	1,159	34,000	745
Korea	157	2,556	5,095

Note: Data refer to December 1999 for Korea and to 1997 to other countries.

Source: Ministry of Labor

#### Mismatch Between Employers and Job Searchers

From the survey in the proceeding, the main characteristics of job seekers that visit PES agencies, we find, are as follows:

- Relative to other unemployed workers, job searchers using the PES have a high level of education. Also, they are relatively young and more likely to have prior working experiences. Only a small portion of the low-skilled and/or disadvantaged workers such as elderly, female,

<sup>5</sup>

The SFHP estimates that the share of PES-induced placements is about 11.2 %

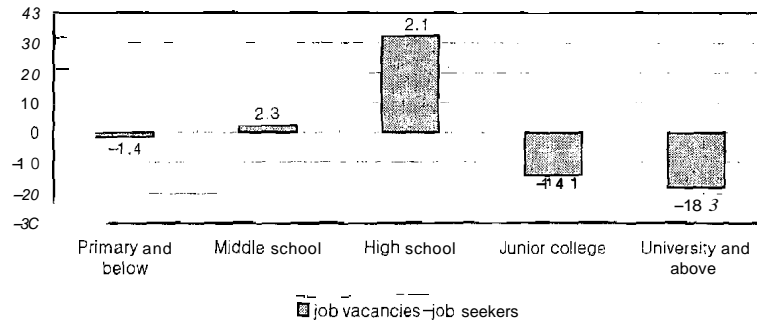
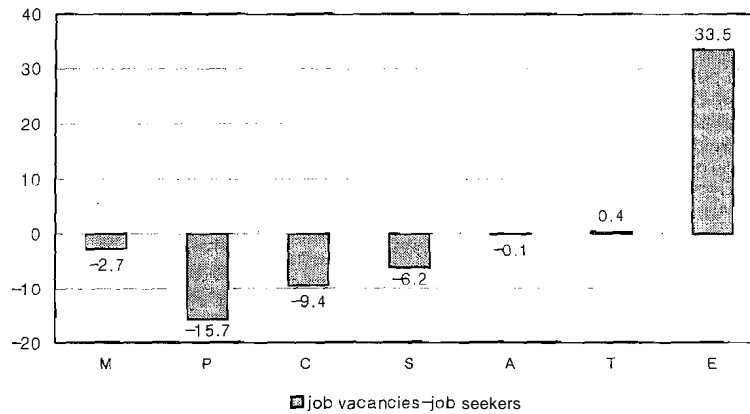


and disabled currently use PES agencies because they do not have much confidence that the PES may provide the timely and necessary information and services.

- ❑ Compare to other unemployed workers, job searchers are actively looking for job opportunities. And they are usually computer literate and can use the Internet. Also, many of them use the PES as an auxiliary method for job search.
- ❑ In general, they have a passive attitude and a large portion tend to visit the PES not for interview and/or counseling but merely to gather information on the 'Work-Net' or bulletin board.
- ❑ Job searchers seem to prefer work in the services sector as opposed to the wholesale, food and hotel industries. Even if they wished to work in the manufacturing sector, they hoped specifically to find work in the electronics or telecommunication sectors.
- ❑ According to occupational type, (associate) professionals, technicians, and clerks are among the preferred type of work, and a full-time regular job is preferred to part-time contingent work.

The survey result shows that only a small portion of disadvantaged workers such as middle-aged, elderly, married females, and disabled, who need governmental support urgently actually use PES agencies because of the ineffectiveness of the PES. Also, even though job seekers look for (associate) professional jobs in the services sector, potential employers have different expectations that are not easily matched given the characteristics of the job seekers using the PES. First of all, there is a difference in the education level with respect job seekers and potential employers. Figure 11.3 shows values, which are  $[100 \times \text{job vacancies for a specific educational level} / \text{all job vacancies}] - [100 \times \text{job seekers for a specific educational level} / \text{all job seekers}]$  for each educational level. Assuming that the number of job searchers and job vacancies are both 100, the figure indicates that employers find themselves short of 32 job seekers at the high school graduate level. Thus, from Figure 11.3 we can conclude that, in general, job seekers are of high education than firm's expectation. Since potential employers wish to hire high school graduates, job seekers of a tertiary education should lower their expectation level to gain employment.

Reflecting the mismatch in education, firms and job seekers also experience a mismatch in occupational type. As seen in Figure 11.4, job seekers hope for (associate) professional and technical positions while employers continue to look for simple labor jobs. This result is also shown by the 'Survey on Firm's Hiring Practice', in which firms have difficulty in recruiting 'Machine Operators and Assemblers'. However, firms also face difficulties in the hiring of 'Professionals and Technicians' because they couldn't find qualified candidates. This result states the possibility of skill mismatch and structural unemployment in Korea.

**Figure 11.3: Educational mismatch between job seekers and vacancies****Figure 11.4: Mismatch in occupational type between job seekers and vacancies**

- M: Legislators and managers**
- P: (Associate)professionals and technicians**
- C: Clerks**
- S: Service and sales**
- A: Agricultural and fishery**
- T: Machine operators and assemblers**
- E: (Simple) laborers**

Weakness in Contents and—Quality of the PES

At present, PES agencies focus on the provision of basic services and information including job vacancy information, job referrals, and programs of employment insurance, while the production of in-depth counseling service and detailed information remains unsatisfactory. 70 - 80 % of job seekers ask for only simple information and consultation service. As for these job searchers the PES meets their demands and during the past year job seekers have been relatively satisfied. But improvement is required in areas such as career guidance counseling, quality of job referrals, counseling for disadvantaged people, and labor market and occupational information provided by the PES.

As for the quality of the PES, the survey results are:

- Within the items of 'promptness of service', 'appropriateness of job referral', and 'effective career consultation', the negative responses of 'somewhat disagree' and 'strongly disagree' are high among job seekers. And similar responses were found with the counselors.
- 41.8 % of job seekers visiting PES agencies never received either interview or career counseling. The average time of interview or counseling is 17.1 minutes on average. And about half of counselors answer that 'interview or counseling time was (extremely) insufficient.
- One third of job searchers state that the interview or counseling environment was not appropriate and that they could not communicate what they had in mind.
- Most of job seekers either partly received or never received information on 'Job Search Techniques', 'Occupational Perspectives', 'Labor Market Trend', and 'Maintenance of Livelihood'. Also, over half of the counselors state that the PES does not currently provide the necessary information and services for the job searchers.
- Even though 35.1 % of job seekers hoped for psychological counseling, more than half of them did not receive any psychological counseling.
- There is the wide practice of the offering of inappropriate jobs to job searchers.
- Despite the wide variety and abundance of information and the convenience of searching through the database, many users complain that the information is not helpful in finding suitable work. Counselors, in general, give a favorable evaluation on the Work-Net. However, counselors also indicate problems in the 'coordination among information flow' and the 'prompt replacement of old information with new relevant information'.
- Not only a small portion of respondents use occupational references for job search activities but also many job searchers do not appreciate the usefulness and effectiveness of these references.

These survey results suggest that more persistent and systematic efforts are needed to improve the quality of services provided by the PES agencies.

Especially, improvements in the areas of 'career guidance', 'occupational information', 'psychological counseling', and 'labor market trends and perspectives' as well as the environment of interview or counseling are needed.

#### Inappropriate Occupational Classification System and Weak Occupational

The employment service system is based on the occupational classification, which constitutes the framework that provides structure and coherence to the system. That is, occupational classification not only provides the foundation for the labor market information system, but also forms the basis for the vitalization of job placements. Currently, job placement in Korea is based on the matching of job orders and job seekers coded to the 5-digit level of the Korean Standard Classification of Occupations (KSCO)<sup>6</sup>. This type of job matching is no longer appropriate because it fails to allow for the fact that the skills for jobs and individuals sometimes overlap in different occupations. Even though the KSCO was revised in 1999, it still has difficulties in labor market application.

To circumvent the problems arising from the unsuitable classification of occupations, public employment offices developed its own placement code system. However, this code system includes only occupations having placement record in the PES and apparently has no criterion of grouping. More critically, there is no connection between the placement information with other information, such as vocational training, career development and labor market trend, through this code system.

Even though the importance and role of the occupational study in the labor market was well recognized, the Korean government invested little in this area before the 1997 financial crisis.<sup>7</sup> Only few researchers in the Central Employment Information Office (CEIO) were involved in tasks such as Korean Dictionary of Occupational Titles, Occupational Handbook, and so on, and worked under inadequate working circumstances. With the crisis, about twenty researchers were recruited in order to strengthen the occupational study. However, several years are needed before tangible progress may be seen because most of the researchers have no previous research experience in this field.

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<sup>6</sup> The KSCO is based on the ISCO88 (International Standard Classification of Occupations). Even though the National Statistical Office (NSO) was aware of the weakness of the KSCO, it could not fundamentally change the KSCO in the 1999 revision because of the statistical consistency problem with previous data.

<sup>7</sup> In order to enhance the study in occupations, the government had established, before the financial crisis, the Korean Research Institute for Vocational Education and Training (KRIVET). However: this institute focuses on research areas such as the development of vocational education textbooks, qualification standard, and the evaluation of vocational education/training.

As a result, the PES currently fails to provide suitable occupational information. Not only relatively small portion of job searchers and counselors use references on occupation but also many of them do not appreciate the usefulness and effectiveness of these references. The low utilization of references implies that information in these references may not be helpful and may have low practical use for job search and career decision.

#### Insufficient Expertise and Low Morale of Counselors

A large number of counselors surveyed are either inexperienced or do not have the required skills. Prior to their present work, only 18.2 % counselors had previous experience on employment and career counseling. So, in most cases, counselors had their first experience in employment and career counseling at the PES agencies. In addition, because counselors reside at their place of work for an average of 10.6 months, most counselors do not have neither sufficient experience nor expertise for in-depth counseling and other specialized services. Hence, counselors also felt the need for the enhancement of their knowledge and skills.' Although the Ministry of Labor (MOL) runs its own training center and in theory all counselors should receive various training sessions, most of the training courses tend also to be short term, with lectures and texts that are weak and in general unsatisfactory. The shortage of useful training and education program becomes one of the reasons adversely affecting counselor's morale and motivation.

In addition to the lack of experience and expertise on the counselors' part, the low morale of counselors is also one of main obstacles preventing the PES from providing effective and efficient services to needy people. More than 70 % of counselors express insecurity and dissatisfaction as regard 'job security' and 'wages'.

#### Lack of Strategic Approaches to the Function of the PES

It seems that only a few people understand the importance of the PES in the area of labor market and human resources development. Some managers of the public employment offices do not have any background knowledge or experience regarding the PES and thus have only a minimal understanding of the importance and significance of the PES in the labor market. Most managers who have been transferred from other departments or positions have relatively little expertise in placement and counseling. In many cases, managers of the public employment offices regard the PES as just another administrative duty such as industrial safety and implementation of labor standards law. Although this kind of attitude is somewhat understandable in

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<sup>8</sup> Almost half of the respondents or 45.8 % state that working times for 'training and education for capacity building' should be extended.

sense since there has been virtually no public employment service before the financial crisis in 1997, a extensive training program for managers is needed in order to improve the efficiency and effectiveness of the PES.

As the economy has bounced back and the unemployment rate is down to 4.7 % as of March 2000, the number of job searchers visiting the PES is visibly decreasing. At this stage, however, it seems that only few officials have concrete ideas on the future direction of the PES. Even if officials and managers have their own opinions and ideas about the function of the PES, these opinions and ideas are at most vague and are not strategic. Thus, as an initial step toward a better PES, a strategic approach and consensus among government officials and experts is required. This consensus will help the improvement of the PES, which in turn helps the labor market function more efficiently by insuring an improved equilibrium between labor demand and supply.

#### Inappropriate Employment Service of Local Governments

Job seekers visiting Si/Goon/Gu<sup>9</sup> Employment Information Center (EIC) have different characteristics as compared to general job seekers and those visiting Employment Security Center (ESC). Those that contact ESCs are relatively young and have higher education than job seekers contacting EICs, where most job searchers are of a higher age, with relatively more females, and lower educational levels. Compared to other types of public employment offices, relatively more persons visit EICs for the purpose of public works. Other individuals aside from those wanting to participate in the public works program are desperately looking for employment opportunities because, in many cases, they either are household heads or don't have means of livelihood. However, job seekers visiting EICs, despite actively looking for work, usually face difficulties in finding employment due to the lack of relevant skills and ability, age and sexual discrimination.

Even though job seekers using the EIC are mostly vulnerable people who need care and services, the EIC does not have the necessary tools to assist these people. Compared to the ESC, the size of the EIC is relatively small, thus making it less probable to benefit from economies of scale. Usually less than ten members of staff work at the EIC and therefore there is no explicit differentiation in tasks among the staff<sup>10</sup> and specialization is also hard to accomplish. Most civil servants working in the EIC were transferred from other departments or positions and have only a minimal expertise in

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<sup>9</sup> Si is the Korean name of city. And Gu is a local administrative unit below megalopolis (District). Goon is a rural jurisdiction (County) below Do.

<sup>10</sup> In general, the staffs of the EIC consist of few public servants and several public works participants. The size of the EIC varies depending on the region. In megalopolises, such as Seoul, Pusan, and Daegu, the EIC has relatively many member of staff compared to provinces.

placement and counseling. Also, participants of public works working in the EIC usually have no previous experiences in employment services. The morale of the staff is usually low. Many members of staff have not received any training after beginning work at the EICs. Even though some members of staff have taken training sessions, most of the training programs tend to be short-term and of low quality.

The EIC offer placement service and counseling and refer clients to training programs and public works. However, they do not handle Unemployment Insurance and do not pay out unemployment benefits. Thus, employers are reluctant to use the EIC since they cannot receive the 'Grant to Promote Employment of Displaced Workers' and other grants of the Employment Insurance System."

Also, in addition to the weak linkage between local public employment offices and the central government, there are no employment information networks at the local level. The acquisition of local labor market information across the many self-governing bodies is very difficult to accomplish. There is also an insufficient supply of necessary information on local labor market characteristics and job searchers' needs. Currently, the Labor Ministry's Work-Net is the only source of information at the local level.

### *Growing Importance and New Directions of the PES*

Survey results and various interviews with counselors, managers of the PES agencies, and experts on the PES raise many issues and challenges that must deal with in order to improve the quality of services and enhance the efficiency of the labor market. The role and function of the PES as a core delivery system for employment policies and development of human resources should be enlarged since economic growth and the well-being of people largely depend on knowledge and human capital. In the past, information on job openings was usually sufficient for job seekers. However, during the financial crisis characterized by high unemployment and economic depression, job seekers increasingly seek information not only on available job opportunities, but also on vocational training, career development, the labor market situation, and occupational prospects. This tendency will continue even after the financial crisis in line with the changing economic environment, namely, the accelerated progress in technology, continued globalization, and increased competition.

The most important function of the PES has been simple labor exchange, which is the finding of jobs for workers and workers for jobs. However, Internet and other networks have become universal and workers with the

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<sup>11</sup> To receive benefits and grants of the EI system, one must visit the ESC. This means that even though an unemployed worker is qualified for the 'Grant to Promote Employment of Displaced Workers', a firm is not eligible to receive this grant if it recruits the unemployed through the EIC.

capacity and skills can find suitable jobs without assistance from the PES. Since people can connect to employment information systems over the computer from anywhere, at anytime and anyplace, visits to the PES agencies should further decrease.

So, the main focus of the PES should shift to the development of human resources. A fully developed PES certainly helps the people, industry and communities adapt to a knowledge-based society. For this, the PES should provide workers, job searchers, the youth and other individuals with information they need to decide on a better-informed career decision. Also, the PES has to establish a system such that job seekers and vacancies may be matched promptly and efficiently, to and from anywhere in Korea. For this, a consensus on the future direction of the PES among labor market players is crucial. All partners and stakeholders, such as individual workers, business and labor organizations, local and central governments, and NGOs, should be involved in and make useful contributions for the improvement of the PES.

More specifically, the PES has to provide in-depth counseling for low-skilled and/or disadvantaged workers as well as dissemination of labor market information, career development, and active labor market programs. Until now, there were virtually no career guidance services for students who have to decide their study field and/or occupations, and for workers, especially middle-aged who want to change their career. To mobilize and to manage scarce human resources effectively in the knowledge-based society, PES agencies have to provide career guidance/counseling services to students and other people. Also, assistance of low-income people having work capacity will become an important role of the PES as the Korean government introduces the 'Productive Welfare' system. The PES agencies and counselors have to provide job placement services to low-income people having work capacity as well as vocational training, public works program, and career guidance service as a package

### **Strengthening of the Public Employment Service**

The future policy direction to be adopted by the public employment offices should aim not only at increasing the proportion of job seekers but also at meeting the demands of job seekers effectively. In order to do this there must be an increase in the number of public employment offices, fully staffed, with the necessary hardware and software that will improve the content and quality of information and service. Additionally, we need the following efforts.



## REVIEW OF THE EFFECTIVENESS OF PES

### *Active Development of Job Vacancy Information*

In general, differences between job seekers and job referrers arise from structural mismatch in the labor market. To minimize structural unemployment, public employment offices should be active in the expansion of job vacancy information. There is need to develop job vacancy information in Korea either by introducing specialists or by increasing the time spent in developing job vacancy information. Those working in the PES should not only put effort in the development of job information but should also help iron out the difficulties and problems of potential employers. Additionally, by finding out about working conditions and environments through visitation of establishments, the PES can increase the possibility of successful job matching.

### *Strengthening of Counseling Service*

Information should be provided after a close examination of his/her ability and the labor market situation. After which the future direction of a job searcher's career can be established efficiently through in-depth counseling. In many cases job searchers wish to have information on job opportunities and future direction but find that they face difficulties in obtaining either of these. Compared to elderly workers, there are relatively more youth and middle aged workers that request in-depth counseling. And often they request 'psychological test and counseling', as well as 'career guidance counseling'. This suggests that in the future there will be increased need to develop and improve career counseling programs and psychological and mental health counseling. Therefore public employment offices should focus on the needs of job seekers of lower ability and qualification when developing various services and counseling programs. Job seekers, especially Korean unemployed workers, tend to be rather passive. Thus, counselors should play an active leading role in sessions and should instill the importance of counseling through special activities and promotion.

### *Improvement of Counselor's Morale and Expertise*

To improve the quality of training programs for counselors, a joint development of training programs together with private institutions specialized in employment service should be made. And these training programs must be provided in the systematic and long-term basis. Beyond short-term and fact-providing training methods, various in-depth training and education courses should be made in the areas of the analysis of labor market situation and trends, economic and industrial environment, occupational classification, psychological in-depth counseling methods, and so on. To materialize the improvement of counselor's knowledge and expertise, participation of private institutions in the training of counselors

may be considered as one possibility.

The analysis of the survey in the Chapter II shows that there are various problems as regards counselor's morale. There is a low opinion as regards 'wages', 'job security' and 'prospective of career development', and so on. Also, despite increased specialty and more counseling experience of counselors in the mid- to long-term, low wages and uncertain job security certainly will act as counter reasons to morale and motivation. Thus, counselors with higher ability and experience tend to seek work elsewhere resulting in the drop in the quality of the public employment offices. To avoid this kind of possibility, systematic efforts should be made to improve wages and reduce uncertainty in job security. Additionally, active efforts should be made to guarantee the independence of duties.

### *Enhancement of Work-Net*

In Korea, the Central Employment Information Office (CEIO) developed the Work-Net based on the Canadian WorkInfoNet, The Work-Net, which is an integrated labor market information (LMI) system improves substantially the quality and contents of the Korean PES. However, Work-Net has various weak points compared to other country's LMI systems. For example, the production rate of information is rather slow and remains cumbersome to use. As such, there is still need for much improvement in the quality and quantity of information

The linkage between information on vocational training and information on job matching is insufficient. Therefore, job seekers and counselors find difficulty in acquiring vocational training information for the occupations at which job seekers want to work. In particular, even where a job seeker wants to participate in vocational training programs, the counselor has difficulty in introducing a suitable training program given the job seeker's ability, skills, and experience. Additionally, there is only partial information about the future prospects of occupations. Moreover information about the local labor market is very limited and hardly usable. Compared to the US and Canada, registration forms are relatively simple and so it is difficult to know about the suitability of a certain job and/or certain candidate. The survey of Chapter II shows that both job searchers and counselors agree that there are deficiencies in the coordination of information and in the prompt replacement of old information with new information.

In order to improve the quality and contents of the Work-Net and to improve user friendliness, information in the Work-Net should be increased together with expansion of its computer capacity, and these should be accompanied with improvements in the method of utilization making the Work-Net more efficient. Moreover, detailed information is required on wages, labor market trend, and employment outlook for each occupational group. The friendliness of the Work-Net should be elevated to that of advanced countries. In particular, easiness and convenience should be

enhanced by the application of Search Machine and structural readjustments of Work-Net. Further users of the Work-Net can be consulted to find about any weakness in the system.

### *Utilization and Expansion of Labor Market Information*

The PES should contact in advance firms with high probability of recruiting and the information on the number of job vacancies, the recruiting method, working conditions and so on, should be added into the employer database. The database should contain information not only on the location, size of firm, type of products, and other basic information but also on firm's credibility, personnel management systems, pattern of employment, job separation rate, working environment, recruiting methods, potential of future growth, and so on. This employer database should initially use the EI data to analyze firms' characteristics and select those firms that have recruiting demand.

To provide occupational information to job seekers and other customers, systematically designed systems like that of Japan's 'Ability Garden' could be constructed. Collection of occupational information from experts and institutions could be organized into an on-line library format easily accessible to workers, firms and other institutions. Furthermore, this kind of Data Bank should be inter-linked with Work Net.

In general, the counseling breadth depends on the worker's academic status. In Korea, there is a high possibility of structural unemployment, and corrective measures are needed to remedy and prevent such problems. Information on wages, future employing industries, job satisfaction and so on, from graduate students on the various occupations they will be engaged in should be collected and utilized to provide proper guidance. Direct survey of individuals graduated college or university, after 2 years and again after 5 years, in the form of a Graduate Follow-up Survey could be carried out and the results may be used in career guidance and counseling.

### *Strengthening of Services to Vulnerable Groups*

Analysis of job seekers shows that the public employment offices provide only minimal services to unemployed people who are of a higher age and have low level of education and skills. As a result, only a small portion of the low-skilled and/or vulnerable workers such as elderly and female household heads actually use the PES. As the quality of the public employment service that currently has minimal competitiveness improves, the ratio of these low-skilled and/or disadvantaged workers using public employment offices should gradually increase.

However, the government needs to invest more resources for the development of specialized employment programs and of job vacancy information for these workers. In particular, the development of specialized

counseling and employment programs should be established directed at dealing with the problems of middle-aged workers, who have various difficulties in re-employment and in many cases want to change their career path. In addition, what is needed is not only the establishment of a Worker Profiling System to provide for the early identification and referral services to harder-to-employ job searchers, but also the construction of "Job Clubs" where the unemployed workers may exchange information and share psychological difficulties with each other. Also, the "Employment Center for Daily Workers" may extend the scope of its service to female household heads and others looking for temporary or part-time jobs.

### *Improvement of Career Guidance in School*

Various activities, such as occupational fairs, will certainly help in establishing common cognition on the importance of career guidance and education. In particular, fairs like the "World of Occupations 2000" organized by the CEIO do function as excellent places for career guidance and education. Annual activities and programs, such as the Manpower Banks' summer vacation "Searching for Future Jobs Class", should be conducted to instill proper cognition and perspective in students. Also, references on occupation could be transformed and stored in various media such as Video, CDs, and so on, so as to be easily accessible to students.

### *Improvement of Local Government's Employment Services*

Despite of various difficulties faced by the Si/Goon/Gu Employment Information Centers, there are several advantages related to EICs over the ESCs. Usually located within Si/Goon/Gu administrative buildings, job seekers and the general public have easy access to EICs. In particular, in small towns and rural areas, where the influence of local governments over their residents is strong, the EIC is usually more active than the ESC. It is also relatively easier for Si/Goon/Gu to collect information on local labor market and job opportunities. In addition, the administration potential of Eup/Myun/Dong offices can be exploited in gathering information and providing services.

Since job seekers visiting local EICs and job seekers visiting ESCs are different in characteristics, mutual collaboration is important in carrying out the duties in the various public employment offices. Especially, considering that the PES-induced placements are only around 10 %, the functions of public employment offices regardless of types should be expanded. At the current stage of Korean PES, the services at EICs focusing on job seekers that are relatively older, having low level of education and lower incomes should complement services provided at ESCs. Job searchers that use ESCs are in general of younger age and have attained higher education, and usually seek work in the professional and/or clerical field. In contrast, those

visiting EICs are of relatively higher age, lower education level and consist of middle-aged females. Thus, the services provided by EICS should focus on the lower income, higher age, unemployed females which should be supported by temporary livelihood measures, while the services provided by ESCs should be directed at the youth and those of higher education levels, emphasizing guidance counseling and vocational training.

The establishment of labor market information systems like Work-Net involves considerable costs and time. And the trend in the Labor Market Information System (LMIS) is towards the construction of a nation-wide integrated system. Thus, rather than developing their own information system, it is better for the local government to participate actively in the LMIS of the Ministry of Labor. Especially, as relates to the Work-Net, the information of local labor markets can be integrated.

#### *Enhancement of Collaboration with Private Sectors*

It seems that there is currently little collaboration between the PES and the private sector. Considering the fact that many colleges and universities, non-profit employment agencies, and other related organizations have various difficulties with respect to the quality and contents of services, a coordinated effort to improve the private employment services is needed. As for the universities' placement service, despite the need for suitable programs for graduates, it is observed that those belonging to high reputation universities tend to favor a more independent information system over a common electronic network because they regard universities with lower reputation as free riders. On the other hand, the preference of those in universities of lower reputation as to whether they favor a common or independent employment network system is varied and different across individual universities. Also, career guidance and education at high schools is urgently required, but at present a practical method is yet forthcoming. To assist these private organizations and schools, the government should assign an ID to selected private agencies allowing them to participate in the Work-Net. An open door policy for non-profit private organizations and schools to participate in the labor information system as partners should be established.

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# 12 Evaluating the Training for the Unemployed in Korea

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## Introduction

In Korea, after the financial crisis, training for the unemployed was expanded by eight times as before, in response to soaring unemployment. Nevertheless it received various criticism, especially on appropriateness of its target group and the performance<sup>1</sup>.

Training for the unemployed as an active labor market policy has its primary purpose in promoting re-employment of the unemployed into the stable job market by improving their skills and qualifications. In this light, impact evaluation of training for the unemployed on the labor market is very important. In order to ensure the substantiality and improve its quality, training for the unemployed needs to undergo some restructuring based on an evaluation of existing policies and their efficiency.

This research has its significance in that it conducts a comparative evaluation between those who participate in training programs and those who do not, and therefore, it allows a more thorough evaluation on the effect of the training for the unemployed<sup>2</sup>. Previous result analyses based on Achievement Management Index, which uses administrative statistics, and re-employment training for the unemployed data base lacked accuracy due to limitations of target group research and lack of comparability with those who did not participate in training programs for the unemployed. This research, therefore, tries to thoroughly evaluate the impact of training for the

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Korea Labor Institute.

<sup>1</sup> For an in-depth discussion on the issue, see Kang (1999).

<sup>2</sup> Participants' questionnaire survey, the "before and after" approach, comparison group evaluation, econometric techniques, and the experimental approach have been used as evaluation methods. In the reliability, cost, and so on, each methodology has weak and strong points. In details, see Hasan, Abrar (1991), Grubb, W. Norton and Paul Ryan (1999).

unemployed by obtaining representative data of participants and non-participants in training programs and conducting a follow-up survey on an individual basis.

In this research, systematic questions on relationship between vocational training and employment, individuals' employment history (before training and/or before being unemployed), employment opportunities (after training) are asked to determine how participation in vocational training affects individuals' economically active status and how the terms and conditions of employment differ for the re-employed from before.

A survey was conducted on those who participated in training for the unemployed in 1998. Economic impact of vocational training gradually takes place over time, and therefore, it is desirable to conduct an evaluation over some length of time as well. However, this research had to be limited to analyze the training program participants' status change within the labor market from 1998 until September 1999.

**Table 12.1: Training for the unemployed in Korea, 1998 and 1999**

	1998		1999	
	(persons)	(%)	(persons)	(%)
<i>Re-employment training</i>				
<i>Sub-total</i>	301	90.9	280	84.6
<i>Re-employment training for the unemployed</i>	170	51.4	200	60.4
<i>Employment promotion training</i>	106	32.0	55	16.6
<i>Training for the high school graduates and newly unemployed</i>	11	3.3	7	2.1
<i>Training for overjunior college graduates in the promising jobs</i>			10	3.0
<i>Training for starting a business</i>	14	4.2	8	2.4
<i>Manpower development training</i>				
<i>Sub-total</i>	30	9.1	51	15.4
<i>Training for skilled workers</i>	15	4.5	15	4.5
<i>Training in the priority jobs</i>	11	3.3	16	4.8
<i>Paid leave training</i>	4	1.2	20	6.0
<i>Total</i>	331	100.0	331	100.0

Note: See Kang, Soon-Hie, Jaeho Keum and Dong-Heon Kim (1999) about training category in details.  
Source: the Ministry of Labor, Korea.

## Evaluation Methodology: Quasi-experimental Method

### *Participants of re-employment training for the unemployed*

Target samples of this research are selected from the participants of re-employment training for the unemployed, who are registered in the

unemployment database of the 1998 re-employment training.

Anyone who had worked at employment insurance applicable establishments is eligible for re-employment training for the unemployed. Therefore, job separation point of the '98 re-employment training for the unemployed participants varies from late 1995 to late 1998'. This research excludes those training participants whose job separation date is prior to July 1997 to investigate the effect of re-employment training for the unemployed in the midst of mass unemployment and also to make it easier to distinguish between participants and non-participants in re-employment training for the unemployed.

Finally, participants of re-employment training for the unemployed are defined as those who participated in 1998 re-employment training for the unemployed (including those who dropped out) and whose job separation date is between late 1997 and the end of 1998. Out of this group of participants 1,000 samples were selected according to their job separation date and a follow-up survey was conducted. Because unidentified addresses, moving, and refusal to participate in survey may act as uncertainties, a sample group of the multiples of eight was randomly selected.

#### *Non-participants of re-employment training for the unemployed: comparison group*

In order to identify a matched pairs comparison group who shares the similar characteristics as participants of re-employment training for the unemployed, we selected non-participants of re-employment training for the unemployed, who are not displaying job-to-job movement, out of the unemployed group whose job separation date fell between July 1997 and December 1998.

As matching criteria, such personal characteristics as sex, age, education, and location must be considered. However, sampling using these variables may add to complication and may ignore the existing visible personal characteristics differences between participants and non-participants of training. Therefore, this research, instead of accepting such personal differences on sampling, uses a quantitative model that controls the personal characteristic differences in order to estimate the economic impact of re-employment training for the unemployed accurately. Meanwhile, this research considers the so-called 'duration dependence effect' that the longer the period of unemployment is, the lower the possibility of re-employment is. In this perspective, this research selected those who became unemployed around the same time and who remained unemployed while the training participants were being trained as matched paired comparison group. In other words, research targets, out of those who became unemployed around

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<sup>3</sup> In Korea, the Employment Insurance System was introduced in 1995. It has three major components: the employment stabilization scheme, the vocational competency development scheme, and Unemployment benefits. For more details on the EIS, see Yoo(1999).



the same time and remained unemployed, are distinguished only by participation in re-employment training for the unemployed.

In order to form the matched pairs comparison group this research attempts to conduct a follow-up survey on 1,000 subjects who are derived by calculating the ratio of "training participants' job separation month x training beginning month" from the July 1997-December 1998 Data Base and corresponding the ratio with the ratio of the non-employed group with the same calculation.

When the participant and the non-participant group of the re-employment training for the unemployed were compared, participation rate appeared higher for the women, under the age of 30, and an education level of junior college degree or higher. Therefore, in order to derive an accurate estimate on economic impact of re-employment training for the unemployed, such personal characteristics must be controlled.

**Table 12.2: Comparison of personal characteristics of re-employment training for the unemployed participants and non-participants**

	Participants		Non-participants		Statistics
	(persons)	(%)	(persons)	(%)	
Sex					
<i>Male</i>	477	47.6	503	50.3	$\chi^2=1.507$ P=0.220
<i>Female</i>	526	52.4	497	49.7	
Age					
<i>Under 30</i>	395	39.4	276	27.6	$\chi^2=122.418$ P=0.001
<i>30-39</i>	330	32.9	228	22.8	
<i>40-49</i>	170	16.9	214	21.4	
<i>Over 50</i>	108	10.8	282	28.2	
Education					
<i>Under middle school</i>	81	8.1	329	33.2	$\chi^2=202.510$ P=0.001
<i>High school diploma</i>	501	50.0	416	41.9	
<i>College graduate</i>	158	15.8	98	9.9	
<i>University degree and up</i>	261	26.1	149	15.0	
Marital Status					
<i>Married</i>	642	64.2	750	75.2	$\chi^2=28.542$ P=0.001
<i>Single</i>	358	35.8	248	24.8	
Position within Family					
<i>Head of Family</i>	404	40.8	486	49.3	$\chi^2=48.593$ P=0.001
<i>Spouse</i>	294	29.7	324	32.9	
<i>Children</i>	280	28.3	156	15.8	
<i>Parents</i>	7	0.7	17	1.7	
<i>Others</i>	4	0.4	3	0.3	
Total	1003	100.0	1000	100.0	

## Performance of Training

### *Comparative Evaluation for Re-employment Training for the Unemployed*

#### Re-employment Rate

On a survey, the following question was asked: "Since participating training (or after leaving your previous job for non-participants) and until present, that is Sept. 1999, have you been re-employed for longer than one week?" Along with this question, their current economically active status was examined. In accordance with these findings, subjects of the survey are divided into the following four groups based on their re-employment experience and current employment status.

- 1) Those who stayed with their first re-employment after training until now
- 2) Those who were re-employed, but then moved to another job
- 3) Those who have been re-employed after training but currently unemployed
- 4) Those who have never been re-employed and currently non-employed

Test of homogeneity ( $\chi^2$  test) of re-employment experience and current employment status depending on participation or non-participation do not show significant difference between participants and non-participants. 49.6% of participants have been re-employed and 37.6 of participants are currently employed. On the other hand, 52.6% of non-participants have been re-employed, which is not significantly different from that of the participants, and 40.3% of non-participants are currently employed.

**Table 12.3: Re-employment experience and current employment status of subjects depending on re-employment training for the unemployed participation**

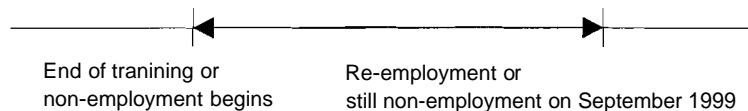
	Participants		Non-participants		Statistics
	(persons)	(%)	(persons)	(%)	
Not been re-employed and currently non-employed	493	50.4	474	47.4	
Re-employed and stayed there until present	300	30.7	308	30.8	$\chi^2=4.857$ P=0.183
Re-employed and then moved to another job	68	7.0	95	9.5	
Re-employed but left the job, not employed until present	117	12.0	123	12.3	
Total	978	100.0	1000	100.0	$\chi^2=1.792$
Re-employment experience	485	49.6	526	52.6	P=0.181
Currently employed	368	37.6	403	40.3	$\chi^2=1.484$ P=0.223

### Performance after Active Job Search

Assessment result of successful re-employment may differ depending on at what point they actively begin to seek jobs within the labor market. Generally, while they are on training they do not actively search for jobs, generating lock-in effect. Therefore, assessing re-employment performance at some fixed point may underestimate the positive impact of training on re-employment possibility in the long run. Let us now take a look at the progress in economically active participation and re-employment performance of the subjects after they begin to actively seek jobs.

The point at which non-participants actively begin to seek jobs is the month from which they became unemployed; for training participants, it is set at the month at which the training ended. Also, spell length of non-employment duration is defined as a period after leaving a job or training ended to the point when they first become re-employed.

#### **Completed (incomplete) spell length of non-employment duration**



Since the end of training for training participants falls after 1998, as comparison group, we limited non-participants in re-employment training for the unemployed to those whose non-employment began after 1998 as well. Therefore, spell length of non-employment duration in this research is categorized as completed spell length of non-employment duration, which ended with the subjects' re-employment or incomplete spell length of non-employment duration, in which the subjects still remain non-employed as of present, September 1999.

Let us take a look at the trend of spell length of non-employment duration for those whose training ended after 1998 or whose unemployment began after 1998 before re-employment depending on their participation in re-employment training for the unemployed.

30.8% of re-employment training for the unemployed participants are observed to take a spell length of non-employment duration of less than three months whereas 51.1% of the same group experience a spell length of non-employment duration of longer than seven months. On the other hand, only 10% of those who lost jobs from employment insurance applicable companies and did not participate in training experience a spell length of non-employment duration of less than three months. Notably, those who experience a spell length of non-employment duration of longer than seven months account for 81.2% of the same group. On the average, spell length of non-employment duration for training participants is 6.7 months whereas the

**Table 12.4: End point of training and beginning of non-employment depending on re-employment training for the unemployed participation**

	End point of training (participants)		Beginning of non-employment (non- participants)	
	(persons)	(%)	(persons)	(%)
Jan. 1998	1	0.1	153	19.2
Feb. 1998	1	0.1	131	16.4
Mar. 1998	9	0.9	155	19.4
Apr. 1998	18	1.8	113	14.2
May 1998	30	3.0	69	8.7
June 1998	42	4.2	46	5.8
July 1998	63	6.3	50	6.3
Aug. 1998	95	9.5	29	3.6
Sep. 1998	92	9.2	20	2.5
Oct. 1998	92	9.2	20	2.5
Nov. 1998	125	12.5	3	0.4
Dec. 1998	62	6.2	8	1.0
Jan. 1999	71	7.1		
Feb. 1999	66	6.6		
Mar. 1999	34	3.4		
Apr. 1999	29	2.9		
May 1999	27	2.7		
June 1999	25	2.5		
July 1999	48	4.8		
Aug. 1999	36	3.6		
Sep. 1999	16	1.6		
Oct. 1999	16	1.6		
Total	998	100.0	797	100.0

same of non-participants is 13.1 months which is different at 1% significant level.

Let us take a look at the completed spell length of non-employment duration, which successfully ended with re-employment, of the subjects based on their participation/non-participation in re-employment training for the unemployed. About one third of re-employed subjects who participated in re-employment training for the unemployed spent on average less than a month before being re-employed, and 54.3% were re-employed within the first three months after training ended. Only 23.4% of the same group spent more than seven months before re-employment. On the other hand, only 21.3% of non-participants of re-employment training for the unemployed, who have been re-employed, spent less than three months before being re-employed, and 59.9% spent more than seven months.

**Table 12.5: Employment trend depending on re-employment training for the unemployed participation by spell length of non-employment duration**

Spell length of non-employment duration	Partidpants						Non-participants					
	Non-employment		Re-employment experience		Total		Non-employment		Re-employment experience		Total	
	(persons)	(%)	(persons)	(%)	(persons)	(%)	(persons)	(%)	(persons)	(%)	(persons)	(%)
1 month	27	5.7	116	32.3	143	17.2	0	0.0	31	8.9	31	4.2
2 months	18	3.8	41	11.4	59	7.1	0	0.0	23	6.6	23	3.1
3 months	16	3.4	38	10.6	54	6.5	0	0.0	20	5.8	20	2.7
4 months	15	3.2	29	8.1	44	5.3	0	0.0	12	3.5	12	1.6
5 months	24	5.1	28	7.8	52	6.3	0	0.0	23	6.6	23	3.1
6 months	32	6.8	23	6.4	55	6.6	0	0.0	30	8.6	30	4.1
7 months	38	8.0	19	5.3	57	6.9	0	0.0	23	6.6	23	3.1
8 months	31	6.6	9	2.5	40	4.8	0	0.0	20	5.8	20	2.7
9 months	64	13.5	17	4.7	81	9.7	5	1.3	20	5.8	25	3.4
10 months	43	9.1	10	2.8	53	6.4	2	0.5	19	5.5	21	2.8
11 months	46	9.7	9	2.5	55	6.6	10	2.5	16	4.6	26	3.5
12 months	48	10.1	8	2.2	56	6.7	10	2.5	26	7.5	36	4.9
13 months	31	6.6	5	1.4	36	4.3	18	4.6	15	4.3	33	4.5
14 months	21	4.4	3	0.8	24	2.9	29	7.4	16	4.6	45	6.1
15 months	10	2.1	3	0.8	13	1.6	20	5.1	8	2.3	28	3.8
16 months	4	0.8	1	0.3	5	0.6	32	8.1	14	4.0	46	6.2
17 months	2	0.4	0	0.0	2	0.2	51	13.0	7	2.0	58	7.8
Over 18 months	3	0.6	0	0.0	3	0.4	216	55.0	24	6.9	240	32.4
Total	473	100.0	359	100.0	832	100.0	393	100.0	347	100.0	740	100.0

We showed in the previous section that re-employment experience rate was slightly higher for non-participant group, although not by much, but looking at the same situation by the point from which they actively begin to seek jobs, we can see that training participants tend to be more successful in finding jobs

#### Re-employment Performance by Cohort

In order to assess the effectiveness of re-employment training for the unemployed in finding jobs, it is useful to compare and analyze the participant and non-participant group by cohort. If we define the cohort by at which point they begin their active job search within the labor market, we can eliminate the problems arising from their not seeking jobs while on training. However, this will also overestimate the effectiveness of training by looking over the spell length of non-employment duration before training. The problem of overestimation may especially be more serious in this

research because we selected a matched pairs comparison group which consists of those whose non-employment began around the same time and who remained non-employed before training began.

Therefore, we will define the cohort by the subjects' spell length of non-employment duration. That is to say, for non-participants, we will define the cohort by the subjects' completed spell length of non-employment duration, from the beginning of their non-employment until the first re-employment, or by the subjects' incomplete spell length of non-employment duration which has not yet ended by re-employment as of present, September 1999. As for training participants, we defined the cohort by the completed (incomplete) spell length of non-employment duration, as defined above, minus the training period.

#### **Completed (incomplete) spell length of non-employment duration**

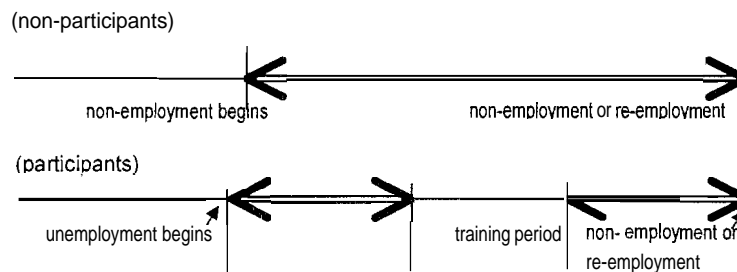


Table 12.6 shows the monthly economical activity change of the subjects since job loss or training in 1998. Since re-employment training for the unemployed participants spend an average of 4.8 months on participating training, their economically active status one month after training ends corresponds with that of the non-participant group six months after their job loss.

For those whose training ended or whose non-employment began in January 1998, we could trace a maximum of 20 months of their economical activities since then until Sept. 1999; however, for convenience purposes we will only describe their economically active status up to the first ten months. It must however be noted that their training end point or non-employment beginning point vary, and therefore the actual months do not necessarily correspond with each other and thus requires more caution in interpreting their economically active status.

Looking at the economically active status of cohorts by corresponding spell length of non-employment duration, employment rate of training participant group appears consistently higher than that of the non-participant group. Employment rate of participants at one month after training ended was 26.8%, which was higher than 24.4% of non-participant group at

**Table 12.6: Trend of economically active status depending on re-employment training for the unemployed participation**

	After 1 mo.	After 2 mo.	After 3 mo.	After 4 mo.	After 5 mo.	After 6 mo.	After 7 mo.	After 8 mo.	After 9 mo.	After 10 mo.
<i>Participants</i>										
<i>Employed</i>	178	202	226	237	248	263	247	229	219	177
<i>Unemployed</i>	486	441	401	363	325	293	256	227	183	133
<i>Non econ. Activity</i>	266	239	230	230	228	211	198	174	166	133
<i>Total</i>	930	882	857	830	801	767	701	630	568	443
<i>Employmentrate</i>	26.8	31.4	36.0	39.5	43.3	47.3	49.1	50.2	54.5	57.1
<i>Participationrate</i>	71.4	72.9	73.2	72.3	71.5	72.5	71.8	72.4	70.8	70.0
<i>Non-participants</i>										
<i>Employed</i>	52	69	84	94	115	132	143	152	166	182
<i>Unemployed</i>	499	485	471	456	434	410	391	377	353	328
<i>Non econ. Activity</i>	246	243	242	247	248	254	262	268	278	278
<i>Total</i>	797	797	797	797	797	796	796	797	797	788
<i>Employmentrate</i>	9.4	12.5	15.1	17.1	20.9	24.4	26.8	28.7	32.0	35.7
<i>Participation rate</i>	69.1	69.5	69.6	69.0	68.9	68.1	67.1	66.4	65.1	64.7

six months after their job loss. This gap was expanded and by the fifth months after training ended, participants' employment rate was 43.3% whereas that of the non-participant group was only 35.7% at ten months after their job loss began.

As previously described, the fact that non-participant group's re-employment experience rate or current employment rate is higher than those of the participant group has its root in their longer period of job search. That is to say, under the same job search period, participant's re-employment experience rate or current employment rate is higher than those of non-participants.

Also, economically active participation rate of the re-employment training for the unemployed participants is also consistently higher than that of the non-participant group. In other words, training promotes re-employment as well as prevents withdrawal of participants from the labor market, increasing opportunities for active participation in economical activities.

#### Period between Beginning of Non-employment/End of Training and Re-employment

Let us take a look at the period from job loss or end of training in 1998 to re-employment of those who were successful in finding jobs. Participants in re-employment training for the unemployed spend on the average about 4.3 months before re-employment. Non-participants on the other hand spend on average 8.6 months before finding jobs. These findings show that training participants find jobs twice as fast. Also, 49.6% of training participants have experienced re-employment, 32.3% who are re-employed found jobs within the first month out of training and more than half of the participants were re-

employed within the first three months. On the other hand, 52.6% of non-participants have experienced re-employment. the most number of people are finding jobs after between six months and a year. More than half of this group is found to be re-employed six months after job loss.

**Table 12.7: Length of period from job loss or end of training to reemployment depending of reemployment training for the unemployed participation**

	Participants		Non-participants		Statistics
	(persons)	(%)	(persons)	(%)	
1 month	116	32.3	31	8.9	
1 - 3 months	79	22.0	43	12.4	
3-6 months	80	22.3	65	18.7	$\chi^2=128.954$
6 months-1 year	72	20.1	124	35.7	$P=0.001$
Over 1 year	12	3.3	84	24.2	
Total	359	100.0	347	100.0	
Average length before re-employment	4.3		8.6		$t=12.8632$ $P=0.0001$

#### Employment Status upon Re-employment

The quality of new jobs is as important as re-employment itself. Let us now look at the employment status upon re-employment. Employment status differed between participants and non-participants in re-employment training for the unemployed, higher percentage of participants held regular status compared to non-participants whereas more number of non-participants held part-time positions, self-employed, and unpaid family worker. Among the

**Table 12.8: Employment status upon re-employment depending on re-employment training for the unemployed participation**

	Participants		Non-participants		Statistics
	(persons)	(%)	(persons)	(%)	
Wage worker					
<i>Regular</i>	218	52.5	210	46.7	
<i>Temporary</i>	94	22.7	92	20.4	
<i>Daily</i>	43	10.4	61	13.6	
Employer	17	4.1	15	3.3	$\chi^2=10.146$ $p=0.0$
Self-employed	36	8.7	55	12.2	
Unpaid family worker	7	1.7	17	3.8	
Total	415	100.0	450	100.0	
Wage worker (%)	85.5		80.7		$t=-1.9181$ $p=0.0554$
Regular (%)	61.4		57.9		$t=-0.9705$ $p=0.3321$



re-employed. higher percentage of re-employment training participants are wage workers than non-participants are.

#### Firm Size upon Re-employment

Companies to which the subjects are re-employed is significantly smaller in size when compared to their previous work places, showing that the quality of employment might be deteriorated.

However, firm size does not differ by much depending on re-employment training for the unemployed participation

**Table 12.9: Firm size upon re-employment**

	participants		Non-participants		Statistics
	(persons)	(%)	(persons)	(%)	
1 – 9	99	28.8	91	26.7	$\chi^2=1.116$ $p=0.953$
10 – 29	73	21.2	79	23.2	
30 – 99	81	23.5	87	25.5	
100 – 299	40	11.6	38	11.1	
300 – 499	13	3.8	11	3.2	
500 –	38	11.0	35	10.3	
Total	344	100.0	341	100.0	

#### *Dynamic Employment Effect of Training*

##### Need for an Analysis of Dynamic Employment Effect of Training

The analysis of employment effect of training defined by cohort by spell length of non-employment duration does not consider personal or previous employers' characteristics, which may have profound impact on the effect. As already identified, training participants tend to be younger and have higher education level than the non-participants, which may act to distort the employment effect of training and thus such influential characteristics need to be controlled.

Also, as time goes on, chances of re-employment may decrease. As previously described, the longer the unemployment period is, the smaller the chances of being re-employed is; the analysis however shows that training leads to fast re-employment. Therefore, evaluating the employment effect of training at a fixed point of time rules out the time factor that certainly plays a major role in determining the accurate effect of training. To prevent this, the time spent between beginning of non-employment/end of training and re-employment needs to be considered for a more comprehensive analysis of the employment effect of training.

The analysis of employment effect of training defined by cohort by spell

length of non-employment duration has its limitation in that it also includes the incomplete spell length of non-employment duration. At the time of the survey, spell length of non-employment duration of non-employed is an incomplete spell, so an analysis based on the least square method using such data without controlling the right censoring loses statistical consistency. Therefore, we analyzed the employment effect of training, which determines the length of period from non-employment or end of training to re-employment, based on the hazard model that considers the censoring factor.

### Method of Analysis

Based on the hazard model, which is widely used to analyze a movement of the subjects from state to state, we defined a movement from non-employment to re-employment as hazard. From this point on, we will look into the factors that affect the trend of hazard change or the size of hazard.

In order to analyze the quantitative effect of training on re-employment hazard, a Cox model which is equivalent to semi-parametric estimation by employing a proportional hazard model is used. In a proportional hazard model, the hazard at period of the observation with an independent variable  $x$  is expressed as follows:

$$h(t) = h_0(t) \exp(X'\beta)$$

Here  $h_0(t)$  represents a baseling hazard at  $t$ . Therefore, in a proportional hazard model, hazard change at every period is determined by the baseling hazard, and it is supposed that the independent variable ( $x$ ) plays a role of scaling up or down the baseling hazard depending on its size and/or the value of  $\beta$ . A Cox model has the advantage in that, without knowing the shape of baseling hazard, it is able to derive the impact of each independent variable on hazard. Also, using the relative risk which is defined as the ratio of real hazard against baseling hazard,  $h(t)/h_0(t)$ , we are able to estimate the impact of independent variables.

Natural logarithm of relative risk is expressed as

$$X'\beta = \beta_1 x_1 + \dots + \beta_k x_k$$

Changes in relative risk from  $i$  change with all variables, other than independent variable  $i$ , fixed, is expressed as

$$\frac{\beta_1 x_1 + \dots + \beta_1 (x_{i+1}) + \dots + \beta_k x_k}{\beta_1 x_1 + \dots + \beta_1 (x_i) + \dots + \beta_k x_k} = e^{\beta_i}$$

Therefore, relative risk of  $AX$ , a change in  $x_i$  is also expressed as  $e^{\beta_i \Delta x_i}$ . Using the value of  $\beta$  and relative risk, we are able to estimate the size of independent variables' impact on hazard. If relative risk is bigger than 1,

then transition probability increases; if relative risk is smaller than 1, then transition probability decreases.

### Variables

Because it is expected that independent variables and training participation's impact on re-employment hazard would certainly differ by sex, we estimated a coefficient for each case of male, female, and overall.

As for personal characteristics, age seems only significant for women; especially at the age of 41, their re-employment possibility is the highest. In contrast, education level does not seem to influence re-employment possibility at all. By sex, men have 73% more chances of being re-employed than women. Marital status does not affect men; however for women, married women have just 33% chance of being re-employed of single women. Eliminating the marriage factor, position within a family as head of household works in favor of men, although not very significantly; however, it works as a disadvantage for women significantly.

**Table 12.10: Variables in reemployment hazard**

Variable factors	Variables	Mean	Standard deviation
Spell length of non-employment (dependent variable: month)	BAYM3	12.04	6.00
Age	AGE	37.51	11.10
Sex	MALE	0.49	0.50
Marital status	MARRIED	0.70	0.46
Education	SCH	12.08	3.28
Head of family	HEAD	0.45	0.50
Employment length in previous job	BTEN	90.50	90.24
Previous job in manufacturing	MANU	0.51	0.50
Previous job in production	PROD	0.38	0.49
Firm with 300 or more	SIZE	0.44	0.50
Previous employment status	REGULAR	0.96	0.20
Involuntary separation	SEPARATE	0.77	0.42
Regional unemployment rate	REGURATE	0.93	1.76
Training participation	TRAIN	0.50	0.50

As for the nature of previous employment, tenure very slightly decreases the chance of re-employment; although not as significant, this implies that tenure factor may work as an obstacle to re-employment. Manufacturing employment experience does not have any influence at all whereas males who were employed in production jobs have 27% higher chance of being re-employed than in other jobs. Also, the large size of previous firm acts as a disadvantage against the re-employment for men. Employment status and voluntariness of separation factors do not seem to affect the re-employment

possibility.

Training participation factor, the main interest of this research, seems to increase re-employment possibility by 28%; this estimation differs by sex. For men, training participation does not seem to exert a significant influence on increasing re-employment possibility; however, for women, training participation increases re-employment possibility by 63% compared to non-participants under same conditions.

**Table 12.11: Estimation of re-employment hazard**

	All		Male		Female	
	Coefficient		Coefficient		Coefficient	
AGE	0.019	1.019	-0.023	0.977	0.100 **	1.106
AGESQ	-0.000	0.999	-0.000	1.000	-0.001 **	0.999
MALE	0.546 ***	1.727	-	-	-	-
MARRIED	-0.499 ***	0.607	-0.014	0.986	-1.113 ***	0.328
SCH	-0.004 ***	0.996	0.009	1.010	-0.004	0.995
HEAD	0.347 ***	1.416	0.295	1.344	-0.434 ***	0.648
BTEN	-0.001 ***	0.998	-0.000	1.000	-0.005 **	0.995
MANU	0.003	1.003	0.007	1.008	-0.159	0.852
PROD	0.181 *	1.199	0.235 **	1.265	0.204	1.227
SIZE	-0.199 **	0.820	-0.315 ***	0.729	-0.035	0.965
REGULAR	0.135	1.145	0.190	1.210	0.044	1.046
SEPARATE	0.068	1.071	0.196	1.217	-0.051	0.950
REGULATE	-0.053 ***	0.948	-0.043	0.957	-0.67 **	0.934
TRAIN	0.249 ***	1.283	0.056	1.058	0.490 ***	1.633
-2 LOG L	7021.331		3882.054		2956.384	
Chi-square	273.832 ***		121.347 ***		146.539 ***	
N	1814		893		921	

Note: \*\*\*, \*\* and \* stand for the significance levels of 0.01, 0.05 and 0.10, respectively

## Analysis of Labor Market Characteristics for those who are not re-employed

### *Economically Active Status of Those Who Are Not Re-employed*

In order to find out if those who are not re-employed are actively seeking jobs, or if they are willing to work but are not seeking because there does not seem to be any jobs, or if they have retreated from the labor market completely, we categorized their economically active status into greater details. In accordance with [Economically Active Population Survey], unemployed persons are defined as "those who do not have any paid work

during the survey period, although are able to begin work immediately, and who are seeking jobs actively". We categorized economically inactive population as four groups by the subjects' length of job seeking activity, willingness to work, reasons for not seeking job, and job seeking activity during the past year. First group is categorized under "OECD standard unemployed" who have actively sought for jobs in the past four weeks; second group is so called "discouraged unemployed" who are willing to work, have sought jobs in the past year, but are not seeking jobs because there seems to be no jobs, that is discouraged by factors of the labor market; third group is categorized under "economically inactive population but willing to work" who are willing to work but have not sought jobs for household maintenance, raising children, education, and health reasons; fourth group is categorized under "purely economically inactive group" who have completely withdrawn from the labor market.

*Current Economically Active Status of Re-employment Training for the Unemployed Participants Who Are Not Re-employed*

Current economically active status showed difference between the re-employment training for the unemployed participants and non-participants at 10% significant level. 41.4% of those who are not re-employed after participating in re-employment training for the unemployed have actively sought for jobs in the past month; but 34.7% of non-participant group have actively sought for jobs during the same period. If we include those who are willing to work but are not seeking jobs because there does not seem to be enough jobs, so called the discourage unemployed, then 51.5% of training participants are found to be willing to work, which is higher than 42.6% of

**Table 12.12: Current economically active status of re-employment training for the unemployed participants and non-participants**

	Participants		Non-participants		Statistics
	(persons)	(%)	(persons)	(%)	
Unemployed	156	32.3	130	28.4	
Economically Inactive group					
<i>OECD standard unemployed</i>	44	9.1	29	6.3	
<i>Discouraged unemployed</i>	49	10.1	36	7.9	$\chi^2=8.817$ P=0.066
<i>econ. inactive but willing to work</i>	73	15.1	74	16.2	
<i>purely econ. Inactive</i>	161	33.3	188	41.1	
<i>sub-total</i>	327	67.7	327	71.6	
Total	483	100.0	457	100.0	

the non-participant group. 33.3% of training participants who are not re-employed were purely economically inactive group who have completely withdrawn from the labor market whereas it was 41.1% for the non-participant group. These findings show that employment training maintain the subjects' desire to work, and contribute to relating them to the labor market.

*Current Economically Active Status of Those Who Are Not Re-employed by Training Categories<sup>4</sup>*

Among those who received training but are not re-employed, there is difference of economically active status between participants and non-participants at 5% significant level. 34.5% of employment promotion training participants, who are not re-employed, have actively sought for jobs in the past month, showing a similar rate with the re-employment training for the unemployed non-participants. Also, 52.9% of re-employment training for the unemployed participants, including the discouraged unemployed group, were willing to actively seek jobs whereas the same for the employment promotion training participants was only 42.1%. Also, purely economically inactive group who have completely withdrawn from the labor market were higher from the employment promotion training participants who are not re-employed than from the re-employment training for the unemployed participants who are not re-employed.

**Table 12.13: Current economically active status of those who are not re-employed by training category**

	Re-employment training for the unemployed participants		Employment promotion training participants		Statistics
	(persons)	(%)	(persons)	(%)	
Unemployed	140	32.9	126	26.3	
Economically inactive group					
<i>OECD standard unemployed</i>	43	10.1	39	8.1	
<i>Discouraged unemployed</i>	42	9.9	37	7.7	$\chi^2=10.854$ P=0.028
<i>Econ. Inactive but willing to work</i>	66	15.5	97	20.2	
<i>Purely econ. Inactive</i>	134	31.5	181	37.7	
<i>Sub-total</i>	285	67.1	354	73.8	
Total	425	100.0	480	100.0	

<sup>4</sup> Re-employment training for the unemployed and employment promotion training for the unemployed are the two most important re-employment promotion programs in training. The former is for the unemployed from employment insurance applicable enterprises. and the latter is for the unemployed from employment insurance non-applicable enterprises.

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# 13 Publicly Funded Training for Unemployed Adults: Germany, the UK and Korea\*

Paul Ryan<sup>a\*</sup>

## Introduction

Training programs have bulked large in the Republic of Korea's response to the labor market difficulties precipitated by the 1997 financial crisis. The rapid increase in unemployment that accompanied the crisis was countered by an even faster expansion of publicly supported training. Participation in the two leading programs for the unemployed rose nine-fold between 1997 and 1998 (Kang *et al.*, 1999).

The rapid expansion of training in Korea has led to concerns about quality and effectiveness. Some providers appear to have taken advantage of a favorable opportunity to sell low quality programs. Participants appear not to have done well in the labor market: only 20 % found a job soon after training in 1998 (Cho and Ra, 1999). The Korean government has reacted to these difficulties in several ways: by stepping up the inspection of training providers and withdrawing funding from those found unsuitable; by basing funding of providers partly on the job finding rates of their ex-trainees (output-related funding); by funding trainees through training vouchers, in order to encourage them to pick better providers; by adopting a 50% target placement rate for 2000; and by favoring training programs tied directly to the needs of employers ('tailor made training'; Kang *et al.*, 1999).

Only limited evidence has been available to guide these reforms. Immediate job placement rates, on which much attention has focused, provide a

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poor criterion of program success. The rate typically rises strongly during the first year after training. Other outcomes matter too, including the acquisition of vocational qualifications, and pay when employed. Moreover, these outcomes describe only the gross outputs of a program, not its value added – i.e., the change in outcomes relative to what they would have been in the absence of the program.

Additional evidence can be sought from two sources. The first is Korea itself. A formal evaluation has recently been conducted for the leading training program for the unemployed in 1998. Its findings potentially change the conventional 'failure' perspective upon Korean training (Kang and Lee, 2000).

The second source is other countries. The track record of adult training programs – particularly the remedial programs that have dominated in the US – is at best patchy (Dar and Gill, 1995; Martin, 1998). A better prospect of useful evidence are countries whose training programs have been evaluated in detail, as for the US, but in which public training services have undergone strains more similar to those experienced by Korea.

Two national experiences that are potentially resonant from a Korean perspective are the East German and the British. German reunification in 1989-90 was followed, in what was formerly East Germany, by a sharp rise in unemployment, inducing the federal government to introduce training programs and expand them rapidly. Similarly, the large rise of unemployment in Britain during 1979-83 led during the mid-1980s to the expansion of public training and the recasting of its role in labor market policy.

As the Korean economic recovery has gathered pace, so the pressure on public training programs has eased. The government has scaled back its plans for public training. The opportunity has arisen to reconsider the role of public training, in terms of its size, quality and role within labor market policy, less influenced by the distortions caused by labor market crisis.

The role of public training in Germany and the UK is discussed in section 2, followed in section 3 by methodological issues in evaluation research. Section 4 considers evaluation findings for German and British programs, section 5 some relevant attributes of Korean training programs. Conclusions follow in section 6.

## **Training Attributes: Germany and the UK**

In both Germany and the UK, economic dislocation has at times produced acute difficulties in the labor market, prompting governments to expand public training programs for the unemployed. This section considers both experiences. The primary emphasis is placed on East Germany, where the speed of developments after 1989 mirrors that of Korea after 1997, and



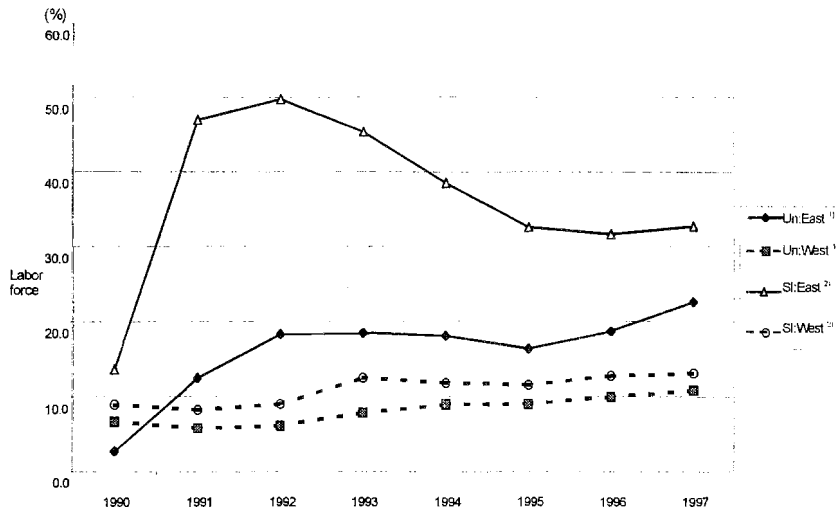
where reunification provided a context similar to, if less acute than, that which may face the Republic of Korea in the future.

*The National Context: the Labor Market and Public Policy*

In mid-1990 the Federal Republic of Germany absorbed the former German Democratic Republic (East Germany). National reunification produced a boom in West Germany, resulting from the new demand unleashed in the East for the West's consumer and capital goods, but a slump in the East, as the demand for its output fell heavily. Eastern producers had to redirect their efforts from the sheltered product markets of ex-communist east Europe to the exposed ones of the international market system. Their competitiveness proved low, as a result of poor products, low labor productivity and, given the 'one for one' terms of currency unification, high hourly labor costs. The demand for labor in the East collapsed.

The result was an employment crisis unprecedented in Germany since the 1930s. By 1992 the Eastern labor force had shrunk by one third. Despite that, the unemployment rate had nearly reached 20 %. One in every two members of the labor force received public support, whether unemployment benefit, training or another labor market measure. The labor market problem in the East eased only moderately thereafter, before intensifying again as the national economy faltered after 1995 (Figure 13.1).

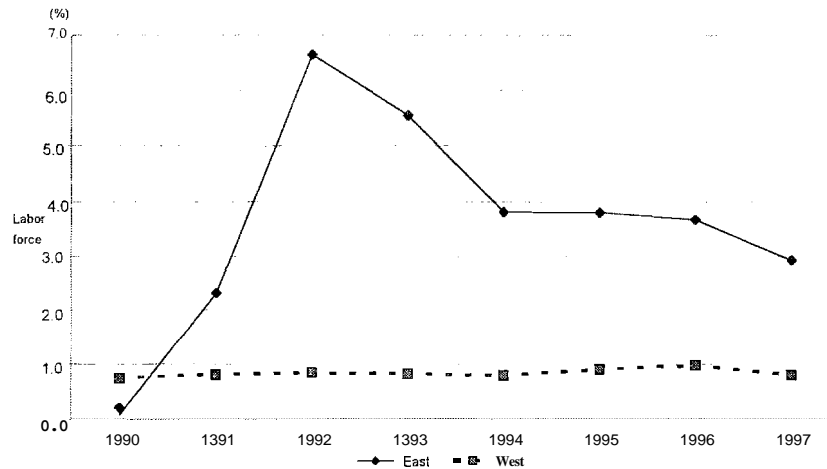
**Figure 13.1: Unemployment and labor market slack in Germany, 1991-1997**



Notes: 1) Un: registered unemployment  
 2) Sl: 'Slack', registered unemployment plus participants in all labor market programs, including short-time working (full-time equivalent)  
 Source: Bach *et al.* (1998), Tables 1,4,11,12.

Labor market policy soon became a major plank in the federal government's response to the East's employment problems. Initially, subsidies for short-time working led the way, followed by early retirement subsidies, but both became unimportant after 1994. Job creation and labor market training were slower to come on stream, but by 1992 training alone accounted for more than 6 % of the labor force. Its coverage shrank to 3 % by 1997, but that was still more three times larger than in the West, where unemployment had by then passed 10 % (Figure 13.2).

**Figure 13.2: Rate of participation in publicly funded adult training in Germany, 1990-1997**



Note. Training defined as in Table 13.1  
Source: Bach *et al.* (1998). Tables 1,4,11,12

The UK context is the employment crisis of the 1980s. Prompted by the 1979 oil price shock and the macroeconomic policies of the Thatcher Government, the unemployment rate rose during 1979-83 from 4 to 12 %, where it remained there until 1986. The policy reaction was less immediate and dramatic than in East Germany, and it concentrated during the first half of the 1980s on youth programs. By 1986, long-term unemployment had reached 4 % of the labor force, most of it adult. Training for the adult unemployed was expanded strongly in 1986-88 and its content reformed.

#### *Public Training Programs: Content and Clientele*

Publicly supported training for adults is heterogeneous, in terms of services, intensity, duration, location and clientele in particular. The point must be underlined, as much of the evaluation literature (section 3, below) treats it as essentially homogeneous, as part of 'training' or human capital formation in

the abstract.

### Germany

Three main categories are typically distinguished in Germany' further training, retraining and familiarization training (Table 13.1). Familiarization training, aimed at new hires, is typically job-based, part-time and short-lived, and does not lead to a vocational qualification. At the other pole, retraining is typically 'classroom'-based, full-time, long-lasting, and it must lead to an occupational qualification. Inbetween, further training, aimed at the already qualified within an occupation, divides into adaptation training, which goes primarily to disadvantaged individuals and female re-entrants, and upgrade training, frequently aimed at advanced qualifications within an occupation. It contains some remedial training, which constitutes the dominant category in the US but which lacks a direct counterpart in Germany. Its content varies from short courses that are not linked to an additional qualification, to longer ones that culminate in the acquisition of *Meister*, *Techniker* and other qualifications (Blaschke, Plath and Nagel, 1992).

All three types of training are eligible for public funding under the Employment Promotion Act of 1969, which was extended to the East after reunification. The key change was the temporary introduction in the East of *ad hoc* short courses, typically lasting for no more than one month, and accounting during 1991-92 for around one-fifth of all publicly supported trainees.<sup>1</sup> By 1993 training in the East had stabilized along lines similar to those in the West. Differences in emphasis between the two regions were still present, with training oriented in the East towards adaptation training and retraining, in the West towards upgrade training (Table 13.1). For the two main programs, adaptation training and retraining, training durations were markedly longer, and training more commonly conducted full-time in the East than in the West (Table 13.2).

The East German training effort was strikingly intense and costly. Retraining was delivered overwhelmingly on a full-time basis, apart from employment, lasting on average (for completers) more than 18 months and containing extensive technical education. Adaptation training shared those attributes, in the East at least, where the great majority of training was full-time, and courses lasted nine months on average (Table 13.2).

These attributes of adult training reflect its link in Germany to the occupational categories defined for the national apprenticeship system. With the temporary exception of the short courses of 1991-2, publicly supported adult training is geared to the same occupations, and in the case of retraining

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<sup>1</sup> Publicly supported adult training programs in Germany are typically grouped together in the category *Fortbildung und Umschulung* (FuU).

Lechner (1996);Hujer and Wellner (2000), Figure 1.

Table 13.1: Shares of training categories in publicly funded training for adult workers, old and new Bundeslander in Germany, 1993(Q3 completers)

Training category	East (%)	West') (%)	All (%)
Further Training:			
a. Adaptation ( <i>Anpassungsfortbildung</i> )	62.6	43.4	53.1
b. Upgrade ( <i>berufliche Aufstieg</i> )	3.5	35.2	19.2
Retraining ( <i>Umschulung</i> )	26.3	18.8	22.5
Familiarization training ( <i>Einarbeitung</i> )	7.6	2.6	5.2
All training (%)	100.0	100.0	100.0
(numbers)	59,600	58,200	117,800

Note: 1) the former West and East Germany constitute respectively the old and new Bundeslander  
Source: Blaschke and Nagel (1995), Table 3.

requires the attainment of the same (craft plus) level of knowledge and skill as does an apprenticeship, albeit in as little as half the time. Adults undergoing retraining must also pass formal examinations, conducted by the same local bodies that examine apprentices (Johansen, 1994).

The clientele for public training programs has traditionally been primarily the unemployed, but in East Germany the widespread need for skill enhancement after reunification led to an informal guarantee of access to all who demanded it. In practice, participation in training has been slanted towards the unemployed, females (except for familiarization training) and the *more highly* educated.

### The UK

In Britain, adult training has evolved through three different programs since the mid-1980s (Table 13. 3).<sup>3</sup> The 'Old' Job Training Scheme (JTS)<sup>4</sup> of the

The New Deal (1998- ) currently constitutes a fourth, evaluations of which have now begun to emerge.

<sup>4</sup> The descriptor 'Old' was subsequently appended to JTS in order to differentiate it from a short-lived replacement of 1987-88, which has been termed the 'New' JTS. The title is clearly unofficial ; the marketing-oriented Government of the time would hardly have chosen such a title for a new program.

**Table 13.2: Attributes of public training programs for adult workers, old and new Bundeslander in Germany, 1993 (all 1993. Q3 completers)**

Training category	Share of females within category and region (%)		Share of part-time trainees within category and region (%)		Average duration of training (months)	
	West	East	West	East	West	East
Further Training:						
a. Adaptation (Anpassungsfortbildung)	47.1	70.6	17.8	14.4	6.6	9.0
b. Upgrade (berufliche Aufstieg)	25.6	45.9	44.1	29.3	n.a.	n.a.
Retraining (Umschulung)	54.8	61.5	2.2	1.5	17.1	19.3
Familiarization training (Einarbeitung)	37.7	31.5	8.8	4.0	n.a.	n.a.
All Training	40.7	64.5	23.9	10.7	9.8 <sup>1)</sup>	12.1 <sup>1)</sup>

Note: n.a.: not available

1) Adaptation training and retraining only

Source: Blaschke and Nagel (1995), Tables 3, 5

PUBLICLY

D TRAINING

NEMPLOYED

**Table 13.3: Attributes of public adult training programs in UK, 1986-1998**

Program	Period of operation	Eligibles		Spell duration months	Services	Participant income entitlement	Public funding basis	Stock of participants ('000) (year)
		Age	Status					
Job Training Scheme ('Old' JTS)	1986-88	18+	Interested individuals	5.0	Occupational off-JT, public provision	No course fees (96%); training allowance (83%)	Trainee starts and time spent in training	18 <sup>2)</sup> (1986)
Employment Training (ET)	1988-93	18+	Unemployed 6+ months	4.9 <sup>1)</sup>	Training leading to a VQ via work, off-JT or project	Unemployment benefit plus £10 per week	Trainee starts and weeks	125 (1992)
Training For Work (TFW)	1993-98	18+	Unemployed 6+ months	4.5	Training, work experience via work, off-JT or project	Unemployment benefit plus £10 per week; employee status permitted	Participant outcomes (VQ, job) <sup>3)</sup>	133 (1994) 51 (1997)

Notes: 1) author's estimate; participants who left within two months not included

2) author's estimate, based on 40,000 completions p.a.; dropout rate of 10 % assumed

3) from 1995.

Sources: Payne (1990), Payne, *et al.* (1996), Payne, *et al.* (1999).

mid-1980s provided occupational training, mostly retraining and upgrade training, to a clientele that included the unemployed, female labor market re-entrants and employees willing to quit their jobs in order to train full-time. The Employment Training (ET) and Training for Work (TFW) programs of 1988-98 offered retraining, remedial training and work experience, based variously at workplaces or in special projects, with eligibility focused on the long-term unemployed.

The replacement of JTS by ET/TFW saw several changes. Training was redirected from occupational training and retraining for a mixed clientele, delivered off-the-job in public training facilities, to job-related training and work experience primarily for the long-term unemployed delivered insofar as possible on the job. The scale of training rose seven-fold during 1986-92, but fell back thereafter. The average duration of training remained around four to five months, but the shift towards work-based training probably reduced training content. Finally, public payments to training providers were rebased in 1995 from inputs (starts plus progress) to outcomes (qualifications acquired and employment rates after training).

The training content of British programs varied from extensive to negligible: from the certified occupational skills that were prominent in JTS to the job search and work experience in which segments of TFW specialized – which should strictly be excluded from the category 'training program'. Training methods included various mixes of off-the-job ('classroom') training, as emphasized by JTS, and on-the-job training and work experience, as emphasized by ET.

### Comparison

East German and British programs therefore resembled each other in terms of their rapid expansion, in the face of mounting unemployment (Germany) and long-term unemployment (the UK), their provision of varied training services according to participants' needs, and their emphasis on acquiring vocational qualifications. They differed in terms of a shorter duration and lower intensity of training in the UK, along with a greater orientation to remedial training, an increasing orientation towards work-based training, and the introduction of output-related funding.<sup>5</sup>

The contrast between the countries is sharpest for the amount and quality of training provided to individual participants. Short course durations, low trainee achievements and limited quality control in work-based training have

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<sup>5</sup> The two countries also differ in the meaning of a training 'program'. In Germany, public training services have evolved to meet changes in perceived needs, such as those in the East after 1989, but within the framework of the 1969 Act (AFG) throughout. The concept of discrete programs with limited individual life-span is more appropriate for the UK, where Governments have frequently discarded an existing program, such as JTS, in favor of a new one, such as ET. The emphasis has been placed in Britain on program innovation, in Germany on institution building, stability and adaptation.

caused concern in the UK. Only one-third of ET/TFW participants gained a vocational qualification, and only a handful at craft, technician or higher levels (Table 13.4). These low attainment rates undoubtedly reflect the low prior skills of the long-term unemployed. They may also reflect employer use of trainee labor for job training and production work, at the expense of occupational preparation, when training is work-based and external quality control is weak (Ryan, 1994).

**Table 13.4: Vocational qualifications gained by leavers from adult programs in the UK, 1986, 1994 and 1997**

	JTS 1986 (%)	ET <sup>1)</sup> Jan-Mar, 1994 (%)	TFW <sup>1)</sup> Jul-Sep, 1997 (%)
Full qualification	63 <sup>2)</sup>	34	38
Level 1 (basic)	n.a.	7	5
Level 2 (semi-skilled)	n.a.	12	14
Level 3 (craft)	n.a.	2	5
Level 4 (technician)	n.a.	0	1
Other	n.a.	13	13
Part Qualification	n.a.	6	6
All	63	40	44

Notes: 1) England only.

2) includes completion certificates issued by training providers (17 % of trainees).

Sources: Payne (1990), p.24.

Department for Education and Employment, unpublished information, trainee database system

## Evaluation Methods

The way to evaluate training is disputed, but the basics are widely agreed. Two issues may usefully be distinguished: the goals of training and the estimation of the counter-factual (Heckman, Lalonde and Smith, 1999; Grubb and Ryan, 1999).

### *Program Goals and Evaluation Criteria*

The standard criterion is whether or not a program improves the labor market prospects of its participants. When unemployment is high, employment tends to be the priority, as measured by rates of employment, stable employment and unemployment after participation.<sup>6</sup> As the presumed

<sup>6</sup> The dominance of employment-related outcomes in the German evaluation literature is also consistent with the explicit goal of the Employment Promotion Act. *viz.* 'achieving and



goals of goal of training (as opposed to, e.g., job creation) include skill enhancement, effects on pay (e.g., hourly wages) should also be considered. Pay effects are regularly considered alongside employment ones in the British literature, but only rarely in the German one.

These two criteria are however not sufficient for effective evaluation. Their limitations become visible when the criteria of applied welfare economics, *viz.*, efficiency and equity, come into consideration. An improvement in participants' subsequent employment rates and pay implicitly suggests an efficiency gain. Two further adjustments are however required before such a conclusion can be reached. The first is to allow for displacement effects on non-participants. Higher subsequent employment amongst participants may come, partly or wholly, at the expense of lower employment amongst non-participants. In that case, the sum of participant's benefits overestimates aggregate employment benefits. The second is to take account of the cost of the program. Cost-benefit analysis is widely used in US evaluation research, but neither it nor adjustment for displacement has featured in its German and British counterparts.

Finally, the equity dimension of program effects is also typically overlooked, even though many training programs are set up to help the disadvantaged, including the long-term unemployed in the UK and the uninsured unemployed in Korea. Adopting here an egalitarian social welfare function defined over economic outcomes, a program has merit from an equity standpoint when its clientele is economically disadvantaged and when that clientele is made better off than it would otherwise have been, during if not after participation.'

### *Evaluation Methods: the Counter-Factual*

The counter-factual is defined as the situation of participants had they not taken part in training, which cannot be observed directly and has to be estimated. The effects of the program are then estimated as the difference between the actual and the counter-factual situations.

Estimation of the counter-factual depends heavily in the US nowadays on *highly experimental* methods: controlled trials, in which eligible workers are assigned randomly to 'treatment' and 'control' groups, with the former receiving training, the latter (ideally) not receiving it. Social experiments are however rare outside the US. The acceptability of refusing training to a control group is especially low when unemployment is high, and when eligible workers are guaranteed access to, or required to undertake, training

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maintaining a high level of employment, constantly improving the structure of employment, thereby promoting economic growth' (Bach *et al.*, 1998, p.15).

<sup>7</sup> The further, non-economic goals, such as reduced dependence on public income support, and cuts in criminality and teenage pregnancy, that have often featured in the goals of training programs in the US (Grubb, 1996) have not done so in German and British programs.

– as in both the UK and East Germany.

Under such conditions, the counter-factual is typically estimated by *quasi-experimental* methods. Some mix of statistical selection and economic modeling is used to control for differences between the attributes of participants and of a 'comparison' group that is typically drawn from national surveys of households, unemployed workers, etc. The experiences of the latter are used to estimate the counterfactual. The difficulty is that the two groups may differ not just in observed (i.e., measured, and therefore statistically controllable) but also unobserved attributes that are relevant to both participation and labor market outcomes. For example, participants may be more able and more motivated than non-participants, and any superiority in post-program outcomes for participants over non-participants may then reflect the underlying difference in attributes rather than any effect of training.

The threat of selection bias in quasi-experimental evaluations is widely recognized. The various ways of countering it divide here into two: matching and modeling. Both have been extensively used in research on East Germany. Matching methods pick for every participant one or more non-participants to minimize the difference between the two in observable attributes (e.g., schooling, age, sex). They use pre-participation period outcomes for the two to test for the presence of unobserved differences. If none are detected, program effects are estimated by the difference in outcomes in the two groups, adjusted for any differences in observable attributes that the matching procedure did not manage to eliminate (e.g., Lechner, 2000).

Model-based methods, by contrast, apply an econometric model of the selection of eligible workers into participant and non-participant status. They seek to remove the selection biases caused by unobserved attributes with the use of such techniques as fixed effects models, instrumental variables and two-step estimators – all of which require potentially restrictive assumptions in order to generate estimates (e.g., Fitzenberger and Prey, 2000).<sup>8</sup> Hybrid approaches have also been used: e.g., the demands made on econometric modeling are reduced by combining it with individual matching, particularly by area of residence (Payne *et al.*, 1999).

The validity of quasi-experimental methods is however limited. The estimates that they generate have been shown to be sensitive to choice of both selection model and comparison group, in evidence for both the US and Germany, notwithstanding the expertise that has been devoted to refining

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<sup>8</sup> For example, fixed effects models, which feature prominently in German evaluation research (Fitzenberger and Prey, 2000), implicitly assume that any unobservable factors that influence individuals' labor outcomes are constant, across both individuals and time. A program's effects can then be estimated as the difference between the two groups in the change in their members' labor market outcomes. To the extent, however, that shocks are specific to both individual and time (e.g., a particular person 'had a bad year'), the technique does not remove selection bias.

them (Lalonde, 1986; Hübler, 1997; Heckman, Lalonde and Smith, 1999).

On the next rung down the ladder of evaluation technique stand *weakly experimental* methods. The counter-factual is suggested by the experiences of groups whose situation bears some similarity to that of participants. Possible choices for such a group include: participants in other programs, similar age groups, similar groups in other countries and even participants' own past situations: (before/after comparisons). Thus in Germany comparisons of participants' outcomes to those of both dropouts and participants in other programs were used before quasi-experimental methods became the norm (Hofbauer and Dadzio, 1984; Blaschke and Nagel, 1995). Uncontrolled differences in the unobserved attributes of the two groups mean however that the validity of such evidence is low.

On the bottom rung, there are gross outcomes, such as the 20 % employment rate of ex-trainees in Korea in 1998. Similarly, in the UK in 1997, 50 % of TFW ex-participants achieve a 'positive outcome', defined as employment or entry to education or other training, as measured six months after leaving (DfEE, 1998). In Germany, the earliest evaluation research had also been limited to gross outcomes: e.g., the 59% employment rate 3 to 6 months after completing further training in the West in 1983 (Hofbauer and Dadzio, 1984). As gross outcomes ignore the counter-factual, however, this evidence is *non-experimental*, and its value for evaluation correspondingly low.<sup>9</sup>

Finally, there is implementation-oriented research: establishing how a program operated in practice, in relation to both its design specifications and programs in other times and places (e.g., section 2, above). How a particular program came to succeed or fail is likely to remain a mystery without such evidence.

In sum, amongst the various evaluation methods in use, even the most sophisticated are imperfect. In addition, evaluation research often handicaps itself by taking a narrow view of program goals, by ignoring aggregation problems, and by emphasizing refinement of econometric technique rather than data quality.

## Training Evaluations for Germany and the UK

The longer operational history of training programs for the unemployed in Germany and the UK than in Korea is associated in each case with a more extensive evaluation record. This section reviews the findings of the relevant national literatures.

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<sup>9</sup> Gross outcomes, such as completion and employment rates, are widely used in the US for administrative purposes, e.g., as indicators of the success of program delivery across localities or providers. Even there, however, selection biases undermine the validity of the information (Barnow, 1992).

### *Findings: Germany*

The evaluation studies for Germany and the UK discussed here (Tables 13.5,6) all concentrate on subsequent labor market outcomes for participants. All are quasi-experimental, applying sophisticated econometric or statistical techniques to micro-data in order to estimate the counter-factual. Their limitations include small sample sizes (Germany only), and the neglect of program attributes (and their implications for equity), of aggregation problems and of operational attributes.

Four recent evaluations of training programs in East Germany are considered, selected from the twelve covered by a recent survey (Fitzenberger and Speckesser, 2000). All of the studies cover the two largest public training categories: further training and retraining (section 2, above). Two include familiarization training as well. All refer to part or all of 1990-94, i.e., the aftermath of reunification. All concentrate on employment-related outcomes for participants after leaving training, covering a maximum period of four years and, for most participants, no more than two years. Hazard rate models of transitions between labor market states are used in three studies.

Methods of estimating the counter-factual divide evenly into statistical matching and econometric modelling (Table 13.5).

The results suggest that publicly supported training has failed. In particular, it has not improved participants' employment prospects. The estimated impact of training is for typically not significantly different from zero, statistically speaking. Two studies even find negative effects: Lechner for the first twelve months after training, and Kraus *et al.* for training undertaken during 1990-92. The only positive finding concerns the effects of training conducted during 1993-4, which Kraus *et al.* find helped participants to find work, relative to having remained unemployed.

This pattern of results matches that in wider literature for East Germany. 'Most evaluation studies produce no significant effects' and 'the positive employment effects of job creation and training measures are in any case small' (Fitzenberger and Speckesser, 2000; 21,22). The same bleak picture applies also to publicly funded training programs in the West (*ibid.*, Table 3). It contrasts however with that for privately funded adult training in the West, evaluations of which suggest favorable employment-related effects, particularly for programs lasting more than one year (Table 13.5; Fitzenberger and Prey, 2000).<sup>10</sup>

Various causes may be suggested for the absence of a favorable or even a stable pattern in estimates of employment effects. The first consideration is sample size. Positive effects may well exist, but, as only small sample sizes

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<sup>10</sup> Again: the findings of various studies diverge. Pischke (1996), studying wage rather than employment effects, finds no general benefits from employee training in Germany.

Table 13.5: Evaluations of adult training in Germany (quasi-experimental methods only)

Study	Territory covered	Training service <sup>5</sup>	Data source <sup>a</sup>	Sample frame	Size of sample [control group]	Evaluation method	Program effects		Pay effect <sup>2</sup>
							Employment-related Variable	Effect <sup>2</sup>	
Public Lechner (2000)	East	1,2	GSOEP 1990-96	Entrants aged less than 53, 1990-93	131 [1280]	Matching by observable attributes	Incidence of unemployment and full-time employment, subsequent 4 years	- First 12 months 0 subsequent	0 <sup>3</sup>
Hujer and Wellner (2000)	East	1-3	GSOEP, 1990-94	Entrants aged less than 51, 1990-93	231 [1401]	Matching by observable attributes	Duration of employment and unemployment, subsequent 3 years	0	n.a
Kraus, Puhani and Steiner (1999)	East	1-3	AMM, 1990-94	Entrants, 1989-94	3.503 [3095]	Corrected for observables (tested for unobservables)	Transitions to employment and inactivity, subsequent 1 year	- 1990-92 + 1993-94 <sup>4</sup>	n.a
Fitzenberger and Prey (1999)	East	1,2	AMM, 1990-94	Entrants w.o. other training, 1989-94	471 [4352]	Observables: controls; unobservables: fixed effects	Employment rates, subsequent 0-4 years	0	0 (real hourly pay)
Non-public Fitzenberger and Prey (2000)	West	All privately funded adult training	GSOEP, 1984-97	Employees aged 25-44 yrs 1984	126 [1113]	Matching by observables, fixed effects for unobservables	Employment and unemployment rates, subsequent 3 years	2% all 6% duration 12+ mos	n.a

Notes: 1) GSOEP: German Socioeconomic Panel (annual household survey); AMM: Arbeitsmarktmonitor (Labor Market Monitor: annual longitudinal survey of East German population of working age).

2) +, - indicate respectively statistically significant positive (i.e., in desired direction) and negative (undesired direction) effects cant effects.

3) unpublished results, reported in paper.

4) off-the-job programs (1-2) only (for men).

5) training categories as in Table 13.2.

are possible in both of the datasets available (GSOEP and AMM; Table 13.5), statistical significance is difficult to establish. This interpretation is consistent with the finding by Fitzenberger and Prey (2000) of positive but statistically insignificant coefficients in almost all the models that they estimate."

A second possible cause is *methodology*: the variety of assumptions involved in implementing the counterfactual may generate unstable results, much as was the case in the US until quasi-experimental methods gave way to highly experimental ones (Lalonde, 1986). For East Germany, Hübler (1997) notes a similar sensitivity of results to choice of estimation method and dataset. This explanation suggests that little will be learned until social experiments are used in Europe."

Thirdly, weak effects may reflect *low quality* training. The possibility is particularly relevant to 1990-92. Some research shows employment effects that change from negative to positive between 1990-92 and 1993-94 (Kraus *et al.*; Pannenberg, 1995, 1996). It is also consistent with the predominance of short courses and an underdeveloped training infrastructure in the East right after reunification. Yet over 1990-94 as a whole, East German programs were both intensive and long-lived by UK and US standards, which hardly suggests low training content. Evidence on the implementation of training in the East, and on vocational qualifications obtained by trainees, is needed to assess the issue.

A fourth explanation might be that not even high quality training can succeed in *slack labor markets*. In the post-unification East, even the markets for more skilled labor towards which trainees are being redirected are glutted, leaving few vacancies for ex-trainees to pursue. This view is certainly consistent with the state of the Eastern labor market at the time. It sits uneasily with evidence from the West, however. Although labor market slack had risen there during the 1980s, it remained much lower than in the East and it fell during the reunification boom of the early 1990s. Nevertheless, eight evaluations of public training in the West, for various periods centred on 1984-93, have also produced a varied and contradictory pattern of employment-related effects, with similar numbers of 'significantly

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<sup>11</sup> Kraus *et al.* does however generate a much larger sample by aggregating across years. Small samples impose two further limitations on research on East Germany. As many participants do not find work, pay effects have to be estimated from even smaller samples, and training effects cannot be broken down, e.g., by type of training.

<sup>12</sup> The problems of sample size and evaluation method interact unfavorably, particularly for evaluation methods that rely on the individual matching of participants and controls. Non-parametric matching techniques confined to the observable attributes of participant and comparison group members (e.g., Lechner, 2000) require that there be no significant difference in the pre-program labor market positions of the two groups. When sample sizes are small, however, the negative finding of no statistically significant difference provides a particularly weak basis for the positive conclusion, that the two groups really are similar. The findings of the evaluation then remain subject to selection biases, caused by uncontrolled differences in unobserved group attributes.

positive' and 'insignificant or significantly negative' estimates (Fitzenberger and Speckesser, 2000, Table 3).

The German evidence suggests therefore that public programs have done little for their participants, relative to having remained unemployed – notwithstanding their exceptional intensity and cost. The point is underlined by a similar absence of generally favorable effects in studies of outcomes at more aggregate levels, such as regional employment rates (Schmid *et al.*, 1999; Fitzenberger and Speckesser, 2000, Table 5).

More needs to be known about the effects of German programs, including their effects on pay, the comparative effects of the different training categories in Table 13.1, and the role of vocational qualifications in mediating labor market outcomes. The evidence provides little support, however, for the hypothesis that poor program results, as commonly found for the US, reflect low levels of investment in each trainee (Grubb and Ryan, 1999). Not even programs that aim as high as in Germany can apparently generate benefits for participants sufficiently strong to be visible in slack labor markets through the fog created by small samples.

If the problem with apprenticeship training in Germany has been that it is hard to make it work in other countries, including Korea (Jeong, 1995), public programs apparently face a more fundamental difficulty: making them work in Germany itself. Unfavorable evaluation findings have increased doubts about public training programs for the unemployed in the East, and encouraged their contraction despite enduringly high unemployment (section 2, above).

### *Findings: UK*

There have been fewer evaluation studies for the UK than for East Germany, but their scope has been wider and their findings more encouraging (Table 13.6). Each of the three major programs has been evaluated by Joan Payne and colleagues. In all three studies, labor market outcomes for participants (here, pay as well as employment) were compared to those for matched members of a comparison group, and statistical methods were used to counter differences between the attributes of the two groups, including unobserved ones in the case of pay.<sup>13</sup> Although the quality of both the matching and the statistical methods used rose across the three studies, continuity of personnel and methods make the findings unusually comparable across programs. The availability of sample sizes several times larger than those typically available for East Germany also increases the

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<sup>13</sup> Controlling for selection processes is potentially particularly important in comparing these three programs. The quality of the participants is likely to have been lower for ET and TFW than for JTS, insofar as the former but not the latter were targeted upon the long-term unemployed; and for JTS and ET than for TFW, insofar as only the latter has involved output-related funding, which encourages training providers to 'cream' for prospective success when selecting participants.

informational content of the evidence.

All three programs show substantial and statistically significant improvements in employment-related outcomes, including both the incidence of employment at a particular point and cumulative time spent in employment. The increase in employment rates ranged from around 14% after one year for JTS to around 22 and 12% after three years for ET and TFW respectively (Table 13. 6). Short-term (one year) effects were substantial only for JTS, but they built up considerably over three years in the other two programs, for which longer post-program data were available.

The pattern of pay effects differs sharply by program. JTS participants gained an estimated 22 % in hourly pay overall. The two-thirds of participants who found a job in the occupational area for which they had been trained gained 31 %. These effects are large, even implausibly large: the private benefits of formal schooling are typically less than 10% per year of full-time study. By contrast, ET and TFW participants as a whole gained little or nothing. Significant benefits were present in both cases for particular participant categories: notably, those who received off-the-job training in ET, and work-based training and an associated vocational qualification in TFW. The estimated pay gains in these two categories – six and nine % respectively – are comparable to the private return on other investments in human capital. Overall, however, it appears likely that JTS did more for participants' earning power than did ET or TFW.

### *Interpretation*

One interpretation of the UK evidence might be that all of the types of training covered by these programs can improve participants' employment prospects, but only occupational training, as in JTS, can systematically improve their pay. This interpretation has some a priori plausibility. It is also consistent with the limitation of pay gains under the other two programs to participants who took off-the-job training and acquired a vocational qualification, under ET and TFW respectively. In the German evidence the interpretation is consistent the apparent rise in the benefits of training when the crisis-generated short courses were withdrawn in 1992.

The interpretation is however open to doubt on two scores. Firstly, the quality of both the data and the matching of participants and non-participants appear to have been lower in the JTS evaluation than in the later ET and TFW ones. Secondly, the long and expensive public programs of occupational training that predominate in Germany appear not to have worked there either.<sup>14</sup>

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<sup>14</sup> That finding may however reflect the limitation of the German evaluation literature to employment outcomes. (Two of the evaluations in Table 13. 5 actually evaluated effects on pay as well as employment, but neither published the results.) In heavily overstocked labor markets, the benefits of occupational training may well be greater for pay than for employment: trained ex-participants may find it hard to find a job but, when they do, their enhanced skills should mean higher pay.



Table 13.6: Evaluations of training programs for adult workers in UK

	Sample		National unemployment rate when outcomes measured (%)	Vocational qualifications gained (% group)	Estimated program effects on participants' subsequent labor market outcomes				
	Frame	Size ('000)			Employment	Pay			
					Time lapse to outcomes (months)	Employment rates (% points)	Cumulative employment (% time since participation)	Time lapse to outcomes (months)	Pay (% hourly pay)
JTS	1986 completers	785	10.4	62	3-15	+17* m +10* f	n.a.	0-15	+22* all +31* it + 3 ot
ET	1993 Jan., Feb. leavers	917	9.6	55	12 24 36	+ 3* +15* +22*	+6* all +8* m +3* f (at 25 mos.)	14	+2 all +6* Off-JT
TFW	1995 Sep., Oct. leavers	822	7.1	44	12 24 36	0 +6* +12*	+14* (at 17 mos.)	16-22	+2 all +9* work +VQ

Notes: \* Statistically significant (p=.10) #, statistical significance cannot be calculated; m: f, male, female; VQ: vocational qualification; it: in trade (i.e., employed in occupation which training related); ot: not in trade. Placement categories for ET and TFW: 'work', on-the-job training and work experience at an employer's premises; 'off-JT', full-time off-the-job training in a college or training centre; 'project', work experience with a voluntary organisation for environmental or community benefit.

Source: Table 13.3.

An alternative interpretation might be that the greater employment effects estimated for British than for East German programs reflect the prominent role of the workplace in two of the UK programs (ET and TFW) and its marginal role in Gennany. An employer who sponsors a trainee, whether directly or simply by providing work experience within a training program, enjoys more scope to tailor training to its own needs and to screen the trainee for subsequent employment than is possible in 'classroom' training. Work-based training might therefore increase employment prospects for participants by more than does other training. The interpretation is also consistent with the difference between the employment effects of British and East German programs in the 1990s, given the greater part played by work-based training in the former than in the latter.<sup>15</sup>

Again, other evidence casts doubt on the interpretation. The UK results suggest that JTS, which had no workplace component, appears to have done more for its trainees, particularly in terms of pay, than did its more work-based successors, ET and TFW.

A further consideration is that, even were work-based training shown definitively to improve employment prospects for participants, that would have to be set against a greater probability of extensive displacement of non-participants by participants, both during and after training. To the extent that work-based training involves productive labor, employment options during the program are reduced for non-participants. To the extent that employers use the program to train and screen future employees, employment options for non-participants decline after the program as well. Employment effects are then less in aggregate than the sum of those for participants – and may even, as in some Swedish and German evidence, be zero in the aggregate (Skedinger, 1995; Fitzenberger and Speckesser, 2000).

All in all, it is difficult to derive a coherent story from the German and British evaluation literatures combined. Publicly funded occupational training appears to have worked in the UK, but not in Gennany. The greater severity of labor market problems, and the greater inherited supplies of skilled labor, in East Germany than in the UK might well explain that – but that cannot account for the failure of publicly (as opposed to privately) funded occupational training in West Germany as well. Work-based, job-oriented training appears to have helped participants to find employment in the UK, but not to a greater extent than has occupational training conducted off-the-job, and it is more prone to displacement-related losses in the aggregate.

### *Equity*

The assistance provided by British training programs to participants may be

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<sup>15</sup> Work-based training, confined largely to *Einarbeitung*, accounted for only 8 % of East German trainees in 1993 (Table 13.1, above), as compared to 44 and 39 % in ET and JTS respectively (Payne *et al.*, 1996, Table 2.1; 1999, Table 2.2.).

valued on grounds of equity as well as efficiency, to the extent that participants are drawn from the socioeconomically disadvantaged. Similarly, even if East German programs have not improved labor market prospects for participants, they may at least have made them better off during the program than they would otherwise have been.<sup>16</sup> In such cases, equity-related benefits are particularly important, although by themselves they do not justify providing training, as opposed to simply income support, which costs less.

The presence of equity benefits depends on two conditions. Were participants disadvantaged, economically and socially? If so, did the program make them better off, taking account of the participation period, not just subsequent labor market experience?

Evaluation research often provides evidence on the first question, by way of the participation equations estimated as part of controlling for selection bias. A mixed picture emerges. In the UK, participants have been characterized disproportionately by an absence of vocational qualifications, a history of frequent and long-term unemployment and membership of a racial minority – criteria all associated with disadvantaged status. At the same time, selection into the two programs with a work-based component (ET and TFW) was slanted towards the more educated, reflecting the interest of sponsoring employers in picking the more promising trainees. Similarly, JTS participants included many female re-entrants to the labor force, whose economic circumstances were unlikely to have been as dire as those of the long-term unemployed.

In East Germany, participation was slanted towards females and the previously unemployed – groups particularly prone to unemployment. Again, however, participants tended to be more highly educated than non-participants, consistent with the high educational requirements of occupational training in Germany and the widespread need of even skilled workers for training to help them deal with the changed requirements of the post-unification job structure.

Neither the British nor the East German programs have therefore been as strongly oriented towards disadvantaged workers as have most of their US counterparts, although taken as a whole they too have probably redistributed resources towards the less advantaged.

The second question concerned the effect of participation on income during training. Evidence on this has typically not been provided by European evaluations, unlike their American counterparts. In the US, the widespread absence of entitlements to unemployment or welfare benefits means that programs that provide training allowances tend to increase incomes during participation. In other countries, including Sweden and Korea, participation in training can improve current income by renewing or

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<sup>16</sup> The Supported Work Demonstration program for disadvantaged youth in the US showed similar attributes: no improvement in subsequent labor market prospects, but a gain in income during the program (Ryan and Büchtemann, 1996, Tables 2,3).

extending entitlement to unemployment benefits. In East Germany and the UK, however, the rules for benefit eligibility suggest that participation probably had little effect on incomes. In Germany, participants remained eligible for their normal unemployment-related benefits. Only the few who gave up a job that might have been expected to last – an unattractive move, particularly under the circumstances of the time and place – in order to take training therefore faced lower incomes. In the UK, under JTS, although fully 83% of participants received a public training allowance, 39% saw their living standards as having been reduced by participation." Under ET and TFW, things were simpler: participants received any unemployment benefit to which they were entitled plus a training premium of £10 (around 20,000 won) per week – which should have made them better off than had they not participated, but not so strongly as to induce many to participate purely to receive the income.

In sum, German and British programs show equity benefits, in that they tended to serve the disadvantaged disproportionately and make them better off than they would otherwise have been. Their main contribution may well have been to stir the unemployment stew, breaking down the 'dumplings' of long-term unemployment into the 'lumps' of short-term unemployment. To the extent that the pain of unemployment is distributed less unequally as a result, equity improves; to that extent that the total pain caused by unemployment is also reduced, efficiency does too.

## **Korean Training Programs**

Like East Germany in 1990, Korea experienced in 1998 a rapid growth in unemployment in the aftermath of a major external shock. Employers made use of their enhanced discretion to lay off workers, particularly those employed on temporary and daily contracts. Unemployment rose to 8.4 % early in 1999, since when it has declined markedly (KLI, 1999). Although the peak unemployment rate was well below those of the UK in the 1980s and East Germany in the 1990s, the low coverage, limited benefits and tight eligibility requirements of the emergent Employment Insurance System meant large increases in inequality, poverty and hardship (Y.-b.Park 1999).

As in East Germany, public intervention curbed the increase in unemployment. Active labor market policies alone covered during 1998 more Korean workers than were formally unemployed (1.60 and 1.46 million, respectively; KLI, 1999; OECD, 1999, Table 39). In Korea too, training played an important but not a dominant role in labor market policy. Participation in training as a whole expanded eight-fold between 1997 and 1998 (Table 13.7). Training accounted in 1998 for 21% of participants in, and 36% of public

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<sup>17</sup> Data taken from an unpublished interim report, kindly provided by Joan Payne.

expenditure upon, active labor market policy (*ibid.*).

### *Program Attributes*

These training programs built upon and extended the existing training system. Established programs, including Employment Promotion (here EPTU) for the uninsured unemployed and Manpower Development, expanded strongly (Table 13.7). The fledgling program for the insured unemployed, Re-employment Training (here RETU), expanded particularly dramatically, moving during 1997-98 from the smallest to the largest training program for the unemployed. New training programs were created specifically to cater to displaced urban workers prepared to return to farming, those who had just lost their jobs, and those interested in forming their own businesses.

In practice, these programs overlap considerably. The two largest, RETU and EPTU, differ more in the constituencies they serve and the income they provide to participants than in the services on offer. Taking the three main programs as a whole, breakdowns by participant attributes indicate that they have served a broad clientele, in terms of sex, age, schooling and previous occupation, and that a wide range of destination skills has been involved (Table 13.8).

Has the distribution of training been equitable amongst the unemployed? A comparison of the attributes of trainees in mid-1998 with those of the unemployed in 1998 as a whole suggests that participation was broadly representative of the unemployed in terms of sex; that it was slanted

**Table 13.7: Training activity by program in Korea, 1997 and 1998**

Program	1997 (persons)	1998 (persons)
Re-Employment Training For The Unemployed (RETU)	1,900	162,400
Employment Promotion Training For The Unemployed (EPTU)	25,900	96,600
Other :		
<i>Agricultural Returners</i>	0	4,100
<i>Newly Unemployed</i>	0	36,600
<i>Business Startups</i>	0	11,600
<i>Manpower Development</i>	14,400	28,400
Total	42,200	339,800

Source. OECD (1999), Table 40.

**Table 13.8: Attributes of training participants and of unemployed workers in Korea, 1998**

		Trainees' (%)	Unemployed (%)
		June 30, 1998 (stock)	1998 (annual mean)
Sex	Male	66.5	67.4
	Female	33.5	32.6
Age	<30 years	41.2	41.9
	30-49	51.2	43.9
	50+	7.6	14.2
Schooling	0-12	55.7	80.4
	>12	44.3	19.5
Program	RETU	43.9	n.a.
	EPTU	41.7	
	Manpower dev.	14.4	
Occupation (previous)	Office/clerical	57.0	n.a.
	Production	43.0	
Occupation (training)	Machinery	20.1	n.a.
	IT	16.7	
	Service	16.6	
	Management	17.2	
	Other	5.6	

Note : n. a.: not applicable or not available

1) participants in the three principal public training programs only (Table 13.7, above)

Sources: Ministry of Labor, Korea (January 1998). *Training for the Unemployed*.

OECD (1999), Table 35.

moderately towards the middle-aged rather than older workers; and that it was slanted quite strongly towards the more educated (Table 13.8). The two latter differences marked East German programs as well. Differences in participation rates by age and education may reflect differences in interest in training, but they may also reflect differences in the availability of training, amongst eligible workers.

Further information on the attributes of Korean training programs is available from a recent evaluation study (Kang and Lee, 2000), covering the training received during 1998 by samples of around 1,000 participants in the two main programs (RETU and EPTU).<sup>18</sup> Nearly two-thirds of sample

<sup>18</sup> The sample's representativeness of trainees as a whole remains unclear. Although the authors sought a randomized selection of participants, they depended on local Employment Service offices to provide names of EPTU participants. At that stage, randomization may not have prevailed over any inclination on the part of public officials to select successful or otherwise more attractive participants. The likelihood that sampling was non-random is increased by the disproportionately high share of females, and low share of young people, in the resulting

participants were married, around one-third were heads of households. Roughly one half of trainees had been out of work for at least six months before participating, though many, particularly female EPTU participants, had been economically inactive. As many as nine-tenths of the previously employed had worked under temporary or daily contracts.

In terms of training itself, the average duration of participation in the two main programs amounted to 5 months, a period similar to that of the UK but less than half that in East Germany. Completion rates averaged around 90 %. Approximately one-fifth of RETU participants, but almost no EPTU ones, took two training courses. Around two-thirds of participants were trained by private institutions, with RETU and EPTU diverging markedly, at 36 and 90 % respectively. As has traditionally been the case for Korean vocational education and training (OECD, 1998), almost nobody was trained on the job or at the workplace. Only one in ten trainees reported having received guidance or counseling from the public employment service, and only one in four from a training provider. Around one in four expressed dissatisfaction with their access to particular counseling services, while more than one half criticized the job search and introduction services, if any, that had accompanied their training (ibid., Tables 7, 9, 12, 13, 17, 18, 19, 22).

Income during training appears to have differed greatly according to program. RETU participants received their benefit entitlement under the EIS system. Participation allowed them to extend their period of benefit eligibility, providing a potentially important motive for participation amongst unemployed workers without interest in or need for training (Yoo, 1999). The same applies, albeit to a lesser extent, to EPTU participants, who do not enjoy EIS coverage, and who have been eligible only for a low training allowance. Those who accept training for traditional manual work in '3-D' occupations have received a special training allowance intended to counter aversion to that kind of work. Although training allowances have not been high relative to average earnings, the limited alternatives available to many of the jobless mean that their training-based incomes probably made many participants better off during training.

Some potentially important attributes of training remain unclear – notably the extent to which trainees acquire recognized vocational qualifications, which may help them find work and raise their pay; the balance between upgrade training, retraining and remedial training; the quantity and quality of training received; and trainee satisfaction with training. On the latter score, a mixed picture may be inferred from the finding that, while 93 % of public trainees interviewed by a 1998 survey rated the quality of their training as 'good' or better, 83 % criticized its scope or effectiveness (Kim *et al.*, 1998).

In sum, Korean training programs have resembled their East German counterparts of the early 1990s in terms of the rapidity of their expansion,

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sample compared to the overall trainee population (Kang and Lee. 2000, Tables 3,6,7; Korean Ministry of Labor 1998).

their initial emphasis on breadth of coverage at the expense of depth of learning, their reliance upon training divorced from the workplace, and the range of participants covered and of training courses provided. The parallel is ominous, given that German training programs appear not to have improved participants' labor market prospects.

### *Program Evaluation*

Have Korean training programs worked? Employment rates immediately after training have been low, indeed no higher than employment rates for the non-participant unemployed. Policy failure has been widely inferred in Korea as a result (section 1, above). The evidence is indeed less than encouraging, but gross outcomes, such as post-training employment rates, cannot indicate the contribution of training (section 3, above).

More direct evidence has recently been provided by a quasi-experimental evaluation of the main program (RETU; Kang and Lee, 2000).<sup>19</sup> The evaluation focuses on an employment-related outcome, the transition rate to employment nine to fifteen months after training, for 1,000 unemployed workers who had separated from employment between mid-1997 and the end of 1998 and who had participated in a RETU course during 1998. The comparison group, comprising around the same number of unemployed workers, comprised those who had also separated from a job in the same period but who had not taken training during 1998.<sup>20</sup>

As the participant and comparison groups differed significantly in terms of age, education, marital and household status (*ibid.*, Table 6), regression analysis was used to control statistically for those differences, within a proportional hazards model of the time path of the probability of leaving unemployment for employment after training.

In terms of gross outcomes, the two groups' experiences were quite similar: roughly 40 % of each was in employment at the end of the observation period, and around 50 % had held a job by then (*ibid.*, Tables 18,19). Regression analysis suggests however that, controlling for the observed attributes of the two groups, the probability of moving into a job after training is significantly higher for trainees than for non-participants

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<sup>19</sup> The absence of any administrative data from which information on eligible EPTU non-participants might be derived made it impossible to evaluate EPTU and RETU together, as would clearly have been preferable.

<sup>20</sup> It is not known how many of those workers received other services, including non-RETU training and job creation; to the extent that some did, the benefits of RETU training are underestimated (contamination bias). Similarly, the decision to exclude non-participants who found a job during the time that participants were in training, as well as to ignore job finding during training by participants (the 'no job search during training assumption' which ignores the 4 % of sample participants who dropped out to take employment; Table 17), distorts the comparison of outcomes between the two groups – biasing the estimated benefits of training upwards and downwards respectively.



(*ibid.*, Table 24). The training effect is found however only for females, for whom training is estimated to have increased the probability of moving into work by more than one half. For men the estimate is positive but insignificant.

The evidence suggests therefore that Korean training programs have indeed helped their participants, at least the females amongst them. But it cannot be treated as conclusive. The load upon regression analysis in correcting for large differences in measured attributes of the participant and comparison groups is increased by the absence of any close matching on those attributes. Moreover, while the set of measured attributes is no smaller than in most evaluation research, it also excludes such potentially important ones as ability and motivation, around which selection into training may well have occurred. As the econometric model does not address that endemic problem, uncontrolled selection bias may well account for part or all of the benefits attributed to the training itself.<sup>21</sup>

Korea's first proper evaluation study has underlined the inadequacy of short-term gross outcomes and suggested that training may have worked, in the specific sense of improving access to employment for participants. The robustness of the conclusion is open to question, and, even if it is firmly grounded, consideration would also have to be given to both any losses incurred by displaced non-participants and to the costs of training before giving public programs the 'thumbs up'. But the case for public training programs at least remains alive in the Korean context – as does that for further evaluation research, building on a promising start.

## Conclusions

The merits of public training programs as a response to mass unemployment and long-term unemployment remain uncertain, despite a voluminous evaluation literature. This paper has surveyed the evidence for two advanced economies with extensive experience in the field: Germany and the UK. The emphasis has been placed on the policies addressed to mass employment in the 1990s in East Germany and long-term unemployment in the 1980s in the UK.

The results prove mixed. The East German training effort appears to have failed its participants, notwithstanding its high cost and its orientation to occupational skills. British programs have, by contrast, helped their participants to find work and – when accompanied by occupational training and vocational qualifications – improve their earning power. In both countries, training programs have tended to make a clientele that exhibited a

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<sup>21</sup> The findings may also be distorted in favor of training by the lack of any correction for the time that trainees spend in training, but non-participants do not, during which re-employment rates were presumably depressed for trainees relative to non-participants.

variable degree of socio-economic disadvantage better off while participating in training than it would otherwise have been in unemployment – though simple income support offers a cheaper way of doing so, were that the only benefit. The pattern of results is however too varied by country and type of training to generate a coherent account spanning the two countries' experiences. The implications for Korean policy are correspondingly limited.

Given that, the advent of evaluation research devoted to Korea itself is particularly welcome. The first formal evaluation of a Korean program suggests that training has increased employment prospects for its participants, particularly for females. The conclusion is potentially sensitive to choice of data and modeling technique, and problems of aggregation and cost-benefit comparisons remain to be addressed. The door has however been opened to further research, which may provide a more coherent picture than has emerged for Germany. The pessimistic alternative, however, has to be acknowledged: unless a well-designed social experiment is used, evaluation research, however sophisticated, cannot lay claim to the robustness required for effective policy making.

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**LABOR MARKET AND GENDER**



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# 14 Were Korean Women More Affected by the Asian Crisis?\*

Kye Woo Lee"  
Kisuk Cho\*\*

## Introduction

Between June and December 1997, a group of newly industrialized Asian countries were hit by a severe financial crisis. Compared with the recent financial crises in other regions, the depth and the costs of this crisis were much more serious. The stock market tumbled, and the national currencies depreciated drastically. During the crisis period, equity prices in Korea dropped by 51 %, and those in Indonesia and Malaysia declined by 45 %. Nominal exchange rates in Indonesian rupiah increased by 122 %, and in Korea, the won depreciated by 80 %. Non-performing loans accounted for between 35 to 75 % of the banking system's total loans, with resolution costs estimated at 45 to 60 % of GDP, and Korea's GDP itself declined by 6.7 % in 1998. The contagious Asian financial crisis aggravated the already distressed Russian economy, negatively affected Latin American economies, and subsequently threatened the stability and growth prospects of the world economy (K. Lee, 1999).

The crisis, which started in the financial sector, quickly spread to the real sectors of the economy, which in turn adversely affected the labor market. The stable unemployment rate of 2.0 % in 1995 and 1996 rose to 2.6 % in 1997 and 6.8 % in 1998, and finally reached 8.6 % in February 1999. Accordingly, the number of unemployed people increased from the 1996

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base figure of 426,000 to about 1.5 million in 1998. By comparison, the World Bank's unemployment forecast was around 850,000 persons. This enormous gap between the forecast and actual unemployment levels is indicative of the severe impact of the crisis on the labor market. This incremental unemployment resulted from bankruptcies, downward adjustment of existing firms, and the economy's inability to absorb new entrants into the labor force.

From the onset of economic reconstruction, experts from international organizations advised the Korean government to pay special attention to the strengthening of social safety nets, especially for the most vulnerable groups of society, such as women, children, and the poor (E. Lee, 1998). As observed in previous crises elsewhere, these groups might bear the brunt of adjustment costs. The measures to ease the social costs of adjustment would complement the other structural reforms and help mobilize social and political consensus on the adjustment process. Scholars and social activists, as well as feminist leaders, expressed concerns about the socially underprivileged groups, especially women, and called for special action programs to protect them.

The purpose of this paper is to analyze the effect of the Asian economic crisis on women in the Korean labor market in comparison with the pre-crisis situation. Particular emphasis will be placed on two questions: (a) Were women more adversely affected than men? and (b) If so, did men discriminate against women? In the following section, we will compare labor market experiences between male and female workers. For this purpose, nation-wide official survey statistics will be analyzed.

This study has found that it is difficult to state categorically that female workers were more adversely affected than male workers. The crisis affected both male and female workers adversely. However, one can safely conclude that female workers had different experiences in the labor market, especially in terms of involuntary disengagement and rehiring status, and were continuously treated differently with regard to labor earnings compared to before the crisis. From these findings, some observers may quickly conclude that the different gender experiences reflect gender discrimination. Therefore, we will next briefly review literature on the theories of gender discrimination to find out which theory most accurately explains the different gender experiences in the Korean labor market. The ensuing sections will test the theories on the basis of nation-wide official survey data published by the National Statistics Office and the Ministry of Labor, as well as a set of regional data collected through a field survey specially designed for this study. The final section will suggest future labor market policies based on the findings.

## Women in the Labor Market

To compare the labor market experiences of males and females before and after the eruption of the economic crisis, five labor market indicators are selected for analysis: labor force participation, unemployment, employment, involuntary disengagement (in particular, dismissals), and labor earnings. Through the analysis of these indicators, it should be possible to state whether female workers experienced greater hardship than their male counterparts.

### *Labor Force Participation*

Before (in 1996 and 1997) and after (in 1998) the Korean economic crisis, the size of the population 15-years of age and older increased by about 1.5 % per year. However, the economically active population (labor force) decreased by 1.0 %, in contrast to an increase of 2 % in 1996 and 1997 (National Statistics Office, 1998 and 1999). This drop originates mainly from the drastic decrease of 3.7 % (329,000 persons) among females, which more than offset the increase of 0.9 % (121,000 persons) among males. Accordingly, the labor force participation rate decreased from 62.2 % in 1997 to 60.7 % in 1998, with this decrease being more pronounced among females (from 49.5 % to 47.0 %), than among males (from 75.6 % to 75.2 %). As a result, the increase in the population of economically inactive females was 6.5 % (585,000 persons), compared with 3.4 % (141,000 persons) for males (Table 14.1).

### *Unemployment*

One of the most noticeable changes between the pre and post economic crisis periods was the sharp increase in unemployment rates from 2.6 % to 6.8 %. This increase was more dramatic among males (from 2.8 % to 7.6 %) than among females (from 2.3 % to 5.6 %). Consequently, females' share of total unemployment declined from 36.7 % in 1997 to 32.7 % in 1998 (Table 14.1). On the basis of unemployment statistics alone, therefore, it is difficult to accept the argument that the economic crisis affected female workers more adversely than male workers.

However, some labor market analysts argue that these unemployment rates mask a more serious unemployment situation among females than males for several reasons. First, employment decreased faster among females (by 602,000 persons) than males (by 510,000 persons), i.e., by 6.9 % for women versus 4.1 % for men between 1997 and 1998. Consequently, females' share of total employment declined by one percentage point. Second, the stark increase in the economically inactive population among females versus males (by 6.5 % vs. 3.4 %) may reflect a lopsided

increase in the hidden female unemployed -- female workers who were so discouraged by employment conditions that they withdrew from the labor force entirely. This may explain the sharper drop in female labor force participation rates than those of males in 1998. Some researchers estimate hidden unemployment at as high as 90 % of those who lost jobs, with only 10 % of them remaining as open unemployment in the labor market (D. Kim, 2000). Other researchers estimate that if hidden unemployment were included, the female unemployment rate in 1998 would increase to 11.4 % and would be higher than the male unemployment rate of 9.5 % (T. Kim and Y. Moon, 1999) (Table 14.2).

**Table 14.1: Economically active population, employment and unemployment in Korea, 1996-1998**

	1996	1997	1998	Change over the year		
				1995-96	1996-97	1997-98
	(000's)					
<i>Population &gt; 15 years-old</i>	34,285	34,842	35,362	621(1.8)	557(1.6)	520(1.5)
Male	16,612	16,888	17,150	-	276(1.7)	262(1.6)
Female	17,674	17,955	18,211	-	281(1.6)	256(1.4)
<i>Econ. active pop.</i>	21,243	21,662	21,456	390(1.9)	419(2.0)	-206(-1.0)
Male	12,636	12,772	12,893	-	136(1.1)	121(0.9)
Female	8,607	8,891	8,562	-	284(3.3)	-329(-3.7)
<i>Employment</i>	20,817	21,106	19,994	-	284(1.4)	-1112(-5.3)
Male	12,345	12,420	11,910	-	79(0.6)	510(-4.1)
Female	8,472	8,686	8,084	-	205(2.4)	602(-6.9)
<i>Unemployment</i>	426	556	1,461	-	130(30.5)	905(162.8)
Male	291	352	983	-	61(21.0)	631(179.3)
Female	135	204	478	-	69(51.1)	274(134.3)
<i>Econ. inactive pop.</i>	13,043	13,180	13,906	232(1.8)	137(1.1)	726(5.5)
Male	3,976	4,116	4,257	152(4.0)	140(3.5)	141(3.4)
Female	9,067	9,064	9,649	80(0.9)	-3(-0.0)	585(6.5)
<i>Labor force participation rate (%)</i>	(62.0)	(62.2)	(60.7)	(0.1P)	(0.2P)	(-1.5P)
Male	(76.1)	(75.6)	(75.2)	(-0.4P)	(-0.5P)	(-0.4P)
Female	(48.7)	(49.5)	(47.0)	(0.4P)	(0.8P)	(-2.5P)
<i>Unemployment rate (%)</i>	(2.0)	(2.6)	(6.8)	-	(0.5P)	(4.2P)
Male	(2.3)	(2.8)	(7.6)	-	(0.5P)	(4.8P)
Female	(1.6)	(2.3)	(5.6)	-	(0.7P)	(3.3P)
Female's share	(31.7)	(36.7)	(32.7)	-	(5.0P)	(-4.0P)

Note: Numbers in parentheses are changes in %, and "P" indicates %age points.

Source: National Statistics Office, Korea (1997-1999). 1996-1998 Annual Report on the Economically Active Population Survey.



**Table 14.2: Unemployment (including Hidden Unemployment) in Korea, 1996-1998**

	<b>Total</b>	<b>Male</b>	<b>Female</b>	<b>Total</b>	<b>Male</b>	<b>Female</b>	<b>Female share</b>
	('000)			(%)			(%)
1996	628	362	266	3.0	2.9	3.1	42.4
1997	903	466	437	4.2	3.6	4.9	48.4
1998	2,197	1,223	974	10.2	9.5	11.4	44.3

Source: Kim and Moon (1999)

However, if hidden unemployment were included, female unemployment rates would be higher than male rates even before the economic crisis, and females' share of total unemployment would decline from 48.4 % in 1997 to 44.3 % in 1998 since male unemployment increased more sharply than female unemployment. Therefore, on the basis of unemployment rates alone, it would be difficult to come up with an unequivocal judgement on whether the 1997 economic crisis affected female workers more severely than male workers.

Using panel data constructed on the basis of the economically active population of 1995-1998, D. Kim (2000) reached more or less similar conclusions. He also shows that if the unemployment spell is measured not only by the employment rate of the unemployed, but by the transition to the economically inactive status, including hidden unemployment (those unemployed who decided to drop out of the labor force entirely), female unemployment spells were shorter than those of males (Tables 14.3 and 14.4).

**Table 14.3: Estimated unemployment spell based on employment rates alone in Korea, 1996-1998**

	1996	1997	1998
	(months)		
<b>Total</b>	3.9	4.5	5.3
<b>Male</b>	4.2	4.6	5.3
<b>Female</b>	3.4	4.5	5.4

Source: D. Kim (2000)

**Table 14.4: Estimated unemployment spell (including transition to economically inactive population) in Korea, 1996-1998**

	1996	1997	1998
	(months)		
<b>Total</b>	3.0	3.1	3.2
<b>Male</b>	3.3	3.4	3.5
<b>Female</b>	2.5	2.8	2.6

Source: D. Kim (2000)

On balance, one can conclude that although unemployment rates do not support the hypothesis that female workers were more adversely affected than male workers during the Asian crisis, female workers also suffered acutely.

### *Employment*

Although unemployment rates were higher among male workers than females after the economic crisis, the level of female worker employment declined more rapidly than that of male workers, suggesting that the Asian crisis inflicted greater damage on the level of female worker employment. Between 1997 and 1998, male employment declined by 510,000 workers (-4.1 %), but female employment dropped by 602,000 workers (-6.9 %) (Table 14.2). Consequently, female's share of total employment declined by one percentage point.

These seemingly contradictory phenomena of a sharper decline in female employment, yet a lower female unemployment rate arose partly because new male entrants into the labor force experienced greater difficulty in getting jobs than their female counterparts (Table 14.7). But a more important aspect of the explanation is that once female workers lost their jobs, they were more inclined to withdraw from the labor market than their male counterparts, as shown in the sharper increase in the economically inactive population among females than males. D. Kim's (2000) panel data support this argument. His panel data study confirms that since the outbreak of the economic crisis, employment rates among the unemployed declined among both male and female workers and reached more or less the same level (around 22 %) in 1998. One difference is that the reemployment rate was higher among female workers before the crisis. Therefore, after the crisis, female reemployment rates declined more rapidly than those of male workers. One more important difference is that job-seeking rates were lower among unemployed females than among unemployed males since unemployed female workers were more likely to withdraw from the labor force as their employment rate shrank.

Interestingly, female employment fell relatively deeper in those industries and occupations where female workers were more represented, and male workers' share in those industries and occupations increased after the economic crisis. This is indicative of some degree of substitution of male workers for female workers during the economic crisis. For example, while employment of male workers increased in the electricity, transportation, storage, and finance industries, as well as in those businesses and services where female workers were relatively more represented, the number of female workers in these industries declined (Table 14.5). By occupation, while male workers increased in administration, service, and sales occupations, where female workers were predominant before the crisis, the number of female workers employed in these occupations declined sharply

**Table 14.5: Employed persons by industry in Korea, 1997-1998**

	Change over the year, 1997-1998					
	Total		Male		Female	
	Change ('000)	Change rate (%)	Change ('000)	Change rate (%)	Change ('000)	Change rate (%)
Total	-1,112	-5.3	-510	-4.1	-602	-6.9
Agr., forestry & fish.	95	4.0	63	5.1	31	2.7
Mining & manuf.	-589	-13.1	-335	-11.5	-253	-15.8
<i>Manufacturing</i>	-584	-13.0	-332	-11.5	-252	-15.8
Social overhead capital & other services	-618	-4.3	-238	-2.9	-381	-6.4
<i>Construction</i>	-426	-21.3	-352	-19.7	-74	-34.1
<i>Wholesale/retail</i>	-234	-4.0	-34	-1.2	-201	-6.6
<i>restaurants &amp; hotels</i>						
<i>Electricity, transport</i>	-8	-0.4	32	2.3	-41	-7.1
<i>Storage, finance</i>						
<i>Business, private &amp; public services and others</i>	49	1.1	113	4.9	-66	-3.2

Source: National Statistics Office, Korea (1999), 1998 Annual Report on the Economically Active Population Survey.

**Table 14.6: Employed persons by occupation in Korea, 1997-1998**

	Change over the year, 1997-1998					
	Total		Male		Female	
	Change ('000)	Change rate (%)	Change ('000)	Change rate (%)	Change ('000)	Change rate (%)
Total	-1,112	-5.3	-510	-4.1	-602	-6.9
Professionals, technicians	48	1.3	32	1.2	15	1.4
Administrative workers & clerks	-154	-6.0	78	6.5	-232	-16.9
Service/sales workers	-132	-2.7	24	1.3	-156	-5.2
Skilled agr. and fish. workers	91	4.0	62	5.2	30	2.8
Craft, plant & machine operators, elementary occupations	-965	-12.5	-706	-12.9	-258	-11.6

Source: National Statistics Office, Korea (1999), 1998 Annual Report on the Economically Active Population Survey.

since the crisis (Table 14.6).

By employment status, male workers maintained their status before and after the crisis. However, among regular (permanent) workers, the proportion of female workers declined (from 37 % to 32 %), while among daily workers, female workers' share rose substantially (from 16 % to 21 %). This suggests that some of the former "regular" female workers might have shifted their employment status from "regular" to "daily" workers (Table 14.7).

Using the panel data, Y. Ahn (2000) confirmed similar findings in a dynamic context. In the case of males who lost regular jobs, 38 % once again found regular jobs. By contrast, only 31 % of female workers landed regular jobs. While 22 % of the males who lost regular jobs found non-regular jobs, 26 % of females landed non-regular jobs. This non-regularization of female workers has been reinforced by the trend among those who lost non-regular jobs. Only 6 % of the unemployed workers who lost non-regular jobs subsequently found regular jobs, and as many as 59 % of them obtained non-regular jobs. For males, these rates were 8 % and 53 %, while for females, they were 5 % and 63 %, respectively, demonstrating that female non-regular job holders found it more difficult to acquire regular jobs. These findings indicate that, after the economic crisis, female workers must have increasingly occupied a greater portion of non-regular jobs, unless this shift was offset by an opposing trend among new entrants into the labor force.

Unfortunately, the study does not report on the total number of employed

**Table 14.7: Employment status in Korea, December 1997 and December 1998**

	December 1997			December 1998		
	Total	Male	Female	Total	Male	Female
	(% )			(% )		
Economically active population	100	100	100	100	100	100
Employment	97	97	97	92	91	93
Unemployment	3	3	3	8	9	7
Employment	100	100	100	100	100	100
Wage earners	64	65	61	62	63	60
Non-wage earners	36	35	39	38	37	40
Wage earners	100	100	100	100	100	100
Regular	52	63	37	51	63	32
Temporary	34	24	47	33	24	47
Daily	14	13	16	16	13	21
Non-wage earners	100	100	100	100	100	100
Self-employed	77	96	52	77	96	51
Family workers	23	4	48	23	4	49
Unemployment	100	100	100	100	100	100
Job losers	58	63	50	75	77	72
New entrants	42	37	50	25	23	28

Source: National Statistics Office, Korea (1998-1999), *Monthly Report on the Economic Active Population Survey*.

workers by employment status. However, the nation-wide statistics on total wage earners report that the proportion of daily female workers has steadily increased from 16 % in December 1997 to 21 % in December 1998 and to 25 % in November 1999. Therefore, based on both the nation-wide and the panel data, one can safely conclude that, since the economic crisis, female workers' employment status steadily deteriorated toward non-regular jobs, which are characterized by lower wages and poorer working conditions.

### *Involuntary Disengagement*

Another study tries to analyze gender differences in unemployment, especially in the causes of unemployment, using unemployment insurance statistics (S. Cho, 1999). When a worker loses insurance membership for voluntary reasons such as old-age retirement, transfer to self-employment, disengagement due to marriage, childbirth and child rearing, continuing education, and enlistment, he/she would not be eligible for unemployment benefits. In contrast, when a worker loses membership for involuntary reasons such as redundancy, resignation at the employer's suggestion, and honorary early retirement, the worker would be eligible to receive insurance benefits. Cho, therefore, tries to analyze whether female workers became unemployed involuntarily for fair and justifiable reasons *vis-à-vis* male workers.

According to the official statistics, male workers became involuntarily unemployed more often than female workers and therefore appear to be more adversely affected by the economic crisis (Table 14.8). Cho rightly argues, however, that absolute numbers of involuntary unemployment distort the more severe effects of the economic crisis on female versus male workers. The important numbers are each gender's relative share of the 1998 involuntary unemployment among the respective total membership before the economic crisis in 1997. Based on an analysis of the relative share of both male and female involuntary unemployment by industry, occupation, age, educational attainment, and scale of enterprises, Cho argues that female workers disproportionately suffered from involuntary unemployment, and therefore suspects that there must have been gender discrimination in the course of enterprise reorganization and structural adjustment.

The share of female involuntary unemployment in 1998 among the total female members of the unemployment insurance system in 1997 (24.7 %) was greater than that of male involuntary unemployment (19.4 %). This is particularly so in those cases where workers fell into involuntary unemployment because of reorganization redundancy, suggested resignation, and other types of dismissals. In this narrow sense of involuntary unemployment, females' share was about 16 %, compared with 12 % for male workers. This suggests that female workers were selected first and more often as redundant workers in structural reorganization.

**Table 14.8: Involuntary disengagement in Korea, 1997-1998**

	Total	Male	Female
	('000)		
Total insurance membership (1997)	4,280.0	3,134.0	1,146.0
Total involuntary disengagement (1998)	891.3	608.3	283.0
(%) change from 1997	145.6	165.3	111.9
(%) of total membership in 1997	20.8	19.45	24.7
Total involuntary disengagement Including marriage, childbirth, nursing (1998)	935.6	614.0	321.2
(%) of total membership in 1997	21.9	19.6	28.0
Dismissals (1998)	572.2	389.1	183.1
(%) of total membership in 1997	13.4	12.4	16.0
Redundancy	123.8	84.6	39.2
(%) of total membership in 1997	2.9	2.7	3.4
Suggested Resignation	260.6	180.5	380.1
(%) of total membership in 1997	6.1	5.8	7.0
Other Dismissals	187.8	124.0	63.8
(%) of total membership in 1997	4.4	4.0	5.6

Source: Cho, Soon-kyung (1999)

### *Labor Earnings*

According to the 1997 and 1998 Survey Reports on Wage Structures (The Ministry of Labor, 1998 and 1999), female workers' average compensation was only 61.7 % of that of male workers in 1998. Although this is a slight improvement over 1997, when female workers' average compensation was 60.1 % of male workers' remuneration (Table 14.9). the gender gap in the average wage remained substantial between the pre and post crisis periods. Moreover, this gender gap in compensation was observed in all occupational groups.

Gender differences in compensation are also observed in the distribution of labor earnings. In 1998, while male workers with low levels of monthly compensation (below 500,000 won per month) accounted for 1.3 % of the total male workers, as many as 6.6 % of female workers belonged to this low level compensation group. Moreover, while male workers with high levels of total monthly compensation (above 2 million won per month) constituted 26.9 % of the total, only 5.5 % of female workers fell into to this group. The key issue is whether these compensation gaps between male and female workers come from gender differences in reasonable determinants of compensation (such as educational attainment, age and on-the-job experience, hours worked, etc.) or from gender discrimination.

**Table 14.9: Average labor earnings by gender in Korea, 1997-1998**

	Monthly earnings	Special annual earnings	Total compensation	Index (Male=100)
	(won in thousands)			
<i>1997</i>				
Total	1,131.6	4,105.5	17,684.7	
Male	1,261.9	4,673.9	19,816.7	100.0
Female	789.1	2,611.4	12,080.6	60.1
<i>1998</i>				
Total	1,148.1	4,152.2	17,943.5	
Male	1,274.8	4,692.0	19,989.6	100.0
Female	804.3	2,686.8	12,334.8	61.7

Source: Ministry of Labor, Korea (1998-1999).

### *Summary*

In conclusion, the impact of the Asian economic crisis on women in the Korean labor market can be summarized as follows:

First, female labor force participation rates declined more drastically than male participation rates.

Second, although female unemployment rates increased, male unemployment rates rose more sharply and reached a higher level than female unemployment rates.

Third, when hidden unemployment is taken into account, female unemployment rates still stood higher than those of their male counterparts. However, the same trend was observed even before the crisis. Moreover, male unemployment rates rose faster than those of their female counterparts, and consequently, females' share of total unemployment declined after the outbreak of the Asian crisis.

Fourth, unemployment spells were similar between male and female workers, and were even a bit shorter among female workers when their transitions to the status of economically inactive population were included.

Fifth, female workers with lower levels of education and with jobs in female-crowded industries/occupations experienced unemployment in a greater proportion than their male counterparts, and some male workers substituted female workers in those industries and occupations.

Sixth, the female employment level declined at a faster rate than the male employment level and unemployed female workers tended to withdraw from the labor force more easily.

Seventh, when female unemployed workers were reemployed, they

tended to obtain non-regular (daily) jobs more often than their male counterparts.

Eighth, incidences of involuntary unemployment were higher among males than females; however, the relative share of involuntary unemployment in total unemployment insurance memberships of each gender group was greater among females, and they suffered more from enterprise reorganization and structural adjustment.

Ninth, the average earnings of female workers were lower than those of their male counterparts, just as before the crisis.

From these findings, it is difficult to draw a definitive conclusion as to whether or not female workers suffered more from the Asian economic crisis. Both male and female workers were adversely affected by the crisis. However, one can safely conclude that male and female workers were treated differently in the labor market, especially in terms of involuntary disengagement and rehiring status during the crisis, and in labor earnings both before and after the crisis.

Some observers therefore argue that the difference in the effects of the economic crisis on men and women in the labor market originates from gender discrimination in the labor market. Hence, as a basis for formulating future labor market policies, it is natural that we review the various theories of gender discrimination and find out which theory best explains the gender differences in the Korean labor market.

## **Theories of Gender Discrimination in Labor Markets**

The existing literature on the theories of gender discrimination fall into four categories. First, we are concerned with the neo-classical economics approach, which stresses the importance of human capital. We then move on to the institutional approach, which emphasizes the structure of labor markets, in general, in terms of political and institutional factors. Third, we consider the feminist approach, which also explains the structure of the labor market in terms of political and institutional factors, but with particular emphasis on gender discrimination. Finally, we discuss the risks and costs approach in explaining gender discrimination.

### *Neo-Classical Economics Approach*

The neo-classical economics approach regards the labor market as just a commodity market where workers sell their labor and are paid according to their productivity, which is affected by human capital such as education, qualifications, training, skills, and experience. It is assumed that the behavior of rational individual workers is to maximize their wages and invest in the development of their own human capital because they expect a



fair return on this investment in terms of future earnings (Bayes, 1988). According to this precept, neo-classical economics theorists try to explain gender discrimination in the employment sphere in terms of women's rational choices and preferences in the labor market.

Becker (1985) argues that women's taste and preference for household work would make them spend less energy and time on paid work than their male counterparts, and they would therefore invest less in human capital to raise their productivity. Hence, their lower earnings can be explained. For Becker, domestic division of labor operates to achieve a full equilibrium within the household; that is, it reflects household rationality by stipulating that women are responsible for household work and other non-economic activities, and men for economic activities. Thus, crowding occurs in a relatively small number of occupations where women find it easier to combine paid work and household responsibilities, and women compete with one another in those occupations. Abundant supply of women's labor in certain occupations is a predominant factor in gender segregation of occupations. This in turn pushes their wages down in the labor market (Mincer and Polacheck, 1974; Becker, 1985; Dunn, 1996; Figart and Mutari, 1999).

However feminist critics argue that a fundamental problem with neo-classical economics theories lies in the assumption of a competitive labor market in which workers are paid according to their worth (Walby, 1990; Crompton and Sanderson, 1990). According to their arguments, neo-classical economics theorists ignore the ways in which power relations structure the labor market unequally for men and women. Occupational segregation and gender-based wage differentials appear not as a result of the rational choice of women, but as the reflection of the labor market's structural problems (Hanson and Pratt, 1995).

### *Institutional Approach*

The institutional approach challenges the neo-classical economics approach by contending that the structure of the labor market is explained not by equilibrium between supply and demand but by a number of political and institutional factors. This approach argues that through a set of administrative rules and procedures employers create segmented labor markets, between which competition is limited, as part of their strategy to enhance profit levels (Doeringer and Piore, 1971; Gordon *et al.*, 1982; Burchell *et al.*, 1994).

However, feminists have criticized that the labor market segmentation theory has developed without any significant concern given to gender since it regards that structured inequality between workers and capitalists is much more crucial than inequality between men and women (England, 1992). Moreover, it treats all female workers as secondary without considering differences among women (Hartmann, 1987; Hakim, 1995).

### *Feminist Approach*

Feminists argue that the structure of labor markets is determined by political and institutional factors (Crompton and Sanderson, 1990; Bradley, 1989). However, feminists are divided into various groups in explaining those political and institutional factors. Some place emphasis on the capitalist system of production, and others on patriarchy. Still others emphasize cultural sex-typing.

Marxist feminists see gender inequality as rooted in social class inequality. It is the capitalistic market system of production that generates social class inequality as well as women's economic dependence on men. They argue that women's inferior position and lower pay in the labor market are formed by the capital-labor relation, and that employers use women as a reserve army of labor to exploit women's labor by regarding it as cheap and disposable (Beechey, 1979). Such a strategy leads employers to replace the male labor force with women in times of economic recession.

However, scholars who explain the segmentation of Labor markets and occupational segregation have criticized this reserve army thesis. They argue that women's labor has not competed with or replaced men's labor because a large number of women have been employed in the new or expanding areas of the economy, rather than having been employed in the core areas that were traditionally recognized as being occupied by male workers (Hartmann, 1979; Collinson *et al.*, 1990).

Another group of feminists suggests that the structure of the labor market must be analyzed and explained in relation to patriarchy (Hartmann, 1979; Walby, 1990). Employers and male-dominant unions largely exclude women from certain occupations by generating gender-based internal labor markets and controlling access to jobs and training. Female labor does not compete with male labor due to patriarchal strategy of employers and unions.

Other feminists consider such structures of labor markets in relation to sex-typing. Cultural distinctions between male and female work bring about discrimination in the workplace because the work done by women is devalued (Bradley, 1989; Crompton and Sanderson, 1990; England, 1992; Ridgeway, 1997). Thus, women's career ladders tend to be shorter than those of men, and a majority of women are concentrated in the secondary labor market.

### *Labor Market Risks and Costs Approach*

A theory of statistical discrimination is set up under the premise that rational employers do not have any specific taste or preference, but rather are generally oriented towards maximizing profits. Gender discrimination occurs as they estimate a degree of risk in a world of imperfect information. For employers, it is difficult to measure *individual* worker's productivity, but differences in *average* productivity between groups of workers are

known to employers. Thus, a profit-maximizing employer seeks the most productive workers to fill jobs which require future training, and he/she would prefer to hire workers who have a higher probability to stay on the job longer and contribute themselves to a rise in productivity (Perlman and Pike, 1994). Since the majority of women will have children and, hence, take maternity leaves or give up their jobs, employers may believe that the average turnover rate of women will be higher than that of men (Banton, 1994). The main point of this argument is that women are discriminated against in comparative labor markets as their work discontinuity, caused by childbirth and child rearing, may bring about, statistically, a greater risk of low productivity, and impose high turnover costs on the employer.

A corollary to this theory of statistical discrimination is the theory of motherhood protection costs. During the Asian crisis, some argued that the ever increasing costs of protecting female workers might have prevented employers from treating female workers equally and resulted in de facto discrimination against women (The World Bank, 1999). As a basis for their hypothesis, they argue that the legal provisions for protecting women workers in Korea are above the international standards. Moreover, the laws place the burden of financial responsibilities for protecting motherhood exclusively on employers. This indicates a stark contrast with international practices, by which financial responsibilities for most protective measures are shared among the state, employers and employees under a social insurance scheme. Thus, they have argued that employers shy away from hiring women or pay women less to avoid the ever-increasing costs of complying with the legal provisions for protecting motherhood.

Indeed, with the advent of the civilian government, which took power in 1987, the outspoken trade unions' and proliferating women's inovements put huge pressure on the government. The late 1980s thus witnessed a series of legislative actions to enhance motherhood protection and gender equality as a sharp reaction to employers' negligence or exploitative practices in the past (E. Lee, 1996). In 1987, the Equal Employment Law was promulgated to improve gender equality in recruitment, training, promotion, assignment, retirement, and dismissal. The amendment to the Equal Employment Law in 1989 ensures equal pay for work of equal value, which was not declared in the 1987 law. The 1989 amendment also broadened its coverage from those enterprises with more than ten workers to those with more than five workers. The 1989 and 1995 amendments not only guarantee gender equality in employment, but also make gender discrimination by employers legally punishable. The Law prohibits employers not only from demanding certain standards of appearance, weight and height (article 6), but also from discriminating against marital status or gender (article 8). For motherhood protection, the Equal Employment Law guarantees women (or their spouses) with a child under one year of age "childcare leave" of up to one year, which is counted as a working period when the worker's eligibility for other benefits is considered (article 11). This has significant repercussions on

other types of benefits such as severance and pension payments. The law also requires employers to provide childcare facilities or allowances to help women continue working after childbirth (article 12). According to International Labor Organization (ILO) conventions (No. 156), this responsibility is imposed not on employers but on the government, which is to develop and promote public and private facilities. The 1989 amendment to the Labor Standards Law also made it more difficult for employers to assign night work to women by requiring not only the approval of the Labor Minister, as in the past, but also the consent of employees.

Those provisions of the Equal Employment Law are over and beyond those of the Labor Standards Law, which have already required more of employers than do the ILO conventions. For example, under the Labor Standards Law, employers should provide a 60-day maternity leave with 100 % regular earnings (article 72). This compares with the ILO convention (No. 103) which stipulates that two-thirds of regular earnings should be provided not by the employer, but rather either by the means of compulsory social insurance or public funds (E. Kim, 1994). The law also requires employers to provide female workers a one-day menstruation leave per month with full regular earnings (article 71), or extra compensatory payments in lieu of the leave. This provision is a result of the 1989 amendment, which forces employers to grant such leave irrespective of a female worker's request or not. Neither ILO conventions nor provisions of many advanced countries mention the menstruation leave, let alone payments. Only a few countries require such leave by law (e.g., Japan and Indonesia) and define it as an unpaid leave. Some feminist scholars and advocates suggested that menstruation leave should be eliminated, and instead a fetal check-up leave should be introduced (The Women's News, 1999). In addition, the Labor Standards Law banned women's night work, work on holidays, and underground work in any mine, without taking into account any specific circumstances. While ILO conventions (Nos. 45 and 89) allow exceptional cases, the Labor Standards Law permits exceptions only with the consent of the workers concerned and approval of the Ministry of Labor.

Although the aims of such provisions are to protect family life and the social reproductive system, the financial responsibilities for implementing such provisions in Korea are imposed exclusively on employers. While provisions for social welfare have increasingly caught up with the trend of advanced countries and have even exceeded the international standards in some cases, the mode of financing the welfare system has not kept up with international practices and has placed exorbitant costs on employers. Therefore, it may be inevitable for a rational entrepreneur to avoid hiring more women and to treat female workers differently from male workers, especially when the going gets tough as during the Korean financial and economic crisis.

## Empirical Tests of Discrimination Theories

### *Test of the Neo-Classical Approach*

To test the validity of the neo-classical economics approach, representative variables for human capital were obtained from the government's *1998 and 1997 Survey Reports on Wage Structures*.

A function of the human capital approach to labor incomes is expressed as follows:

$$Y_{ji} = X_{ji} + \sum r_{it} C_{it} \quad (14.1)$$

That is, earnings of individual  $i$  in period  $j$  ( $Y_{ji}$ ) are expressed as the sum of the returns ( $r_{it}$ ) of all his/her previous net investments ( $C_{it}$ ) and the earnings from his/her original endowment ( $X_{ji}$ ). In the current application, the schooling and on-the-job experience model is employed, following Mincer's approach (Mincer, 1979). That is:

$$\log Y = a_0 + a_1E + a_2T + a_3T^2 + a_4G + e \quad (14.2)$$

where  $Y$  is the average annual earnings,  $E$  is the number of years of formal schooling,  $T$  is the number of years of on-the-job training or experience, and  $G$  is a dummy variable for gender. This equation has been estimated for each and all occupations in 1997 and 1998. Nine occupational categories have been used in the analysis: managers, professionals, technicians, clerks, service workers, agricultural and fishery workers, crafts, plants and machine operators, and elementary occupations.

The results for all occupations in 1997 and 1998 are as follows (numbers in parenthesis are t-statistics).

#### **1997**

$$\ln Y = 13.027 + 0.064E^{***} + 0.078T^{***} - 0.002T^{2***} - 0.299G^{***} + e \quad (14.3)$$

(4629.415) (312.425) (322.420) (-149.994) (-240.755)

$R^2 = 0.555$       d.f.: 403742

#### **1998**

$$\ln Y = 12.936 + 0.069E^{***} + 0.077T^{***} - 0.001T^{2***} - 0.214G^{***} + e \quad (14.4)$$

(4377.263) (321.657) (304.476) (-133.614) (-0.282)

$R^2 = 0.566$       d.f.: 383610

As illustrated, approximately 56 % and 57 % of the observed variations in earnings have been explained by differences in educational attainment, on-the-job experience, and gender. Coefficients of all variables are significant at

a high level of probability; at less than either the .01(\*\*) or .001(\*\*\*) level and only a few are at the .05 ( ) level. Those unexplained parts (44 % and 43 %) may be due to the innate ability of workers, scale effects of enterprises, difference in hours worked, etc. The Ministry of Labor has not yet cross-classified the scale effects with the level of education, on-the-job experience, and gender.

As to equations (14.3) and (14.4), educational attainment has a highly significant effect on earnings. The level of earnings generally rises with the level of education. An extra year of schooling increases labor earnings (measured in natural log) by about 7 % across all occupations in both 1997 and 1998. This suggests that men and women who acquire a higher level of education would be better off economically. Similarly, an additional year of on-the-job experience or training improves one's labor earnings (measured in natural log) by about 8 %, contributing more than that of an additional year of education.

$T^2$  is significant across all occupations. The results may reflect that the productivity level of workers gradually increases up to a certain point in the life cycle and then generally starts to decline as they get older. Therefore, the findings may underscore the rationality of employers' behavior to dismiss inefficient older-aged workers first and more often during the economic crisis.

The gender variable,  $G$ , has a statistically significant and negative coefficient in both sets of equations. The regression analysis indicates that, first, although the observed average labor earnings gaps between men and women were about 40 % and 38 % in 1997 and 1998, respectively, as indicated by the nation-wide wage statistics (Table 14.9), these gaps cannot entirely be attributable to discrimination. And a large part of them (5 % points and 14 % points in 1997 and 1998, respectively) is explained by differences in human capital, as the neo-classical economics approach argues. Second, even after the differences in human capital were taken into account, there still remains a substantial degree of gender gap in average workers' earnings (about 35 % and 24 % in 1997 and 1998, respectively). Women earn less than their male counterparts. Third, the labor earnings gap between men and women, after accounting for the differences in human capital accumulation, was closing by about ten %age points before and after the economic crisis. By comparison, this gap was either five % or 25 %, depending on whether women were with or without children, respectively, in the U.S. labor market in 1991 (Furchgott-Roth and Stolba, 1999). The neo-classical economics approach (or human capital theory) attributes this remaining gender gap in workers' compensation to the rational behavior (taste or preference) of female workers, who try to combine paid work and household responsibility in an optimum way by concentrating on a few occupations and thus lowering their earnings *vis-a-vis* those of male workers.

It is here where various theories of gender discrimination differ in offering reasons for this earnings gap and different treatments between male and

female workers for other employment conditions. Contrary to the neo-classical approach, all other theories attribute this and other differences to gender discrimination by employers in the workplace. Unfortunately, nationwide official statistics do not shed any light on this issue. To test the validity of these other theories, we will have to construct a new database showing employers' behavioral motives.

### *A New Survey Database*

To date, most empirical studies on gender discrimination have focused on workers. However, if one suspects discrimination in the workplace, focus should be placed on the agent who exercises discrimination. Therefore, in this study, a new database has been constructed to explain the behavior of employers despite the difficulty of data collection.

Data were collected through personal interviews, which were conducted by Hyundai Research Institute from January 15 to February 20, 2000. The unit of survey was individual firms and respondents were personnel managers of the firms. A sample of 800 firms located in the metropolitan Seoul area was selected from the Ministry of Labor's annual establishment survey database, using a systematic sampling method. The initial sample list contained 800 firms, but the final sample size was reduced to 114 firms, from which all data were collected. This sharp reduction in the sample size was caused not only by a high refusal rate, but also by the high rate of bankruptcy, closure and relocation of many firms.

The sample covered five industries with a relatively high proportion of female workers according to the nation-wide statistics. They are: the manufacturing industry (25 firms, 42 % female); wholesale and retail trading industry (17 firms, 10 % female); real estate industry (23 firms, 9 % female); finance industry (21 firms, 8 % female); and transportation and communication industry (21 firms, 4 % female). Although a greater %age of female workers are employed in the health and social services industry, this has been excluded from the sample since it contains mainly gender-wise segregated occupations. The sample also contains more or less the same number of firms distributed by following scale: 30-99 employees (28 firms), 100-499 employees (36), 500-999 employees (21), and above 1000 employees (29).

To test the validity of various discrimination theories, the following hypotheses should be tested.

### *Neo-Classical Approach Revisited*

**Hypothesis 1: Female workers are concentrated in a few sectors to combine work and household responsibilities in an optimum way.**

Female workers were found to be most concentrated in the manufacturing,

wholesale and retail trading, real estate, finance, and transportation and communication industries, in that order (Table 14.10). By size, females were more crowded in smaller firms (25 % in firms with 100-500 employees) than in larger size firms (7 % in firms with 500-1000 employees and 10 % in firms with over 1000 employees) (Table 14.11). By occupation, females were more concentrated in such occupations as administrative and clerical jobs, sales and service jobs (Table 14.12). However, there is no firm ground to believe that women perceive the female-crowded sectors as more convenient for combining work and family responsibilities. Investigation of female worker's opinions was outside the purview of this study and must be followed up in a future study.

**Hypothesis 2: The earnings gap between genders is larger in those female-crowded sectors, after controlling for the level of education and on-the-job experience.**

When the starting earnings of men and women who have no previous work experience and have only a high school or university level of education were compared, there was no statistically significant gender difference in earnings, especially among high school graduates. Statistically, the only significant variation found was that the earnings of female university graduates differed by industry: the highest pay being in finance and manufacturing, and the lowest in real estate (Table 14.10). For university graduates, both female and male earnings were correlated with the size of the firms ( $p < .025$  and  $p < .002$ , respectively) (Table 14.11.). The smaller the size of the firm, the lower the earnings were for both male and female workers. However, this variation did not show any earnings gap between genders. Nor did the order of the industries have any systematic relation with female concentration. Therefore, the neo-classical hypothesis that the earnings of female workers in those female-concentrated sectors are lower than the earnings of male workers is rejected. Again, the neo-classical approach

**Table 14.10: Starting earnings level by industry in Korea**

Industry	High school graduates		College graduates	
	Male	Female	Male	Female
	(won)		(won)	
Manufacturing	844,099 (48)	806,341 (24)	1,104,452 (45)	1,107,151 (21)
Wholesale	876,201 (30)	860,814 (16)	1,101,737 (29)	1,086,680 (15)
Real estate	742,433 (32)	700,866 (19)	976,689 (25)	960,935 (14)
Transp. & commun.	975,524 (49)	951,615 (26)	1,056,182 (42)	1,065,059 (20)
Finance	856,795 (35)	847,426 (18)	1,140,450 (38)	1,125,582 (19)
Total	867,779 (194)	839,197 (103)	1,082,484 (179)	1,075,176 (89)
Significance	$P < .110$	$P < .754$	$P < .191$	$P < .002$

Note: Figures in parentheses are the number of persons



**Table 14.11: Starting earnings level by size of firm in Korea**

Employees	High school graduates		College graduates	
	Male	Female	Male	Female
	(won)		(won)	
30-99	813,106 (44)	762,341 (24)	952,471 (40)	916,414 (20)
100-499	846,474 (58)	807,084 (30)	1,019,790 (49)	1,014,107 (24)
500-999	862,017 (41)	845,841 (21)	1,103,586 (38)	1,111,721 (18)
1000~	943,810 (51)	934,498 (28)	1,226,152 (52)	1,222,698 (27)
Total	867,779(194)	839,197(103)	1,082,484(179)	1,075,176 (89)
Significance	P<.191	P<.222	P<.002	P<.025

Note: Figures in parentheses are the number of persons.

**Table 14.12: Occupational concentration of female workers and gender earnings gap in Korea**

	Female concentration		Female earnings
	1997	1998	1998
	(% )		(male=100)
All occupations	100	100	61.7
Managers	0	0	82.0
Professionals	12	13	76.4
Technicians			62.8
Adm./ clerks	16	14	64.4
Service/sales	36	37	69.6
Crafts	10	10	53.8
Plant/machine oper.	12	11	61.4
Elementary	9	15	70.5

Sources: Ministry of Labor, Korea (1999); National Statistics Office, Korea (1999 b)

is convincing in explaining the gender difference in earnings on the basis of the human capital theory only up to a point, but cannot fully explain it.

### *Test of the Marxist Feminist Approach*

#### **Hypothesis 3: The cheap and disposable reserve army of female workers replaced male workers during the Asian economic crisis.**

This theory argues that employers' strategy to exploit female workers has segregated cheap and disposable female workers from male workers, and during the economic recession, employers replace male workers with female workers to maximize their profits. However, during the Asian crisis, exactly the opposite situation developed. As seen above, during the Asian crisis, employment of male workers increased in the electricity, transportation,

storage, and finance industries, while the number of female workers in those industries actually declined. Likewise, employment of male workers increased in administration, service, and sales occupations, while the number of female workers in these occupations declined sharply (Tables 14.5 and 14.6). Therefore, contrary to the Marxist feminist theory, male workers replaced female workers to some extent during the economic crisis, especially in those industries and occupations where female workers have held a relatively greater share *vis-a-vis* male workers.

#### *Test of the Patriarchal Approach*

#### **Hypothesis 4: Trade unions are predominated by male employees; and also, trade unions strengthen gender discrimination because of male dominance.**

Patriarchal feminists argue that male-dominant employers and labor unions create patriarchal structure by generating gender-based internal labor markets and controlling job entry and access to training. Trade unions appeared to be predominated by male employees, who occupied 79 % of union membership. However, males on average accounted for 81 % of the total employees of the firms with trade unions, hence, the hypothesis is not sustained.

#### **Hypothesis 5: Trade unions strengthen discrimination against women.**

An analysis was made on the correlation between the existence of trade unions and discrimination practices in wage determination, disengagement of workers, recruitment, and motherhood protection. Our findings are as follows: (a) We failed to find any statistically significant difference in the starting earnings of the males and females who graduated from high schools or universities regardless of whether or not a trade union exists in the firm. (b) We also failed to find any statistical difference ( $p < .44$ ) in the rate of disengagement between men (20.1 %) and women (23.3 %) in the presence of a trade union. Neither was there statistical difference in the rate between men (20.6 %) and women (20.6 %) when trade unions were absent. (c) We again failed to find any statistical difference in the rate of recruitment between males and females irrespective of the presence of a trade union (Table 14.13). (d) The only statistically significant relationship found was between the presence of trade unions and motherhood protection practices.

Trade unions tended to promote the practice of menstruation and maternity leave. Of the 60 firms that had a trade union, 50 firms (83.3 %) offered menstruation leaves to their female workers. Of the 54 firms that did not have a trade union, 31 firms (57.4 %) practiced menstruation leave. Likewise, of the 60 firms with a trade union, 34 firms (56.7 %) offered maternity and childcare leaves to female workers, whereas of the 54 firms without a trade union, only 19 firms (35.2 %) practiced these kinds of leave. This last finding on the positive role of trade unions on motherhood

**Table 14.13:** Recruitment by firms with/without trade unions

		Firms with trade unions			Firms without trade unions		
		Firms	Mean (persons)	Sig.(P)	Firms	Mean (persons)	Sig.(P)
1997 HS grad	Male	49	9.42	.295	47	11.02	.146
New recruit	Female	48	13.15		46	17.70	
1998 HS grad.	Male	52	8.82	.411	50	9.29	.145
Experience	Female	51	11.35		49	13.89	
1997 college grad.	Male	51	5.98	.910	48	15.11	.886
New recruit	Female	50	5.61		47	14.07	
1998 college grad.	Male	53	7.03	.295	50	8.54	.962
Experience	Female	53	4.29		49	8.38	

protection practices is consistent with the results of previous research (H. Chung, 1996).

### *Cultural Gender-Typing Approach*

#### **Hypothesis 6: Women are less loyal and less committed to the company in comparison with men.**

Cultural feminists maintain that gender-stereotyping prejudice devaluing women's work brings about discrimination in the workplace. For example, it is a generally accepted notion in Korean society that women are less loyal, less committed to the job, and less able than men. If this notion is not proved in the workplace, it is really a cultural gender-stereotype.

For measuring commitment, we investigated whether there existed any gender difference in the degree of absence, tardiness, taking time off, and working overtime. There was no significant difference in mean attitudes toward work between men (53.2 times per year) and women (39.9 times per year) in terms of tardiness ( $p < .69$ ) and in taking time off (2.78 times per year for men and 2.20 times per year for women, at  $p < .46$ ). Regarding absence, however, there was a statistical difference between men (18.5 times per year) and women (2.8 times per year) at  $p < .015$ . Men were more likely than women to be absent from work. For measuring loyalty to the firm, we examined whether women were as participatory as men in meetings and meals after work and in overtime work. Although it is debatable as to whether these measures are good indicators of loyalty, women were as participatory as men, and there was no statistical difference between men and women in attending after work meetings and meals. Women (2.47 on a scale of 1 to 4), however, were slightly less willing to participate in overtime work than men (2.79). Hence, there is no ground to assume that women are less loyal or committed to the company, and the hypothesis is merely a

culturally gender-biased prejudice.

**Hypothesis 7: Cultural prejudice works adversely against women's recruitment and disengagement, and earnings level.**

To test whether the cultural stereotype adversely affects women in the workplace, we investigated differences between men and women in recruitment. The results suggested that there were no statistically significant differences in recruitment criteria between men and women, except for the category of qualifications. For both men (34.9 % of the firms) and women (39.7 % of the firms), interview scores were the most highly valued criterion in recruitment, and recruitment exam scores were the second highest, 14.1 % for men and 13.2 % for women, respectively.

Statistical differences were observed, however, in the criteria of certificates/licenses and appearance. Men's (11.2 %) qualifications were more important than that of women (5.9 %) at  $p < .001$ , whereas women's appearance (6.8 %) was more considered than that of men (4.8 %) at  $p < .024$ . The results imply that gender-type bias might differently affect the recruitment criteria for male and female workers. In response to one direct question to employers whether they believe men and women have different talents that are suited to different types of work, 46 firms responded positively and 43 firms answered negatively. However, the survey data did not show that the cultural gender-type adversely affected women in recruitment, disengagement, and earnings level. Rather, firms that responded that there were no gender differences in work ability actually hired more women (15.2 and 10.7 persons per company on average) than men (7.8 and 7.1 persons per company on average) at significance level of  $p < .006$  and  $p < .043$ , before (1997) and after (1998) the economic crisis, respectively.

*Labor Market Risks and Costs Approach*

**Hypothesis 8: Low productivity and high turnover rates of female workers due to childbirth and child rearing are the major causes of female disengagement in the workplace.**

Data showing discontinuity of female workers are prevalent. The nation-wide aggregate data show that female workers have, on average, a shorter on-the-job experience with their current employer than do their male counterparts (4.3 years vs. 6.8 years). The current survey confirms this as well. While male workers have worked 7.2 years on average with their current employer, female workers have worked only 4.7 years. Cho's study (1999) shows that a greater percentage of female workers (5.7 %) than male workers voluntarily disengaged during the Asian crisis (5.7 % vs. 5.1 %). Contrary to the nation-wide statistics; the current sample survey data show that 28.4 % of male workers voluntarily left their current employer while only 20.6 % of female workers left their job voluntarily.

However, the current survey data show that the major reason for female

workers to cut their career short during the economic crisis was marriage, childbirth and child rearing (68.4 % of total firms), while for male workers, a better offer from other firms was cited. The survey also reports that in those female disengagement cases due to marriage and childbirth or rearing, it was not the firm, but female workers (93.9 %) themselves who initiated the disengagement. However, when 66 firms dismissed female workers due to childbirth or rearing, the major reasons were low productivity (29.8 %), difficulty of replacement (19.4 %) or costly motherhood protection (3.5 %). The rest of the firms do not specify the reason. It can be construed that the firms may foresee risks in hiring women due to discontinuity of work and turnover costs. It is also possible that since the majority of female workers know of the employer's negative perception of their productivity after marriage and childbirth, they may have often voluntarily quit their jobs.

**Hypothesis 9: Legal provisions demanding motherhood protection above the international standards burden employers with financial responsibilities and encourage employers to discriminate against female workers on the job.**

The survey data show that motherhood protection costs are not a major concern of employers. The costs do not bring about discrimination in earnings, recruitment, and disengagement. For example, the menstruation leave practice does not encourage gender discrimination in recruitment. Rather, more women (17.2 %) were hired than men (12.01 %) in companies with the menstruation leave practice in 1998, whereas companies without it do not exhibit any gender differences. The results seem to directly refute the theory of motherhood protection costs. The effect of maternity leave is consistent with that of menstruation leave. Companies with the maternity leave practice hired more women (14.5 and 14.3 persons per company on average) than men (7.8 and 8.0 persons per company on average) in 1997 and 1998, respectively. Companies with this protection practice are more favorable toward hiring women. At least, it does not appear that motherhood protection costs are the direct source of gender discrimination in recruitment.

These findings contradict our observation based on the nation-wide statistics that there was some substitution of female workers by male workers during the economic crisis, especially in the female-crowded industries and occupations. One can suspect that the size of the company is correlated with affordability, the presence of a trade union, and the motherhood protection practice. The motherhood protection practice is more often observed in larger firms, which offer a higher level of earnings in general and also often have trade unions lobbying for the motherhood protection practice. Others may suspect that those firms that practice the motherhood protection measures might have predominantly female workers. Still others may suspect that since costs are one part of the definition of efficiency, employers' negative perception about motherhood protection costs is already subsumed in their perception of the risk in hiring women.

Such risk was clearly borne out in this survey in terms of inefficiency and discontinuity of female worker employment, as shown in the test of hypothesis 8.

In sum, our survey data do not conclusively support any of the discrimination theories. Nonetheless, they render more support for the cultural gender-type theory and the statistical discrimination or labor market risk theory. From these results, we can infer that these two discrimination theories are the potential candidates to be confirmed with further examination and studies once we improve some defects of the design of our survey. We call for further studies in this area.

## **Lessons Learned and Policy Recommendations**

Although this study has not brought out any conclusive findings about discrimination theories, it has shed informative light on the issues related to women in the labor market. We may be able to draw lessons useful not only for Korea during the economic crisis period, but also for many developing countries in general.

### *Special Labor Market Action Programs for Women*

During an economic recession or crisis, the government may want to take special measures focused on tackling the problems and issues of female workers separately from the general approach taken for all workers. Although this study could not support the general statement that female workers were more adversely affected by the Asian crisis, there is no doubt that female workers were acutely affected nonetheless. Moreover, this study shows that female workers have gone through a different labor market experience from that of male workers, especially in the incidence of hidden unemployment and involuntary disengagement, reemployment status, concentration of employment, and labor earnings.

Special measures that should be taken by the government may include: (i) labor market information systems with special emphasis on monitoring the situation of female workers, (ii) special job counseling for women so as to help them stay in the market and actively search for a job, (iii) special employment services and training programs and facilities for female workers, and (iv) a reinforced labor inspection system with a focus on motherhood protection.

### *Investment in Female Capital*

For an efficient and equal utilization of the human potential of both genders, both feminists and the government should focus on the gender difference in

human capital investments in terms of educational attainment and on-the-job training. The human capital theory accounted for more than a third of the observed labor earnings differentials (14 % out of about 38 %) between male and female workers in 1998. This implies that employers have not been completely arbitrary or discriminatory, but have been behaving rationally to some extent. The basis for the Korean employers' rational behavior has been gender differentials in human capital accumulation. There has been a substantial difference in the level of educational attainment and on-the-job experience between male and female workers. For all occupational groups, the average educational attainment of male workers was 12.8 years, but female workers, on average, had only 11.8 years. Likewise, the gender gap in on-the-job training and experience shows 6.8 years vs. 4.3 years for males and females, respectively. On a national scale, this gap was further widened in each individual occupational group and in different sizes of firms. Of course, significant progress has been made in females' educational attainment. For example, there is practically no gender difference in enrollments through the high school level, and female's share of bachelor degree earners markedly increased from 37.0 % of all bachelor degree earners in 1985 to 46 % in 1999. However, more progress is needed at higher degree levels. In 1999, female's share of master's and doctoral degree earners was only 31 % and 20 %, respectively.

More studies should be carried out on the gender difference in the motives for making different types of human capital investment, and on the ways to help guide females to attain equity not only in the level but also in the type of human capital investment. Besides the gender difference in the level of education and training attainment, differences also exist in the content and field of studies at every level of human capital investment, which would lead to the different gender status in the labor market. Males may focus more on those investment opportunities (e.g., specialties that would bring higher earnings) in which they may be able to enhance their productivity efficiently, while females may do it less efficiently. For example, at the tertiary level, female and male enrollments specializing in social studies have attained equity over time (from 14.6 % vs. 32.5 % between females and males in 1985 to 25.5 % vs. 26.8 % in 1999). However, female students are still concentrated in humanities, arts, and teacher training (21.8 %, 13.01 %, and 7.5 % of all female enrollees, respectively), while much fewer male students are enrolled in these fields (9.4 %, 5.3 %, and 2.3 %, respectively). Male students are specializing more in natural science and engineering (53.0 % in 1999), with which they can earn a higher level of earnings. Although the proportion of female students specializing in this field increased, it has reached only half the proportion of male students (27.5 % vs. 53.0 % in 1999). When the gender gap in a field of studies is substantially closed, such as in social studies, medicine, and pharmacology, labor earnings differentials would be substantially reduced. This is because the gender gap in labor earnings at managerial and professional levels is much smaller than in other

occupational groups, and the field of studies predominated by male students commands a higher level of earnings.

### *Changes in Cultural Gender-Typing*

The government should prepare a comprehensive plan to change the cultural gender-typing among citizens, especially employers, managers and employees. This study reveals that more than half of the observed labor earnings difference (24 % to 35 %) in the labor market could not be accounted for by the human capital theory. Therefore, the remaining gender difference should have been explained by other theories of discrimination. The study indicates that the cultural gender-type theory and the labor market risks and costs theory are more likely to explain the remaining gender difference in labor earnings and other employment conditions. This study confirms that strong cultural gender-typing is prevalent among employers, which may have contributed to some extent to the concentration of female workers in certain occupations and unequal treatment of female workers in the labor market.

The government plan should include not only the narrow legal approach, but also formal and non-formal education programs. It should also include a partnership with non-governmental organizations for public education and behavioral changes. Successful cases of active and equal participation of female workers in productivity increase should be identified and disseminated.

### *Changes in Motherhood Protection Systems*

The government should amend the social security system so as to share the motherhood protection and child rearing costs among employers, employees and government. Motherhood protection, a sort of public good, is justified for the betterment of family life and social well being, and therefore the costs should be shared among all members of society in an equitable manner. This study construed that although motherhood protection costs have not been independently shown as a major cause of discriminatory practice, they may have contributed to the employers' negative perception of marriage, childbirth and child rearing, and about the risks of high female turnover rates.

The government should, first, exonerate employers from the heavy burden of financing the motherhood protection costs alone. Continuation of the current system has had a boomerang effect on the equal employment of women. Second, the government should amend the legal provisions for motherhood protection to a more realistic level, and then enforce them rigorously with strong sanctions. The legal provisions should lay down only the minimum baseline, over and beyond which employers and employees should strive to reach an agreement on higher standards through negotiations. Reinforcing the motherhood protection measures ever more generously by



legislative actions is not a panacea. Currently, motherhood protection practices are observed in so few firms, especially among small-sized firms. Unrealistic and impractical legal provisions have created a tendency among employers to eschew hiring of female workers and to treat them unequally in personnel management. They have also created a non-compliance culture, and yet no sense of guilt among employers. Third, the Ministry of Labor should resume the periodic general inspection and monitoring of compliance by employers, which it has ceased to do since 1992, thus limiting itself to reacting passively to those cases filed by workers as violations of the labor law provisions.



**PART VI**

**THE KOREAN EXPERIENCE IN  
A N INTERNATIONAL CONTEXT**



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# 15<sup>th</sup> Labor Adjustment, Non-Standard Work, and Employment Programs: Korea in an OECD Context

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Makoto Ogawa'

## Introduction

The 15 years prior to the crisis were years of unprecedented growth for Korea. Per capita GDP grew at 7.5% per annum, life expectancy rose by 20%, and enrollment in primary and secondary education reached close to 100%. Korea went from being a lower-middle income country to a nation with a living standard appropriate to the (lower) ranks of OECD countries (with a per capita GDP of US\$10,550 in 1997). On the labor market front, employment grew strongly; real wages increased by over 50% between 1990-97; and unemployment rates remained around 2%. This transformation touched all aspects of society and the economy, including the labor market. As development proceeded through the 1970s, 1980s, and 1990s, the need for formal labor market policies and institutions increased accordingly. Indeed, by the mid-1990s, the foundations of an "industrial-era" labor market regime had been put in place including a vocational training system, employment services, a collective bargaining framework, and unemployment insurance.

The onset of the crisis in 1997 marked an important event for labor policy-makers. Certainly, the crisis raised some issues particular to the extraordinary situation, most notably the need to provide income support to the rapidly expanding pool of impoverished workers. However, the spotlight of the crisis also exposed more generic development concerns about the labor market – for example, inadequate protection offered by the new unemployment insurance system; limitations of existing employment services and programs; and difficulties in sustaining constructive social dialogue between labor, employers, and the government.

Fortunately, Korea now appears to have emerged from the crisis with

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\* Social Protection Unit. Human Development Network, the World Bank.

impressive momentum. After a decline of 5.8% in 1998, real GDP growth in 1999 was 9.5% and is forecast to expand by 6% in 2000. Unemployment has now fallen below 5%. Real wages have turned around as well with the 1998 decrease of 9.3% followed by a rapid increase in 1999, with estimates as high as 11.1%.<sup>1</sup>

While the immediate hardships of the crisis for Korean workers may have been moderated (if not eliminated) by the recovery, the more durable labor market concerns revealed during the crisis remain as significant issues for the future. But the policy agenda does not stop there. As Korea directs its focus forward, it must now address a new set of issues associated with the "knowledge-based" economy. Future improvements in living standards will increasingly be tied to knowledge-intensive industries and services and success in these sectors will depend in part on a high-quality labor force and on appropriate labor market policies and institutions. Korea thus faces a dual task: completing the industrial-era reforms while preparing for the knowledge era. In the process, policy-makers will need to learn from more advanced OECD countries while assessing the opportunities for "leap-frogging" their experience.

Within this context, three labor market challenges are critical for the ongoing development of the Korean economy: First, unemployment will need to be addressed as a regular feature of the labor market. Unemployment rates may not approach the levels that characterize some European countries but the days of 2% rates appear to be over. Consequently, a long-run strategy for mitigating unemployment shocks through a mix of active and passive policies will need to be established and implemented. Second, developing a skilled and innovative labor force will have to be a priority. In addition to what this means for education, it also will call for an emphasis on lifelong learning and on organizational innovation in the deployment of human resources. Third, the benefits of growth will need to be broadly shared through the workforce. This is closely linked to the preceding two challenges but also to the importance of minimizing the dualism between regular and non-regular employees in terms of labor market regulation and social protection.

This chapter considers aspects of these challenges from an international perspective. In addressing these issues, policy-makers will find the experience of OECD countries more relevant than that of World Bank client countries even in East Asia. This corresponds to the reality that, after the decades of growth, the Korean labor market more closely resembles the former group of countries (even with the impressive growth in many of the latter countries). However, Korea's particular development path, culture, and institutions are obviously important factors as well.

We begin in the next section with a statistical overview of Korean labor market trends. First, we review some of the main Korean structural

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<sup>1</sup> This was reported in a press release from the Ministry of Labor. February 22, 2000

characteristics and indicators in an international context. We then summarize how the Korean labor market adjusted to the financial crisis and compare this to the adjustment paths of other affected countries in the region and then selected OECD countries that have also experienced aggregate shocks. The main point of this section is to establish that, even as the Korean labor market has been transformed to a point where it increasingly resembles (some) OECD countries, the crisis demonstrated that it remains a very flexible labor market.

In the following two sections, we turn to selected labor market policy issues that are central to the broader challenges identified above. In each case, the discussion of Korean policy is grounded in the OECD experience. First, we look at the growth of non-standard employment, an issue of growing concern in Korea. The second topic discussed is active labor market programs and how they can best contribute to the employability and future earnings of unemployed or low-income workers. Conclusions are offered in the final section.

## Korean Labor Markets in a Comparative Context

This section starts off by offering a brief comparison of Korea's economic and labor force characteristics with that of its East Asian neighbors and other OECD countries. This is followed by an overview of recent tumultuous labor market developments in Korea and a comparative analysis of the labor market impacts of the crisis with those of countries in the region which were also impacted by the crisis (Malaysia and Thailand) as well as other OECD countries at the time they were affected by declines in GDP (Canada and U.K. in the early 1990s and Japan in the late 1990s). While the magnitude of the shock was significantly more dramatic in Korea (and the other East Asian countries) than in the other OECD countries chosen (Table 15.1), it is

**Table 15.1: International comparison of GDP growth rates <sup>1)</sup>**

	Year -1	Year 0	Year 1	Year 2
	(%)			
Korea	7.1	5.5	-5.8	9.5
<b>Malaysia</b>	8.6	7.8	-7.5	<b>8.0</b>
<b>Thailand</b>	5.5	-0.4	-10.0	4.0
<b>Canada</b>	-0.2	-2.0	-0.5	2.1
Japan	3.9	0.9	-2.8	
<b>United Kingdom</b>	0.4	-2.0	-0.5	2.1

Note: 1) Year -1 refers to the year prior to economic slowdown; Year 0 refers to the year in which economic growth slowed significantly/declined, Year 1 refers to the year immediately following the decline and Year 2 refers to two years following decline.

Source: Various sources

nonetheless useful to compare how labor markets have adjusted since in many ways Korea may be more similar to other OECD countries than to other countries in the region as demonstrated below.

### *Economic Trends and Labor Force Characteristics; A Comparative Picture*

Table 15.2 provides a comparison of economic indicators for Korea relative to other OECD and East Asian countries included in our analysis. From this table it is clear that Korea is rapidly catching up other OECD countries. The structure of the Korean workforce is rapidly becoming more similar to that of Canada, Japan and the U.K. – with low and shrinking agricultural employment and a growing majority of the employment in the services sector. It should be noted that a similar trend has also been observed in Malaysia and Thailand although at an earlier stage. Unlike these two countries though, where a significant proportion of the population still resides in rural areas, almost 80% of Korea's population is urban – a proportion similar to that in Canada and Japan and just slightly lower than in the U.K.. Korea's per capita GDP is also significantly higher than that of Malaysia and Thailand (though it is still significantly lower than that of the three other OECD countries listed here).

Overall labor force participation rates are highest in Thailand due to high participation rates among women (Table 15.3). While they are lower in Korea, participation rates in Korea are roughly the same as in Canada and Japan (even though the participation rates among women are still quite low as compared to other OECD countries).<sup>1</sup>

The skill composition of the Korean labor force is also relatively high. In 1995, just over a quarter of the labor force had attained primary education or less as compared to 50% in Malaysia and 80% in Thailand. As the table above shows, the educational attainment of the Korean labor force compares favorably to that of high-income OECD countries, making it well placed to tackle the challenges of the knowledge-based economy.

We now discuss how Korea's labor market has responded to the crisis in comparison to the selected countries.

### *Labor Adjustment to Crisis*

Table 15.4 highlights trends in unemployment, underemployment and employment in the years immediately prior to and following the crisis.

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<sup>2</sup> In the first year of the East Asian crisis participation rates fell in all three crisis countries discussed here – while participation rates fell for both men and women, there was a disproportionate decrease in women's labor force participation rates. These trends were somewhat reversed in Canada and the U.K. when their GDP's declined in the early 1990s. Women's participation rates rose slightly while those for men fell to a small extent.



**15.2: Summary of economic trends in selected countries, 1980-1998**

	GDP growth (annual ave.)(%)	Labor force structure % distribution. 1996 (% change since 1980)			Urban population (% of total)	GDP per capita (US\$)
	1990-98	Agriculture	Industry	Services	1998	1998
Korea	6.1	11.6 (-5.9)	32.5 (29.0)	55.9 (37.0)	80	8,600
Malaysia	7.4	19.4 (-7.8)	32.2 (33.6)	48.4 (25.1)	56	3,670
Thailand	5.7	50.0 (-9.4)	20.8 (101.9)	29.1 (54.0)	21	2,160
Canada	2.2	4.1	22.8	73.1	77	19,170
Japan	1.5	5.5	33.3	60.8	79	32,350
United Kingdom	2.2	2.0	26.8	71.0	89	21,410

Sources: World Bank, *World Development Indicators*; ILO, *Key Indicators of the Labor Market*

**Table 15.3: Selected labor force characteristics, in crisis countries, 1995-1997**

	Labor force participation rates by gender (1997)			Labor force participation rates by gender (1998)			Educational attainment of the labor force (% distribution, 1995)			
	Female	Male	All	Female	Male	All	< 1 year	Primary	Sec.	Tertiary
Korea	49.5	75.6	62.2	47.0	75.2	60.7	8.7	18.2	51.9	21.1
Malaysia <sup>1)</sup>	46.8	80.8	63.8	41.6	79.1	60.7	16.7	33.6	42.8	6.8
Thailand <sup>2)</sup>	67.4	82.2	74.8	65.8	81.5	73.6	10.7	69.6	11.4	5.1
Canada	57.4	72.5	64.8	58.1	72.4	65.1		20.8	31.2	48.1
Japan	50.4	77.7	63.7	50.1	77.3	63.3		20.5	48.8	30.6
United Kingdom <sup>3)</sup>	43.0	56.0	49.2	43.0	55.7	49.2	13.5		45.7	22.8

Notes: 1) Malaysia labor force participation rates are for 1995.

2) Thailand educational attainment figures for 1990.

3) United Kingdom's labor Participation rates are based on the entire population, not just individuals aged 15+. Education Attainment does not include "Education not defined by level" 18.1%.

Sources: International Labor Organization (2000). *Key Indicators of the Labor Market*; Horton and Mazumdar(2000).

Quantity-related adjustments were greatest for Korea and Thailand. In both countries, unemployment rates – which had been in the 2% range at the time of the crisis – more than doubled in the year immediately following the crisis. The adjustment was more muted in the other OECD countries, where unemployment rates rose by 20-30% from their initial – albeit higher – levels. Similar changes are observed when we look at the statistics on underemployment. In terms of employment, Korea saw the highest decline in the year following the crisis (5.3%). All the other countries examined also saw declines in employment ranging from 3.3% in the U.K. to 0.7% in Japan.

What seems to distinguish Korea from these other countries is the rapidness of recovery from the crisis. While the 1999 data (second year post-crisis) from Malaysia and Thailand are unavailable for comparative purposes, Korean data show a reversal of the trends for the past two years – by the third quarter of 1999, unemployment declined by 1.8 % points and employment increased by 1.4%<sup>3</sup> (though a significant proportion of this increase in employment is in non-permanent jobs). This is in strong contrast to Canada, Japan and the U.K. which were all experiencing growth in unemployment and underemployment as well as declines in employment – albeit at generally slower rates as compared to the first year – in the second year following the crisis. This is undoubtedly related to the rapid economic recovery – as Table 15. 1 shows GDP grew by about 10% in Korea in the second year after the crisis, while the corresponding growth rates in other OECD countries were about 2%.

Similarly, price-related adjustments were also significant in Korea (Table 15. 5). After growing at 6.7% in the year preceding the crisis, real wage growth slowed dramatically and real wages fell by 9.3% in the first year following the crisis.<sup>4</sup> Other countries had varying responses – real wages fell quite steeply in Thailand in the year following the crisis and also fell more modestly in Malaysia, Canada and Japan. In the U.K. on the other hand, adjustment to their GDP decline seems to have been entirely quantity-related, as real wages grew by over 4% in the first year after declines in GDP.

Wages recovered faster than quantity-related indicators in all countries – wages in the U.K. continued to rise, Canada experienced positive wage growth within two years of its downturn and while wages declined in Japan they did so by less than 1%. However, again, Korea's recovery on the wage front was very swift. In 1999, real wages grew by 11.1% thus reversing any decline that took place as a result of the crisis.

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Korean government forecasts for 2000 are also optimistic – employment is expected to increase by 3.6% and unemployment is expected to fall to 4.5% (Republic of Korea, 2000).

<sup>4</sup> The wage decline following the crisis has been partly attributable to significant cuts in bonuses and overtime payments - which account for a large part of wages - following the crisis. These payments increased in 1999 leading to robust wage growth. However, it should be mentioned that bonuses and overtime payments are usually not part of the remuneration for non-regular workers, who, as we shall see in Section III, are a growing proportion of Korea's workforce.

Table 15.4: Summary of unemployment, underemployment, and employment trends in selected countries<sup>1)</sup>

	Unemployment						Underemployment <sup>4)</sup>					Employment	
	Year -1 <sup>2)</sup>	Year 0	Year 1 <sup>3)</sup>	Year 2	% change Year 0-1	% change Year 1-2	Year 0	Year 1	Year 2	% change Year 0-1	% change Year 1-2	% Change Year 0-1	% Change Year 1-2
Korea (1996-)	2.0	2.6	6.8	5.0	161.5	-7.4	7.3	9.3		29.2		-5.3	1.4
Malaysia (1996-)	2.6	2.6	4.0		53.8		7.3	7.9		8.2		-2.7	
Thailand <sup>5)</sup> (1996-)	2.0	2.2	5.2		136.4		0.9	1.2		33.3		-2.8	
Canada (1989-)	7.5	8.1	10.4	11.3	28.4	8.7	17.0	18.1	18.5	6.5	2.2	-1.9	-0.8
Japan (1996-)	3.4	3.4	4.1	4.7	20.6	14.6	20.8	20.9	21.5	0.5	2.9	-0.7	-0.8
United Kingdom (1989-)	7.3	7.1	8.8	10.1	23.9	14.8	20.1	20.7	21.5	0.5	3.9	-3.3	-2.2

Notes: 1) Thailand figures for February; Korea and the Philippines are averages of quarterly estimates.

2) Year -1 refers to the year prior to economic slowdown; Year 0 refers to the year in which economic growth slowed significantly/declined,

3) Year 1 refers to the year immediately following the decline and Year 2 refers to two years following decline

4) Underemployment (as % of employed population) defined as: Canada, Malaysia, and UK less than 30 hours per week; Japan. Non-Agriculture, less than 35 hours, Korea, 35 hours or less per week; Thailand, less than 40 hours per week and available for more hours.

5) Working age population in Thailand defined as 13 years of age and older.

Sources: Mahmood and Arya (2000) ; Kang et al. (2000) ; Mansor et al. (2000) ; Kakwani (1996) ; World Bank (January 2000) ; Thailand Economic Monitor ; For Japan, Labour force survey ; For Canada and UK, ILO (1999). Key Indicators of Labour Market

**Table 15.5: Real wage trends in selected countries**

	% change in real wages			
	Year -1	Year 0	Year 1	Year 2
<i>Korea (1996-)</i>	6.7	<b>2.4</b>	<b>-9.3</b>	11.7 <sup>5</sup>
Malaysia (1996-)	2.1	3.3	-1.1	
Thailand (1996-)	2.3	1.4	-7.4	
Canada (1989-)	0.5	-0.6	-0.4	1.9
Japan (1996-)	1.6	0.4	-2.0	-0.9
United Kingdom (1989-)	2.3	0.1	4.2	3.6

Sources: For UK, *ILO Year Book of Labour Statistics*; For Japan, Ministry of Labour, *Monthly Labor Survey*; For Canada, OECD, *Manufacturing wage "Historical Statistics 1990-1995"*.

These data indicate that the Korean labor market has demonstrated significant flexibility – both in terms of prices and quantity during the crisis. This is true in comparison to other east Asian countries and especially true in relation to OECD countries. Significant downward and upward adjustments, especially on the wage front, indicate a high level of responsiveness to shocks (it should be noted though that growth rates fell and rose much more sharply than in other OECD countries). The economic strategies that Korea adopts in the aftermath of the crisis as well as the ability of the labor market to respond to shocks will go a long way in determining if and when Korea will join the ranks of the high-income OECD countries.

## Non-Standard Employment

The quality of employment has become a growing concern in recent years. Between the fourth quarters of 1997 and 1998, total wage employment declined by 8.3%, with the only growth in the wage sector in daily work. Even during the initial phases of recovery in the labor market, the number of workers in regular employment has continued to decline while all employment gains have been in the temporary and daily categories. This development has raised a number of questions. Is the growth of “non-regular” employment merely linked to the crisis and its immediate aftermath or does it reflect an underlying structural change in the economy? If it is a more fundamental trend, what is driving it? Should policy-makers respond and, if so, how? In this section, we consider these questions by reviewing the

<sup>5</sup> This growth rate is based on numbers in a press release from the Korean Ministry of Labor (February, 2000). While fixed monthly wages grew in 1999 by 6.1%, overtime wages and bonuses grew by 30.1% and 28.3% respectively, which contributed to an overall wage growth of 11.1%.

Korean experience with non-regular employment and then considering this experience within the international context. Ultimately, more time and more data will be required to conclusively assess the significance of the recent trends.

### *What Do We Know About Non-Standard Employment?*

The issue of non-regular work has had a high profile in many OECD countries over the past decade or so. Various labels have been applied to the phenomenon (such as "non-standard" work and "atypical" employment) but the underlying notion is work forms that depart from the traditional concept of a full-time position of indeterminate length with a single employer. Definitions of "non-standard" employment have also varied but in the OECD region, it has generally included part-time workers, short-term or temporary workers, temporary-agency or "dispatch" employment, and the "own-account" self-employed.<sup>6</sup> As we will see below, these categories represent roughly two-thirds of all employment in Korea, a proportion that is relatively high by OECD standards. The composition of non-standard employment is also somewhat different in Korea than in many other OECD countries, with a relatively large share in self-employment and unpaid family work.

There is a general perception that non-standard work has been increasing in many industrialized countries. This reflected in the attention that non-standard work has received from academics and policy-makers.<sup>7</sup> In fact, the empirical trends are less definitive than might be expected. The incidence of part-time work – generally the largest category -- has been increasing in most countries but only marginally.<sup>8</sup> The share of self-employment has been rising moderately in about one-half of industrialized countries and declining moderately in the other half.<sup>9</sup> Trends in short-term, temporary contract, and temporary agency (dispatch) work are the most difficult to establish empirically in many countries. At least through the mid-1990s, the incidence of temporary employment had not changed significantly with some OECD countries reporting increases (Australia, the Netherlands, France, and Spain) and others reporting decreases (Belgium, Greece, Luxembourg, and Portugal). Job stability measures such as tenure and retention rates also do

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<sup>6</sup> This latter group includes self-employed workers who themselves have no employees

<sup>7</sup> For example, the annual OECD *Employment Outlook* has devoted a number of chapters to aspects of non-standard work over the past decade. At the national level, there has also been considerable attention.

<sup>8</sup> The proportion of OECD employment in part-time jobs was 14.9 % in 1997, compared to 14.4 % in 1990. In 8 countries (Canada, France, Ireland, Japan, Luxembourg, New Zealand, Spain, and the UK), part-time shares did increase by 2 % points or more (OECD 1998).

<sup>9</sup> Of 21 industrialized countries where data are available for 1990-97, 10 had increasing shares of self-employment, 10 had decreasing shares, and one had no change (ILO 1999).

not show any major or systemic shifts in the industrialized countries (OECD 1997).

Where non-standard employment has increased, a number of explanatory hypotheses have been offered:

- ❑ One focuses on changes in labor supply and, specifically, the increasing female and (and to a lesser extent) youth participation rates in some countries. This argument is based on the fact that these groups have a relatively high propensity for certain non-standard work arrangements (part-time and short-term/temporary) because of the flexibility they offer to combine work with other activities (e.g., family responsibilities, school, etc.).
- ❑ A second hypothesis emphasizes changes in the nature of economic activity that may be shifting optimal labor contracting towards non-standard employment forms. This is the "new economy" or "knowledge-based economy" hypothesis. For example, while the scale, capital investment, and production process in many manufacturing industries call for standard work arrangements, many service activities require or are amenable to part-time, short-term, or independent contractor arrangements. At the same time, the revolution in information and communication technologies has opened up new possibilities for organizing work in non-traditional ways. Finally, globalization and technology have raised the premium on flexible production which can be served by a variety of non-standard employment patterns.
- ❑ Third, labor regulations and other policy variables can affect non-standard employment. In some countries, there have been restrictions on part-time work or temporary jobs. Where these restrictions have been lifted, it has been typical to observe large increases in the relevant non-standard category (e.g., Spain and France with temporary work). There are also many examples where the differential application of labor standards or payroll tax contributions creates incentives towards different forms of employment (e.g., where short-term or part-time workers are outside the system).
- ❑ Finally, there can be cyclical elements in non-standard employment patterns. During recessions, employers will want to limit labor costs and, as a consequence, it can be expected that their preference for part-time and short-term/temporary work forms will increase. Also, when labor demand is slack, some unemployed workers are likely to respond to a lack of job opportunities by becoming self-employed.<sup>10</sup>

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<sup>10</sup> In fact, there are competing forces that can neutralize these cyclical tendencies. For example, seniority rules may protect standard employees with the result that layoffs are concentrated among short-term or temporary workers. Examining the patterns of self-employment in the 1980s, the OECD (1992) found that a "pull" factor (i.e., interest in setting up businesses when times were good) could counteract the "push" factor (of scarce job opportunities)

*Korean Evidence on Non-standard Employment Trends*

Our analysis of non-standard employment trends in Korea is primarily based on employment status data from the Economically Active Population Survey (EAPS). This covers self-employment, unpaid family work, and three categories of wage employment (regular, temporary, and daily).<sup>11</sup> Our analysis, based on the EAPS data, does not include part-time and temporary agency (dispatch) jobs as separate categories though they are largely embedded in the employment status numbers.<sup>12</sup> We begin in this sub-section by comparing wage vs. non-wage employment since 1980. Following this, we turn to the trends in non-standard employment.

Chart 15. 1 compares trends in wage and non-wage employment between 1980 and 1999. The former category includes regular, temporary, and daily workers while the latter includes the self-employed and unpaid family workers. This chart shows an enormous shift over this period from non-wage to wage employment. In 1980, less than half of Korean workers were in wage employment but by the end of the 1990s, about two-thirds were wage employees. This change was particularly dramatic during the 1980s when wage employment grew from about 6.5 million to almost 11 million.

The transformation of the Korean labor market summarized in Chart 15. 1 reflects the rapid urbanization and industrialization (especially during the 1980s) that remains a remarkable story in international development. In fact, when we look at employment status trends separately for the farm and non-farm sectors, the balance between wage and non-wage employment has changed very little. In the farm sector, self-employment and unpaid family work accounted for 84% of total employment in 1980 and 82% in 1999. In the non-farm sector, corresponding figures are 29% and 26%.

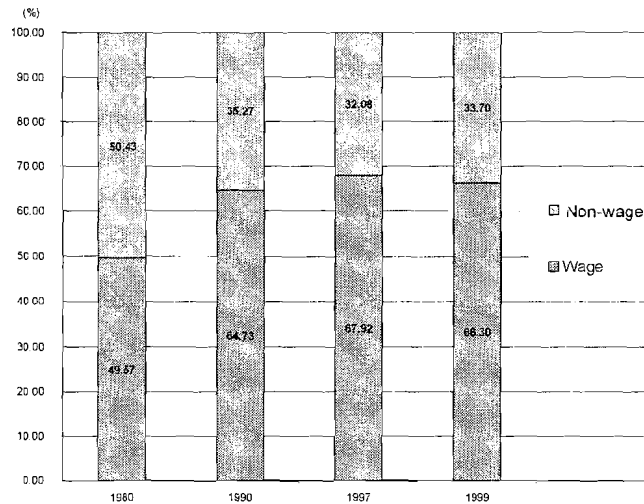
Table 15.6 presents the 1990 and 1999 shares of non-standard work on an aggregate basis and then for the farm and non-farm sectors. Standard work includes regular wage employment and nonstandard work includes self-employment, unpaid family work, and temporary and daily jobs.<sup>13</sup> Overall, the data indicate a high proportion of non-standard employment (around

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<sup>11</sup> It also includes employers (i.e., the self-employed with employees) but this group has been excluded from the analysis. We use the term "self-employment," then, to mean the self-employed who do not themselves have employees (i.e., "own-account")

<sup>12</sup> The only exception would be part-time work where the employee has regular (i.e., permanent) status. This group is likely to be very small. Part-time work, in fact, has had a relatively low incidence in Korea. In 1997, it accounted for 5.1% of total employment. Temporary agency or dispatch work has been a relatively small category historically in part because of legal restrictions. The official estimate at the end of 1998 was 42,000 workers employed in temporary agencies (Kim *et al.* 2000). This may well change as restrictions are loosened.

<sup>13</sup> "Regular" wage employment refers to jobs where employees work more than one year, "temporary" workers are employed for a fixed period of time (usually less than one year); and "daily" workers are employed on a daily basis (though they may be with a particular employer for more than a day).

**Figure 15.1: Wage and non-wage employment growth in Korea, 1980, 1990, 1997 and 1999**

two-thirds) with some modest increase over the decade. However, this overall picture of relative stability masks two counteracting trends. On the one hand, the shift from non-wage to wage employment already discussed has supported the growth of standard employment. However, this has been offset by the growing non-standardization of wage employment in Korea during the 1990s.<sup>14</sup>

**Table 15.6: Proportion of non-standard employment in Korea, 1990 and 1999**

	1990	1999
	(% )	
Total	64.9	68.0
Farm	93.3	94.4
Non-Farm	57.7	64.0
Male	55.2	58.1
Female	78.0	81.3

Source: Bureau of Labor Statistics, Korea (Various Years), *Economically Active Population Survey*.

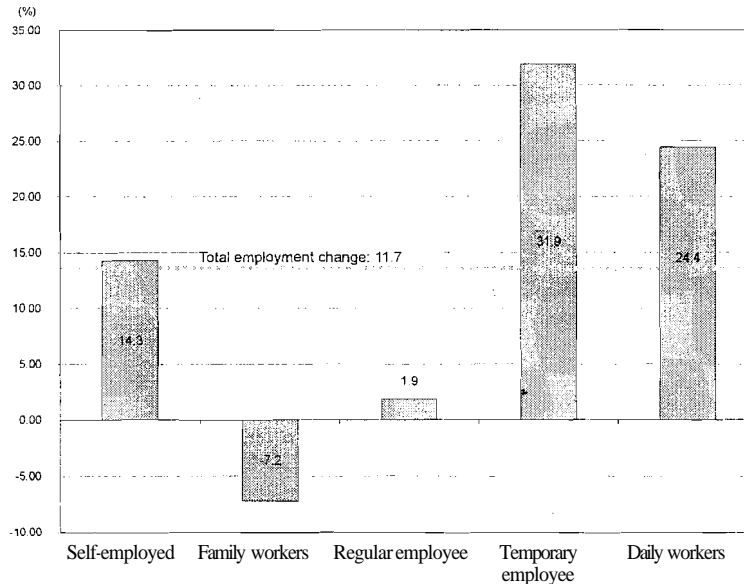
This non-standardization of wage employment is evident in Chart 15. 2 which presents the 1990 trends in more detail. During a decade when aggregate employment increased by 11.7%, regular employment grew by

<sup>14</sup> Non-standard figures cannot be calculated from the EAPS prior to 1989 because no distinction was made between regular and temporary wage employment.



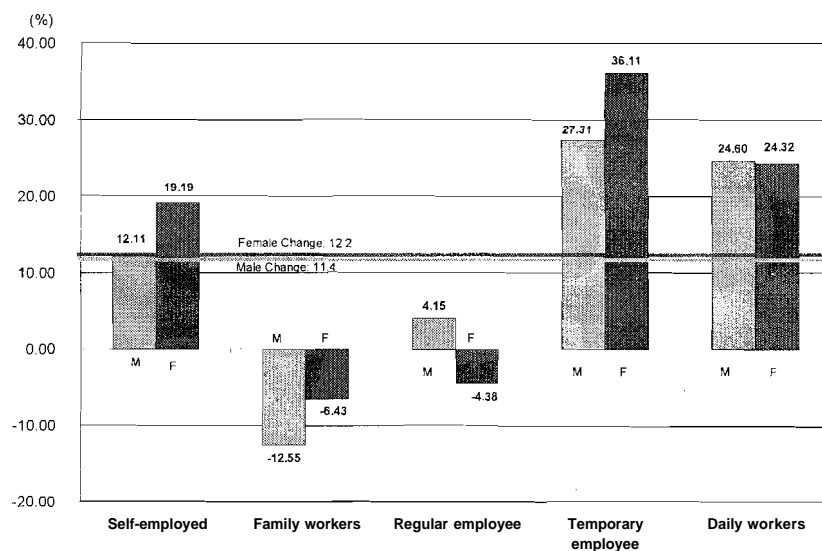
just 1.9% while temporary and daily jobs increased by 31.9% and 24.4%, respectively. It is these trends in wage employment that are at the heart of concern regarding non-standard employment.

**Figure 15.2: Percentage change in employment by status in Korea, 1990-1999**



In order to assess the significance of the growth in non-standard wage employment and to draw appropriate policy implications, it is important to understand how much of the trend is due to the immediate impacts of the crisis and how much to more fundamental underlying factors. As we have noted, in many other OECD countries, one non-cyclical explanation for increasing non-standard work has focused on labor supply and specifically female and youth participation. As Chart 15.3 indicates, the aggregate pattern of relative declines in regular wage employment and increases in temporary and daily work has been slightly more marked in the case of women. However, a crucial element in the labor supply hypothesis is rising participation rates for women and for youth – yet these rates remained relatively unchanged in Korea during the 1990s.<sup>15</sup> The other key structural (non-cyclical) hypothesis for growth in non-standard work relates to technological innovation, sectoral change, and the growth of the knowledge-based economy. This is more difficult to assess empirically and we do not address this in this paper.

<sup>15</sup> Female participation rates were 47.0% in 1990 and 47.4% in 1999. Corresponding figures for the 15-24 year age group were 35.0% in 1990 and 31.3% in 1999.

**Figure 15.3: Employment change by gender and status in Korea, 1990-1999**

Turning to cyclical factors, it has been widely recognized that non-standard wage employment has grown substantially in the immediate aftermath to the crisis. Between 1997 and 1998, all forms of wage employment declined – temporary and daily as well as regular (Table 15. 7).

**Table 15.7: Percentage change in employment by status in Korea, 1990-1999**

Status	1990 to 1997	1997 to 1998	1998 to 1999
	(%)	(%)	(%)
Total	15.1	-4.6	1.8
Self-employed	11.5	0.1	2.5
Family workers	-8.1	6.8	-5.4
Regular employee	20.4	-9.7	-6.3
Temporary employee	31.9	-4.4	4.6
Daily workers	2.8	-8.3	31.9

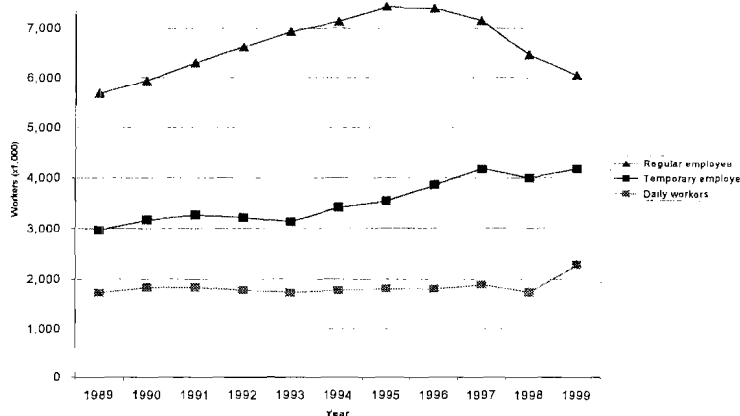
Source: Bureau of Labor Statistics, Korea (Various Years), Economically Active Population Survey.

However, as the recovery was established in 1999 and aggregate job growth resumed, all of the gains in employment were accounted for by non-standard work forms. This was particularly dramatic in the case of daily work which increased in 1999 by 31.9% while regular wage employment continued on a downward trend declining by 6.3%.

Is increasing non-standard employment likely to be an ongoing feature of the Korean labor market? There are two views on this, leading to different answers. One posits that as the recovery takes hold, employers will adopt longer-term planning horizons and will start to invest more in their workforces, including creating regular jobs. There is limited support for this view in the experience of the other OECD countries that have had real GDP declines. In both Canada and the UK, for example, part-time work increased during the recessions and, in fact, continued to increase in the first few years of recovery before starting to recede again.<sup>16</sup> However, in each case, the post-recession declines were only modest.

The alternate view is that, while the crisis may have exacerbated the situation, Korea has a more fundamental issue with high rates of non-standard employment. There are two pieces of evidence that support this argument. First, the shift from regular to non-regular wage jobs was already occurring prior to the crisis (Chart 15. 4). By the mid-1990s, when the economy was still growing at substantial rates, employers were already substituting non-regular (largely temporary) jobs for regular ones. In part, this may reflect responses to mounting competitive pressures. Kim *et al.* (2000) makes the argument that the cost competitiveness of Korean labor had been declining since the late 1980s. These conclusions are supported by World Bank estimates which found that unit labor costs in Korea increased in the late 1980s, continuing at least through the early 1990s.

**Figure 15.4: Standard and nonstandard employment trends in Korea, 1989-1999**



<sup>16</sup> In Canada, the share of part-time work was 17.0% in 1990 (immediately prior to the recession), 18.1% in 1991 (the recession year) and 18.5%, 19.1%, 18.8%, and 18.6% in the four subsequent years. In the UK, the pattern was similar: 20.1% (pre-recession), 20.7% (recession), then 21.5%, 22.1%, 22.4%, and 22.3%.

The second piece of evidence is that, relative to other OECD countries, Korea has a high level of non-standard employment (and did even before the crisis). This is true even when comparisons are made with countries at the lower end of the OECD development continuum. For example, while regular wage jobs account for only about 30% of Korea's total employment, the corresponding 1998 figures for Greece and Portugal are 48% and 59%; the incidence of non-standard wage employment is 7% in Greece and 12% in Portugal compared to over 30% in Korea."

On balance, the Korean labor market seems to have a propensity towards the creation of non-standard employment that cannot be fully explained by the crisis nor by the country's stage of development. Labor market institutions, including compensation practices, labor standards, and social insurance contributions, seem to create incentives for non-standard job creation at the expense of standard work forms. Four aspects seem especially relevant. First, regular workers receive a large portion of their total compensation in the form of bonuses which are not generally paid to temporary or daily workers. Second, working conditions and contract provisions mandated by the Labor Standards Act primarily apply to regular workers. Severance pay arrangements (applicable to workers with at least one year of tenure) are relatively generous in comparison to many other OECD countries. Third, dismissal procedures for regular workers are somewhat cumbersome and costly.<sup>18</sup> Finally, the Employment and Insurance System (EIS) implemented in 1995 initially required payroll contributions for each regular employee in enterprises over 30 workers. Coverage of the EIS has expanded to enterprises of all sizes and some temporary workers, but still does not apply to part-time or daily workers.

Recent policy changes may alter the incentives towards non-standard employment. On the one hand, the loosening of restrictions on temporary agencies obviously will lead to increases in this form of work. On the other hand, the current thrust of labor policy is to extend social insurance and regulations to all firms and more categories of workers. This is evident in the recent changes to both Employment Insurance and the Labor Standards Act. However, the continued importance of bonuses in the overall compensation of regular employees and the generous severance system remain as significant incentives for employers to meet staffing needs through non-

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<sup>17</sup> Two indicators of stage of development are the sectoral composition of employment and GDP per capita. In terms of the former, these two countries are roughly similar to Korea. In terms of the latter, Greece and Portugal have slightly higher GDP per capita (in 1998, US\$11,740 and US\$10,670 compared to US\$8,600 in Korea). The non-standard figures for Greece and Portugal come from unpublished OECD data.

<sup>18</sup> Termination for non-performance, allowable under the law but rare, must meet high standards of "just cause." A Tripartite Commission agreement in 1998 allowed employers to lay off workers for economic reasons but continued to require a 60-day advance notice, consultations with worker representatives and, in the case of large firms, notification and justification to the Ministry of Labor.

standard arrangements. To the extent that the playing field can continue to be leveled for labor institutions, social insurance, and labor regulation, Korea will not only improve the social protection offered non-standard workers but will also reduce the incentives towards these work arrangements. The question is what the price will be in terms of the job creation and labor market flexibility that have been so characteristic of the Korean economic success.

### **Active Labor Market Programs<sup>19</sup>**

Unlike most OECD countries, a strong tradition of Active Labor Market Programs (ALMPs) does not exist in Korea. One of the main reasons has been the low rates of unemployment prior to the crisis. However, the crisis has led to a significant expansion of these programs as the increases in unemployment, the difficulties facing many laid-off workers in reestablishing employment and earnings, and the obstacles facing young people trying to enter the labor force have all underscored the need for policy-makers to consider new options.

In many OECD countries, ALMPs have been an important employment policy tool for over four decades. This policy envelope includes a wide range of activities, intended to increase the quality of labor supply (e.g., retraining); to increase labor demand (e.g., direct job creation); or to improve the matching of workers and jobs (e.g., job search assistance). They are often targeted at workers with special difficulties in the labor market. The objective of these measures is primarily economic -- to increase the probability that the unemployed will find jobs or that the underemployed will increase their productivity and earnings. More recently the case for active labor market policies has also emphasized the potential social benefits in the form of the inclusion and participation in the labor force.

While ALMPs have become an attractive option for labor policy-makers, evaluative evidence on the effectiveness of the programs in the OECD demonstrates that designing and implementing effective ALMPs poses many challenges. This section looks at these issues in more detail. We compare active labor market programs provided in OECD countries and Korea, summarize the evidence on their impacts, and discuss some of the key issues that should be considered as policy makers aim design and implement more effective programs in Korea.

As Korea moves towards a knowledge-based economy, the importance of skills upgrading is going to become increasingly important. The likelihood of worker transitions will also increase as activities will become more project-based. The transition to knowledge-based economy will have some

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<sup>19</sup> This section draws heavily on Betcherman *et. al.* (2000).

implications for active labor programs in terms of new delivery techniques (greater participation of the private sector and civil society), increasing reliance on technology, and innovations in financing of these programs. As discussed later in this section, these transformations are already evident at the cutting edge of some OECD ALMPs.

*What are ALMPs?*<sup>20</sup>

The more common ALMPs are:

- direct job creation (public works schemes, micro-enterprise development, wage subsidies);
- public employment services/job search assistance agencies;
- training/retraining for unemployed adults and those at risk of unemployment;

The OECD has collected statistics on public expenditures by member countries on active labor market programs since the mid-1980s. Average national expenditures (as a % of GDP) increased in the 1990s as compared to the 1980s – from about 0.6% to over 1%. This increase reflects both an increasing preference on the part of governments for ALMPs and the higher unemployment in most countries in the 1990s compared to the 1980s.

OECD countries generally see active and passive programming as complements rather than substitutes. Where spending is relatively high in the former area, it is also likely to be relatively high in the latter. In 1990, the correlation coefficient between national spending on active and passive programs was .60 (OECD, 1993). After diverging in the early nineties when income support jumped to accommodate workers laid off in the recession, the strong correlation resumed in 1993, with spending on active programs slightly increasing relative to passive.

However, there are major differences across OECD countries in terms of the level and composition of spending on ALMPs. Annex Table 1 highlights these differences for a subset of countries using the latest expenditure data available.

While increasing focus has been paid to ALMPs in Korea following the crisis, expenditures on ALMPs remain low relative to other OECD countries. In 1993 (the first year for which data was available), Korea spent 0.08% of GDP on ALMPs. By 1998, this had gone up to 0.18% (along with expenditures of 0.02% of GDP on passive programs). It is anticipated these expenditures will decline 30-40% in 2000 as the crisis subsides (Republic of Korea, 2000).

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<sup>20</sup> For a more thorough discussion also see Martin (2000)

*ALMP's in Korea and Other OECD Countries: A Description*

Korea adopted an Employment Insurance System (EIS) in 1995. The purposes of the EIS are two-fold: (a) to help unemployed workers by providing unemployment benefits to them and; (b) to enhance employment stability and job competency of workers through active labor market policy measures. The EIS has three major components: the employment stabilization scheme, the vocational competency development scheme and unemployment benefits. Each of the three schemes has its own premium. The premium for unemployment benefits is 1.0 % (shared by employers and employees) of total payroll. The premium for the employment stabilization scheme is 0.3 % of total payroll financed by employers. The premium for the vocational competency development scheme, also entirely financed by employers, varies from 0.1 % to 0.7 % of total payroll, depending on the size of the firm (Kang *et. al.*, 2000).<sup>21</sup> This section will focus on the active labor market programs.

Employment Services

Employment services serve brokerage functions, matching jobs with job seekers. This assistance comprises many different types of activities: for example, initial interviews at employment offices, in-depth counseling during the unemployment spell, job clubs, etc. In most OECD countries, workers have access to job referrals, job counseling, skills assessment, job search training, resume preparation and job clubs. In most of these countries, public and private services coexist, usually serving different clientele - public employment services target the disadvantaged and the long-term unemployed while private agencies usually target the employed, skilled, and white-collar workers (Fretwell and Goldberg, 1994). Often employment services are integrated with the other ALMPs, as well as passive programs – e.g. the employment office provides job search assistance as well as providing unemployment benefits.

Korea has a long, though modest, history of public employment services. Following the crisis, the Korean government expanded and reinforced public employment service agencies for job placement and created a nationwide network for job information. Private employment services have always played a larger role than public services in job placement since the 1960s when they were legalized and the crisis has also seen a significant expansion in the number of such centers (Table 15.8.)

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<sup>21</sup> When the EIS was created, its coverage extended to firms with over 30 workers (with some exceptions). However, after the onset of the crisis coverage was extended to smaller firms. and since October 1998 coverage has been provided for all workers – with certain exceptions (e.g. part-time workers, older workers, government officials). However, owing to these exceptions, only 65% of all workers are eligible to avail of the EIS and only 70% of these are actually insured.

**Table 15.8: Employment service agencies in Korea, 1997 and 1999**

Number of...	Public		Private	
	1997	1999	1997	1999
Agencies	337	427	1,432	1,756
Staff	1,210	...	...	...

Source: Ministry of Labor, Korea

Since 1998, in order to improve the quality of public employment services, the government has merged various active and passive labor market functions to create employment centers that are based on the concept of "One-Stop Service" and are designed to provide job seekers with all kinds of information and services, from job vacancy information to vocational training. Unemployed workers can also receive unemployment benefits at these centers.

The government has also recently moved towards using information technology for employment services. Public employment offices in different areas are now able to share information about job seekers and vacancies via networks and the internet through the recent launching of an electronic labor exchange system, "Work-Net," which provides information on job vacancies, vocational training, career guidance, employment policies, employment insurance and labor market statistics. However, this system is yet to be evaluated (Kang *et al.*, 2000).

### Training and Retraining

Most OECD countries focus on three types of training programs: (a) Retraining aimed at the long term-unemployed (e.g., unemployed for more than 12 months); (b) Retraining displaced workers, especially those displaced *en masse* as a result of enterprise/industrial restructuring; and (c) Training programs aimed at young people, often with special attention to school drop-outs. Support can come in the form of direct provision of training, financial support for trainees, or provision of information on training services. In many OECD countries, governments are moving away from the role of direct provision of training and focusing more on addressing market failures in information and financing, while leaving more of the delivery to private providers.

Korea has long-standing experience with vocational education and pre and in-service vocational training. In this section, we will not focus on these issues,<sup>22</sup> limiting our attention to training and retraining measures that have been implemented by the government for the unemployed. Since the onset of severe economic difficulties, the government has set up training programs

<sup>22</sup> For a more intensive discussion of these issues see Gill and Ihm (2000); Kim (2000)



available to the unemployed as a social relief strategy. Individuals are allowed to receive training/retraining for a duration of up to one year in new skills and the government pays for the cost of training. Almost a quarter of all the unemployed have received government sponsored training. A pilot program of training vouchers was also launched in **1998**. The objective of the training voucher system was to provide the unemployed with more choices and promote competition among institutions providing training. Measures that have been implemented in **1999** include efforts to make training more demand-oriented; expansion of training in knowledge-based, high technology fields; improving unemployed workers' transition from training programs to jobs; enhancement of information systems; and extension of private sector participation in training (Kang *et. al.*, 2000).

#### Direct Job Creation

In Korea, job creation measures have been the primary labor market policy in response to the economic crisis. Public works programs, support for small and medium sized businesses, internship programs for new labor market entrants, and wage subsidy programs are among the job creation efforts planned by the government since the crisis. Interventions that have been designed in Korea have been somewhat similar to those in other OECD countries.

#### Public Works Programs

The idea behind these programs is generally to help disadvantaged and long-term unemployed groups to regain contact with the labor market, thereby minimizing the probability of stigmatization, skills obsolescence, and marginalization.

Public works programs have been instituted in Korea at both the local and central government levels primarily since the crisis to provide temporary employment opportunities for the unemployed and provide them with a safety net. These works were generally of three month duration and any individual could not participate in more than three such projects consecutively (Kang *et. al.*, 2000; Republic of Korea, 2000).

#### Micro-Enterprise Development

Technical assistance, credit, and other support can contribute to the creation and promotion of small-scale new businesses and self-employment. Micro-enterprise development assistance (MEDA) programs have been offered both on a universal basis or to particular groups – the newly unemployed or the long-term unemployed. Program conditions also vary. Participants may receive assistance to set up their businesses as a lump-sum payment or periodic allowances. Often there is "screening" whereby potential benefi-

ciaries undergo a rigorous assessment which evaluates their likelihood of success (Wilson and Adams, 1994). In most cases participants may also receive business advisory services and counseling.

While such assistance has increased in Korea since the crisis, it is still quite insignificant. Individuals have been provided with financial support (3-500 million won per business) to start up small- and medium-sized businesses and venture enterprises. Business Incubators have also been established to provide advisory services to assist entrepreneurs with management training.

#### Wage/Employment Subsidy (WES)

In OECD countries, these programs have been targeted at the long-term unemployed and youth. They aim to reduce social exclusion, that is, to help these individuals regain contact with the world of work by providing employers with an incentive to hire these individuals. They are instituted under varying economic conditions, though usually during slack periods (NERA, 1995). The level and duration of these subsidies varies significantly between programs and countries.

Following the crisis, Korea's subsidy programs expanded significantly. In 1998, wage subsidies were provided for 6 months for the following firms:

- Those that were closed for at least two days a month: 112 to 213 of the temporary shutdown allowance that must be paid to employees was subsidized.
- Those that reduced regular working hours by more than 10%: 6-10% of the wage bill prior to the reduction was subsidized.
- Those that provided training to workers: 50-66% of the wages along with training expenses subsidized.

Firms that granted paid leave to their employees and those that switched to a new line of business while retaining 60 % of their employees were also paid a subsidy.

#### *Evaluations of ALMP's: Evidence from OECD and Korea*<sup>23</sup>

In spite of the large public expenditures on active labor market programs, rigorous evaluations of their impacts have been limited. However, policy-makers are increasingly realizing the importance of good evaluation in improving program design. They want to know what programs accomplish, what they cost, and how they should be designed to be cost-effective. Over the past few years increasing emphasis is being placed on scientific

<sup>23</sup> For a more rigorous discussion of evaluation techniques and results from evaluations of OECD ALMPs, also see Martin, 2000; and Dar and Tzannatos (1999).

evaluation techniques -- which compare the outcomes of the "treatment" group of program participants relative to a "control" group of non-participants -- to determine program outcomes. As a result there is a growing body of evidence on the effectiveness of these programs -- especially in OECD countries.

In this section, we provide a brief overview of the evidence from evaluations of active labor market programs in Korea and other OECD countries.<sup>24</sup> While these programs have not been evaluated with the same rigor in Korea, some preliminary evaluative evidence is presented.

#### Job Search Assistance (JSA)/Employment Services

Evaluations of about 20 of these programs suggests that JSA is one of the most successful active labor market programs: it costs little to provide and the program is not any less effective than alternative and more expensive ALMPs. However, much depends on whether the economy is growing and on the availability of public funds (which can be scarce during a recession).

Most evaluations indicate positive results. Less successful programs are generally associated with periods of recessions and rising unemployment (Fay, 1996). Conversely, the effectiveness of job search assistance seems to increase when economic conditions improve and when new jobs are being generated (OECD, 1993; O' Leary, 1998a, b; Fretwell *et. al.*, 1999). Job search assistance is one of the most-cost effective of the ALMPs. For example, Leigh (1995) finds that JSA measures cost 2-4 times less than training, but appear equally effective in terms of impacts.

While rigorous evaluations of public employment services has not been done in Korea (and little evidence exists on the effectiveness of private employment services), evidence is more discouraging than in other OECD countries. Employment services may not be highly successful in placing workers -- the rate of employment has never exceed 20% and declined to 7.4% in 1998 (Table 15. 9. This compares unfavorably to over 50% employment rates in most other OECD countries for which such data is available. The declines in placement rates in 1998 are to be expected as there were few vacancies during the crisis.

A survey on "Unemployment and Welfare Needs of Workers" found that most workers feel that the employment services do not provide timely and locally reliable labor supply and demand information to customers (KLI, 1998). Most job seekers felt that the public employment services failed to provide adequate job opportunities and counseling on career development.

Some of the reasons that may underlie the low effectiveness of these agencies include the high workload of job counselors (an average of 4000 workers per counselor in 1997 compared to 364 in Germany and 325 in

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<sup>24</sup> Most of the evidence for OECD countries is drawn from the U.S., Canada, Sweden, Germany, France and the U.K..

Sweden) and the inadequate use of information technology though that is slowly changing with the advent of "Work-Net". No evidence exists on the relative effectiveness of these programs for participants as compared to non-participants.

**Table 15.9: Effectiveness of public employment service agencies in Korea, 1994-1998**

Year	Vacancies (A)	Job seekers (B)	Employed (C)	(A/B) x 100	(C/B) x 100
1994	225,652	148,597	28,141	152	18.9
1995	196,319	116,147	20,938	169	18.0
1996	215,925	150,668	20,939	143	13.9
1997	245,223	243,467	36,425	101	15.0
1998	410,005	2,130,687	157,442	19	7.4

Source: Kang *et al.* (2000)

### Training Programs

A review of close to 50 programs training programs targeted at long-term unemployed, those laid off en *masse* and youth yield somewhat mixed results. The success of programs for the long-term unemployed tends to be dependent on the business cycle: programs have performed better when instituted at times of economic expansion. Longitudinal studies indicate mixed results; while in some cases positive effects dissipated within two years of program completion, in some cases the impacts persisted. Programs targeted at those laid-off en *masse* have resulted in some modest increase in reemployment probabilities, however, this result is often statistically insignificant (Corson, Long and Maynard, 1985). The results for post-program earnings are more discouraging: relative to the control group, wage effects on participants are rarely positive and in most cases are negative. Programs targeted at youth often yield the most discouraging results - training rarely has an effect on earnings or employment probabilities of program beneficiaries (Fay, 1996). While costs are available only in some cases, cost-benefit analysis usually show that costs are so high relative to the benefits of most of the program that, even if the effects persisted for 10 years, the social return of the program may remain negative (Friedlander et. al., 1997).

Rigorous evaluations of training programs for the unemployed have not been carried out in Korea in the aftermath of the crisis - evaluations do not compare outcomes of trainees with that of a control group. However, as is the case in other OECD countries, the completion rate of training is extremely low and the re-employment rate for those who completed training also appears to be quite low (Table 15.10).

**Table 15.10: Training programs for the unemployed in Korea, 1998-1999**

	1998	1999 (till June 1999)
Trainees	362941	181273
Completion Rate (%)	53.4	12.3
Employment Rate (for those who completed training) (%)	22.4	44.4

Source: Ministry of Labor, Korea.

#### Public Works Programs/Public Service Employment

Public works programs have been evaluated in both OECD and developing countries. Evaluations of close to 20 programs point to some general conclusions. Some scientific evaluations suggest very high displacement effects which can reach 100 %, as they did in Sweden (Skedinger, 1995). Participants tend to have a smaller probability of being employed in a non-assisted job after participation in the program, and are likely to earn less than their counterparts in the control group. These programs also do not seem to have a significant impact on reducing long-term unemployment and whatever small short-run impacts may exist tend to diminish over time (Webster, 1998).

However, these programs can be effective as short-run anti-poverty interventions. For this reason, some countries – including Korea - have used them extensively in periods of hardship. In 1998, 440,000 people participated in public works projects, with a total government expenditure of almost 1 trillion won. Participation for 1999 has been estimated around one million with a budget of 2.5 trillion won.

Preliminary evidence indicates that programs have not been well-targeted. Some public works projects are considered as wasteful (Yoo, 1999). In the early stage of the program, leakage rates were high as some well-off people participated in the program, while many poor unemployed were excluded from public works because local governments often selected participants on a first-come-first-served basis regardless of the selection criteria. Another criticism is that the program may be distorting the labor market - the daily wage rate for participants is still 30-40% more than the minimum wage – which may have led to crowding out of jobs in the private sector (Kang *et.al.*, 2000).

#### Micro-Enterprise Development/Self-Employment Schemes (MEDA)

Evaluations of 15 of these programs lead to the conclusion that MEDA programs have high deadweight loss. Estimates of these losses vary from about 30% in the self-employment experiments in the U.S. to over 50% in Canada and Denmark in the early 1990s (Fay, 1996). Evidence shows that

businesses assisted through mentoring and business counseling are more likely to succeed. However there is only a small multiplier effect - Most surviving businesses create, on average, half an additional job (Wilson and Adams, 1994). Cost-benefit issues have rarely been addressed in the context of these programs and hence it would be premature to draw any conclusions on the cost-effectiveness of these programs. These programs have also not been evaluated in the Korean context to date.

#### Wage/Employment Subsidies (WES)

Evidence from 22 such programs in OECD countries suggest that WES programs have rather low take-up rates, high deadweight loss and substitution effects. In the extreme case of Ireland's wage subsidy program, these losses combined totaled over 95% – alternatively, the net incrementality of the program was a meager four % (OECD, 1993). Evaluations of similar programs in Australia, Holland and the U.K. also indicate high deadweight and/or substitution effects exceeding 60%. Equally disappointing are evaluations which compared wages and employment outcomes of participants with those of a control group – with a few exceptions, over time participants are likely to earn less and are also less likely to be employed (OECD, 1993).

Again, while Korea's programs have not been scientifically evaluated, initial results point to somewhat similarly disappointing performance. In 1998, 1,805 firms received employment maintenance subsidies, covering a total of almost 800,000 workers. Contrary to initial hopes, these employment subsidy programs have been used by less than one % of private employers – though there is a strong positive correlation between the size of the firm and the likelihood of utilizing the subsidy programs. A recent study which investigated the employment effects of these subsidy programs using employer surveys as well as case studies showed low net employment creation of these schemes (Kim *et al.*, 1999). According to this survey, while there were variations by type of subsidy program, on average the deadweight loss was around 70%, somewhat similar to OECD countries.

#### *ALMPs in Korea: The Way Forward*

The relative scarcity of rigorous evidence on the effectiveness of ALMPs in Korea does not allow a definitive conclusion as to whether such interventions have been justified on economic or social grounds. However, the general conclusion emerging from international evidence as well as preliminary evidence from Korea suggests that large scale application of these programs should be avoided without knowledge of their effects. It is clear that designing and implementing of active labor market programs should take into account the general state of the economy and set the right objectives and expectations. Different programs are needed for different

scenarios. Also, expectations should be modest: rarely can a program simultaneously meet criteria of economic policy (efficiency and distribution) and also political considerations.

However, policy-makers in Korea should not avoid this area in the future as the country emerges from the crisis. Active labor market programs serve social objectives, as well as economic and little research has been done to examine these social impacts, which may be more positive. Furthermore, the disappointing performance of these programs in the aggregate masks the fact that some program designs do seem to lead to positive outcomes for some types of workers. The challenge is to learn from existing experiences.

As policy-makers in Korea aim to improve on the design and implementation of these programs while moving towards a knowledge-based economy, they should keep the following issues in mind:

#### Priority Setting.

As we have noted, active labor market programs can have various policy objectives including reducing unemployment in cyclical downturns, correcting structural imbalances, improving labor market functioning, and assisting disadvantaged groups of workers. In designing an overall strategy, it is important to identify which of these are the priority objectives since it is the objectives that should determine program choices and program design.

#### The Roles of the Public and Private Sectors.

This is a key consideration both in developing an overall strategy and in designing and implementing programs. At one time, governments in the OECD developed and delivered virtually all ALMPs but, increasingly, governments have reconsidered the respective roles of the public and private sectors. In many countries, possibilities have opened up for the other sectors to play important roles, at least in the delivery of services. This seems to be happening in Korea too as in the case of the voucher system pilot for training. This can lead to more diverse and cost-effective services. However, governments must remain responsible for the overall system, ensuring that it remains focused on public priorities. They must also address distributional issues and provide critical public goods.

#### Promoting Partnerships and Dialogue.

The identification of priorities for active labor market policy and can benefit from ongoing dialogue between government, business, labor, and other relevant organizations. Where this dialogue is conducted effectively, policy-makers can maintain a close connection with the needs of the labor market and can maximize support for ALMPs. In Korea, the dialogue needs to be carried out both at the national policy making level (e.g., through the

tripartite commission) and locally where programs are delivered.

#### "Infrastructure" for the Labor Market.

Infrastructure services are critical if ALMPs are to be a useful policy instrument. By "infrastructure," we mean labor market information, a viable network of employment service offices, and certification and accreditation systems. These services are the cornerstones of an effective system: They inform the program choices that should be made. They provide the bridge between the labor market, service deliverers, workers, and employers. As largely public goods, these are the responsibility of governments. Korea is in the process of developing these services and they should continue to be a high priority.

#### Policy and Administrative/Operational Capacity.

Designing and implementing ALMPs requires considerable capacity within government. Capacity needs differ significantly by program. For example, employment services require a network of facilities with extensive geographic coverage, the resources (e.g. technology) to generate and disseminate accurate labor market information, skilled counselors, and reliable connections with the employer and educational communities. Training programs require labor market information plus training and occupational standards, monitoring and evaluation capabilities, and capacity to deliver effective programs. Governments must recognize that capacity building is a slow but essential process.

#### Monitoring and Evaluation.

This is a key part of capacity and deserves special mention. In spite of the large public expenditures on ALMPs in OECD countries, rigorous evaluations of these programs have been relatively uncommon. Korea is no exception. In an effort to improve the targeting and efficiency of social programs, sound impact evaluation techniques should be used to evaluate these programs. A good evaluation compares labor market outcomes for individuals who have gone through a particular program with those of a control group of their peers, and also utilizes data on program costs to attempt to answer questions such as: what are the impact estimates of the program on the individual; are the impacts large enough to yield net social gains; and is this the best outcome that could have been achieved for the money spent.



## Conclusion

We have not attempted to provide a comprehensive analysis of Korean labor market issues in this paper. A number of key issues have remained untouched including labor-management relations, unemployment insurance, and women in the labor market. Using international experiences to provide context, we have focused on Korea's adjustment to the economic crisis and two labor market issues of growing importance – active labor market programs and non-standard employment.

Our review has highlighted the flexibility apparent in the Korean labor market. It is true that the rapid development of the economy has transformed the labor market dramatically over recent decades. In many respects, it now resembles labor markets in other OECD countries. However, our analysis of both the adjustment to the crisis and non-standard employment indicates that the Korean labor market is significantly different and, indeed, more flexible than what we see elsewhere in the OECD region. This has been beneficial in terms of job creation (including in the wake of the crisis) but it raises questions for social policy and labor market segmentation. The challenge emerging from our paper is for Korea to improve social protection for all workers, to create incentives for broader access to secure work, and to provide support for workers in transition without constraining job creation.

Looking first at active labor market programs, these have the potential to reduce unemployment, enhance human resource development, increase the employability of disadvantaged workers, and improve the overall functioning of the labor market. However, rigorous evaluations of these programs in OECD countries show that economic conditions, worker characteristics, and program design contribute significantly to their effectiveness. Otherwise, the potential of ALMPs will not be realized. Korea's transition towards a knowledge-based economy will have implications for active labor programs in terms of institutional capacity building, delivery techniques (e.g. greater participation of the private sector and civil society), increasing reliance on technology, innovations in financing, and monitoring and evaluation of these programs. These transformations are already evident at the cutting edge of ALMPs in some OECD countries and Korea can benefit from learning from those experiences.

The analysis on non-standard employment has concluded that Korea has an underlying propensity towards such forms of job creation. While the crisis has exaggerated the situation, there were already tendencies in this direction prior to the crisis, and, from an international perspective, Korea has a high share of non-standard employees. While this has been key to the country's labor market flexibility, we view this as an issue that rightly concerns policy makers. What results is a segmentation between relatively

well paid regular workers with access to severance, employment protection, and social insurance and non-standard workers in an insecure situation. Continuing in this direction is not beneficial from a distributional perspective. Nor is it likely to be beneficial from an efficiency perspective when, increasingly, the country's growth will depend on a skilled and productive work force.

At least in part, the high level of non-standard employment in Korea is due to labor policies and practices that create incentives for these types of jobs. Recent reforms intend to level the playing field by extending the coverage of labor standards and social insurance. Minimizing differential treatment of standard and non-standard workers will alter these incentives. However, further analysis will be required to strike the optimal balance between protection and job creation.

Over the past two generations, Korea has experienced dramatic economic progress which obviously has led to huge improvements in the living standards of its people. In a couple of generations, Koreans have gone from a rural agricultural existence through industrialization and now their prosperity increasingly depends on success in service industries and high technology. Many other OECD countries have taken a century to make this transition. While this pace of development has created pressures in the labor market and formidable challenges for policy-makers, workers, and employers, it also raises the prospect of leapfrogging on the experiences of other countries and thus moving up the "learning curve" quickly in preparing for the knowledge-based economy.

**Annex 15.1: Expenditures on labor market programs in selected OECD countries**

<i>Labor market program</i>	<i>Australia</i> (1997/18)	<i>Denmark</i> (1998)	<i>France</i> (1997)	<i>Germany</i> (1998)	<i>Japan</i> (1997- 98)	<i>Italy</i> (1996)	<i>Spain</i> (1998)	<i>Sweden</i> (1998)	<i>U. S.</i> (1997- 98)
<i>Public employment services &amp; administration</i>	0.21	0.14	0.16	0.23	0.03	0.04	0.07	0.30	0.06
<i>Labor market training</i>	0.07	1.07	0.35	0.34	0.03	0.01	0.21	0.48	0.04
<i>Training unemployed adults and those at risk</i>	0.06	0.73	0.31	0.35	0.03	-	0.10	0.47	0.04
<i>Training employed adults</i>	-	0.34	0.04		-	0.01	0.11	0.01	-
<i>Youth measures</i>	0.06	0.08	0.26	0.07	-	0.42	0.07	0.03	0.03
<i>Measures for unemployed &amp; disadvantaged youth</i>	-	0.08	0.07	0.06	-	0.04	0.07	0.03	0.03
<i>Apprenticeship and related form: of general youth training</i>	0.05	-	0.19	0.01	-	0.38	-		
<i>Subsidized employment</i>	0.13	0.30	0.52	0.39	0.02	0.61	0.35	0.58	0.01
<i>Subsidies to employment in the private sector</i>	0.04	0.03	0.32	0.03	0.02	0.56	0.24	0.15	-
<i>Support of unemployed persons starting enterprises</i>	0.02	0.04	-	0.03	-	-	0.03	0.09	-
<i>Direct job creation (public or non-profit)</i>	0.07	0.23	0.20	0.32	-	0.04	0.07	0.35	0.01
<i>Measures for the disabled</i>	0.06	0.30	0.08	0.25	-	-	0.02	0.62	0.04
<i>Vocational rehabilitation</i>	0.02	0.30	0.02	0.10	-	-	-	0.04	0.04
<i>Work for the disabled</i>	0.04	-	0.06	0.15	-	-	0.02	0.58	-
<i>Unemployment compensation</i>	1.17	1.86	4.50	2.29	0.43	0.68	1.64	1.91	0.25
<i>Early retirement for labor market reasons</i>	-	1.88	0.35		-	0.20	-		
<i>Total</i>	1.69	5.63	3.22	3.56	0.52	1.96	2.36	3.93	0.43
<i>Active Measures</i>	0.52	1.89	1.37	1.27	0.09	1.08	0.72	2.01	0.18
<i>Passive Measures</i>	1.17	3.74	1.85	2.29	0.43	0.88	1.64	1.91	0.25

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# 16 Korean Labor Market and Social Safety-Net Reforms: Challenges and Policy Requirements\*

**John P. Martin "**  
**Raymond Torres "**

## **Introduction**

Korea has long registered one of the most impressive economic records of modern times. During the past four decades, GDP growth averaged more than 9 % on an annual basis, permitting current per capita income to reach 65 % of the OECD average.

The financial crisis which started at the end of 1997 brought the growth process to a sudden halt. The crisis forced the government to agree to a rescue package with the IMF. Unemployment rocketed from 2 % to a peak of 8 % in early 1999, and more than one million Koreans were thrown into poverty. The difficult economic and social situation provoked by the crisis forced the authorities to implement quickly a wide range of macroeconomic and structural reforms. The economy has now turned the corner, permitting the unemployment rate to fall rapidly to below 5 %, and short-term prospects point to a continuation of the solid recovery. In 1999, the economy grew by over 10 % and the latest OECD projections show a growth rate of 8.5 % this year, followed by 6 % in 2001.

This recovery owes a great deal to market forces -- the significant depreciation of the Won that took place short after the start of the crisis, combined with significant nominal and real wage cuts in 1998, have improved international competitiveness, export performance and firms'

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\*\* Directorate for Education, Employment, Labor and Social Affairs, OECD.

profitability. But government policies have also played a role in ensuring the recovery. The Korean government has implemented over the past three years many structural reforms, not only in the areas of banking, corporate governance and financial markets, but also covering labor markets, industrial relations and social protection. Indeed, the range and scope of these reforms, together with the speed with which they were implemented, is unprecedented by the standards of other OECD countries.

Now that the recovery is well underway, it may be tempting to assume that the crisis was just a blip in an otherwise high-growth path and that, as a consequence, a pause in the reform agenda is called for. On the contrary, Section II of this paper argues that the Korean economy and society is still facing key challenges on the fronts of industrial relations, labor markets and social protection. Section III sets out reform proposals to tackle these challenges. The final section presents some concluding remarks.

### **Outstanding Problems in the Areas of Industrial Relations, Labor Markets and the Social Safety-Net**

OECD (2000a) highlights several outstanding problems in the areas of industrial relations, labor markets and social protection which need to be tackled if the Korean economy and society is to achieve its stated objectives. This section summarizes the arguments.

#### *Reforms to Labor Laws to Bring Them into Line with Internationally Accepted Standards*

When Korea joined the OECD in 1996, the Korean authorities made a commitment to the Organization that they would reform existing laws on industrial relations in line with internationally accepted standards, including those concerning basic rights such as freedom of association and collective bargaining. The OECD's Employment, Labor and Social Affairs Committee has since been monitoring closely progress on labor law reforms in Korea in the light of that commitment.

The Korean authorities have taken a number of important steps over the past three years to meet this commitment, steps which have been welcomed by the OECD and the ILO. However, as documented in OECD (2000a) and in several recent reports of the ILO's Committee on Freedom of Association, there remain some outstanding problems. The most prominent are:

- Prohibition of remuneration of full-time union officials: The 1997 Trade Union Act prohibits the remuneration of full-time trade union officers by the employer, as well as any financial payment for regular

trade union operations. This clause is supposed to take effect by the year 2002.<sup>1</sup>

It is not clear why the law should have to regulate this matter, rather than leaving it to be decided by collective bargaining. A survey of practices in other OECD countries shows that paid working time off for trade union representatives is a common feature of industrial relations systems. Additional time off for works council members (where these exist) is also widespread. In large enterprises, hours credits for both these functions often imply that many union officials devote their full time to union matters while being on the company payroll. In some countries, hours credits and time-off for union officials are regulated in detail through labor law, while in other countries the matter is left to collective agreements.

- Union status of dismissed workers: According to the Trade Union and Labor Relations Adjustment Act, an organization will not be regarded as a trade union when persons who are not workers are allowed to join it. In particular, dismissed workers are not allowed to retain their membership in a trade union as soon as the dismissal has become valid.

As the long drawn-out saga over the recognition of the second national trade union center, the Korean Confederation of Trade Unions (KCTU) has shown, the fact that some trade union officials are dismissed or unemployed workers can lead to difficulties in securing legal recognition of a trade union by the authorities. If the law remains unchanged, this problem is bound to reappear as new unions are formed and seek to register with government authorities<sup>2</sup>. This particular provision of Korean labor law has no counterpart in other OECD countries which consider qualifications for membership as a matter for the union itself to decide and not to be set down in legislation<sup>3</sup>.

- Multiple trade unions at the enterprise level: Though the revised 1997 *Trade Union and Labor Relations Adjustment Act* makes it legally

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<sup>1</sup> The law has thus incorporated employer concerns that they will at that time be forced to support large numbers of paid full-time union officials from both FKTU- and KCTU-affiliated enterprise unions. Already under current conditions, employer associations complain that their members are forced to pay an unusually high number of union officers in relation to the workforce members they represent compared with the situation in other OECD countries

<sup>2</sup> Although the February 1998 Tripartite Commission Agreement did recognize unemployed workers' rights to join a trade union or remain a union member (although not at enterprise level), a corresponding bill subsequently submitted by the government was rejected by the National Assembly. Despite repeated statements of intent by the government, no further bill has been submitted, as there seems to be disagreement among the Ministries concerned as to which groups among the unemployed might be allowed to join upper-level trade union organizations (in particular, as concerns the length of their unemployment spell).

Most trade unions in OECD countries have varying proportions of students, self-employed, unemployed and retired workers among their ranks (OECD 1991, Chapter 4).

possible to form multiple trade unions at industrial and national levels, on the enterprise level, multiple unions will only be allowed from January 2002 onwards.

- Union rights of civil servants: Civil servants are not allowed to join trade unions. Following agreement in the Tripartite Commission in February 1998, the establishment of workplace associations in the public service is allowed since January 1999, but due to certain restrictions over one third of public service personnel is ineligible to join such associations.

The ILO has expressed concern over these restrictions, in particular that there is no timetable for allowing union rights to public servants.

- Right to strike in the public sector: Strikes by workers in central and local government and those engaged in the production of military goods are prohibited, which is not unusual in OECD countries. However, the law also restricts the right to strike in the more broadly defined public sector, including regular public transportation services; gas, electricity and water; oil refineries and oil supply; hospitals and other medical services; banks and the Mint; broadcasting and communication.

The ILO has repeatedly asked the Korean government to ensure that restrictions on the right to strike only apply to essential services in the "strict sense of the term", under conditions of an "imminent threat to the life, personal safety or health of the whole or part of the population" (ILO, 1996 and 1998).

Korea is not unique in restricting the right to strike in some public services. However, Korean labor law provisions seem to go farther than in other OECD countries in that they set out an unusually broad definition of "essential services" where a strike ban covering entire sectors is maintained.

### *Lack of Trust among the Social Partners*

It is more necessary than ever to create a less confrontational and more consensual system of industrial relations if the Korean economy and society is to modernize and prosper. Trust and co-operation among the social partners can play an important role in fostering a dynamic, knowledge-based economy. Unfortunately, past confrontational attitudes between the social partners have re-surfaced recently in a context of economic recovery. The result is that consensus on wage moderation and necessary reforms of employment conditions and workforce practices are increasingly difficult to achieve. Moreover, the social partners have not even agreed on a common agenda for discussions by the Tripartite Commission and the prospect for the Commission to find satisfactory solutions to outstanding issues seems rather

remote at present.

One manifestation of these confrontational attitudes is the long-standing practice of arresting and imprisoning trade union leaders and members for violations of existing laws. This particular feature of industrial disputes in Korea is a matter of considerable concern to the OECD and the ILO. Successive waves of arrests of trade unionists not only represent a threat to fundamental workers' rights, but they also damage trust among the social partners. During the economic crisis and its aftermath, many union members reacted strongly to the announcement of business restructuring and collective dismissals. This included takeovers of plants and equipment, acts of violence and strike action in some essential services where, as noted above, Korean law prescribes conflict resolution through arbitration. These events gave rise to a sharp upsurge in arrests of workers and union officials. The ILO's Committee on Freedom of Association has repeatedly urged the Korean government to take appropriate measures so that the persons detained or on trial as a result of their trade union activities are released or that the charges against them are dropped. It has objected, in particular, to the use of the clause in the Penal Code relating to "obstruction of business" as a basis for the arrest of union demonstrators and strike participants.<sup>4</sup> The Korean authorities, for their part, argue that the concerned trade unionists have been arrested on such grounds as violence during strikes, unlawful occupation of premises or serious damage to company facilities. They have also announced a plan to "minimize" the number of arrests through focusing mainly on strike leaders and through applying fines, but not detaining other participants.

In sum, although it is not possible to assess the extent to which these pending issues have undermined labor-management relations, it is likely that addressing them urgently will contribute to a better climate of trust between the social partners. This, in turn, is an essential element in fostering a less confrontational system of industrial relations. Not only would this benefit Korean workers and firms but it would also increase the attractiveness of Korea as a location for foreign direct investment.

### *A Low Employment-Population Ratio*

The sharp fall in the open unemployment rate recently (to 4.7 % in March 2000) is most welcome news. However, there remains considerable room for increasing the number of jobs. Indeed, the employment-population ratio in Korea is relatively low by international comparison. In 1999, the overall employment-population ratio was less than 60 % -- 5 % age points below the OECD average (Table 16.1). The employment-population ratios

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<sup>4</sup> The OECD's Employment, Labor and Social Affairs Committee has repeatedly expressed the view that the definition of "unlawful activities" in Korea is unusually broad and encompasses union activities that would be regarded as lawful in most OECD countries.



of women and youth are particularly low by international standards<sup>5</sup>.

In addition, though the open unemployment rate is currently below the OECD average, there is a substantial degree of labor market slack. This is illustrated by the high numbers of discouraged workers (the total participation rate in 1999 was 1.7% points lower than in 1997) and participants in labor market programs such as public works. Finally, economic restructuring among the chaebols is still underway and its completion may entail further significant job losses.

### *An Extremely High Degree of Labor Market Duality*

More fundamentally, Korea has one of the most "dual" labor markets in the OECD area, as illustrated by the following facts:

- In 1999, more than half of all employees had either a temporary or a daily contract, the remaining having a "regular" (*i.e.* open-ended) contract. In international comparisons, Korea has the highest share of non-regular jobs in total employment, followed by Spain, while the number of workers holding a permanent job is the lowest among OECD countries, followed by Turkey (Table 16.2). Younger and higher-educated men hold most regular jobs, while the incidence of non-regular work is particularly high among women, older workers and the lower-educated (Chart 16.1). The incidence of self-employment is among the highest for OECD countries together with Mexico and second only to Turkey. Unpaid family workers make up about 10% of total employment in Korea, while this figure varies between 0% and 3% in most other OECD countries.
- Reflecting the high incidence of non-regular employment, average job tenure (*i.e.* the length of stay in the same enterprise) is low by international comparison. In 1998, the average Korean worker stayed slightly over six years with the same employer-- in 1995, the figure was almost ten years in the case of the European Union and over eleven years in Japan (Table 16.3). Average tenure is even lower in Korea than in the United States. Job tenure is especially low for Korean female workers. Average job tenure for men was almost seven years in 1998, while average job tenure for women was just over four years in 1998 -- by contrast, in 1995, the unweighted average for OECD countries was 10.4 years for men and 8.4 years for women. It also appears that workers with a college degree enjoy longer job tenures than lower-educated ones. However, tenure is higher for the lower-educated (those

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<sup>5</sup> On the other hand, the employment-population rate of workers aged 55 to 64 is among the highest in the OECD area. Given the modest level of retirement pensions, Koreans tend to work until late in their lives.

**Table 16.1: International comparison of employment/population ratios," 1999**

	Total				Men	Women
	All ages <sup>2)</sup>	15 to 24	25 to 54	55 to 64	All ages <sup>2)</sup>	All ages <sup>2)</sup>
Australia	68.2	60.8	75.4	44.3	76.5	59.9
Austria	68.2	54.9	81.3	29.2	76.7	59.7
Belgium	58.9	25.5	76.4	24.7	67.5	50.2
Canada	70.1	54.6	79.2	46.9	75.5	64.7
Czech Republic	65.9	40.1	81.9	37.5	74.3	57.4
Denmark	76.5	66.0	84.4	54.2	81.2	71.6
Finland	66.0	38.8	80.3	39.2	68.4	63.5
France	59.8	20.8	77.0	34.2	66.8	52.9
Germany	64.9	46.8	78.2	38.5	73.1	56.5
Greece <sup>3)</sup>	55.6	28.1	69.9	39.1	71.6	49.0
Hungary	55.7	35.7	72.3	19.4	62.6	49.0
Iceland <sup>4)</sup>	84.2	65.1	90.9	85.9	88.2	80.2
Ireland	62.5	46.4	73.2	43.8	73.5	51.3
Italy	52.5	25.5	66.9	27.5	67.1	38.1
Japan	68.9	42.9	78.7	63.4	81.0	56.7
<b>Korea, 1997</b>	<b>63.7</b>	<b>31.7</b>	<b>75.0</b>	<b>63.7</b>	<b>76.0</b>	<b>51.6</b>
<b>Korea, 1998</b>	<b>59.5</b>	<b>26.3</b>	<b>70.3</b>	<b>59.0</b>	<b>71.7</b>	<b>47.4</b>
<b>Korea, 1999</b>	<b>59.7</b>	<b>26.8</b>	<b>70.4</b>	<b>58.1</b>	<b>71.5</b>	<b>48.1</b>
Luxembourg	61.6	31.7	76.7	26.3	74.4	48.5
Mexico	61.2	50.8	67.8	55.2	84.8	39.6
Netherlands	70.9	62.7	80.6	35.3	80.3	61.3
New Zealand	70.0	54.6	77.6	56.9	77.3	63.0
Norway <sup>4)</sup>	78.0	57.8	85.5	67.3	82.1	73.8
Poland <sup>3)</sup>	58.9	28.6	75.0	32.3	65.8	52.2
Portugal	67.3	43.2	80.8	50.8	75.5	59.4
Spain <sup>4)</sup>	53.8	33.9	65.6	34.9	69.6	38.3
Sweden <sup>4)</sup>	72.9	43.8	82.6	64.0	74.8	70.9
Switzerland	79.7	64.7	85.2	71.7	87.2	71.8
Turkey	51.9	42.6	57.8	42.6	71.7	32.0
United Kingdom <sup>4)</sup>	71.7	60.8	79.7	49.4	78.4	64.9
United States <sup>4)</sup>	73.9	59.0	81.4	57.7	80.5	67.6
Total OECD <sup>5)</sup>	65.9	46.7	75.9	48.9	76.6	55.4

Notes. 1) Employment/population ratios refer to persons in employment divided by the working-age population for the relevant groups.

2) 'All ages' refers to 15 to 64.

3) Data refer to 1998.

4) Age group 15 to 24 refers to 16 to 24, and "All ages" refers to 16 to 64.

5) For above countries only.

Source: OECD (June 2000). Employment *Outlook*, Statistical Annex. Tables B and C.

**Table 16.2: International comparison of employment by status of workers, 1999<sup>1)</sup>**

	Employees			Unpaid family workers <sup>2)</sup>	Self-employment
	Total	Permanent/regular	Non-permanent/Non-regular		
(% of total employment)					
Australia	86	63	23	1	14
Austria	86	80	7	3	11
Belgium	82	75	6	3	15
Canada	82	73	10	0	17
Czech Republic	86	80	7	0	13
Denmark	91	81	9	1	8
Finland	86	71	15	1	14
France	89	77	12	0	11
Germany	89	78	11	1	10
Greece	55	48	7	12	33
Hungary	85	81	5	1	14
Iceland	82	73	9	0	18
Ireland	79	72	7	1	20
Italy	72	65	6	4	24
Japan	83	73	10	6	12
<b>Korea, 1997</b>	63	34	29	9	28
<b>Korea, 1998</b>	61	32	29	10	29
<b>Korea, 1999</b>	62	30	32	9	29
Luxembourg	93	90	3	0	7
Mexico	61	51	10	10	29
Netherlands	88	77	11	1	11
New Zealand	80	n.a	n.a	1	19
Norway	92	81	10	1	8
Poland <sup>3)</sup>	70	n.a	n.a	5	26
Portugal	71	59	12	2	27
Spain	77	52	25	3	20
Sweden	89	78	11	0	10
Switzerland	87	77	10	2	11
Turkey	44	35	8	25	31
United Kingdom	87	81	6	1	12
United States	92	n.a	n.a	0	8

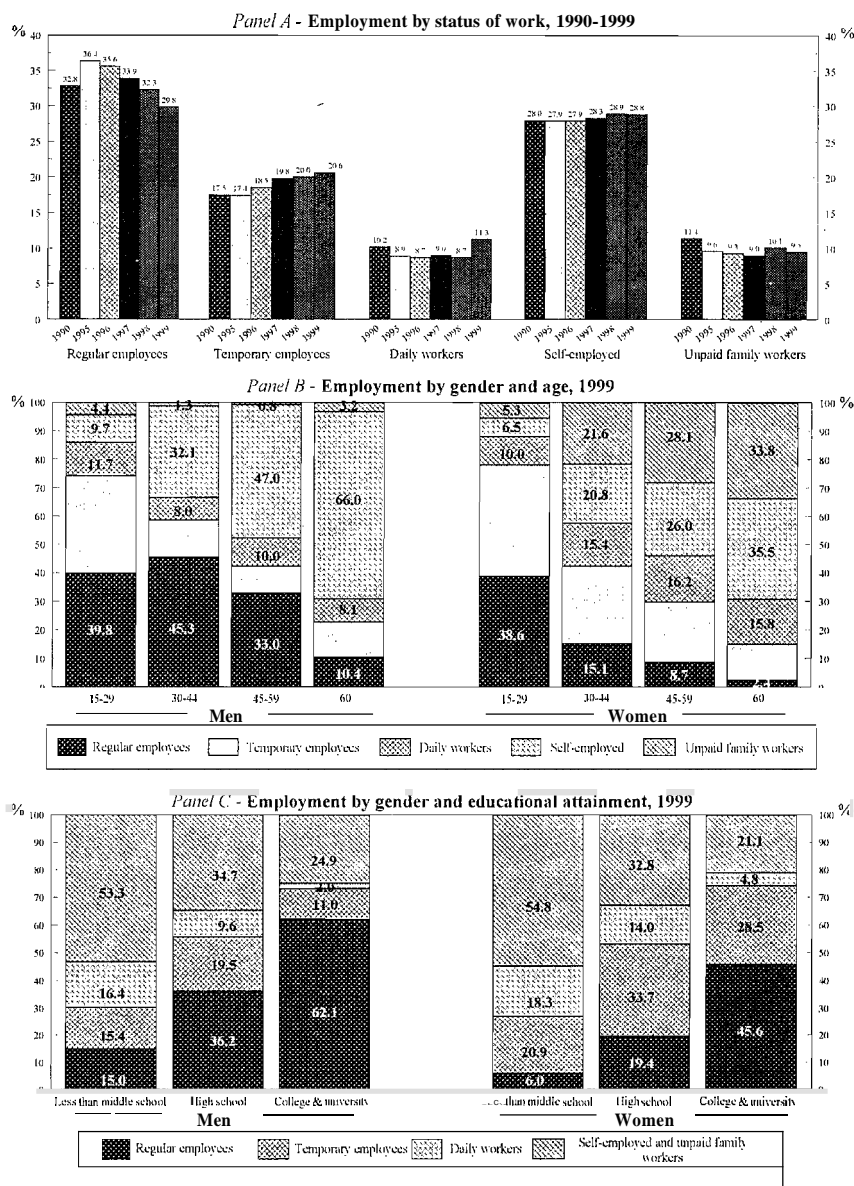
Notes: 1) Data relate to 1997 for Greece, Ireland, Luxembourg and Portugal; and as indicated in the case of Korea.

2) Figures less than 0.5 appear in the column as zeros in italics.

n.a) Data not available.

Sources: Korea: National Statistical Office (1997 and 1998), Annual Report on the *Economically Active Population Survey* (December 1999), Monthly Report on the *Economically Active Population Survey* Japan: Ministry of Labor (1998), Year Book of *Active Population Labour Statistics*; and for other countries: OECD (1999), Labour Force Statistics (for data on total employees, unpaid family workers and self-employment), and OECD/DEELSA Statistics and Indicators Division, temporary-work database (for the breakdown of permanent/non-permanent work)

Figure 16.1: Composition of employment by status of work in Korea, 1990-1999



Sources: Panel A. National Statistical Office (1998), Annual Report on the *Economically Active Population Survey*, and (December 1999), Monthly Report on the *Economically Active Population Survey*. Panels B and C. Direct submissions by the Korean authorities

Table 16.3: Job tenure in Korea and selected OECD countries

	Korea		European Union <sup>1), 2)</sup>		Japan <sup>1)</sup>	United States <sup>1)</sup>
	1996	1997	1998	1995	1995	1995
	(average number of years with the same employer)					
Total employees	5.4	5.7	6.1	9.8	11.3	7.4
Men	6.1	6.3	6.8	10.5	12.9	7.9
Women	3.7	4.0	4.3	8.8	7.9	6.8
Middle school and below	5.7	6.1	6.4	10.1	15.3	5.8
High school	5.1	5.4	5.8	9.4	11.4	7.9
Junior college	4.5	4.6	5.1			
College and university and over				10.1	9.5	7.4
	6.2	6.5	7.0			

Notes: 1) Average for different levels of educational attainment are based on weighted averages of mid-points of tenure classes. The two highest educational levels are not shown separately and correspond to some or completed tertiary education. These data were published in Table 5.6, CECD employment Outlook, July 1997.

2) Unweighted average on the different breakdowns of tenure for the 15 member countries.

Sources: For Korea: Direct submissions by the Ministry of Labor on the basis of the report on Wage Structure Survey; For other countries: OECD (July 1997), Employment Outlook, Table 5.6.

Table 16.4: Coverage of the employment insurance system (EIS) in Korea, July 1995 to February 2000

	July 1995	January 1998	July 1999	February 2000
	('000s)			
Paid workers	12824	12500	12603	12819
Eligible workers	4280	5190	8342	8700
Insured workers	4204	4309	5876	6172
As a proportion of eligible workers (%)	(98.2)	(83.0)	(70.4)	(70.9)

Source: Direct submission by the Korean authorities, and Secretariat estimates

with educational attainment of middle school and below) than for those with high-school education or junior college -- signaling problems in the school-to-work transition.

- Regular workers tend to work in large firms. This is important because the wage gap between large and small firms has been growing in recent years (Chart 16.2). Working in a large firm entails other benefits to workers: *a*) in 1995, the unionization rate in firms with more than 300 workers exceeded 80 %, whereas it was only 5 % in firms with less than 100 workers (and probably almost nil in small businesses); *b*) workers in large firms are covered by both the Employment Insurance System and the National Pension System which, despite government efforts to expand coverage, is far from being the case in small firms; and *c*) in 1999, nearly 40 % of workers in large firms received in-plant training, compared with less than 3 % in small firms.

While there are probably many factors which account for such a pronounced degree of duality in the Korean labor market, employment protection is an important part of the story. Indeed, regular workers enjoy a relatively high level of employment protection. For instance, severance pay amounts to one monthly wage per year of seniority (with no maximum) and dismissal procedures remain complex and cumbersome despite recent reforms.<sup>6</sup> In addition, the preconditions for dismissals based on economic reasons (advance notification to a trade union, verifiable efforts to avoid dismissal, etc.) make conditions in Korea resemble closely those in other high-protection countries such as Japan, Portugal, France or Germany. Finally, the new provisions on notification of collective dismissals to the Ministry of Labor correspond to the strict regulations in force in EU countries. Overall, the OECD has ranked Korea as the second strictest country out of 27 Member countries in terms of protection of regular (or permanent) employment contracts<sup>7</sup>. By contrast, employers are under no obligation to provide severance pay to temporary and daily workers who stay less than one year in their enterprise.

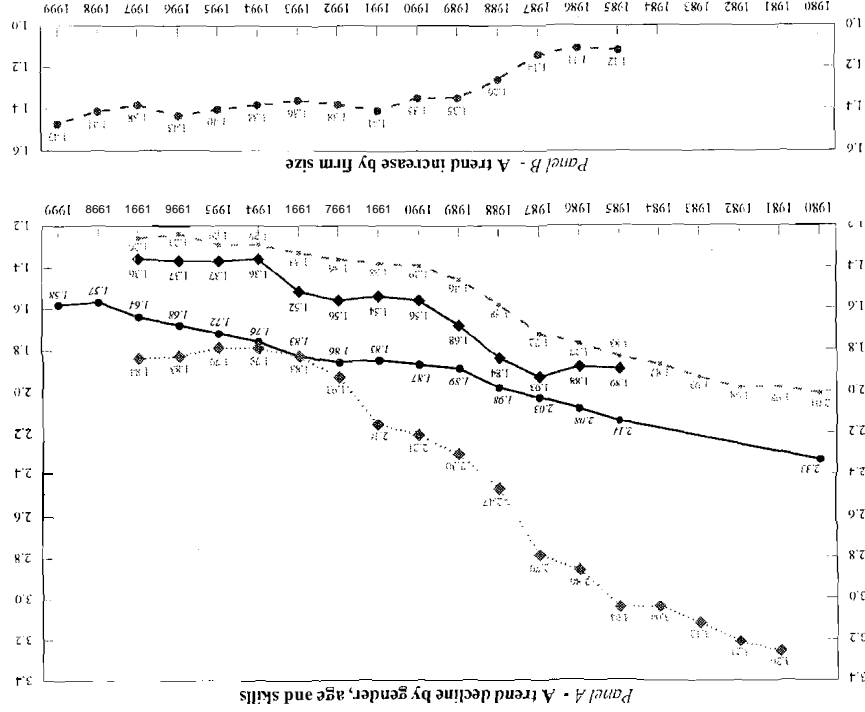
Another possible explanation is the structure of product markets. Competition among large firms is weak (domestically), reflecting cartel-type arrangements. At the same time, large firms have managed to sub-contract work to small ones, to remain competitive. As noted above, regular workers are concentrated in large firms, implying possibilities for rent-sharing between them and their employers.

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<sup>6</sup> While the one-month notice period, even for workers with high tenure, is low by international standards, the legal severance pay requirements applying to regular workers would seem to be relatively onerous.

<sup>7</sup> For details, see OECD (1999a, Chapter 2)

Figure 16.2: Wage differentials (ratios) in Korea, 1980-1999 1)



Note: 1) Average annual wages including all wage components as in Chart 2.3, referring to establishments with 10 workers or more.

Sources: Ministry of Labor (Various Issues), *Survey Report on Wage Structure*, for data by gender, age groups and educational attainment; (Various Issues), *Monthly Labor Survey*, for data on firm size; and direct submission from Korea Labour Institute for data on occupational status. Figures for 1998 and 1999 are provisional estimates supplied by the Korean authorities.

If the recovery continues, the expectation is that employers will become more confident about future economic prospects and that, as a result, they will be less reluctant to convert non-regular jobs into regular ones. However, it should be stressed that the incidence of regular employment did not increase much in 1990-97, a period characterized by near-full employment. Thus, job precariousness seems to be a structural characteristic of the

Korean economy, which is problematic not only from the social point of view, but also for reasons of economic efficiency. Indeed, as noted earlier, job precariousness seems to be associated with a relatively low incidence of vocational training (in particular in small businesses), in turn inhibiting productivity growth.

### *A Relatively Modest Social Safety Net*

As part of its response to the crisis, the Korean government implemented many temporary measures such as public works programs and temporary social assistance support in order to provide income support to displaced workers and their families. Despite this welcome expansion of the social safety-net, OECD (2000a) concludes that it is still too modest relative to equity and social insurance considerations in the following dimensions:

- The Employment Insurance System (EIS), which is the main pillar of the social safety net, was created in 1995 and, despite the recent extensions of its coverage, still does not cover all eligible workers. According to the latest available data, 71 % of workers eligible for the EIS are actually insured (Table 16.4). Reflecting the legal eligibility requirements as well as practical difficulties in increasing the coverage of the EIS, the proportion of unemployed workers who receive an unemployment benefit is very low: in the first half of 1999, only one in eight of the unemployed (Table 16.5). In all other OECD countries for which data are available, the share of the unemployed that receive benefits is significantly larger -- in certain countries, almost all unemployed workers are granted an unemployment benefit.
- Not only is EIS coverage limited by comparison with other OECD countries but, in addition, benefits are rather modest for the limited number of unemployed workers who receive them. The (daily) job-seeking allowance amounts to 50 % of the so-called "basic daily wage" at the time of separation<sup>8</sup>. The maximum duration of payment of unemployment benefits ranges between three and eight months, depending on the age at the time of job loss of the recipient and the period of contribution to the EIS (the insured period)<sup>9</sup>. OECD (2000a)

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<sup>8</sup> The job-seeking allowance is subject to a ceiling and it cannot fall below a minimum level. The ceiling for the job-seeking allowance is set at 30,000 Won per day, i.e. approximately US\$ 25 per day or 56 % of the average daily wage. Since January 2000, the minimum job-seeking allowance has been raised to 90 % of the minimum wage (up from 70 % before January) or about US\$ 9.5. The minimum job-seeking allowance is now slightly above the minimum cost of living, which in December 1999 was officially estimated at 268,500 Won per month, or US\$ 7.5 per day.

<sup>9</sup> It is, however, possible for a job seeker to obtain an extension of the payment of benefits --thereby lengthening the maximum duration of benefit payment. This possibility



shows that, in most respects, benefits provided by the Korean unemployment insurance system are less generous relative to expected earnings than is the case in the majority of the other OECD countries where such benefits exist.

**Table 16.5: Characteristics of unemployment benefit recipients in Korea, first semester of 1999**

	Unemployed workers	Number of unemployed workers who acquired the right to receive unemployment benefit	
	(000s)	(000s)	Percentage of unemployed workers
Total	1,592	187	11.7
Gender			
Men	1,071	126	11.8
Women	521	61	11.7
Age			
Less than 30	617	42	6.8
30 to 39	403	57	14.1
40 to 49	326	40	12.3
More than 50	246	47	19.1
Educational attainment			
Primary school and under	179	12	6.7
Middle school education	262	21	8.0
High school education	844	94	11.1
College and university	307	60	19.5
Firm size			
Less than 10 workers	971	27	2.8
10 to 299 workers	530	102	19.2
300 workers and over	91	58	63.7

Sources: National statistical Office (February 2000). Monthly Report on the Economically Active Population Survey; and Korea Labor Institute (1999b)

arises in three circumstances. *First*, the Employment Security Center may decide to extend the payment of benefits for a period of up to two months to any qualified recipients who have exhausted their ordinary benefits and face particular difficulties in finding a job -- this is termed "individual extended benefit". The job-seeking allowance for recipients of the individual extended benefit is 70 % of the ordinary job-seeking allowance, *i.e.* 35 % of the basic daily wage at the time of separation. But this is subject to the same floor as in the case of the normal job-seeking allowance, *i.e.* 90 % of the minimum daily wage. Second, in special circumstances such as when unemployment increases markedly, the Minister of Labor can decide to provide unemployed recipients who have exhausted their benefits with "special extended benefits" for a period of up to two months. The level of the special extended benefit is calculated as in the case of the individual extended benefit and is therefore subject to the same floor. Third, a recipient who participates in a training program on recommendation of the Employment Security Center can receive 70 % of the job-seeking allowance until the end of the program. The "training extended benefit" is paid for the entire duration of the training program, with a limit of two years.

- Training programs for the unemployed were expanded considerably during the crisis<sup>10</sup>. In both 1998 and 1999, more than 50,000 unemployed attended a training course, accounting for roughly one fifth of the unemployed in the period considered. However, most training programs for the unemployed appear to be insufficiently targeted at disadvantaged labor market groups. Available evidence suggests that unemployed workers covered by the EIS are more likely to receive training than other unemployed individuals and they also receive a higher training allowance than other trainees. Moreover, training programs for the unemployed tend to suffer from relatively high drop-out rates, while re-employment probabilities of those who complete the courses are low -- the estimated drop-out rate for the first six months of 1999 was over 23 % (Kang, 1999). This suggests some mismatch between the contents of the courses and labor market requirements. Finally, public training institutions have suffered from the fact that the increase in the number of trainees has not been accompanied by a corresponding increase in staff members, so that the average number of trainees per instructor has increased considerably. As a result, the quality of public training may have worsened.
- In the face of the sudden rise in unemployment and given the low coverage of unemployment benefits and training programs, the Korean authorities decided to expand considerably public works programs. Available data suggest a certain success in terms of number of participants. In 1998, almost half a million people were involved in these programs and the figure was 50 % higher in 1999. However, the implementation of the programs has been criticized on different grounds. First, selection criteria for participation have been applied with some laxity. In contrast with the official targets, the incidence among total participants of well-educated individuals and prime-age workers has been relatively high. Second, some individuals have allegedly participated in a public works program while continuing to receive unemployment benefits or other public income support. Third, these programs may have crowded out private-sector jobs. Indeed,

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<sup>10</sup> The main training programs available to the unemployed are a) re-employment training of the unemployed, a program targeted to workers dismissed from enterprises covered by the EIS, independently of whether these workers are entitled to unemployment benefits or not; b) training for employment promotion, which focuses on dismissed workers not previously insured under the EIS, *i.e.* mostly temporary, daily and part-time workers; c) training for unemployed new entrants into the labor market (but most young unemployed have been granted internships under public works programs, as discussed below); d) training for business start-ups, targeted at elderly unemployed, disabled individuals and school drop-outs; and e) manpower development training, which comprises initial training for craftsmen and training for "3-D" jobs. Of these, only the first program is set up under the EIS and therefore funded by the Employment Insurance Fund. The others are financed out of the general government budget.

wages paid to participants on public works programs are higher than market wages for certain occupations in agriculture and 3-D jobs. The average daily wages of public works participants vary between 19,000 Won for basic skills work and 29,000 Won for professional and skilled jobs. This is much higher than the minimum wage, which is currently set at 12,800 Won per day. In addition, it comes close to the average wage in occupations for unskilled workers, which is about 25,000 Won per day.

Second, social assistance programs do not cover adequately those in need and benefits are below the poverty line. The number of beneficiaries of the main social assistance programs -- Livelihood Protection Program (LPP) and Temporary Livelihood Protection (TLP) -- is close to 2 million in 2000, or about 4.4 % of the population. Nevertheless, coverage of LPP and TLP beneficiaries did not exceed 55 % of the poverty population in 1999 -- the remaining 45 % do not receive any social assistance benefits. To some extent, the relatively low coverage rate can be explained by the fact that some would-be beneficiaries do not apply for benefits because either they are not aware of their existence or receiving benefits entails a certain stigma. However, other factors have also played a role, notably the relatively strict eligibility criteria, the low level of benefits and benefit administration problems:

- ❑ Strict eligibility criteria: Benefits under both the LPP and TLP are subject to means-tests based on specific family income criteria. But in the case of the LPP, the means-test is based on the capacity (to earn) of extended-family members." Among OECD countries, this is an unusually strict interpretation of family support criteria. The usual practice is that actual income is taken into account -- as, for example, in Switzerland (OECD, 1999b).
- ❑ The low level of benefits: The level of social assistance payments depends on the type of program, but also on family and income criteria. At maximum, social assistance payments are equivalent to 60 % of the official poverty line (Table 16. 6). Income support to recipients who are supposed to be unable to work (*i.e.* the recipients of home-care and *institutional-care* support) is more generous than payments to able-bodied recipients (self-support care recipients -- see grey-shaded area in the Table). In addition, income support to home-care beneficiaries under the LPP is provided throughout the year, whereas *self-support*

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<sup>11</sup> Thus, under present rules, a person with an income barely above subsistence level may not be entitled to social assistance benefits if the combined earnings' capacity of the individual and his/her family exceeds a certain threshold. It is unclear, however, how the earnings' capacity (as opposed to actual earnings, which are easier to verify) is assessed in practice.

Table 16.6: Monthly benefit levels per household, under the livelihood protection program in Korea, 2000<sup>1)</sup>

	Household size (% of the monthly minimum cost of living)					
	1 person	2 persons	3 persons	4 persons	5 persons	6 persons
<b>Benefit level for a household qualifying for home-care support, by level of household income</b>						
Household income (won)						
240,000 to Minimum cost of living (MCL)	9	9	9	- <sup>2)</sup>	- <sup>2)</sup>	- <sup>2)</sup>
200,000 to 240,000	25	29	29	28	28	- <sup>2)</sup>
160,000 to 200,000	28	33	33	33	33	33
120,000 to 160,000	31	34	34	34	34	35
80,000 to 120,000	35	38	38	38	38	38
40,000 to 80,000	47	44	44	44	44	44
0 to 40,000	60	51	51	51	51	51
<b>Benefit levels for a household qualifying for self-support care and temporary livelihood protection, by level of household income</b>						
Household income (won)						
240,000 to MCL	9	9	- <sup>2)</sup>	- <sup>2)</sup>	- <sup>2)</sup>	- <sup>2)</sup>
0 to 240,000	25	29	29	28	28	27
<b>Memorandum items</b>						
MCL(won)	324,011	536,614	738,076	928,398	1,055,588	1,191,134
MCL(US\$)	270	447	615	774	880	993

Notes: 1) Payments to home-care clients vary with household size, not with the age of household members.

2) No benefits are paid.

Source: Ministry of Health and Welfare, Korea.

*care* clients receive benefits during six months only (October to March).<sup>12</sup> Benefits provided to able-bodied recipients amount to about one quarter of social assistance payments in Switzerland, and half of what a Czech family in a similar situation would receive (OECD, 1998a, and 1999b).

- The impact of restricted public budgets on the adequacy of welfare provisions: Each year, each local government is provided with a budget for social assistance programs. As the budgetary allocations awarded by the Ministry of Planning and Budget are generally considered short of what is needed to serve all the poor, there is inevitably some rationing in benefit awards. Clients may therefore receive less than what they might have been legally entitled to and, in certain cases, they will receive no benefits at all.

Because of these deficiencies, social assistance programs have not counteracted the increase in income inequalities -- over the past three years, average incomes of the poorest 20 % of households have declined by over 8 %, while average incomes of the richest 20 % of households have increased somewhat. Nor have they eradicated poverty. In 1999, 8 % to 12 % of Koreans (depending on the source) were officially estimated to live in poverty -- based on a minimum monthly cost of living representing the equivalent of US\$ 350 (in purchasing power parity terms). While it is the case that the extended family has long provided an effective source of income support in Korea, the supportive role of the extended family has weakened in recent years and the public social safety-net has not expanded sufficiently to take up all the slack.

### *Weak Multi-Factor Productivity Gains*

The prospects for continuing convergence in Korean living standards towards the OECD average depend crucially on continuing rapid economic growth. Economic growth, in turn, is mainly determined by *a*) the investment effort; *b*) the extent to which unused labor supply can be mobilized in the economy; and *c*) multi-factor productivity growth, which is a measure of the underlying efficiency gains recorded by firms. As is well-known, the fast growth recorded until 1997. was mainly based on the first factor, namely a spectacular investment effort. Thus, over the period 1990-96, Korea devoted 37 % of its yearly national income to real fixed capital accumulation. On the other hand, over the 1990s, multi-factor productivity practically stagnated, whereas it grew in nearly all other OECD countries

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<sup>12</sup> About 30% of self-support care clients receive these benefits. The remaining 70% can receive education benefits, medical aid and funeral grants.

(Table 16.7).<sup>13</sup> This is all the more surprising because multi-factor productivity is generally expected to grow faster in countries such as Korea which are catching-up on the most advanced OECD countries.

**Table 16.7: International comparisons of multi-factor productivity growth," 1980-1998**

	1980-1990	1990-1998 <sup>2)</sup>
	<b>(Average annual growth rates)</b>	
<b>Australia</b>	0.8	2.1
<b>Austria</b>	1.0	0.6
<b>Belgium</b>	1.1	0.7
<b>Canada</b>	0.3	0.7
<b>Denmark</b>	0.8	1.9
<b>Finland</b>	2.1	3.1
<b>France</b>	1.5	0.9
<b>Germany<sup>3)</sup></b>	1.1	1.0
<b>Greece</b>	0.0	0.4
<b>Iceland</b>	4)	0.4
<b>Ireland</b>	3.3	3.5
<b>Italy</b>	1.2	1.2
<b>Japan</b>	1.6	0.8
<b>Korea</b>	1.3	0.0
<b>Netherlands</b>	1.1	1.1
<b>New Zealand</b>	0.6	1.0
<b>Norway</b>	0.6	1.8
<b>Portugal</b>	0.9	1.9
<b>Spain</b>	1.4	0.7
<b>Sweden</b>	0.9	1.7
<b>Switzerland</b>	0.1	-0.1
<b>United Kingdom</b>	1.9	0.4
<b>United States</b>	0.8	1.1
<b>Memorandum items(Korea)</b>		
<i>Investment to GDP ratio(%)</i>	30.0	37.0
<i>Total employment growth</i>	2.8	2.3
<i>Business-sector capital stock growth</i>	10.9	11.5

Notes: 1) Multi-factor productivity is calculated as the weighted average of capital and labour productivity, with the weights measured as average factor shares: the weight attached to labour productivity equals the ratio of total compensation of employees to GDP averaged over the period under consideration; the weight attached to capital productivity equals one minus the weight attached to labour productivity. No adjustment has thus been made for the imputed wage income of the self-employed.

2) 1997 for Australia, Belgium, Canada, Italy, Japan, Norway, Spain and the United States; 1996 for Austria, Finland, Greece, Ireland, Korea, Sweden and the United Kingdom; 1995 for New Zealand and Switzerland; 1992 for Iceland and Portugal.

3) For Germany, data relate to 1991 instead of 1990; Western Germany before 1991.

4) Data not available

Source: Secretariat estimates. For Korea, estimates for the capital stock of the business sector were supplied by Professor Hak K. Pyo.

<sup>13</sup> See Pilat (1993) for a similar finding

It is therefore essential that future policy strategies focus on improvements in productivity, as well as a greater mobilization of individuals who are presently on the margins of the labor market. The experience of other OECD countries suggests that effective training, labor and social policies, which are reviewed in the next Section, are vital ingredients in such a strategy.

## Policy Requirements

Addressing the outstanding problems identified in the previous section would contribute to creating a more stable socio-economic climate, while also making the growth process more socially sustainable. In order to achieve this, this section puts forward a range of possible policy reforms.

### *Freedom of Association and Collective Bargaining Rights*

As noted above, there is no doubt that recent legislative reforms have shifted Korean labor laws significantly in the desired direction. Major examples include the recognition of the principle of trade union pluralism at the industry and national levels, the legalization of teachers' unions, freedom for many civil servants to engage in workplace associations, some reduction of the list of so-called "essential services" where compulsory arbitration applies, as well as the recent recognition of the KCTU as the second national trade union center. In addition, the government has decided to allow trade union pluralism at the enterprise level from 2002.

However, Section II also highlighted some outstanding issues and resolving them would probably contribute to create a climate of trust between the social partners. *First*, civil servants are not allowed to join trade unions and bargain collectively. *Second*, trade unions face legal and practical impediments in deciding who to accept as members and these should be removed. *Third*, the law will, as of 2002, prohibit the payment of full-time union officials. On these three issues, the government, in consultation with social partners, should explore avenues for amending the relevant provisions of the law. Finally, over the past few years, waves of militant trade union action and subsequent arrests and imprisonments of trade unionists have succeeded each other. It will thus be particularly important for the Korean authorities to take all the necessary steps to avoid large-scale arrests and detentions of trade unionists. In particular, legal provisions, which are often used to arrest trade unionists engaged in the pursuit of what other OECD countries consider legitimate trade union activities, need to be revised or used with utmost restraint.

Alongside further progress on the legislative front, the present climate of industrial relations in Korea at both the national and enterprise levels must be improved. The repeated withdrawals by both labor and business representatives from the Tripartite Commission and the lack of any agreed agenda and timetable for its discussions are disturbing. In order to foster social dialogue and mutual trust in the Tripartite Commission, the government could take the lead by presenting reform proposals for discussion in the Commission. Needless to say, the government should also make appropriate efforts to act upon compromises reached within the Commission (as required by the 1999 Tripartite Commission Act). While the social partners need to recognize the futility of "empty chair" attitudes and come forward themselves with constructive proposals rather than always looking to the government to solve deadlocks. Perhaps more importantly from the point of view of Korean productivity performance, tripartite agreements at the national level need to be supplemented by active labor-management consultation and effective co-operation at the enterprise level.

### *Labor Regulations and Public Pensions*

Dismissals of regular workers have long been heavily regulated in Korea. In the past, employers faced considerable legal and practical difficulties for laying off workers. An amendment to the Labor Standards Act adopted in 1998 makes it possible to dismiss workers for "urgent managerial needs". However, while the new lay-off provisions are clearly a step in the direction of increasing numerical flexibility in firms, "regular" workers still enjoy a relatively high degree of employment protection compared with their counterparts in other OECD countries.

There would, therefore, seem to be room for easing the legal severance pay requirements for regular workers. This reform, however, should take place gradually, and be dependent on a) the Employment Insurance System (EIS) becoming more firmly established in coming years (see below); and b) the public pension system being adequately funded, which is far from being the case at present, and pension benefits providing sufficient income support.

Relaxing relatively strict employment protection for regular workers, under the above conditions, could also help ease job instability for temporary and daily workers (who form the core of "outsiders" in Korea). This would hopefully encourage employers to convert more non-regular contracts into regular ones, thereby reducing the degree of labor market segmentation, which is presently very pronounced, and laying the ground for greater investment by both workers and firms in on-the-job training.

At the same time, it would be highly desirable to undertake more research on the causes and implications of the marked duality that presently exists in the Korean labor market. For instance, it would be useful to examine workers' perceptions of the non-regular forms of employment -- certain workers may prefer temporary jobs rather than permanent ones. In addition,



labor market duality has gone hand-in-hand with a stagnant multi-factor productivity performance -- itself one of the symptoms of the 1997 crisis, and more attention should be devoted to the possible causality at work. Analyzing the transition between non-regular and regular jobs would help to determine which groups are at greatest risk of getting trapped in non-regular jobs. Finally, the possible links between the stringency of employment protection legislation and the lack of competition in product markets on the one hand and the incidence of non-regular forms of employment on the other should be investigated.

#### *Labor Market Program and the Public Employment Service*

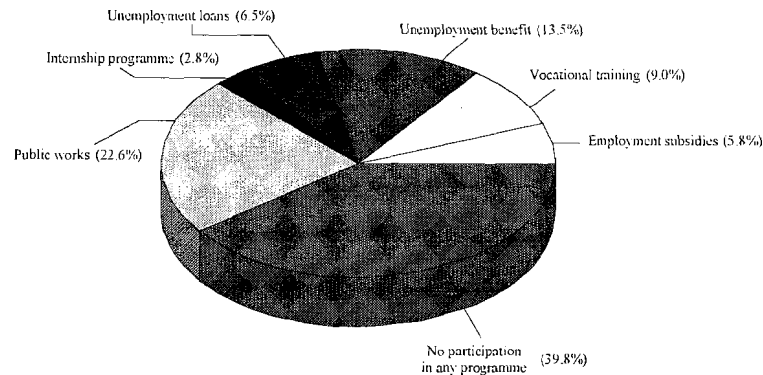
Labor market programs have to be evaluated in the light of their twin objectives, namely *a*) to provide income support to the unemployed; and *b*) to foster the future employment and earnings prospects of unemployed workers, while minimizing the dead-weight, substitution and displacements effects often associated with such policies.

Regarding the first objective, the portfolio of labor market programs in Korea has been expanded considerably in the past two years. However, as noted above, only one in eight of the unemployed receive unemployment benefits (in addition, Chart 16.3 shows that less than half participate in some type of labor market program, the others being potential clients for social assistance benefits). It has recently been decided to expand the scope of the EIS to cover daily workers, but there remain serious implementation problems, in particular among small firms which often evade the payment of social contributions. The current situation is not satisfactory and the government should assign a high priority to increasing the coverage of the EIS and ensuring that vulnerable groups are not left unprotected, as is presently the case.

As to the effects of active labor market programs (ALMPs), it is not possible to draw clear-cut conclusions in the absence of any systematic evaluations. However, based on the examination of specific design features of the programs, the following observations can be made:

- There is a general lack of targeting in many of the programs. As a result, it is unclear whether they really reach disadvantaged groups, such as unemployed workers not covered by the EIS and young unemployed workers. Targeting is especially important in the case of subsidies to SMEs, given that this program is the largest in terms of government spending on ALMPs;
- despite a general lack of targeting, some of the programs are not much used. This suggests that some consolidation of programs may be called for, notably in the area of employment maintenance subsidies;

**Figure 16.3: Participation of unemployed workers in different labour market programs in Korea, 1999**



Source: Korea Labour Institute estimates

- ❑ now that a brisk recovery is underway, there is a strong case for scaling back substantially public works programs. International evidence (see Martin, 2000) suggests that these programs, unless they are well targeted on hard-to-place groups, are particularly susceptible to large dead-weight losses;
- ❑ there may be cases where work does not pay -- leading to a risk that some benefit recipients prefer to stay in the program rather than look actively for a low-paid, private-sector job. For instance, as noted in Section 2.5, remuneration in public works programs competes with market wages in certain unskilled occupations;
- ❑ training institutions have had difficulties in coping with the rapid and massive expansion of training programs. In addition, the type of training provided by some of them may not be closely tied to the requirements of a complex, modern economy such as Korea. For these reasons, there is a good case for a greater involvement of the social partners at the local level in program design, while also expanding the training capacity; and
- ❑ the outcomes of the programs should be monitored and evaluated rigorously.

Finally, the role of the public employment service (PES) in the design and implementation of ALMPs could be enhanced. The concept of the "one-stop office" is a good one, and should be generalized by integrating the separate networks of Employment Security Centers and Manpower Banks. Also, while it may have been useful in the period of rising unemployment to operate another chain of placement offices under the authority of municipalities and other local governments, the rationale behind the co-existence of two types of "public employment services", one operating under the Labor Ministry and the other under local government, that are involved in the same types of tasks (apart from benefit payment), should be reviewed.

As mass unemployment declines, PES officers will need to devote more efforts to counseling and monitoring of those job-seekers who are at high risk of long-term unemployment and benefit dependency -- at present there is little "profiling" of the unemployed. Needless to say, the efficiency of the PES crucially depends on the quality of its staff and the high turnover of counselors is problematic in this respect. In present circumstances, improving training and job prospects for the PES staff might be more important than increasing the number of officers. The steep decline in unemployment should provide the necessary breathing space to concentrate on improving the quality of PES staff.

In addition, Korea should seek to take advantage of the extensive network of private employment agencies that presently exist. Even after the recent expansion of the PES, private employment agencies outnumber PES offices by a factor of twelve to one. These agencies have an excellent intermediation record in the unskilled labor market and the PES could seek complementarities with them, for example by contracting out the placement of low-educated unemployed. Many OECD countries are beginning to rethink the role of the PES and expand the opportunities for market forces to improve its effectiveness. Given that Korea already has a large infrastructure of private employment agencies in place, the authorities should seek to exploit this potential to the maximum.

### *Social Assistance Programs*

The weaknesses of the present social assistance system (see Section 2.5 above) have prompted the Korean authorities to enact a new system, namely the National Basic Livelihood Security Law (NBLSL), to take effect as from 1 October 2000. The concept underlying the new social assistance law is that of "productive welfare", i.e. the purpose is to provide adequate income support while also encouraging benefit recipients to participate in the labor market. Thus, it is officially estimated that the proportion of individuals living in poverty who will receive benefits will be increased to two thirds

after the new law comes into force. In addition, the level of benefits will be raised.

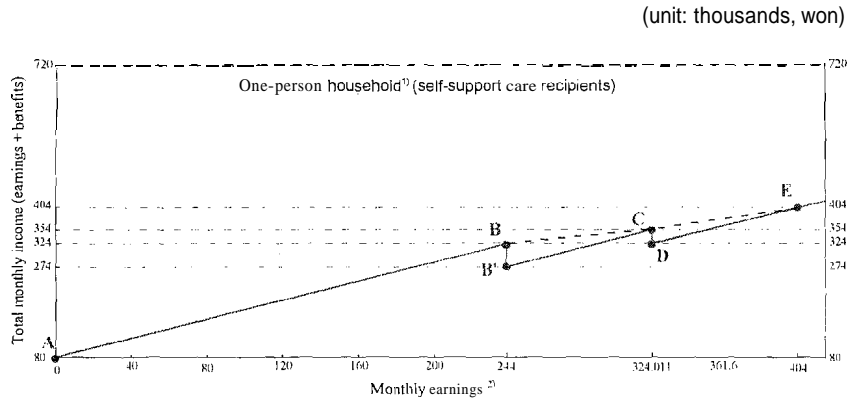
However, it is important to stress that many low-income individuals will still remain unprotected under the NBLs. This partly reflects the fact that benefit entitlement is subject to unusually strict income criteria, based on the income capacity (and not the actual income) of the extended family. This particular provision of the law may have to be revised if the official target of providing benefits of last resort to all those in need is to be reached. Also, despite their increase, benefits will remain very modest. The authorities should consider raising them further, perhaps in stages, so that they reach at least the official poverty line.

In addition, making productive welfare a reality requires local government officials responsible for the delivery and administration of the system to screen recipients on their work ability and provide them with effective employment-oriented counseling services. Based on the experience of other OECD countries, it is possible to identify certain policy avenues which could help meet these goals:

- at present, there are about 250 recipients to each welfare officer, compared with an OECD norm of 80 to 120 recipients per officer. Korean welfare officers simply do not have the time to screen and adjudicate clients on their work-ability or provide intensive job-counseling services. The authorities have undertaken to hire additional welfare officers so that the number of recipients per welfare officer declines to 200, but many more would need to be hired and trained in order to arrive at an acceptable caseload;
- welfare officers will require adequate funds to provide a range of effective employment services. In this regard, the authorities could consider the implementation of pilot projects, allowing private agencies to tender for the provision of employment services to NBLs clients;
- to encourage job search: it may be helpful to introduce in the NBLs a mechanism of earnings disregards which permits recipients to keep their benefits while at the same time earning some work income, up to a certain threshold. Such a system would have to be rather different from the one embodied in the current set-up. Indeed, the present system is such that social assistance clients do not always have an incentive to accept a job – at points B and C of Chart 16.4, a small rise in earnings leads to a disproportionate reduction in benefits, translating into lower total income (represented by the drops to B' and D, respectively). In order to avoid this, benefits should be withdrawn only gradually. For example, Chart 16.4 (dashed line) illustrates the case of benefits being

withdrawn by one Won for each two additional Wons of earnings.

**Figure 16.4: Financial incentives to work for social assistance clients in Korea, 2000**



Notes: 1) For more explanations on this chart, see text.

2) The minimum cost of living for a one-person household is 324,001 Won; the minimum wage as from September 1999 is 361,600 Won; the average wage in 1999 is 1,599,000 Won.

Source: Secretariat estimates.

Current financial arrangements between different levels of government may be conducive to a waste of resources. At present, most of the budget for social assistance benefits comes from central government, while local governments (and their welfare officers) are in charge of the delivery of benefits. In such a setting, local governments have a weak incentive to enforce the different eligibility criteria and they might therefore be inclined to provide benefits to whoever asks for them. Up to now, the central government has addressed this problem by announcing strict budget limits, effectively imposing hard-budget constraints on local governments. It seems desirable to maintain the current budgetary "grant-based" system and not give the certainty to local governments that their financial demands will always be satisfied.

### *Education and Training*

The average educational attainment of the Korean population and work force has increased spectacularly over the past decades, contributing to the rapid growth performance. Practically one fifth of the total Korean population has a college degree, the highest figure in the OECD after the United States and the Netherlands (OECD, 1999b).

At the same time, however, this rising educational attainment has not come cheaply. OECD (2000b) shows that in 1997 Korea spent 7.4 % of GDP on education, the highest proportion in the OECD<sup>14</sup>. There is also a need for improving the *quality* of this heavy investment in education and training, in order to raise labor and multi-factor productivity and allow Korean firms to compete effectively in the 21<sup>st</sup> century. In particular, vocational education curricula should be made more relevant to labor market requirements.

### *Financing of Programs*

Some of the measures advocated above will exert upward pressures on government spending, raising the issue of how they can be financed. In the case of an expansion of the EIS, extending the coverage of benefits to workers of small enterprises, which often do not pay the required social contributions, risks creating a deficit in the EIS. In order to prevent this, it is essential that the government steps up its efforts to make all firms pay their social contributions. Otherwise, the government may face pressures for subsidizing the EIS from general revenues. In the case of programs financed by central government, notably social assistance benefits for which an expansion is also planned, resources can be found by scaling down programs such as public works and unemployment loans. Further savings could materialize if rigorous evaluations of ALMPs were carried out and resources shifted to the most cost-effective programs, thereby reducing the risk of waste of existing resources.

Should these savings prove insufficient, the government could consider raising tax revenues. Preferably, this should be done by enlarging the tax base (through an intensified campaign against tax evasion and a reduction of the generous tax allowances and exemptions that presently exist) rather than raising marginal tax rates which, at between 10 and 40 %, are not particularly low by OECD standards. In any case, general government revenues represent about 25 % of GDP which is, after Mexico, the lowest figure among OECD countries for which comparable data exist.

## **Concluding Remarks**

*In sum*, despite the recovery, now is not the time to reduce the momentum of reforms. Korea has managed to catch-up rapidly vis-a-vis other OECD countries, but further progress may be more difficult than is often thought.

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<sup>14</sup> This figure covers public *and* private spending on educational institutions. In terms of public spending alone, Korea spends below the OECD average: 4.4 % of GDP compared with an OECD (unweighted) average of 5.1 %.

Indeed, future improvements in living standards may have to rest on using resources more efficiently, rather than more intensively as was the case before the 1997 crisis. A more qualitative approach to the development strategy may be called for, encompassing an increased emphasis on enterprise training, a reduced labor-market duality and the establishment of a well-functioning social safety-net that covers all individuals. It is particularly important to *a*) improve the quality of education and foster enterprise training; *b*) effectively expand the coverage of both the EIS and social assistance benefits, while scaling back some ALMPs adopted as a temporary response to the crisis; *c*) ensure that employers pay their contributions to the employment security and public pension systems and, provided that is the case, gradually reduce enterprise retirement allowances for regular workers, thereby helping to reduce the marked duality that presently exists and laying the ground for higher productivity gains; *d*) better target ALMPs, enhance the quality of the PES staff and undertake rigorous evaluations of the programs; and *e*) make sure that work continues to pay in Korea.

Obviously, these measures need to be adopted in a context of full respect for basic workers' rights and, in this sense, resolving remaining industrial relations' issues should rank high on the policy agenda. In a modern, productive economy, it is important that all social actors be involved in the reform process in a climate of mutual respect and trust.

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# **17 The Challenge of Labor Reform in Korea: A Review of Contrasting Approaches to Market Enhancement and Experiences from Chile and Denmark\***

**Louise Haagh\*\***

## **Introduction**

An unprecedented financial crisis hit Korea in late 1997, which led open unemployment to reach politically and socially unsustainable levels. The rate of 8.4 percent reached by early 1999 represented more than a tripling of historical levels and Korea's social institutions were not designed to cope with job losses of this scale. There is a growing literature on the causes and direct effects of the crisis, including the immediate response of policy-makers and the introduction of social emergency measures. In this paper we will take a step back and focus on some general implications in the area of institutional innovation that can be drawn for the Korean case from contrasting experiments with labor market and training reforms. These implications have to do with how best to support individual mobility in labor markets. The article points to the importance of an individual-centered approach to labor flexibility issues. This approach is not only relevant from the perspective of individual security and social protection in a more flexible labor market, such as the one towards which Korea is heading, but is increasingly central as human resources have become the basis for growth.

Useful insights may be borrowed from countries which, like Korea, are trying to introduce de-centralization and demand-based approaches into the training market. Among them we will emphasize the role of non-market institutions - like the public sector and social associations - in this endeavor. Building transparent markets in human resources depends on effective collective action. The countries we refer to in our discussion have relatively long histories of welfare provision. Among them Chile and Denmark are

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highlighted because they bring out the great variations that exist within the realm of market enhancing reforms. There are important differences in GDP between the cases discussed. However, if we accept Sen's premise that levels of development should be measured in terms of the substantive freedoms that institutional and market arrangements provide individuals with, levels of GDP (as he intimates) becomes an independent, not the dependent, factor.<sup>1</sup> The countries assessed are chosen precisely because they provide interesting policy lessons for Korea as this country is at a crossroads in terms of institutional design. Indeed, Korea was not only a latecomer in her economic development. She is a latecomer in the maturing of welfare and supra-firm labor market institutions as well. Not only is her welfare system in its infancy, but the recent crisis has greatly spurred efforts to develop new means of social protection and individual mobility fast. How far is Korea going to be able to foster the individual-centered approach to flexibility in future? The assumption we make is that how you start the process of institution-building matters,

The paper is organized into four sections. In the first we provide a conceptual discussion of the link between issues of labor flexibility and public policy. We point in general terms to the importance to the advancement of an individual-centered approach of a strong link between labor institutions and welfare reform. We then look in general terms at the accelerated pace of change in these two domains that the crisis of 1997-1999 produced, and argue that labor reform must be comprehensive and link the two domains better than they have been in the past. This leads us to look at two cases that illustrate specific issues where this link has been weak or strong. The last section summarizes the importance of this link by issue area and draws some connections back to the Korean case.

## **A Welfare Reform and Corporation Versus Individual-Centered Approaches to Flexibility**

### *The Corporation-Centered Approach*

Issues of labor market flexibility and social sector reform have tended in the literature to be regarded as separate. As labor markets have become more fluid, however, and as human skills have become more central to growth it is increasingly unproductive to view them as such. The writing on labor flexibility has tended to focus on the micro-level, where flexibility is visualized mainly in terms of firms' needs for immediate flexibility in the face of change. This method well suited the standard neo-classical approach in which the firm seeking short-term survival in the competitive market is

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<sup>1</sup> Sen (1999), pp.3-6.

the main focus.' The typical way to proceed is to make distinctions between specific forms of flexibility, like wage flexibility, task flexibility, contract (inter-firm) flexibility, and so on.' The problem with this approach is that it ignores the possible tensions between different flexibility measures at micro-level. For example, there are trade-offs between short-run quantitative flexibility and flexibility forms that require a sense of trust, like wage restraint or task diversity in exchange for job stability. Where certain forms of flexibility are practiced systematically at a high level, for example where turnover is high, other important features of labor management, like the development of skills and the retainment of skilled workers, become negatively affected.<sup>4</sup> In response to this obvious scope for negative trade-offs, second-order distinctions have been developed, the most well known between so-called quantitative and qualitative forms, or (the equivalent) numerical versus functional flexibility forms.' The problem with such approaches was that they in turn tended to ignore the real need at times for quantitative flexibility (like lay-offs or wage cuts). In this approach human development is rigidly counterpoised with all quantitative flexibility forms.<sup>6</sup> In response to this problem, third-order distinctions have been put forward, as between You's market versus strategic behavior-driven flexibility or Haagh's efficient flexibility forms, where the possibility is raised of an explicit choice between social actors about flexibility trade-offs at different levels.'

Even the third-order perspectives on flexibility, however, remain corporation-centered. Ultimately, the rationale behind the flexibility drive is that corporations need a free hand if they are to contribute to growth in the new market place. The assumption that all corporation-centered approaches hide is that development is uniquely defined in terms of growth produced directly by corporations. There are two fallacies in this view worth reiterating in brief. The first is a long-standing and much-debated contradiction in liberal theory and economics between the ideal of individual liberty and the legal personification of rights in corporations.' The argument that maximizing the liberty to act of corporations is ultimately beneficial for growth and for the expansion of markets, consumer choice and liberty retains some persuasive power, yet is increasingly unable to stand alone as

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<sup>2</sup> Krueger (1983), Hayek (1980).

<sup>3</sup> For good overviews on flexibility forms, see Poire (1986), OECD (1986), pp.8-9, Boyer (1988), Blank and Freeman (1993), Lagos (1994).

<sup>4</sup> Williamson (1985) is the now classical treatment of the institutional dimensions involved in the investment in idiosyncratic goods like human resources.

<sup>5</sup> OECD (1992), p.97.

<sup>6</sup> The supposition is often made (as in OECD (1992) and Lagos (1994)) that functional flexibility is by definition associated with skill development. This problem is also recognized in You (1997).

<sup>7</sup> You (1997), Haagh (1999).

<sup>8</sup> On a good recent discussion, see Burchill (1998).

human capital and (mobile) individuals become the locus of growth.' As labor markets have become both more fluid (people move around more) and more insecure (with social protection now based more on private insurance) the costs of unsupported mobility have further increased. Those include corporations' direct costs in terms of loss of skilled manpower in crisis situations, their indirect costs in terms of lost trust with remaining employees, and the long-term expense to society of the increasing number of people potentially facing unplanned mobility. The prior individual search involved in individual quits directed at furthering education or relocating to a better *relevant* job (to use Sen's term a job that the *individual has reason* to consider relevant given past experience and so on)"', would not have been made. In the context of more fluid and insecure labor markets, therefore, involuntary unemployment may enhance the difficulties involved in continuing an unbroken trajectory in terms of acquired skills and productivity. We could call that trajectory a person's productive development course (PDC). In short, the societal and individual costs of lost investment in skills are difficult to detach.

The second fallacy in the corporation-centered view is therefore the way in which it seems to conflate two distinct demands of the new labor market. Those are the short-term needs of firms for flexibility, on the one hand, and the long-term needs of individuals to renew their means of mobility, in effect to replenish their human capital, on the other. The corporation-centered view admits only the one, and sees the second as a function. This is despite the fact that even individual firms ultimately depend on a steady reproduction of the stock of human capital, and on the currency of skill (the likelihood of being able to contract certifiably good human resources in future). The methodological implications are that our thinking about flexibility has to be more directly focused on the individual, the moving agent and the carrier of skills. In the new economy, the relationship between the liberty of individuals and corporations needs to be carefully balanced.

### *The Individual-Centered Approach*

Individual-centered approaches are more commonly found in the field of public policy studies." However, in this case the link with problems and issues of labor flexibility in labor reform are not often explored. Analytical tools frequently used are the household survey or the performance of policy programs targeting particular groups. Individuals tend to be seen as subjects of assistance, victims of the market rather than active participants in the production process. It seems therefore that the challenge ahead is to begin to

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<sup>9</sup> As accepted in recent growth theory, for example Romer (1986). Barro (1991)

<sup>10</sup> Sen (1999), p.10.

<sup>11</sup> In volumes ranging from concern with acute poverty (Dreze and Sen, 1989) to more developed social security systems (Haagh and Helgø, forthcoming).

analytically connect the new problems posed by labor markets and the capacities of both labor market and public policy actors and institutions to respond to them. [The policy and institutional issues involved range from social insurance and social assistance, through unemployment insurance to skill certification and labor training and relocation. These are increasingly difficult to divide.] Following the recognition by You and others that 'numerical' forms of flexibility may be necessary, even on a relatively large scale at times, the problem does not lie with the dismissals as such. Korea's new firing laws of 1997 are in fact not that liberal." It lies with the lack of an institutional framework that helps to ensure that, in the event of involuntary quits, the human resources involved are recycled in a way that is least destructive to the individual PDC and to individual choice in this field. Firms alone cannot respond to this challenge, but nor can public policy institutions that are not linked well with firms or with networks of firms.

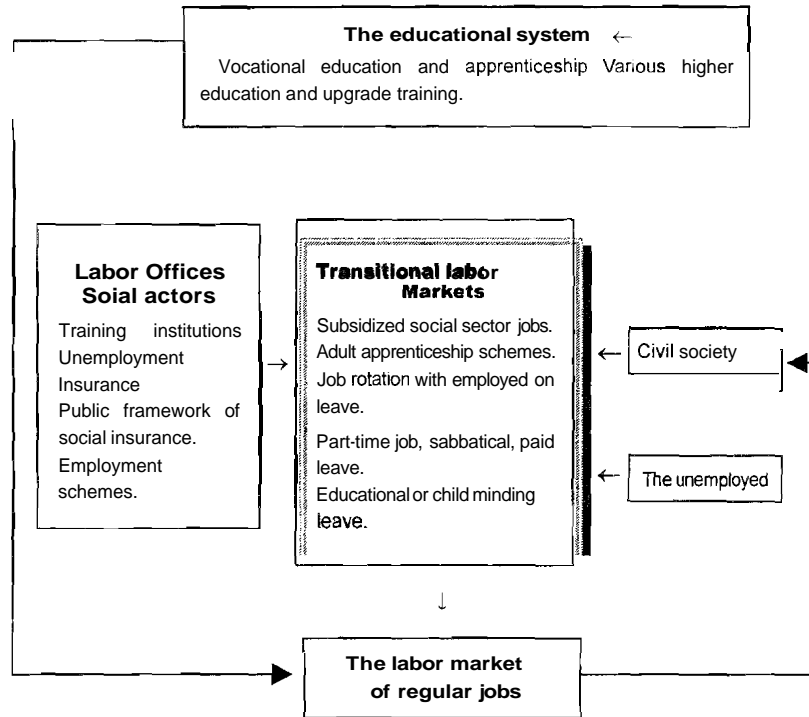
The success of and shaping of public policy is also inter-dependent with changes in management of labor. The problem of dismissals is difficult to separate from labor relations. Changes inside corporations could lead to greater transparency in personnel decisions, as for example pay in conglomerates in Korea becomes associated with more observable criteria of performance and merit. In one argument that would force a greater understanding and transparency as well in decisions pertaining to lay-offs. However, whether that is the case will also depend on what opportunities individuals have, and how far they are able to exercise choice. Figure 17.1 illustrates some of the relevant connections between institutions. Transitional labor markets group the kind of arrangements through which individuals can leave and re-enter the regular labor market whilst retaining a continuous association with it.

The forms of public policy and labor institutions that are relevant to individual choice can be linked in a myriad of ways (Figure 17.2 illustrates such links in more detail). Indeed, the recent experience with labor market reforms is rich and varied and it would be impossible to present an exhaustive list of relevant lessons for a single case like Korea. It is also not possible to distinguish clearly between pure individual- or corporation-centered approaches. The distinction is partly a heuristic one, as each labor market design will have elements of each. However, in general what characterizes an individual-centered approach is an efficient link between the labor market and public policy institutions. What we wish to emphasize here is that the degree to which the combination of policies and institutions enables individuals may be of greater importance (even for firms) than often assumed.

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<sup>12</sup> Despite the impression to the contrary one might draw from the stance of the union movement. If anything the problem lies in the enforcement of the rules stipulating consultation with unions. See Haagh (2001), for a comparison with Chile's tiring laws.

Figure 17.1: Linkages in an individual-centered system of labor flexibility"



Note: 1) The idea of the transitional labor market is inspired in Kongshøj Madsen (1997).

**Figure 17.2: Linkages between individual mobility and efficient flexibility, and policy implications**

Individual mobility	Efficient flexibility	Policy implications
<p>Enhancing the productive development course (PDC) of Individuals</p> <p>Access to Training</p> <p>Broad currency of gained skills and work experience.</p> <p>Form of income security.</p> <p>Continuity in social security</p> <p>Real opportunities for re-entry to labor market, through access to life-long learning and re-training.</p> <p>Individual access to form of membership of labor markets.</p> <p>Real opportunities for re-entry (as above)</p>	<p>Making the flexibility of corporations compatible with the development of human resources.</p> <p>Regulation of quality of entry-level training (for ex. of young people) to ensure long-term viability</p> <p>Creating incentives for long-term investments by firms.</p> <p>Certification of skills to maintain tradable value and possibility for link with further training.</p> <p>Ensuring that long-term return to training are reaped.</p> <p>Adequate labor market information.</p> <p>Encouraging organization in labor Markets.</p> <p>Creation of training opportunities with local linkages.</p>	<p>Policy implications</p> <p>Lasting point of entry into labor market for the young, through socialization standards for instruction and apprenticeship.</p> <p>Flexible tax rebate schemes including careful re-adjustment of subsidies to suit firms' needs, and empowering employees to access schemes directly.</p> <p>Making sure that training provision falls within some (adjustable) gamut of occupational streams or mid-streams identified as relevant by employment providers.</p> <p>Involvement of business and labor associations in this and in certification of skills.</p> <p>Unemployment benefit insurance with added protection covering other forms of social insurance, as well separate forms of access for transitional unemployed and special groups.</p> <p>Giving social actors a stake in social insurance system.</p> <p>'De-centralized' regional development focus involving business and labor.</p>

## Recent Labor Issues in Korea

Korea faced the schism between welfare and labor reform to perhaps a marked degree. In late 1997 she experienced an acute financial crisis followed by an economic downturn that lasted for over two years. In response to this Korea's open unemployment rate went from 2.6 % in 1997 to 8.4 % in early 1999. Policy-makers had no warning and little time to find ways to compensate workers. Social insurance was well developed solely in the area of health, pensions and industrial accident compensation. Pension insurance had only achieved national-level coverage in principle in 1988, and medical insurance was still based on regional funds. There was no social welfare system as such, except limited services for specific groups like the aged, children, women, disabled and the family. The country's nascent employment insurance system (of 1995; henceforth EIS) was only beginning to find its feet. Less than 40 % of full-time waged workers were insured as of 1997, and it alone could not cope with an employment crisis of the magnitude Korea faced. The scheme was not intended to cover large-scale unemployment, or even to cover the labor market as a whole. Only in 1998 was it expanded to cover firms with less than 30 workers, and even when coverage was extended to all firms in October that year, few of those covered had been in the system long enough to receive adequate payments. Daily and part-time workers, the majority of workers in small and medium-sized firms on precarious contracts and informal workers, estimated at around 50 % of Korea's labor force (economically active population) were not covered by the EIS. Consequently, even at the height of the crisis, it is estimated that only around 7 % of the unemployed were covered by EIS payments. In 1999 a further 21 % of the 1.4 million unemployed participated in the public works program in an average month. These two programs, then, covered less than 30 % of the unemployed. Outside of these two schemes, Korea had a very limited public assistance program, the main component being the livelihood protection scheme, which barely extended its coverage during the crisis, partly due to strict eligibility rules.<sup>13</sup> Finally, Korea's public training and relocation system was still in transition from a supply- to demand-oriented system and was not well tied in with firms.

The Korean government responded with a series of rapid measures, two of the most important being the creation of public works schemes and the expansion of the Employment Insurance, both in terms of coverage and in terms of systemic revisions to cover more types of employment-related

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<sup>13</sup> This and associated schemes are estimated to have covered upwards of 1.6 million workers for short periods of time during 1999 and in the region of 1.25 million workers in 1998, not including regular claimants (Park and Lee, 1999) against 1.414 in 1997. The characteristics of this scheme and proposed innovations to it are discussed by Prof. Young-bum Park elsewhere in this volume.

problems. Some of these measures will be discussed later in the paper in light of the experiences of other countries. By mid-1999 the Korean economy began to show signs of a real recovery, and this trend became consolidated during 2000. The labor market also responded well, with unemployment down below the 5 % mark in the last months of 1999. The lower unemployment figures reflect both actual job creation and growth (10.2 % in 1999, with a forecast of 6 % for 2000) and public policy efforts such as the public works' scheme, of which the large majority of participants (85 %) were not eligible for other unemployment policy measures.<sup>14</sup> It is important to be clear, however, that not all Korea's employment problems can be attributed to the crisis. Nor have they been resolved by recent growth. A series of changes in the labor market and in labor relations were already underway, or were waiting to happen. An integrated labor market reform is one that does not seek merely to provide ad hoc remedies for cyclical problems of open unemployment. It must also engage the obligations of labor market actors and provide long-term services for both individuals and firms. It must be capable of responding to changes at the micro-level.

The crisis served to accelerate the pace of change that was already underway in this domain. A combination of factors led employers to intensify their search for greater flexibility in the use of labor from the mid-1980s onwards. Korea's labor markets had been on some accounts very flexible up to then.<sup>15</sup> Greater union strength after the opening of the period of re-democratization in 1987, however, put upward pressure on wages, and voluntary quit rates also seem to have decreased, according to You, down from an average of around 4 % during the 1970s to around 3 % after 1988.<sup>16</sup> High-ranking managers of top conglomerates interviewed during 1999 and 2000 confirm that the crisis of the late 1990s was in some ways an opportunity to speed up long overdue changes in labor management. It made the phenomenon of short and medium-term contractual work more acceptable. In the year up to mid-1999, Samsung contracted the size of its personnel by nearly 30 % through spin-offs and early retirement schemes. The attempt to level out seniority and lifetime employment practices was intensified, and from 1998 pay was formally severed from ranking according to the formal (pre-existing) ladder of sequential promotions. For example, although formal pay-scales were still used in 2000, they were becoming increasingly meaningless compared with only five years before, as many lower rank positions offered higher pay, and overlaps in ranks had been introduced. As a senior manager put it, 'experience no longer equates with ability. It may be better to have someone untainted by unwanted past

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<sup>14</sup> As Lee notes in this volume.

<sup>15</sup> See You and Chang (1993), and You (1994, 1997) for a discussion.

<sup>16</sup> You (1997), pp.358-361. According to You, the separation rate was as high as 6.4 monthly in the 1970s in labor-intensive industries, whereas the 4 % figure refers to capital-intensive, larger firms.



experience.<sup>17</sup> The experience at Samsung reflects wider changes. In a survey conducted by the Labor Ministry in 1999 of 5,116 firms with more than 100 workers, it was found that 18.2 % had introduced the so-called 'annual salary system' by which individual pay varies according to productivity and performance over the preceding 12 months. This compares with only 3.6 % of firms in a similar survey of October 1997. An additional 29.9 % of firms were preparing or had plans to introduce the annual salary system in future. A further 23.3 % were contemplating overall profit share deals with employees to help boost productivity (16.3 % already used them).<sup>18</sup>

When the upturn came in 1999, the methods of hiring had also changed. Conglomerates were no longer looking towards a long-term learning curve, where skill investments are realized over the span of life-time, but for persons with acquired abilities, who might stay for shorter or longer periods of time with the firm. There are important variations in the exact means of labor restructuring pursued by the conglomerates, depending on the labor relations of the past. Samsung, with no union, could cut more employees and institute more drastic changes to the seniority system. Myundai faced massive opposition from a very combative labor union to what was in some respects more moderate change (against a planned reduction of 11,672 employees, only 1,538 personnel were cut, of which 1,261 were on leave without pay). LG with good, conservative relations with its union did cut roughly 20,000 personnel out of a total of 105,000 in the first year and a half of the crisis, although it also relied heavily on wage cuts to minimize job losses.<sup>19</sup> Despite such differences, however, none of the conglomerates could escape the constraints of a labor market where scouting for skills crowds out the reproduction of human resources. Samsung's offer of above market wages has traditionally enabled it to attract talent, but quit rates of skilled individuals increased sharply as the up-turn came.

These represent more general problems of human development within a labor market where skill upgrading becomes of ever-greater importance, yet where institutions for shared investment have remained weak. Korea's pool of human capital in the form of initial schooling has been credited with playing an instrumental role in the country's spectacular growth, particularly in the early stages of industrialization.<sup>20</sup> It is widely recognized however that the state-administered scheme of initial training of the 1970s has long been outdated. Lack of interest by firms to invest led to the introduction and expansion of the compulsory levy system, followed by reforms like

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<sup>17</sup> The information for Samsung was provided in interviews with senior managers during 1999 and 2000.

<sup>18</sup> The Labor Ministry, Korea.

<sup>19</sup> With cuts ranging between 10 and 30 %, the latter taken at the top management end. Interview with senior managers at LG, during 1999 and 2000.

<sup>20</sup> Amsden (1989), Sen (1999), p.41

exempting large firms who do carry out firm-specific training." The trouble is that even for the large conglomerates, the in-house training institutions do not necessarily deliver or up-grade the skills companies like LG or Samsung are scouting for, such as gained expertise in electrical engineering and computer science. Institutions like Samsung Human Resource Development Center or LG's Academy and Learning Center are mainly geared towards inspiring company loyalty and to train individuals in a way that is directly productive to the firm. Their activities are not tied within a network of broadly certified and recognized skills. Although in theory classical, Korea's skill markets hence are not effective or transparent, for firms or individuals engaging in them. Korea's firms engage in a classical prisoners' dilemma problem. As there is no effective guarantee against free riding by other players (firms), every company wishes to minimize the investment in broadly certified and directly transferable skills. As firms in Korea increasingly face competitive pressures which both impose the need for short-term adjustments (dismissing and re-hiring workers) *and* to upgrade the quality of products, it will be in their long-term interest to develop shared mechanisms to finance and certify skills. Only in that way can they ensure a ready supply of re-employable workers, not just from the early recruitment level, but at later re-employment stages as well.

Such systems are also important for individuals in labor markets. As they become more mobile both through quits and redundancy it is not clear that Korea has adequate systems of skill re-training or certification to support the new patterns of movement. The share of non-voluntary quits in job separations in Korea used to be very low, but non-voluntary quits dominated among EIS claimants during the crisis, with a share of 81 % in 1998.<sup>22</sup> From the last quarter of 1998 to the last quarter of 1999, the number of temporary and part-time workers in Korea also rose; by 15 %, from 6 million in 1989 to 6.9 million in 1999. Unskilled labor jobs increased by 13,4 %, whilst positions in the managerial branch and upwards increased by 3.3 %. The wage gap between occupational categories in Korea has widened too. According to the National Statistics Office, white-collar workers earned 1.52 times more than blue-collar workers did in 1995, 1.57 times in 1996, 1.63 times in 1998 and 1.7 times in 1999.

Other social problems associated with the labor market that lay outside the purview of the EIS persisted or became intensified in the late 1990s. When

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<sup>21</sup> Kang and Lee (2000). Jeong, J. (1995). Park (1994)

<sup>22</sup> If 'Restructuring (19.2 %), bankruptcies and shutdowns (13 %), and 'strongly advised to retire' (48.9 %) are counted. A further 5.1 cover those who ended their contract or retired, and 13.8 % under 'other'. The year before, in 1997, of 745202 separations, 92.7 % were due to quits (resignation), with 1.3 due to death or sickness, 1.1 % to 'one's own misdeed', 1.4 to 'unemployment by convenience', 1.4 % to 'retirement' (the category that most closely resembles the 'strongly advised to retire' category), and 2.1 to 'completion of contract'. Yearbook of Labor Statistics, Labor Ministry of Korea, 1998, and Trends in Employment Insurance, Korea Labor Institute(1999), Vol. 4, No. 1.

unemployment is stratified by groups, it remained high in many categories, including the young, and in urban centers like Seoul, where it jumped to 6.3 % in January 2000. Korea's income inequality worsened. The percentage of people living below the poverty line rose to 7.5 % in the third quarter of 1998, from 3 % just prior to the 1997 crisis. The Geni coefficient rose to 28.19 in the third quarter of 1999, from 24.49 in late 1997.

The public works scheme was set up to combat such problems where growth alone could not. However, it was by its very nature a temporary measure. For most people participating it provided income assistance during only a small period (five months) of the total period of unemployment experienced (according to Lee on average just over 14 months counting the stage both of active job search and the economically inactive phase).<sup>23</sup> Most importantly, the scheme was not integrated with the mainstream job-relocation and re-training programs. It was active only in an immediate sense, in making the participants work for the assistance they claimed. Less than 20 % relied on public employment services of any kind (local labor office, manpower bank or public employment centers for daily workers) to find new jobs. The majority of people surveyed who found jobs (less than 30 %) after participating found inferior jobs to those they had prior to the

In some ways, changes in Korea's labor markets skipped the phase of deliberate institution building. Labor market actors did not cater in a planned fashion for the changes that were brewing. Employers sought to expand immediate flexibility in the use of labor, and workers sought to maximize wage gains in the period of mobilization that followed political opening from 1987. In this initial phase, attempts to increase flexibility focussed on corporations' immediate needs. The state meanwhile, took realistic but very slow steps towards providing a safety net to support increased mobility. When the crisis hit in 1997, the two phases of change in the Korean labor market accelerated simultaneously, as employers sought to shed labor, and the state to provide emergency relief for the unemployed. The crisis also brought some of the other emergent labor market issues to the fore, for example as more women who had not previously been registered as job seekers entered the labor market to cover for lost family earnings. The need to accommodate more women, to tackle structural and long-term unemployment of older age groups, as well as to deal with new bottle-necks in the demand and supply of skills are all problems that the better growth and employment figures of 1999 and 2000 do not clearly reflect. The challenge that Korea faces is how to make supra-firm labor institutions, including the welfare system, a service center to diminish the costs and enhance the benefits that increased labor mobility potentially holds for individuals and firms.

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<sup>23</sup> Lee (1999), p.16.

<sup>24</sup> Lee (1999), p.25.

## **Institutional and Policy Lessons from Latin America and Europe**

Although it is not possible to identify pure corporation-centered or individual-centered approaches, it may be useful to look briefly at instances of labor reforms that demonstrate one or the other trend. The cases of Chile and Denmark clearly illustrate different dimensions of the problems involved in the individual-centered approach. They represent recent comprehensive attempts at institutional re-design of public policy and labor markets and therefore are quite interesting for us to consider.

### *The Labor reform in Chile of the 1970s and 1980s*

Chile is a fairly clear example of a country that has followed the corporation-centered approach. In the context of the failure of state-led industrialization and the Socialist experiment of the Allende Government, the Pinochet regime that took power in 1973 began a series of market reforms. These reforms were characterized by a perspective that saw social associations and state institutions as anathema to markets. Economic freedom was defined primarily in terms of firms' immediate ability to respond to competitive pressures or external shocks. The different elements of what we would characterize as labor market reforms (including both those that have to do with labor management and labor flexibility and those that have to do with social assistance) were accordingly carried out separately and in each case primarily with a view to untying firms from short-term constraints. For this reason, the reforms, although each may have had individual merits, did not perform well as a social policy network. They did not work well together as a labor market reform. Even though each measure was undertaken over some time and at different speed, it is possible to identify the following separate institutional changes:

- Training reforms: Training (together with education) was one of the first areas to come under review. The training market set up from 1976 onwards continues to be regarded by many in Chile as a model of a well-functioning, self-contained market in training. The reforms included privatization and leasing out of public training institutions and the creation of a public regulator under which new private training providers were encouraged to register and compete with each other. The functions of the public regulator were deliberately defined as minimal, and the role of the new institution, SENCE (*Servicio Nacional de Capacitaci3n y Empleo*) limited largely to the distribution of public funds through various leasing out and rebate schemes. The establishment, by the mid-1980s of over 800 registered providers marks one aspect of the reforms'

initial reach and success."

- ❑ Labor code reform: Following the suspension of collective bargaining and the forced election of new union leaders during the 1970s, in 1979 a new labor code was enacted, which aimed at increasing firms' flexibility in the use of labor. Facilities for multi-unionism, and parallel bargaining with groups outside the union were also set up, so as to maximize the possibility for employer discretion in the use of labor and minimize the collective facilitation of rules for individual mobility. Reform of the labor code during 1990-1991 confirmed the essential features of the earlier changes.<sup>26</sup> Chile's unionization rate in the 1990s peaked at 15 %, but never reclaimed the historical heights of 30 to 40 % of the 1960s and early 1970s.
- ❑ Social security reforms: The privatization of social security, first pensions and then health, went ahead in separate stages from the late 1970s through the 1980s. Chile's pension reform was the first effort of any country at a wholesale privatization of social security. Apart from the creation of a uniform and simpler system (breaking up the contributions systems built along occupational lines) a central rationale was to gradually free employers from the burden of social contributions and like indirect wage costs. For new labor market entrants membership of the private system was compulsory. In the area of health, individual private account insurance covered around 20 % of the population. The individual account insurance systems helped to increase Chile's national savings rate, but it is too early to judge their efficiency in delivering both pensions and health."<sup>27</sup>
- ❑ Social assistance reforms: In view of the broader belief that markets and growth would ultimately take care of individual welfare, social assistance programs since the mid-1970s became concentrated on what was considered marginal groups (for example specific groups of youth or rural poor). Alternatively, resources would be targeted for very specific, limited but crucial needs, such as the provision of adequate nutrition for infants and help for pregnant mothers.

The lack of a binding network between the different labor market institutions we have highlighted represented a general failure of labor reform. However, the most important misconception possibly lay in the idea that only a limited framework of public assistance (the fourth feature in the reforms listed above) would be needed to support individual mobility. It is possible to narrow down the reasons behind this failure to the confined

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<sup>25</sup> For a more extensive review of the training reforms, see Haagh (1999)

<sup>26</sup> Bargaining groups (non-union ad hoc formations) accounted for 26 % of workers involved in collective bargaining in 1998, up from 10 % in 1987. Haagh (2000).

<sup>27</sup> Although thoughtful critique points to its many problems in coverage already. For a recent comparative review, see Barrientos and Lloyd-Sherlock (forthcoming), and Barrientos (1997).

corporation-centered view of labor flexibility that inspired the overall reform process in Chile. I have discussed the flaws in Chile's disjointed labor reform extensively elsewhere, but a few points can be summarized here particularly as they relate to the role of training. Essentially, they point to the manner in which Chile pursued economic liberalization whilst undermining the social and political capital necessary to establish viable contracts to further the development of human resources.

As we have already noted, training lies at the inter-section of the labor relations and public policy aspects of labor reform. An efficient training system needs to balance the demands for flexibility (of firms) and the needs of mobility (of individuals). This requires an efficient network of (supra-firm) labor market and social policy institutions to ensure that firms can continue to hire and fire skilled workers, and that individuals retain the means to PDC. Perhaps the most evident failure found in the Chilean approach was in the design of the training system itself. The corporation-centered view is clearly evident in the dominant role in public finance played by tax incentives to firms. In the mid-1990s, these made up over 90 % of public finance destined for workers' training. No specifications in public subsidies (for example to distinguish the needs of small firms, or provide employment incentives) were made. Instead the use of the funds remained at the employers' exclusive discretion. Individual employees had no access to them. It was found that some 65 % of the money was consistently spent on management or supervisors' training throughout most of the 1980s and 1990s. Coincidentally, the tax rebate scheme was favored relative to an individual-centered approach over time. In 1977, at least 60 % of public funding for workers' training was channeled through a grant scheme targeting workers directly at the municipal level but by 1985 this was down to 35 %, and by 1990 it had been distilled to 3 % only."

A plausible external reason for the low propensity to invest in workers was the lack of a national certification system integrating the hundreds of private training centers and weak measures of co-financing which would ensure a pool of skilled labor. Institutions to pool institutional and informational resources for training purposes existed on a recognizable scale only in the area of management training.<sup>29</sup> For good reasons Chile had abandoned the very centralized system of the 1960s where the state training corporation single-handedly set manpower targets. However, the theory of a pure demand-led system, where firms would freely choose between training provided ad hoc by a host of training institutions was too radical a response. It did not work out well in practice either because *as* in the previous system, the communication with firms was poor and the institutional mechanisms to consult on and research training needs among firms were absent. The

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<sup>28</sup> Haagh (1999).

<sup>29</sup> As in the case of an institution named Achezyd Achezyd alone commanded a year budget similar to the total size of the public (SENCE) budget for workers' training. Haagh (1999).

evidence from Chile was that skilled workers were in demand. In a SERCOTEC survey, 43 % of employers said they lacked training. 13 % of employers, however, complained that they did not have the technical expertise to carry out training inside their firms, and 95 % noted that the training offered by private training institutions were not suited to their needs. The tax rebate scheme in Chile also did little to encourage forms of shared training or the institutional generation of tradable skills from inside firms, such as apprenticeship. Only 17 % of employers in 1990 were aware of the rules governing apprenticeship contracts, and in 1998, only 0.1 % of labor contracts were of this kind.<sup>30</sup> Other problems in the Chilean training system included the blanket nature of public subsidies, which in effect discriminated against smaller and medium-sized firms. The short-term contracts typically awarded individual training institutions (on public franchise at the most six months) led to weak incentives to up-grade the infrastructure of training institutions in a way that would suit firms' needs. As a result of these various shortcomings, the public sector was unable to effectively connect the training system to job relocation. In the long run, it was possibly the most serious flaw of the labor reform in Chile taken as a whole, a reform that (through the locus of the market) was designed to help in the movement of people.

In essence, the training system in Chile was misconceived because it was not geared towards supporting the mobility of the agent of human capital. This seemed contradictory when set in the context of the reform of labor law a few years later, which, as noted, put a clear emphasis on the external flexibility of firms. It is possible to spot a direct contradiction between these two reforms. From survey work in Chile it has been found that the increase in more precarious contract forms could be associated with lower investments in training at the firm level." Similar results have been found in Britain, a country that in the 1980s also simultaneously moved towards more irregular contract forms and de-regulation of the provision of training (although not in so radical a form as Chile).<sup>32</sup> Finally, training was weakly related to social security and to social assistance. Severe arrears and phantom registrations of pensions fund contributions and memberships have remained extensive." Despite being a pioneer in private social insurance, Chile had by the year 2000 still not instituted an unemployment insurance

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<sup>30</sup> Compared with 5 % in Germany, and 1 % in Britain. Gospel (1994, 1998). See Haagh (1999) for the details on Chile.

<sup>31</sup> For example, it was found that of the firms with low training (less than 1 % of the workforce in the last two years) 46 % had low levels of formalisation (where less than 80 % of workers had formal contracts and the wage system was not known). This compared with 26 % for firms which had provided training for up to 10 % of the workforce, and 18 % for those which had provided training for more than 10 %. The association remained strong when checked for the effects of size and sector. Haagh (1998), p.226.

<sup>32</sup> Gospel (1992, 1998).

<sup>33</sup> Haagh (1999).

scheme. One of the most important reasons why was the failure to agree on a system of administration that would allow for a connection with other social and labor services, including the training system.<sup>34</sup> There are important political and institutional reasons for this, which are beyond the scope of this paper. They have to do with the fact that independent compromise between labor and employers has historically been weak in Chile. During dictatorship, unions were repressed and association between national federations banned. After 1990, in the period of redemocratization, relations were encouraged, but due to employer resistance to modifications to the deregulated industrial relations system, such relations did not venture far into substantial policy themes in the area of training or employment insurance. Interestingly, the union movement remained very moderate during this period, due to a strong sense of loyalty and responsibility for ensuring the stability of the democratic regime.<sup>35</sup>

### *The Danish Labor Reforms of the 1990s*

The Danish labor market reforms of 1992 onwards represent an interesting contrasting case to the Chilean from an institutional angle. In this case, it is the links between different elements of labor reform that are important to highlight. It was possible to connect various elements in labor market reform from the outset in Denmark because of an institutional history in which national employer and union associations and public agencies were used to negotiate with each other. Although the differences are marked between the Chilean and Danish reforms, some of the aims were shared. The Danish labor market reforms also aimed at reducing the role of the state, increasing self-reliance of individuals in labor markets, making training more suitable to firms' needs and de-centralizing services in labor markets.

Therefore, before we highlight some features of the Danish reforms, it may be worth posing the following question. How is it possible that two sets of reforms that appear so different, could in fact both come under the same heading of 'market-enhancing' reforms? The answer is that the notion of 'market-enhancement' itself is not well defined. It appears to suggest that only those countries that pursue a radical de-regulation of supra firm labor institutions (i. e. those that follow a strict corporation-centered approach) are enhancing markets. It does not allow for the possibility that making it easier for individuals to move in labor markets is *also* a form of market enhancement. The Danish reforms show that it is possible to enhance the

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<sup>34</sup> Already in the early 1990s, the labor sector, represented in the CUT (Central Unitaria de Trabajadores) reluctantly accepted a private administration of the system, but various drafts failed to pass throughout the decade. The private sector, represented in the national employer association, the Confederacion de la Produccion y el Comercio(CPC) remained strongly in favor of maintaining the administration of the system strictly separate from other aspects of social security and labor institutions. Haagh (forthcoming).

<sup>35</sup> On an extensive history of this period, see Haagh (1997).



labor market in this sense without necessarily reducing the flexibility of firms. This can be seen in the high levels of intra- and inter-firm labor mobility that continued to characterize the Danish labor market throughout the 1990s, and in the fact that restrictions on dismissals remain highly liberal, despite the steadily less extensive period of benefit coverage provided by the state. The Danish labor market has retained one of the highest employment rates in the OECD for the last four decades, at around 70 %. In the 1990s, the co-ordination between different elements of policy was increased, more people were brought into active policy programs and unemployment fell to a steady and more acceptable level. These aspects deepened what can be termed an individual-centered approach. Before we highlight different areas in the Danish employment system where reform played a part some important contextual factors need to be mentioned.

#### Contextual Factors

The period of reforms initiated with the so-called Zeuthen-council in 1992 was underwritten by a general agreement between the social partners to keep wage growth moderate and in line with international levels. Wages rose on average by 4 % in the late 1990s compared with 7 to 8 % ten years before.<sup>36</sup> The Danish economy experienced two phases of economic boom over the past twenty years. It is significant, however, that the boom period of the late 1990s, in contrast with ten years before, did not result in either wage or price inflation or in an increased unemployment rate. The commitment to moderated wage increases as part of the broader reform process cannot be dismissed as a key factor in the maintenance over this period of a steadily falling unemployment rate, down to 7.8 % in 1997 from a height of 12.4 % in 1993, and low inflation.

Specific features of the industrial relations system help to explain the ability to sustain low wage growth in combination with long-term structural labor market reforms. Union density has traditionally been high in Denmark (around 80 %), but the continued membership strength of the unions lies not in the unions' ability to wage conflict. It lies in the fact that the unions' role has become embedded within the structure of the welfare system itself. This gives security to the unions as actors, and strengthens their willingness to draw their members into compromise in the interest of long-term change.<sup>37</sup> Unions have taken and been given wider responsibilities, and with this has

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<sup>36</sup> One of the chief policy advisors in the national Danish labor organisation LO (Landsorganisationen), Finn Larsen, emphasized the important responsibility that LO has to ensure that all Danish workers can enjoy long-term prosperity. That would be achieved only through structural reforms and control over wage rises across sectors. Interview, October 1998.

<sup>37</sup> See LO (1998c) for example, shows the active support of the union movement for activation policies.

followed responsible action. Two areas in particular are of interest in the unions' embedded role in the welfare system. First, the historical link between membership of union-controlled unemployment insurance funds (although the state in practice pays out roughly 80 % of the actual benefits), and the unions' key role in vocational education. Both explain the interest at all levels of the union movement in the plight of the economically active population as a whole. Individuals remain members during unemployment. The concept of life-long learning, of flexibility that is combined with protection and development of individual capacities, is in this way almost an institutional feature of the employment system. The unions' embedded role was strengthened during the 1990s reforms, as access to a number of new schemes of job rotation (to be surveyed later) depended on (the voluntary) membership of the unemployment insurance funds. At the same time, the high level of facilitation of individual flexibility is one important counterpart to the freedoms that firms in Denmark enjoy. Little relatively speaking is compulsory in the Danish employment system. This, however, has required the building of sophisticated incentive systems in labor markets. The reforms of the 1990s can be seen as an attempt to adjust (in some ways increase) the elements of compulsion and to further strengthen the flexible links between different labor market institutions that help to build individual choice and transparency. For heuristic reasons we may divide the inter-linked reforms into different parts.

#### Social Insurance Reforms

Social insurance reforms under the heading of 'activation' were the anchor in the reform process. These went ahead with the formal introduction of labor market reform from January 1, 1994. The right to return to unemployment insurance payments after receiving training following the end of the 2 ½ years of assistance was derogated, and individuals had to re-earn this right through regular employment (of at least one year's duration). Thus, following the first period of activation, the individual would pass directly to income support (which is means tested and often lower than unemployment insurance payments, on average at around 60 % of maximum unemployment benefits), and to other mechanisms of activation. After 1999, the period of passive receipt of unemployment benefits was reduced by a further year, to one year only, and for those under 25, to six months. As in other cases of labor market reforms, the key aim was to reduce unemployment. However, unlike the low wage-high labor supply and precarious contracting strategy pursued in countries like Chile, Britain and the US in the 1980s, the methods used implied seeking to combine the central goal of early employment with the generation of individual capacities. For example, the element of compulsion was introduced concomitantly with the introduction of a number of new avenues for movement in labor markets, both for the unemployed and those already in employment, following the principle of so-called

rotation, to be surveyed below. Institutional reforms like further decentralization and the introduction of the 'individual action plan' were a part of the new framework of opportunities. The fact that the Danish system went *from* one of passive benefit reception may help to explain the extra effort made to establish more lasting opportunities in labor markets for individual former claimants. In order to enforce the conception of the *individual* duty to be productive, the state had to offer something in exchange, in this case the duty to provide lasting routes to self-reliance in labor markets. However, the transition from high dependence does not alone explain the individual-centered approach that was adopted. From the outset of the involvement of the social actors, the contextual factors were also of crucial importance. This scenario includes the strong sense of social egalitarianism that permeates a labor market with a high unionization rate, and –perhaps more importantly - where unemployment is not an uncommon experience. On average 25 % of the workforce is affected each year (661,500 persons in 1997). Hence, the individual tends not to be stigmatized for receiving unemployment benefit for reasonable periods of time (the average is relatively short -just over one-third of the year per person affected) to the same degree as in other countries.<sup>38</sup> The unions' partial role in the administration of the unemployment funds, more than the high unionization rate per se, explains the unions' stance to unemployment.<sup>39</sup> The unions tend to consider the plight of the unemployed as well, who moreover are likely to remain members of their industrial union while out of a job. The role that the public welfare system plays in making this broad-based attitude possible is not often considered.

#### Mobility and Flexibility.

Indeed, the Danish employment system (as in general those of welfare state regimes) tends to be seen as rigid, and hence it is worth briefly reiterating some features of the high mobility and flexibility that characterizes the labor market in Denmark. Hiring and firing is very lax. The degree of freedom that Danish firms enjoy in this domain was only overtaken by the USA in a sample of 16 countries assembled by the OECD. Average tenure is 8 years, lower than that of most other countries in the group.<sup>40</sup> In fact, close to 40 % of all existing jobs in Denmark are opened each year.<sup>41</sup> Severance payments are virtually non-existent, social insurance payments and corporate taxes are

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<sup>38</sup> Between the third quarter of 1997 and the second quarter of 1998. the average period was around 15 weeks. LO (1998b), p.2.

<sup>39</sup> In fact, it is more likely that the unions' role in the funds (union membership. although otherwise voluntary, is compulsory in order to participate in the fund) explain the continued high unionisation rate.

<sup>40</sup> Cited in Smith (1997), p.109.

<sup>41</sup> Cited in ILO (1999), p.17.

low (with income tax taking a very large share of the tax burden), and regulation of working hours minimal. Legislation is used mainly to enforce the so-called 11-hour rule, which determines the period of rest between situations of work. The flexibility of firms was further expanded in the 1990s through the increased use of general guidelines at national level and performance-based pay in firms. These features suggest that a high level of social partnership at the national level is not necessarily incompatible with increased flexibility at the level of firms. The counter-part to this, though, is that individuals also retain a high level of flexibility. There are a number of indications that mobility is to a notable extent not only secure, but also individual-driven. As noted by Kongshøj-Madsen, it is significant that in the boom period of the second half of the 1990s, the share of the unemployed facing low degrees of unemployment (shorter periods) increased, whereas those facing longer-term unemployment fell.<sup>42</sup> This appears to indicate that the movement in labor markets was individual driven. In support of this the OECD study cited earlier suggested that individuals in the Danish labor market are less likely than in other OECD countries to feel that their job is not secure.<sup>43</sup> This suggests that the institutional engineering that accompanied the activation reforms had some positive effects.

#### Training and Job Rotation - the Labor Policy Reforms.

This engineering more than a new reform implied an attempt to perfect the networks that had been carefully crafted over the years to provide opportunities for individual movement. In the 1990s the Danish government explicitly sought to retain compatibility between the principle of flexibility (for firms) and mobility (for individuals). It did so by retaining flexible hiring and firing laws, but improving the public infrastructure further in training and job-relocation. This implied a significantly different view as to where to place the responsibility for social exclusion from the pure market or corporation-centered approach. Structural unemployment for example was seen as a challenge that merits public attention. If an oversupply of particular qualifications were to develop (leading to a share of unemployable people) this would be considered a market mismatch that requires intervention to provide the surplus individuals with the chance to change or redirect their occupational stream. Hence, although it is no doubt the case that certain individuals may genuinely not wish to take up available jobs for which they are trained, as a rule this kind of mismatch is seen as a social problem. It is felt that structural unemployment is by definition not attributable to an individual fault but to bottlenecks in the economy.<sup>44</sup> The

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<sup>42</sup> Roughly 90 % of employees have no time limit on their employment contracts and ILO (1999). pp.18-21.

<sup>43</sup> Smith (1997), p.109.

<sup>44</sup> Studies (for example Bach. 1999) have shown that only a small number of the unemployed

presumption made in a Danish government publication was explicitly that the equity implications of pursuing work incentive merely through a lowering of benefits are unacceptable. As stated, 'the Danish model of relatively good social protection and a small wage spread presupposes that the differentiation in qualifications and skills must be kept at a level that is sufficiently low to be compatible with the (low) wage-spread.'<sup>45</sup> A further consideration made is the high flexibility firms have in hiring and firing. As a result the reforms to social assistance and unemployment benefits were closely tied to job location and training reforms. The most important overall structural reform implied an attempt to expand the local flexibility and resources for various social and job matching services (de-centralization), whilst also improving the central co-ordination of policy targets.

*a. Training reforms*

Some reforms were made directly to the training system. Since 1 January 1997, the opportunities for individuals, both employed and unemployed to participate in publicly funded educational courses were expanded. It was also sought to focus the educational options for individuals better. Those with shorter qualifications were given priority (trying to avoid what often happens in a purely market-driven system where those with a certain skill level are more attractive sources of investment). As part of the de-centralization process, the local job centers were given a greater role in making educational options available which suited the needs of the labor market. Incentives for the participation and development of private training suppliers in the system were given, and finance for the local job centers became more directly tied to the number of individuals receiving training.<sup>46</sup> These are fairly standard financial de-centralization reforms that may be compared to those in Chile. In reality, however, reforms to the training system itself were minor. The important reforms were those to job-location and rotation, and the way these built on pre-existing features of the *mainstream* system of training, which in Denmark has traditionally been targeted at the workforce in general, not just at those marginal to labor market. Thus, the aim of the 23 regional labor market education (AMU - *Arbejdsmarkeduddannelse*) centers is explicitly three-fold, to strengthen the qualifications of the already employed, to help with relocation, and to generally lift the level of skills on the labor market.<sup>47</sup> Even in the mid-1990s,

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are unwilling to work, and up to 40 % are ready to take on lower-paid jobs.

<sup>45</sup> The Danish text reads, 'Men den danske model med gode dagpenge og lille lønspredning forudsætter, at forskellen i kvalifikationer må holdes nede på et niveau, som er foreneligt med lønspredningen.' 'Arbejdsmarkedspolitikken under forandring'. Arbejdsministeriet/Finansministeriet, May 1996, p.7.

<sup>46</sup> ILO (1999), pp.30-32.

<sup>47</sup> Arbejdsministeriet (1997), p 48.

at the height of the attempt to halve unemployment, the unemployed made up just 28 % of those taking part in VTE courses.<sup>48</sup> The area of activation of the young unemployed seems to have had a particular success. Almost all in this age group either re-entered a mainstream education or a regular job.<sup>49</sup> As we mentioned, this age cohort was to begin the activation phase after only 6 months in unemployment. Those that did not have a vocational qualification were obliged to accept educational options that would last for *a minimum* of 18 months within the mainstream system, for example in apprenticeship programs (normally of this duration). In a study by Anker it was found that two-thirds of apprentices would continue employment in other firms, and more than 80 % in jobs in their area of training in the following years.<sup>50</sup> Then, the young unemployed in Denmark were given more than an 'experience of work' as in the cases of youth training schemes in countries like Chile and Britain." They were provided with an actual qualification, which was likely to lead to a trajectory of life-long learning and membership of the labor market.

*b. The paid leave and job rotation reforms*

Aside from the efforts to activate the unemployed earlier and provide a better regional focus, the most striking feature of the labor reforms of the 1990s was the introduction of a number of paid leave schemes. The idea of job rotation was central. It implied giving a set of stronger incentives for those employed to enter into different forms of leave (sabbatical, educational or child-minding), and for employers to hire substitutes for a significant period. The central goal was to help more people into employment whilst providing those already in jobs with opportunities for planning periods out of work for reasons of education, family or recreation. In the case of sabbatical leave, hiring a substitute was compulsory, but otherwise the system operated purely on a voluntary basis. The schemes became hugely popular. In 1997, 47,448 people were on paid leave at any one time, of which 68.2 % were for educational purposes.<sup>52</sup> In a study of Socialforskningsinstituttet, it was found that a large share of employers (close to 75 %) did hire substitutes even in the case of leave schemes without hiring compulsion (child-minding and educational leave). 12 % of paid leave schemes formed part of a formal arrangement of collective job rotation,

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<sup>48</sup> Arbejdsministeriet (1997), p.58.

<sup>49</sup> ILO (1999) pp.57-58

<sup>50</sup> In the 1990s, apprenticeship engaged 30 % to 40 % of young people in Denmark Anker, *Eleverne. virksomhederne og de nyuddannede*, Ph.D. serie 7.98 (Socialforskningsinstituttet, Copenhagen, 1998), pp.253.263-269.

<sup>51</sup> On the British YTS (Youth Training Scheme). see Ryan (1994. 1995).

<sup>52</sup> Arbejdsministeriet (1997). p.71.

involving the taking of several substitutes through the labor offices." More importantly, of those hired 53 % were unemployed. Although the share of long-term unemployed is quite low (at 13 %), this result is nonetheless significant. Job rotation is rightly said to help the so-called re-employment barrier of the long-term unemployed.<sup>54</sup> Overall it is estimated that leave schemes reduced open unemployment by 60,000 to 70,000 people in 1995. In addition to the paid leave schemes a number of other arrangements were set up for the unemployed, including various options of adult training (re-insertion into the mainstream vocational system) and the so-called '*puljejobs*', or pooljobs.. In this case the unemployed are integrated into public sector jobs with the intention of gaining training and permanent jobs in a particular field of public service. Qualitative evaluations of the scheme suggest that learning activities have been genuine.<sup>55</sup>

In general, the indications are that new labor market policies have contributed to building more secure so-called 'transitional' labor markets depicted in Figure 17.1, to share out more evenly the lapses of unemployment amongst the population and ensure that such periods are planned and productive. They represent a way of distributing the reduction of working time between more individuals and over the course of their lifespan.<sup>56</sup>

### *c. Regionalization and the labor offices*

The local labor offices and social actors also had other important roles to play in relation to strengthening the tie between continuous training (the established training system) and job relocation. The Regional Labor Market Councils (*Regionale Arbejdsmarkedsråd*) have decision-making authority in deciding policies to be pursued by the job relocation centers. Research by Larsen og Langager of individual action plans, a new concept introduced with the 1994 reforms, showed that individual mobility through the labor offices and the councils displayed a high degree of planning.<sup>57</sup> The fact that planned mobility was larger in the regions - where bottlenecks tend to be worse - suggests that labor policy was effective. The example of the county of Ringkøbing is typical. This was a vulnerable spot faced with large layoffs after textile factories moved abroad and fisheries and farming could no longer absorb the labor force. A strategy was worked out with the public training centers and the private sector to establish new apprenticeship programs in the wood and iron industries, thereby reducing unemployment

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<sup>53</sup> These results are reported in ILO (1999), pp.52-54.

<sup>54</sup> The discrimination that has to do with the negative perception of long-term unemployed per se, possibly overriding their actual qualifications and potential.

<sup>55</sup> See for instance Rosdahl (1998).

<sup>56</sup> For discussions of the new concept of transitional and 'inclusive' labor markets in the Danish debate, see further Holt (1997) and Due, Madsen og Mailand (1997).

<sup>57</sup> Reported in ILO (1999), pp.32-34.

by more than 300 % over half a decade.<sup>58</sup> By making apprenticeship a key aspect of the relocation process, unions helped to safeguard long-term occupational security for workers on the programs. In summary, the Danish reforms were geared towards an individual-centred approach that nevertheless involved extensive flexibility for firms. Many of the links illustrated in Figure 17.2 were in use in the present example. The training system remained extensively socialized which solved the problem of bias against skills investments in a highly mobile labor market. In short, the labor market reforms provided a number of new ways to socialize the problem of unemployment.

### **Issue Areas in Employment Policy**

It is difficult to draw detailed policy lessons from the cases we have discussed. So many elements go into defining the unique characteristics of the employment system of for instance a country like Denmark. Indeed, it would be unrealistic to expect a replication of the experiences of this system by taking isolated elements from what is an active network of social and political institutions, and transport those to another case. In drawing more detailed implications one has, therefore, to proceed with great caution. Both Korea's labor relations and the country's public bureaucracy are particular and the problems of labor market reform unique. This being said, some general and specific implications can perhaps be tentatively outlined that can be of some relevance for a case like the Korean, in which welfare reforms are at an early stage of inception. The value of describing a case like the Danish in some detail lies in showing how important the link in general between labor institutions and social policy networks is to the kind of flexibility that a labor reform is likely to foster.

The existence of a strong network between public policy and labor institutions was important to two key elements in the individual-centered approach. These included the following: (i) How flexibility for firms was combined with secure mobility for individuals and the exercise of individual choice. (ii) How the phenomenon of marginality was treated within a mainstream framework, thereby feeding a virtuous cycle that reduces marginality itself. Below we summarize first some general and then some more specific implications that follow from this.

#### *The Unity of Labor and Social Policy Reforms*

The unity of labor and social policy reform was a key factor in the coherence of the Danish labor market reform. The want of accord between the two

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<sup>58</sup> *Information*, 19. August, 1998, p.3



elements, on the other hand, became a long-term negative factor in the Chilean labor reform (as to some extent in other similar cases like the British). In the Chilean and British cases lack of unity was in part an ideological choice made by policy-makers who sought to optimize classical markets in welfare and in labor use.<sup>59</sup> By contrast, in the Danish case, the historical strength and continued broad legitimacy of labor market accords as a means of regulating social security and labor rights was the platform for a concerted reform effort aimed at expanding individual choice. Contextual factors of this kind matter to labor reforms in general, and in particular to how training policy fits within the whole. As we have argued this fit in turn tends to be an important determining factor in how far the kind of labor flexibility that thrives is of the individual-centered kind.

It is important therefore to be aware of the contextual factors that influence the coherence of labor reform in Korea. Two are particularly important to mention. First, Korea had a strong tradition of public policy and administrative capacity within the apparatus of the state. Second, Korea did not have a strong tradition of labor market mediation by social actors. Its labor relations institutions were weak and underdeveloped. These two conditions have powerfully influenced the approach to labor market reform so far, the place of training within it, and the prospects for the development of a balanced approach to corporate and individual flexibility. Up until the late 1990s changes in Korea's labor markets had been piece-meal, with each of the key actors focusing on separate issues even despite the attempt since the Kim Young-Sam government to establish social consensus on institutional reforms. Korea's problems of labor market reform are in large measure political. Relations between unions and employers remained too conflictive in the second half of the 1980s and throughout the 1990s to focus on building labor institutions that would help to ensure that greater mobility in labor markets would offer opportunities for both parties. After breaking down in 1999, the tripartite commission established by the Kim-Dae Jung government never really came back to life, despite the measure to legally 'institutionalize' the committee taken in spring 1999 as a way to seek to draw both labor organizations permanently into the body. In the bargaining rounds of 2000 the FKTU and KCTU, the two national labor federations, were looking for wage rises of 13.2 and 15.2 %, respectively, for their affiliates, compared with the 5.4 % considered acceptable by the Korea Employers' Federation (KEF). This is a notable contrast with experiences of labor reform where longer-term institutional issues have taken precedence, and the regulation of wage growth has been more consensual (as in both Chile and Denmark).

After the crisis of 1997 job security became the most important theme for

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<sup>59</sup> Although for Britain it has been argued that the decline began earlier, in the 1960s, with the failure to up-date the system, as did the Germans at that time, with the 1969 Vocational Training Act. Gospel (1998), pp.438, 454.

labor leaders.<sup>60</sup> At least to begin with, however, the position taken was mainly purely defensive.<sup>61</sup> In part this has to do with lack of resources. In a survey undertaken of member unions by the Korean Metal Workers' Federation, it was found that 69,4 % of local unions do not provide any services to members who are dismissed or quit.<sup>62</sup> National leaders in turn became aware of such deficiencies, and therefore began to take an increasing interest in the social security system and in how it far this protects citizens at large. This greater awareness of broader issues of labor mobility (and not just wage issues) may potentially have a long-term beneficial effect on the priorities of the labor movement. Yet, how this kind of orientation will depend on what kind of stake the union movement is given in the wider system of welfare in Korea. Looking at the various issue-areas in labor reform point to some of the challenges Korea faces in terms of strengthening the role of social actors and connecting this role with that of the state.

### *The Role of the State in Social Security and Employment Policy*

One of the choices which a country like Korea that is building or reforming its welfare system faces is where to place the administration of different areas of social insurance. In the area of employment insurance, Korea chose to leave administration of the system in public hands. This is an area in which Korea's labor reform emerges as potentially strong. This is not because of the level of coverage, because in this respect the reform is still in its infancy (as noted), nor is it in the development of social assistance per se, since Korea is only beginning to extend what could be termed a social safety net. However, with the creation of the employment insurance system in 1995, the Korean government explicitly sought to link various elements of labor reform. In this way it avoided many of the co-ordination problems faced in a country like Chile, where elements of social insurance were placed under separate systems of private management. In contrast, the EIS established a direct functional link, at least at the administrative level, between social insurance (unemployment insurance), training and job redeployment as well as job stabilization. Job stabilization covers many innovative elements that fit under the umbrella of transitional labor markets (Figure 17.1), including employment adjustment subsidies to promote the retainment and/or re-assignment of employees during down-turns, and transition training, as well as regional-specific jobs, among others. The central features of the EIS have

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<sup>60</sup> Interviews with Yoon, Youngmo International Secretary of the KCTU, and Kim Seung-Ho (Director of Research and Statistics of the Korean Metal Workers' federation. Other labor leaders interviewed echoed this view.

<sup>61</sup> In a survey done in 2000 by the employers' federation (KEF) of 261 member firms, only 6.1 % had managed to introduce the right to terminate work in the collective agreement. KEF internal material provided by Lee, Dong-eung, Director of the Labor Relations Department.

<sup>62</sup> Koyongkucho Pydnhwawa Nodongchohap-ui Koyongchông Cheak. The Korean Metal Workers' Federation, 1999.

been documented elsewhere, but can be summarized briefly. Employers and workers contribute (the former at a level depending on size) into three distinct funds covering unemployment insurance payments, payments for employment stabilization (mainly subsidies for firms) and re-training and relocation of the unemployed. All these elements are administered by the bureau of employment insurance, a state organization. The state assumes all administration costs. The EIS was planned as a phased response to a gradual liberalization of the Korean labor market, which it was expected would increase the levels of involuntary dismissals. It was not intended as a crisis-management machine, as it effectively became, and hence it would be unfair to judge the EIS, including the training undertaken for the unemployed in this light. Indeed, the training for the unemployed was predictably not too impressive. Re-employment rates were around 15 % and the courses were typically very short and of low quality.<sup>63</sup> This is in line with international experience, where training for the unemployed is outside the mainstream educational system. This rule is confirmed by the exception, such as courses for the unemployed undertaken at KOMA, the state training institution in charge of national certification, where re-employment rates were close to 80 %. This being said, the nature of the role which the EIS was forced to play shows some of the wider potential capacities of the system. Between January and October 1998 alone, the system expanded its coverage from 120,000 firms to just over 1 million firms. From the low of 7 % of unemployed covered in mid-1999, the level a year later was closer to 15 % as the period after which claims could be made was progressively shortened. The share of active measures (vocational training and job placements) in public expenditure remains quite high even when excluding the public works' projects (which are only nationally active in terms of improving future job chances), at just under 50 % of passive measures, such as unemployment benefits, loan schemes and livelihood protection. In defense of the EIS, the scope for constructive trial-and-error of policy measures should also be noted. This included the fine-tuning of employment subsidies, expansion of coverage of the unemployment insurance and tinkering with the role of the employment stability centers in relocation and training during 1998 and 1999. It is difficult to say whether the EIS was an ideal institution to respond to crisis in the labor market. But at the very least it would have been impossible to respond with the kind of rapidity and agility had the system been divided into separate privately run institutions.

The challenge facing the EIS is whether it is able to make the transition into a more regular role as facilitator of phased change and renewal in labor markets. Although the Korean economy and labor market have bounced back, new labor market challenges have arrived which are there to stay. The rate of involuntary quits is likely to remain higher than it has been, and this challenges the labor offices to come up with instruments similar to the

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<sup>63</sup> See Ryan and Kang in this volume.

individual action planned invented in Denmark and with new ideas of job rotation that suits Korea's labor institutions. The Korean labor market is making the transition towards a kind of flexibility that is more like the Danish variant, with more frequent unemployment and shorter spells of employment. This in turn means the EIS must strengthen its ability to provide access to meaningful training. For instance, the rate of those who lost their employment insurance benefits within two years of acquiring them made up 61 % of the total workforce in the last quarter of 1999, compared with 48 % the year before.<sup>64</sup> Employment information services in the making, like the 'Work-Net', a nation-wide computer network linking employers and job-seekers, although innovative and necessary, are still not well-connected with for example training and markets in skills. Simple labor jobs made up almost 60 % of those who found work through the 'Work-Net'.<sup>65</sup> Such concerns raise the question of how well labor offices are connected with the training system as a whole.

### *Demand Versus Supply-Led Training*

This is the Achilles' heal in Korea's labor reform. The debate on training reform in Korea has focused on the question whether training should be more demand-oriented. This is in line with the discourse worldwide. In Korea there seems to have been a particular justification for the concern that training was too supply-driven. From the 1960s onwards the state was the driving force in providing both initial education and training through vocational schools for firms.<sup>66</sup> Although firms participated through levies and later in the case of large firms through the expansion of in-plant training facilities, these measures were always compulsory and guided from above. Neither unions nor employers were particularly concerned with training outside the firm. This being said, there is a misconception about what 'demand-driving' entails and therefore about what the alternatives for Korea might be. Training can be organized in many different ways. It can be mainly firm generated, which tends to occur where employment stability is very high and labor markets not very fluid, leaving an incentive for firms to invest in employees. There is also the ideal-typical classical market where firms demand individually from private providers without any regulation of training quality or supply. In turn, the existence of a competitive market of this kind can form a part of a wider training system. However, the classical market in training is not compatible with the flexible labor market because of the lack of certification that would ensure tradability of skills, and the

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<sup>64</sup> According to a report titled 'Korea's Employment Trends in the Second Half of 1999' published by the Central Employment Information Office (CEIO), of March 2000.

<sup>65</sup> According to a report titled 'Korea's Employment Trends in the Second Half of 1999' published by the Central Employment Information Office (CEIO), of March 2000.

<sup>66</sup> Park (1994).

absence of systems to support planned mobility. Chile is a good case of the kinds of problems involved in investing in idiosyncratic goods like human capital in systems that try to imitate pure market regimes.<sup>67</sup> The main flaw in the Chilean case was not per se the orientation of subsidies to firms, but that the power to demand was so exclusively centered in firms and that no institutions existed either at this or higher levels to provide employers with the incentive to invest in workers. With direct and blanket tax rebates making up over 90 % of public funding, there were not sufficient channels to empower individuals directly in labor markets. Korea will want to avoid such problems. Most importantly, Korea does not yet have the institutions to support the kind of regulation and shared investment that a demand-driven system requires. Indeed, the same reasons that enter into explaining the very dependence on the state that tended to characterize training provision in Korea, also explain how moving too rapidly or completely towards a classical market system would not be helpful. The real problem faced in Korea is that firms did not and were not interested in taking the initiative to invest in skills themselves. Although a good deal of investment in initial training is made, it is doubtful how useful in quality this is as a tradable *currency*. There are a number of reasons for this, including *traditional product markets* that rely on high levels of imported technology and firm-based learning-by-doing, and *labor relations* based exclusively in firms and of an authoritarian to paternalistic nature.<sup>68</sup> To a large extent these reasons remain. Leaving training to be organized in this context through a market that is largely unmediated is unlikely to make firms invest more in training than they did under state direction. As technological dependence as well as labor relations are changing, the feasibility and need to develop tradable and continuous education systems will further increase. Therefore, in order to develop transitional labor markets and integrate those with the mainstream educational system, subsidies such as those placed under the employment insurance (employment security activities) should be made more directly available to individual employees. It is also possible to think of measures such as job rotation, although these would require much closer co-operation between labor offices and firms. On the other hands, such innovation will not come about without active policy co-ordination. In some respects Korean employers are at a crossroads. When asked senior managers indicate that they want both more liberal firing laws *and* that they value certified skills (such as the certification provided by KOMA).'' The answer to this combination of demands from firms is not a pure 'demand-driven' training system, but more flexibly organized and expanded kinds of occupational

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<sup>67</sup> Williamson (1985), Eggertson (1990).

<sup>68</sup> On product markets and training, see Jeong (2000).

<sup>69</sup> Interviews with executive vice president of the human resources division in LG, Mr. Young-Keek Kim and General Manager of Business Development at Sanisung. August 1999, and May 2000.

markets. It follows that employers will have to take a leading role in organizing such markets if the training provided is to be meaningful and useful for firms. At present, however, neither the conglomerates nor the employer associations, like KEF, have plans to take on a leading role in this field.<sup>70</sup> The initiative is still very much in the government's hands.

There are other indications that Korean employers will need to assume new responsibilities if their changing expectations of employees are to be fulfilled. As You and others have suggested, the Korean labor relations system does retain some important features of commitment, although as they also acknowledge these remain paternal and will be challenged by new performance systems.<sup>71</sup> Managers state that they want their employees to have less expectations of job stability. But they also want to retain employee loyalty.<sup>72</sup> Meeting these potentially conflicting demands will require that labor relations be based on a different, more rational, transparent and negotiated logic of commitment, like that provided by truly independent enterprise councils or labor unions. In that context it is also in the interests of employers that unions more broadly develop a stake in the labor institutions of a more flexible labor market. As we saw from the Danish case, this kind of stake tends to lead unions to focus on longer-term issues and take an interest in workers' rights more broadly as citizens' rights. The Chilean unions also have developed an interest in broader citizenship issues, after economic liberalization and political democratization placed new demands on labor leaders. These Korean unions have, by comparison, quite a way to travel. The most combative national union central, the KCTU, has remained outside the advisory national tripartite commission since early 1998. Its demands for industry-wide industrial relations are concerned mainly with wage bargaining, and not really with issues of social insurance or training. In turn employers in most sectors reject talks with unions at this level, thereby providing little incentive for the unions to change their issue preference ranking. Hence, inertia in the industrial relations system also acts as a barrier to innovation in the wider system of training and in employment policy.

In short there is the impression that Korea may be moving a little too fast in creating a market of training providers relative to the generation of non-market institutions capable of supporting this market. The most visible institutions are the labor offices and employment security centers. These however are not well staffed (one staff in relation to nearly 6,000 workers, according to the Labor Ministry, compared with an average of around 500 workers per staff in European countries). The staff requires training and a career structure as outlined by Hunter in this volume. There have been efforts, as I was told when visiting Kangnam employment stability center in

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<sup>70</sup> Interview with Lee, Dong-eung, Director of the Labor Relations Department of the Korean Employers' Federation, August 2000

<sup>71</sup> You (1997).

<sup>72</sup> Interviews with managers in the Samsung and LG groups.

Seoul last year, to set up advisory bodies involving social actors and other civic members, to oversee training courses. The committee at Kangnam, however, had met only once in six months. Other centers visited in the Seoul region had never heard of the initiative. The capacity of the centers to deliver firm-level networks is also doubtful. Not all training institutions are at the disposal of the centers. Korea's skill markets are still sharply segmented, with the training centers of conglomerates tailored to internal labor markets, and the quality of many new private institutions poor and unsupervised. The curriculum offered to the unemployed, in particular, is weak.<sup>73</sup> Overcoming the gap between training institutions and the firm is Korea's central problem. There are no quick solutions, as imported models that can be implemented only partially are unlikely to be the best guide.<sup>74</sup>

In summary, the private sector deficit in co-operative forms of training in Korea therefore places extra responsibilities on the public sector. International experiences show that the process of building networks between employment offices and firms is slow and arduous. Even in the case of Denmark, it was found that firms participating in job rotation schemes tended to favor traditional forms of hiring, such as informal channels providing a further inducement for labor offices to develop more attractive non-compulsory incentives for firms and to increase the links with them. Over the long-term, efforts in this direction can be fruitful. In the Danish case, for example, the firms that had actually used job rotation schemes also had a much better evaluation of the schemes, 60 to 90 % depending on the level of satisfaction, compared with 20-30 % among firms who had no experience of them.<sup>75</sup> This is an indication that greater efforts to build links with firms, though not without problems, are likely to pay off in the end.

## Conclusion

Flexibility in labor markets and security through welfare systems have tended to be seen as opposite ends. This limits our understanding of what labor market flexibility is. An often-heard argument in favor of a more laissez faire (a corporation-centered) approach to labor reform is that more integrated systems that offer support for individuals diminish the incentive to look for work. This has had a special resonance in a country like Korea which like Japan has deliberately refrained from developing social welfare

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<sup>73</sup> This was also the evaluation of a German advisor at KOMA with several years' experience of working with training in Korea. Interview. August 2000.

<sup>74</sup> The same German advisor believed the so-called two-plus-one scheme pioneered in Korea in the late 1990s, modelled on the German format where the student combines theoretical training with a period of practice in a firm, could not work without a general programme of training instructors inside firms.

<sup>75</sup> ILO (1999), pp.55-58.

outside the workplace.<sup>76</sup> The dangers that Korea could fall in a welfare-dependency trap like the traditional welfare state at one time faced, are however remote. The culture of dependence does not exist, the assistance offered at present is so minimal, the public budget so small and the tone of amendments to the system too moderate to fear such a development. Without pretending to resolve the broader debate about incentives here, we can note that it has at least been broadly accepted, as clear in the Scandinavian reforms, that security has to be complemented by duties. On the other hand, it is also recognized that individuals respond to opportunities (not just constraints), and that corporations and public institutions have a duty to try and provide them. The evidence accumulating from countries that pursue the pure *laissez faire* approach to providing incentives to work points towards the danger of a 'low-skill equilibrium' arising from the increase in the kind of precarious, low-wage jobs that employers tend to offer individuals forced to seek any type of work.<sup>77</sup> The Danish reforms, in contrast, represented an explicit attempt to use the public sector and private institutions to create a 'high-skill equilibrium' and protecting certain equity standards. We may suppose that generating a high-skill equilibrium is a generally desirable goal. This takes us back to the broader issue of what flexibility is. We saw that by traditional standards (the corporation-centered view), Danish firms do have a high level of freedom in labor use. Moreover, when a broader set of parameters for what labor mobility and labor market flexibility is were used, our understanding of how flexible the Danish labor market is, was enhanced.

The analyst needs to judge not just what firms do, but what public institutions provide. The parameters for defining what flexibility and security is can be confusing. The incidence of part-time jobs in relation to full-time jobs, for instance, has been seen as providing an indicator of both. In a recent report by the Economic Policy Institute, figures showing a rise in full-time relative to part-time jobs in the US are taken to indicate an enhanced sense of security in labor markets. A parallel argument made is that the period of insecurity (in the unregulated labor market), where real wage growth declined for nearly 15 years and wage disparity increased, was eventually justified. It is quoted that the proportion of US employees covered by non-standard jobs finally experienced a fall in the late 1990s, from 26.4 % to 24.8 % between 1995 and 1999. Non-standard here is defined as less than full-time.<sup>78</sup> Yet, the recent Danish experience shows that insecurity is not necessarily related to the level of part-time jobs. In other words it is not necessary to deregulate in order to have the flexibility of part-timers in the economy. The level of part-timers in the Danish economy in 1996 was 25.1 %. Among women the figure is higher, at 34 %. The point to

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<sup>76</sup> Garon (1997).

<sup>77</sup> Finegold and Soskice (1988).

<sup>78</sup> Economic Policy Institute, reported in *The Financial Times*, September 4<sup>th</sup>, 2000, p.16.



note is that part-timing is regulated by the same employment standards as full-time work, though collective agreements. As a rule, part timing is secure and not associated with a high wage spread. In addition, the high figure of female part-time jobs related to child-minding duties is an indication of the voluntary, or individual-driven, nature of part timing in Denmark. An important issue that has arisen in the debate on labor market reform in Korea is about non-standard work, including so-called dispatched workers, who are affiliated with agencies that contract them out on temporary contracts. It is difficult to see how such services can be repressed, but they point to a new challenge to labor market actors: how to agree to allow for more flexible working methods, whilst making sure that new forms of work are connected with the social welfare system, including employment insurance, and that it is individuals that make the choice.

The issue of security and work incentives in the case of Korea gave rise to a lively discussion at the conference giving origin to the present book. Prof. Fields proposed a two-tier system, where a lower tier would cover individuals not insured in the EIS, and desperate for work and income assistance. He referred to this as an 'employment guarantee system', which would provide daily work for all regardless of gender, age or qualification who cared to turn up at local employment offices, at some fraction or indeed at the minimum wage. There are a number of problems with a scheme of this kind. It could lead to high dependence and huge costs, without providing participants access to mainstream options. On balance, an ultimate safety-net of the kind described, on condition that the administration costs could be kept down and the work to be carried out socially useful, might not be dismissed out of hand for a country with a small welfare budget like Korea's. However, it is possible to think in terms of a 'third' or middle tier for those not in or no longer in the EIS, which would still provide access to the kind of employment and training services offered through the employment stability centers and therefore act as a transitional labor market. The existence of a lower tier of this kind could also allay some of the fears of those who worry that expanding monetary coverage through the employment insurance would provide disincentives to work in the future. A critical reading of the Danish experience could be useful here. In this case the higher benefits paid out through the unemployment insurance have come to act as a clear incentive to find work, as the income support provided when benefits run out tends to be a good deal lower (in part due to the means test). Since the possibility to renew 'activation options' whilst on the higher provision have been abolished, the incentive has been strengthened for the individual to return to the labor market within a reasonable period of time. This, though, points again to the importance of integrating what has traditionally been seen as 'passive' programs of income support, the middle or lowest tier, with the 'active' parts of the system typically linked with employment insurance. The challenge for Korea is how to reduce marginality by drawing those excluded back into the mainstream, and provide greater scope for individual choice.

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