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Economic and Social Development in the Republic of Korea: Processes, Institutions and Actors

How did this country rise, like a phoenix from the ashes and destruction of the Korean War, to become the "miracle of the Han" within such a relatively short period of time? What insights and policy lessons can be drawn from the Korean experience for countries facing development challenges in the early twenty-first century?

From war-torn and aid-dependent to economic miracle

In 1945, the Republic of Korea was a poor, predominantly agrarian economy that could not attain food self-sufficiency. In addition to the political instability caused by the confrontation with the North, leading to the Korean War (1951-1953), widespread poverty bred social instability. The war destroyed already meagre economic infrastructure, further depressed the standard of living and deepened dependency on aid, in particular emergency relief. Donations of food and fertilizer from the United States constituted the lion's share of aid between 1945 and 1965. Grants and technical assistance, mainly for the physical and institutional infrastructure of agriculture and rural development, were prioritized until the mid-1960s when aid, in particular the US share of total foreign capital inflows, began to decrease and an intensive export-led industrialization policy was launched.

Between 1965 and 1989, as foreign aid in the form of grants fell dramatically in both absolute and relative terms, GDP per capita grew by around 7.2 per cent per year on average. Income inequality and poverty rates were reduced dramatically, with Korea outperforming most middle-income countries. By the 1980s, aid had fallen to 0.6 per cent of GNP (from 9.3 per cent in 1960, one of the highest levels in the world at that time). The Republic of Korea graduated from the World Bank's lending list in 1995, and became a member of the OECD–DAC in 2010.

Making International Development Cooperation Effective: Lessons from the Republic of Korea

In 2011–2012, UNRISD and the Korea International Cooperation Agency (KOICA) collaborated on a joint research project, Making International Development Cooperation Effective: Lessons from the Republic of Korea, to shed new light on the development experience of the Republic of Korea, and consider the insights and policy lessons of the Korean experience for countries facing development challenges in the early twenty-first century.

The project looked at how foreign aid and non-aid policies interacted with domestic policies, processes, institutions and actors to achieve developmental outcomes across economic, political and social dimensions, with a focus on achievements related to economic growth, democratization, and the reduction of poverty and inequality.

The research findings have helped position the Republic of Korea as an emerging international actor in the context of the OECD–DAC and G20. Because the analysis points to some critical factors that challenge existing understandings of the Korean development experience, it also provides insights to other donors and aid recipients alike.

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Social policy synergies between land redistribution and investment in human capital laid the foundations for structural change and economic growth

Severe inequality in landholdings, with more than 80 per cent of farmers tenants paying usurious rent, was a significant cause of poverty and social disorder in the Republic of Korea in 1945. Two land reforms, entailing redistribution of previously Japanese-owned lands and the lands of large Korean landowners, were implemented by the US Military Government in Korea (1945-1948) and the Rhee government (1948-1960), with the political and economic purposes of preventing social disorder and increasing agricultural productivity. Under the Rhee government, 74 per cent of land subjected to reform was redistributed. The government acquired the land, compensating landowners with government bonds whose value was below the market value of the land. The reform thus had a strong wealth redistribution effect. This was compounded by increasing fiscal instability and rising inflation, which further reduced the value of the bonds. The proportion of families owning all or part of the land they farmed rose dramatically, from 48.4 per cent in 1945 to above 90 per cent after land reform in the 1950s.

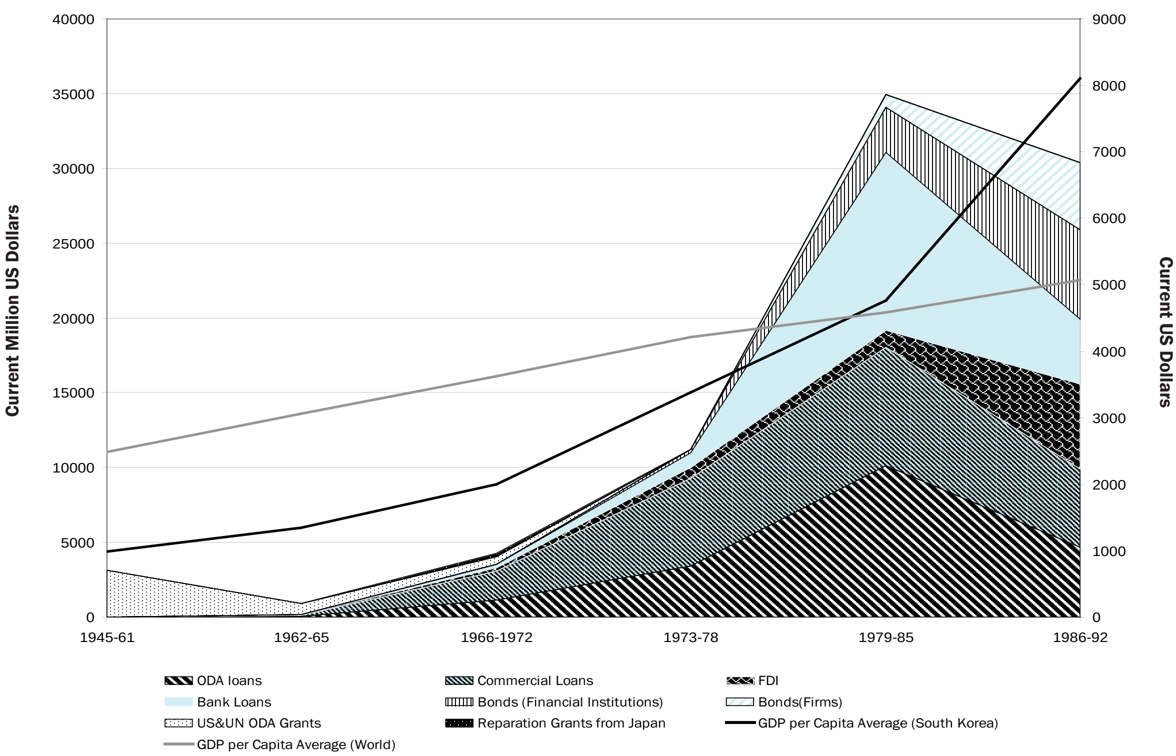
In addition to wealth redistribution, the Rhee land reform also had the effect of encouraging investment in human capital formation. It did so by offering landowners a choice: as an alternative to receiving government bonds in exchange for their land, landowners could use the land for establishing private schools. As a result, the share of private secondary schools increased from 20 per cent of the total number of secondary schools in 1945 to 42 per cent in 1957, mostly in rural areas where the land was located.

Policies to improve children's access to schools in rural areas were implemented simultaneously. A large government budget for education was spent on building rural primary schools, and on educating and training teachers who were dispatched to both rural and urban areas. The increase of private schools, mostly with lower or upper secondary education provision, made it feasible for those students to transit from primary to higher education. Enhanced education levels in rural areas made a significant contribution to supplying educated and skilled workers for labour-intensive export industries in the 1960s (Project paper by Yi, Cocoman, Rhee and Chung).

Aid conditionality and a lack of developmental vision undermined investment in the productive sectors

The Rhee government (1948-1960) focused on maximizing the volume of aid, rather than the productive investment of aid resources. But aid

Foreign Capital Flow and GDP per Capita



Sources: Chung-yum Kim (2011). *From Despair to Hope*, Korea Development Institute, Seoul; and Groningen Growth and Development Centre (2012), Total Economy Database, www.rug.nl/feb/Onderzoek/Onderzoekscentra/GGDC/data/ted came with a number of conditions. Under the US–initiated counterpart fund, meant as a price stabilization mechanism, the government was required to establish local currency reserves corresponding to the value of aid goods. From 1945 to 1961, lacking both a significant source of foreign exchange and a long-term plan for investment in the productive sectors, the government set artificially high exchange rates and low local prices for goods imported through aid to increase the purchasing power of the counterpart fund despite donor demands for depreciation of the Korean currency. This led to inflationary pressure, as well as uncertainty around prices and the exchange rate, undermining incentives for long-term investment. Furthermore, the power to allocate and use aid resources was concentrated in the hands of the president and a small group of elites who did not have a national development plan. In this context corruption grew, involving both government and business actors who were more interested in rent-seeking than in the potential returns from real investment.

Under state-directed development plans, aid resources were allocated to productive investment

Beginning in 1962, fiscal, exchange rate, inflation, employment, industrial, education and technology policy areas were integrated into five-year economic development plans. The focus was on long-term, centralized planning of the mobilization, allocation and use of resources for productive investment, and a competitive export sector in particular. Aid resources were pooled with other foreign and domestic resources for the implementation of projects set out in the economic plans.

By the beginning of Park's first elected term in 1963, the US security commitment was weakening and US aid policy was gradually replacing goods and large grants with loans. The Park government prioritized the allocation of aid resources to productive investment rather than maximizing the value of aid. It took measures to reduce the inflation rate, so that it would not undermine investment in industrialization. The exchange rate was set considering the competitiveness of industry, in particular export sectors. The Park government actively diversified aid sources to meet investment requirements, and provided administrative support to the private sector with the aim of attracting foreign resources. Sometimes business actors negotiated with foreign donors on behalf of the government. The government strategically allowed or even encouraged voices opposing donor demands and conditions so as to drive negotiations towards more favourable results (Project paper by Yi, Cocoman, Rhee and Chung).

Nationally owned firms were crucial to investment, employment and growth

From the 1960s, the government implemented macroeconomic, trade and industrial policies to protect and promote nationally owned companies, both small and large. Concentrating aid and non-aid resources on nationally owned industry, applying strong rules and regulations protecting and promoting local content, and actively promoting small and medium enterprises ensured an enabling environment for the accumulation of national production skills, managerial capabilities and technological expertise. Being heavily dependent on the visible and invisible benefits of this support, nationally owned firms created jobs and income domestically rather than abroad. Companies' dependency on the support of state institutions also reduced the threat of (and actual) capital flight and brain drain. Policies to promote the local content of products and services during heavy and chemical industrialization in the 1970s resulted in the growth of SMEs that supplied parts to large enterprises (Project paper by Amsden).

Mechanisms for developing and utilizing human capital aligned with industrialization were crucial to employment generation and economic growth

The government systematically coordinated policies shaping, accumulating and utilizing human capital when target industries and skill/labour requirements were mandated by the economic development plans.

Photo by UN Photo/Grant McLean
Aftermath of the war in Korea: Youngsters keeping warm around a fire in the ruins of Seoul, 1950.

During the period of intensive industrialization, particularly in the 1960s and 1970s, the state was at the centre of adoption, innovation and diffusion of knowledge and technology, both through state-owned R&D institutes and through indirect and direct support to private sector R&D institutes and industries. This built individual and organizational capacities to absorb and diffuse knowledge and skills in a wide range of disciplines, and facilitated the translation of knowledge into "productive knowledge".

To establish a direct link between education and technology development, the government planned and regulated vocational training in school curricula, and made on-the-job training compulsory at factory premises to fill knowledge and skill gaps. Quotas were established for students and faculty at universities to align graduates to labour demand in key industries. A number of state-owned or -supported institutions were also established, including the KIST (Korea Institute for Industry and Science, established in 1966) and the KAIST (Korean Advanced Institute for Science and Technology established in 1971). These played a leading role in the development of advanced technologies for key industries in the public and private sectors in the 1970s, such as steel, chemicals and electronics. To staff the institutions, the government directly contracted and offered scholars and technicians attractive terms and working conditions.

Photo by UN Photo/PB
Increasing agricultural production: An assistant soil chemist weighing samples in the laboratory of the Soil Fertility Unit, 1964.

Two features of this approach are noteworthy. First, the state's role as financier. Although the share of R&D was as small as 0.5 per cent of GDP until the mid-1970s, state-owned institutes represented more than 80 per cent of the total. And second, government coordination of R&D, education, training, skill development and public investment in key industries, linking education, technology and industrialization across a range of sectors, created synergies for economic development (Project paper by Kim).

Industrialization went hand in hand with redistribution towards rural areas

Contrary to the conventional view that agricultural development is a precondition or precursor to industrial development, rural development in the Republic of Korea followed the take-off of labour-intensive export-oriented manufacturing industries.

The Saemaul Undong (New Village Movement) was initiated by the government in 1970, when rural communities continued to suffer from relatively poor infrastructure and services while urban livelihoods were rapidly improving. The Saemaul Undong became a nationwide programme of rural development and a symbol of government-guided participatory development. Even though poverty remained widespread in the 1970s, extreme poverty fell significantly and rural infrastructure was greatly improved.

The success of the Saemaul Undong as a rural development project was grounded in a range of complementary policies to redistribute wealth and income towards rural areas, and to put the rural labour force into productive employment.

These policies included land reform; the centrally planned and controlled rural credit system, and private debt cancellation facilities; and the development of agriculture-related industries, such as fertilizers, machinery and high-yielding rice varieties. These policies transferred both foreign and domestic resources, such as aid and tax revenues gained by export industries which would otherwise have been invested in urban areas, to rural development. The income gap between rural and urban areas had almost disappeared by the late 1970s (Project paper by Douglass).

Public policy drove a unique public-private mix in education and health provision

In the Republic of Korea, the state allocated resources towards priority areas, and enforced sophisticated rules related to the use of private property and the private provision of services for public purposes: the public-private mix was driven by public rather than private interests.

Apart from fees for university education, there is no significant difference in terms of service quality and costs borne by users between public and private provision of education and health services. This is an interesting phenomenon in the context of debates on quality and affordability of social service provision, which tend to position public vs. private as an either-or choice.

Primary and lower secondary education are predominantly public, and upper secondary and higher education are predominantly private. Since 1945, public schools have provided education to more than 98 per cent of primary school students. The proportion of students in public lower secondary schools increased from 55 per cent in 1965 to 81 per cent in 2005. In contrast, about a half of students in upper secondary education and more than 80 per cent of students in higher education are in private institutions.

In education, the government directed public resources towards compulsory primary education in the 1960s and lower secondary education in the 1980s. It simultaneously encouraged private investment in higher secondary and tertiary education with guarantees of investors' property rights and substantial subsidies. In terms of total annual budgets, state subsidies accounted for approximately 76 per cent for private lower secondary schools, and 54 per cent for upper secondary schools in the early 2000s. Regulation reached down to the micro-level management of private institutions—including annual admission quotas, caps on tuition fees, number and content of courses, graduation requirements and teacher qualifications—effectively equalizing cost and quality between public and private education.

Given the reliance on government subsidies, the owners of private schools had a choice between conforming to state policies and regulations, or extracting rents from subsidies and fees while investing less. That the vast majority chose the former was the result of strong state control, laws and regulations, as well as an active and organized civil society.

With regard to the provision of health services, in 2010 88.2 per cent of the total beds were in for-profit establishments, compared with 41.8 per cent in 1962. In 1989 government-regulated national health insurance was extended to cover the whole population. The government fostered a symbiotic relationship between public and private provision, with the state's primary role being regulator rather than service provider. Various public policies, such as tax-exemptions and subsidies, served to mobilize private investment in the health sector. At the same time, incentives such as exemption from military service were used to draw medical personnel to public health centres and hospitals. Public support to both private and public providers contributed to gradual expansion of health facilities and personnel.

State control over the health sector never reached the same proportions as it did in education. The government's primarily regulatory role, and the strong organizing power of the private hospitals and medical personnel, have shaped a health system characterized by contradictions: "universal" health insurance coverage, but a comparatively small benefit package with high out-of-pocket expenditure (33.8 per cent in 2010); low expenditure on health as a percentage GDP (6.5 per cent in 2009); widely available advanced medical technology; and low expenditure on disease prevention, sanitation and public health administration (Project paper by Yi).

Policies underlying developmental success undermined authoritarianism and sowed the seeds of democracy

As Amartya Sen has pointed out, there is no persuasive evidence that any of the policies underlying developmental success are inconsistent with greater democracy and had to be sustained by authoritarianism.

Photo by UN Photo/PB

Increasing public health services: A mother registering her baby at the Mother and Child Clinic in the Health Centre in Seoul, 1964.

Contrary to authoritarian regimes' intentions in the Republic of Korea, the highly educated workforce resulting from educational and human capital formation policies, the growth of rural organizations under rural development policies, the involvement of civil society organizations in social service delivery, and trade unions and workers organizations for occupational welfare—all products of the developmental process under authoritarian rule—were vital forces driving democratization (Project paper by Yi and Mkandawire).

Gender inequality is an enduring social cost of the development trajectory

The gender dimension of the Republic of Korea's development experience highlights various trade-offs between policies for production, poverty reduction and reproduction. Female-targeted family planning policy, one of the major components of policy to control population growth and increase the active female labour supply under the authoritarian regime between the 1960s and 1980s, was successful if seen in terms of reducing the fertility rate but overall it failed to enhance women's position in workplaces and households due to its targeted and top-down manner. The perception of women as "reproducers" rather than "producers" was not changed but was in fact strengthened.

Furthermore, low-income labour-intensive export industries, male-biased employment in heavy industry and vocational training policies, while highly successful in terms of economic growth, further marginalized female workers as producers. Additionally, long working hours served to reinforce the male-breadwinner model and gendered the division of labour. The literature on women's role in Korean development has focused principally on the manufacturing sector; however, women were predominantly active in the primary sector in the 1960s and 1970s and undertook important roles in social service delivery and rural development projects. In these roles, they have assumed the double burden of work and care. This double burden in production and reproduction grounded in the overall identification of women as "reproducers", and persistently low wages paid to women (Korea has the largest gender wage gap of the 29 OECD countries) continue to underpin high gender inequality in the Republic of Korea (Project paper by Lee).

Environmental deterioration is a result of policy failure, not policy absence

Policies driving the Republic of Korea's industrialization and economic growth were not matched by effective environmental protection measures. Indeed, environmental degradation due to war and poverty in the 1940s and 1950s was compounded in the 1960s and 1970s by the push for industrialization.

Environmental policies have evolved in four phases. In the first phase, from the 1960s through the 1980s, policies protecting the environment took a back seat to policies promoting the development of industry. This was the phase of ex-post restrictions, and command and control under authoritarianism.

The second phase can be characterized as governmental response to the voice of the people. Coinciding with democratization, the 1990s were a period of ex-ante restrictions, economic incentives and cooperation. It was a time of environmental awakening which saw the establishment of environmental NGOs as well as civil society organization around quality of life issues. Environmental NGOs engaged with policy processes through various methods, and the government began to make comprehensive environmental protection laws and associated regulations. Public sentiment shifted from a desire for "harmony of economic growth and environmental protection" in the 1980s, towards a preference for environmental protection over economic growth the 1990s.

The third phase of environmental policy began in 2000 with the establishment of the Presidential Commission on Sustainable Development. This

Photo by UN Photo/PB
Business education: Seoul Girls Commercial High School, 1964.

was a period of "environmental governance" based on principles of participatory decision making, cooperation and partnership among multiple stakeholders including civil servants and experts, as well as representatives of civil society, NGOs and the business sector. A low-carbon "green growth" agenda has driven environmental policy since 2008.

Thus in the Republic of Korea, the deteriorated environment is not due to the absence of environmental policy per se, but rather to inadequate implementation. Only when a consultative, cooperative approach has been pursued, based on free and open public discussion, has progress been made (Project paper by Huh and Pawar).

Photo by Hae Ji Jeong.
Science education: Ewha Girls' High School, 2011.

Further reading

The following papers, commissioned for the UNRISD-KOICA project, fed into this Research and Policy Brief.

Amsden, Alice (2011), *Securing the Home Market: A New Approach to South Korean Development*

Chung, Moo-Kwon (2012), *The Transformative Role of Social Policy in a Skill Formation Regime*

Douglass, Michael (2011), *Rural Development Policies: The Saemaul Undong in Historical Perspective and in the Contemporary World*

Evans, Peter (2011), *The 21st Century Transition to a Capability-Enhancing Developmental State*

Huh, Taewook and Manohar Pawar (2012), *Responses to Environmental Challenges: Origins, Drivers and Impacts of Green Growth on Development*

Kim, Eun Mee (2012), *Capability-Enhancing Alliances: The Case of South Korea*

Kim, Taekyoon (2012), *Learning through Localizing International Transfers in South Korea*

Lee, Jinock (2012), *Changes and Continuity in Gender Policy*

Lee, Joo Ha (2012), *Institutional Linkages between Social Protection and Industrialization*

Mkandawire, Thandika (2012), *Social Policy and Development: An Interrogation*

Yang, Jae Jin (2012), *Social Policy Responses to Economic Crises: 1979-81 vs. 1997-98*

Yi, Ilcheong (2012), *Developmental Social Services: Education and Health Policies*

Yi, Ilcheong and Thandika Mkandawire (2012), *Learning Lessons from Developmental Success*

Yi, Ilcheong, Olive Cocoman, Hyunhoo Rhee and Youah Chung (2012), *Aid and Development Effectiveness in South Korea*

About this Brief

UNRISD Research and Policy Briefs aim to improve the quality of development dialogue. They situate the Institute's research within wider social development debates, synthesize its findings and draw out issues for consideration in decision-making processes. They provide this information in a concise format that should be of use to policy makers, scholars, activists, journalists and others.

This brief was written by Ilcheong Yi. Download this publication free of charge from www.unrisd.org/publications/rpb14.

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Lessons from the experience of the Republic of Korea

The research re-enforces our understanding of development as a multifaceted process. Success in the Republic of Korea was grounded in synergies between economic and social policies, and across public and private sectors, linked to each other to build human capital, increase employment, and redistribute assets and income across sectors and geography. Yet economic growth and social development were accompanied by a range of "bads", such as corruption, bureaucratic inefficiency, authoritarianism, cronyism and lack of transparency, gender inequality and a deteriorated environment.

Today's conditions differ dramatically from those which enabled the "miracle of the Han"—Korea's developmental success—and each country's experience must be understood within its specific context. Nonetheless, the research findings challenge some mainstream development policy approaches, including the "growth first, redistribution later" view of social policy; the ideology of market fundamentalism and a minimal role for the state; and the definition and assessment of "good" institutions based on whether they enhance the functioning of markets. Because many such policy approaches continue to be pursued in spite of lacklustre results, the Korean experience may provide insights to aid donors and recipients alike.

The research findings suggest that:

- Aid is more effective when it is designed to facilitate investment in the productive base of the economy as well as meeting basic needs.
- Aid that is conditional on macroeconomic stability without a coherent plan for productive investment can create economically unproductive and socially unsound incentives for the recipient government and private sector, resulting in corruption, speculation and hoarding.
- Diversification of aid sources and mobilization of non-aid resources can strengthen the negotiating power of aid recipients. Increased negotiating power combined with coherent and comprehensive national development strategies and implementation capacities are the foundations for "ownership" of development.
- Social policies for redistribution (such as land reform) can be combined with those promoting productive investment (such as human capital formation) and consequently contribute to industrialization.
- The choice between public and private provision of social services, such as education and health, is not an either-or dilemma. An effective and well-functioning regulatory regime can ensure a public-private mix that mitigates negative impacts of private provision (such as a hollowed-out public sector, unequal access or unaffordability).
- Industrial policy, in particular the kind protecting and promoting nationally owned firms which generate employment, productive skills, managerial capabilities and technical expertise and reduce brain drain, can be a key element of a successful development strategy.
- Education policies can be coordinated with other policies, in particular industrial policies, in ways that reduce the mismatch between education supply and labour demand, and generate employment. Both macro- and micro-level planning in education and relevant sectors are crucial.
- The state can both proactively invest in R&D and share results with the private sector, and provide incentives for private sector R&D, to generate employment and resources for development.
- Redistributive policies (such as land-to-the-tiller agrarian reform, and income redistribution from successful urban areas to the countryside) can provide a material basis for rural development. But the full benefits of these policies are realized when they are coupled with complementary measures to generate rural employment and improve infrastructure.

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www.unrisd.org, info@unrisd.org

The United Nations Research Institute for Social Development (UNRISD) is an autonomous research institute within the UN system that undertakes multidisciplinary research and policy analysis on the social dimensions of contemporary development issues. Through our work, we aim to ensure that social equity, inclusion and justice are central to development thinking, policy and practice.

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