

Economic Crisis and Reforms of Pension and Social Security Programs In Korea

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1. The impact of the Economic Crisis Occurred in November 1997

Korea was said to have become an advanced industrial economy before the 1997 economic crisis, participating as an OECD member country and recording over \$10,000 per capita income during 1995 to 1996. However, the Korean economy is currently experiencing a severe setback resulted from foreign currency crisis taken place in November 1997. Coupled with the economic restructuring efforts made, which were voluntarily promoted with a view to adapting the economy to the process of globalization, by the government, the panic of the economic depression hit labor market and lower income classes. As a result, it has created a large number of unemployed and poor households, raising the percentage to four to five times the previous amount. The economic crisis attacked every sector of the Korean economy. The adverse impact includes the negative influence on the household, social life, individual psychology and physical states. Furthermore, the process of globalization will continuously exert considerable influence on the future economic and social life of Korean people.

Drastic changes have continuously taken places in Korean economy in such a sort period as the nation experienced the unprecedented low economic growth rate of - 6.7% in 1998, followed by a rapid recovery with a growth rate of 10.7% in 1999. And another setback in economy after the end of 2000 is now bringing further worries over the possibility of returning to high unemployment and prolonged employment instability. They are recognized as stemming from both additional economic restructuring efforts including reforms of major commercial banks and conglomerates like Hyundai and Dawoo and recession in chief export and import-leading industries like semi-conductor and petroleum.

The aftermath of this economic instability had a drastic impact upon every corner of Korean society, especially for poor households. Korea faces a number of difficulties in a new era of social issues including poverty, the labor market, and family life and structure.

First of all, the rate of unemployment had been setting new rates every month after the crisis, starting from 2.0% in 1996, 2.6% in 1997, 6.8% in 1998, and 6.3% in 1999, with the peak 8.6% in February 1998, though the rapid economic recovery from the end of 1998 reduced the rate to 4.1% in 2000. The long-term effect of high unemployment is now developing into increased proportion of the long-term unemployed. The proportion of the long-term unemployed (6 months) has linearly and steeply increased from 5.6% in January 1998 to 13.6% and 15.8% in January and October 2000 respectively, wandering around 14% since then. Other severe insecure factors in labor market and workers' life are the increases in the p

roportion of irregular jobs and economically inactive population, which reduce inevitably their wages and exclude the entitlement to social insurance programs. The proportion of irregular workers¹—composed of temporary workers (66.5% in 1999) who are under contract less than one year and daily workers (33.5%)—rose from 42.0% in 1995 to 51.7% in 1999 and 52.4% in 2000. The rate of economically active population also has decreased from 62.2% in 1997 to 60.7% in both 1999 and 2000. These trends inform us that, as a result of economic and labor market restructuring, part of the unemployed and inactive population is becoming a hard-core group of long-term unemployment and poverty in Korea.

(Table 1) Trends in Proportions of the Number of Workers by Employment Type (UNIT, %)

	Total (1,000 PERSONS)	Wage Workers			Self-Employed	
		Regular	Fixed-Term Contract	Daily	Self-employed	Unpaid Family Workers
1997	21,106	33.9	19.8	9.0	28.3	9.0
1998	19,994	32.3	20.0	8.7	28.9	10.1
1999	20,281	29.8	20.6	11.3	28.8	9.5
2000	21,061	29.7	21.4	11.3	28.5	9.1

Source: National Statistics Office, Monthly Employment Trends, 1997-1998.

The poverty incidence for urban workers' households had sharply risen from 1.7% in 1996 and 2.9% in 1997 to 7.5% in the 1st quarter of 1999, thereafter declining to 5.3% in the last quarter of 1999. The post-1996 poverty rates are estimated by applying a time series of real values of the minimum cost of living in 1994 (859,000 won or \$7544 in 1999 value), which might be a lower bound of poverty line. This is an attempt to keep the cost of living from the influence of consumption patterns and the reduced income level that has been experienced after 1997 crisis. The result gained for the year 1999 is compared with the results estimated on the basis of the three other standards, namely, the minimum cost of living estimated in 1999, 50% of average income of urban worker's households and 50% of median income of urban worker's households which might be an upper bound of poverty line (as shown in Appendix Table -1).

The poverty rate of the total households rose rapidly during 1998 and 1999. This may be attributed to the increase in proportion of non-workers and irregular households in the whole households, among which the poverty rate is relatively high, as well as the rise in poverty rate of urban workers households, which is used as the base to further estimate the national-wide poverty rate. The income data for urban workers' households are used to estimate national incidences of poverty because there are no periodical publications on income of the total households. The national poverty rate of household members is shown to be much lower than its household counterpart. But there has been a threefold increase from 3.1% in 1996 to 10.9% in 1998, and the latter figure remained the same throughout 1999. However, the poverty rate marked its highest at 12.6% in the 1st quarter of 1999 and decreased thereafter.

¹ Professor Bae, Ginhan in Choong-Nam National University insists the rate would down to 17.3% from 50% if the OECD criteria is applied, but the rate is still higher than France 13.5%, Germany 12.4%, Japan 12%, Italy 8.3% and United Kingdom 6.9%

r until reaching 8.8% in the 4th quarter of the same year. The decrease in the poverty rate in 1999 seems largely due to the rapid drop of unemployment rate during the same period along with the overall enhancement of income level. However the pace of the decrease in the poverty rate has been much slower than that of unemployment rate, even when the time lag relation between the two indices were taken into account. When the OECD standard is applied, the relative poverty rate in 4th quarters becomes a staggering 11.7% and the annual poverty rate 12.7%.

(Table 2) Poverty Rates (%) of the Whole and Urban Worker's Household Members, '96 to '99

	'96	'97	'97. I	'97. II	'97. III	'97. IV	'98	'98. I	'98. II	'98. III	'98. IV	'99	'99. I	'99. II	'99. III	'99. IV
Members of Urban Worker's Household																
(A)	1.7	2.9	3.5	2.8	2.3	3.0	6.3	6.1	6.6	7.0	5.6	6.5	7.5	7.3	5.9	5.3
(B)												7.3	8.5	7.9	6.7	6.0
(C)	4.9	7.3	8.4	6.3	7.8	6.7	9.7	10.6	8.9	10.1	9.3	9.7	10.9	8.7	10.2	9.1
(D)												12.2	13.8	13.3	11.4	10.3
Whole																
(A)	3.1	4.9	5.9	4.7	3.9	5.0	10.9	10.5	11.4	12.1	9.7	10.9	12.6	12.2	9.9	8.8
(B)												11.4	13.4	12.4	10.5	9.3
(C)	6.7	9.3	10.7	8.0	9.9	8.5	12.6	13.7	11.5	13.0	12.0	12.7	14.1	11.7	13.2	11.7
(D)												14.3	16.2	15.6	13.3	12.0
Unemployment Rate	2.0	2.6	3.1	2.5	2.2	2.6	6.8	5.6	6.8	7.4	7.4	6.3	8.4	6.6	5.6	4.6

Note: A is the real value of the 1994's minimum cost of living; B is the estimated minimum cost of living of 1999; C is 50% of median income of urban worker's households; D is 50% of average income of urban workers.

Source: "Survey on Actual Condition of Household Income and Expenditure"

The expansion of income and wealth disparities within and among countries has become a major social problem in the wake of dynamic industrial restructuring process. Even the United States with its long-time economic boom in the recent period has failed to reduce income inequality. For instance, the poverty incidence in the United States during the severe economic depression was 13.5% in 1986 and 15.2% in 1983, but was still 13.3% in 1997 and 12.7% in 1998. Also, the income of the upper 20% increased by 15% as compared to only 1% increase by the lower 20%. During the period between 1979 to 1989, the income increased from 39.0% to 42.1% for the former class but dropped from 5.6% to 6.4% for the latter class. Therefore, the American economy can be assessed as having continuously aggravated income distribution since its intensified investment in venture industries during the Reagan administration.

Korea seems to have a similar trend in poverty incidence. The distribution of urban worker's income, which is only available as quartile data found in Korea, has worsened until the 1st quarter of 1999 since the economic crisis and shown to have improved thereafter. They have all become much worse, though, compared with the levels in 1997 as shown in Table 3. The Gini index in 1999 shows a record high since 1988. The rate of occupied income by top 20% with respect to lower 20% also returned to the 1988 level at the same time.

Furthermore, income disparities between rich and poor appear more distinct in comparing top 5% and lower 5-10% of urban workers households. Highest 5% own 16.0% in 1999 while lowest 5% and 10% own 1.0% and 2.7% respectively. The income gap between two classes has widened since 1996, during which the highest 5% occupied 13.6% and lower 5% and 10% owned 1.2% and 3.3%. On the whole, the proportion of income possessed by the lower 50% of urban worker's households declined to 27.8% in 1999 from 30.1% in 1996. Hence, the impact of the economic crisis and the resulting economic restructuring has widened the income gap between classes, enlarging the size of the lower class (Bark, 2000(3))

<Table 3> Trend of distribution of urban workers' income

	80	88	96	97	98	1999
Ratio of occupied income (%)						
upper 20%	45.4	42.2	37.9	37.2	39.8	41.3
lower 20%	5.1	7.4	8.2	8.3	7.4	7.1
Ratio of upper 20% to lower 20%	8.90	5.70	4.63	4.49	5.41	5.85
GINI coefficient	0.389	0.336	0.291	0.283	0.316	0.333

Source: Ministry of Finance and Economy

The economic crisis also changed the poverty profile especially of the vulnerable and marginal groups. The pre-crisis poor mainly consist of the aged, single parents, handicapped, chronically ill, small-sized households. Most of them lack ability to work or have low compatibility in the labor market owing to poor skills schooling. The present poor is composed of a wide range of groups including new participants in labor market, the unemployed who have been laid off, and poor workers who were transferred to underpaid jobs after the crisis or were enforced to get low nominal wages.

Several important changes are can be detected. First, one or two member households with income below 200,000 won per capita occupied 48.7% of the total poor in 1996 but decreased to 28.9% in the survey conducted in 1999. Most of the poor (50.2%) came from standard size households in 1999.

<Table 4> Distribution of the poor according to household size (Unit: %)

	1 person	2	3	4	5	6	7	8	9
1996	22.9	25.8	16.0	17.9	11.2	4.7	1.1	0.2	0.1
1999	10.6	18.3	18.9	31.3	13.5	5.2	1.6	0.4	0.1

Second, the proportion of aged households (households largely composed of aged members) in the poor has appeared to decline significantly since the economic crisis. Single-person households, most of which are aged households, accounted for as low as 10.5% of the poor in 1999, much lower than the rate of 34.6% in 1996. Another vulnerable group was single-parent households that also showed lower rate in 1999 than in 1996. Meanwhile, there has been a substantial increase in poverty incidence among general households composed of the unemployed, irregular and temporary workers, and other working poor.

<Table 5> Poverty incidence according to household type (unit, %)

	Single households	Single parents	General
1996	34.6	3.6	61.9
1999	10.5	4.2	85.3

Third, residential type also has been subject to significant influence in this short recession period. There was a mass move of the poor from chartered houses to rented houses with deposits, raising the proportion of the latter type from 10.9% in 1996 to 19.7% in 1999. This change could be interpreted as a reflection of the deteriorated economic situation of the poor. More specifically, 2.1% of the poor sold their assets and 13.1% reduced their savings.

<Table 6> Residential type of the poor (Unit: %)

	Owner occupied	Chartered	Rent with deposits	Rent or others
1996	49.5	29.6	10.9	10.0
1999	48.6	21.5	19.7	10.2

Fourth, poverty in rural areas appears to be more severe than urban poverty, despite the fact that urban poor greatly outnumber the rural poor. Using the 1996 data set, in which only nation-wide income data is available, it can be seen that the rural poverty incidence, with exception of farmers, is 7.1% - 13.0% in total population and 11.0 - 18.2% in households, whose rate is almost three times higher than the national average. The most severe impact of the economic crisis penetrated into urban households especially in metropolitan cities, increasing metropolitan poverty incidence by almost 10% to 48.2% while decreasing the rural incidence by nearly the same rate.

<Table 7> Regional incidence of poverty in 1996 (Unit: %)

	Nation	Cities			Rural
		Total Cities	Metropolitan	Other	
Nation (A)	4.3(3.1)	3.2(2.5)	2.8(2.2)	3.9(3.1)	11.0(7.1)
(B)	8.6(6.7)	7.0(5.8)	6.3(5.3)	8.2(6.8)	18.2(13.0)
Workers (A)	1.9(1.9)	1.7(1.7)	1.5(1.6)	2.0(2.0)	3.3(3.2)
(B)	5.4(5.3)	4.9(4.9)	4.7(4.7)	5.2(5.1)	8.8(8.5)
Non-workers (A)	8.2(5.0)	5.7(3.7)	4.9(3.1)	7.6(5.2)	21.0(12.9)
(B)	13.7(9.0)	10.5(7.3)	8.8(6.1)	14.1(10.1)	30.3(19.8)

Source: National Survey on Household Consumption, National Statistical Office, 1996

Note: A is the minimum-cost-of-living in 1994 and B is the OECD poverty standard, 50% of median income

<Table 8> Regional occupied proportion of poverty (unit, %)

	Metropolitan	Medium-sized	Rural
1996	39.2	27.2	33.6
1999	48.2	26.8	25.0

Employment is very important, particularly after the 1997 economic shock. The nation-wide survey, conducted in July 1999 conveys several implications in this respect. The jobless occupy 41.2 % of the poor with per capita household income less than 250,000 Won. Some 20.8% of the poor have casual and temporary jobs and 15.2% are self-employed households while merely 11.2% are engaged in regular occupations.

<Table 9> Occupational classification of poor household-heads, 1999

	Whole		Poor*	
	Frequency	Ratio (%)	Frequency	Ratio (%)
Salary workers	4,152	33.51	570	11.18
Self-employed	2,257	18.22	777	15.24
Farmers/fishermen	1,182	9.54	659	12.93
Daily workers	1,067	8.61	654	12.84
Temporary workers	653	5.27	355	6.96
Jobless	2,645	21.35	1,828	35.86
Non-paid family workers	38	0.31	21	0.40
Housewives	336	2.72	205	4.02
Middleclass students	3	0.03	3	0.07
High school students	2	0.01	2	0.04
College	21	0.17	7	0.13
Graduate school	19	0.15	9	0.17
Army service	3	0.03	2	0.04
Others	11	0.09	7	0.13
Total	12,389	100.00	5,097	100.00

Note: * poverty line is 250,000 Won of per-capita income

Poverty is connected simultaneously to many characteristics such as age, disease, separation of family, unemployment, low skill and education, sex, and so on. Poverty caused chiefly by unemployment results in health problems. Despite the fact that more people are contracted with illnesses, hospitals are visited less for treatment while pharmacies are used more. Some 21.9% of households with at least one member who became ill in the last three months, have abandoned medical treatment

Some poor households have several factors lessening their ability to earn their living. For instance, the most typical poor group is aged households with one or two members. They are considered low skilled, poorly educated, largely unemployed, sometimes chronically ill or disabled, and mostly are women. In particular, the poverty rate of aged households (7.1% of the total households) was 31.7% in 1996 while the poverty rate of female-headed households (2.1% of the total households) was 10.1% in the same year. Therefore, aged and mother-headed households contributed 45.1% and 4.3%, respectively, to the total poverty incidence (4.3% of the total households) in 1996.

The mild decrease occurred in distribution index and poverty incidence since early 1999 seem to reflect strong economic recovery and its effect on reducing the unemployment incidence and raising income. However, reducing poverty to a pre-crisis level only with a strong economic growth is not easy to achieve in near future. Many structural factors, such as industrial restructuring into an information and knowledge-based economy, increasing dependence on labor saving techniques, polarization of wage structure and more instability in employment, work to extend income inequalities. The U.S. Department of Commerce insisted that the unequal distribution of Internet information use widened the income gap between the rich and the poor in 1998. Therefore, the strong economic potentiality of Korea does not guarantee any positive expectation of further significant narrowing of rich and poor differences.

The social impact of economic crisis can make deep and long-lasting imprints on the social fabric of society. Various social problems take place in individuals' quality of life. Problems associated with health, family, and regional conflict accompanied with economic hardship is still waiting for an appropriate diagnosis and counter-measures. Long- and short-term effects of current social problems should be determined systematically and appropriate policies should be suggested to prevent or reduce the negative social impacts of the economic crisis.

The Korean government has taken a number of prompt counter-measures in order to overcome difficulties accrued in households which have lost jobs, and as a result, become impoverished, investing new and special government budgets in various programs.

However, the government policy still inclines to lay priority to economic recovery but the importance of coping with newly generated social problems has not been sufficiently emphasized. The results can be easily seen in the further deterioration of poverty and income distribution, increased instability in the household and social order, the deterioration of quality of life in the areas of employment, health, education, and residence. The social responses to these problems are conservative, bureaucratic, supplier-oriented and temporary and as a result these policies have not been effective for the past two years despite the unprecedented expansion of counteractive programs and budget. For instance, most of the targeted groups have been excluded from policy participation and the levels of benefit, if any, were inappropriate. We still have inadequate political concern on the social impact of the current economic crisis. The number of broken families and the homeless have rapidly increased.

II. Pension Insurance Policies

During the last forty years, Korea has developed fragmentary social security programs appropriate to the socio-economic conditions prevailing in the country. The beginning of social security programs can be traced back to the early 1960s, when the adoption of civil servant pension law was introduced in 1960 and the military pension law was enacted in 1963.

Professors and teachers in private educational institutions were also provided with public pension benefits beginning in 1975. Industrial accidents insurance program was introduced in 1964. The national medical insurance program, the principal insurance program in Korea, was inaugurated in 1977. However, it was not until 1988 that Korea implemented the national pension insurance scheme for workers in the private industrial and commercial sectors, the law of which was enacted in 1973 but was not implemented for a long time because of economic depression caused by the first oil shock. Korea introduced an unemployment insurance program in 1995, which has a very important role in social safety net in Korea after 1998. Thus, all four major social insurance programs are in operation now.

The coverage of social insurance programs has been expanded with certain limitations such as financial ability of private companies to share premium. Both medical and pension insurance schemes are mandated to cover all population at present but it took relatively a long

time to realize full coverage, for instance, about 12 years for medical and pension insurance. National pension scheme was applied only to the private firms with 10 or more workers in 1988. The coverage was extended to include firms with 5 or more employees in 1992. The rural and urban sectors were incorporated in 1995 and 1999 respectively. The present contribution rate is 9% of the payroll, burdened half-and-half by both employee and employer since 1999. Full pension is paid when 60 year old after 20 years contribution. Hence the first full pension benefits will begin to be paid in 2008 and average income replacement rate would be about 60% for 40 years contributors with present benefit rule, which composes two parts of equal benefit and income proportional benefit.

The large two social insurance programs have crucial financial problems. The medical insurance showed deficit of 720 billion won in 1999. And the deficit is expected to exceed 1 trillion in 2000 and it would be more aggravated because the prescription, the dispenses, and the treatment costs were allowed to rise a lot with the introduction of the separation policy of prescription and dispense since July 2000. It would accelerate exhaustion of medical insurance fund. The deficit expenditure is supplemented by the central government budget. In the same way, public pension programs confront the exhaustion of funds in the near future. One of hottest practical issue is civil servants pension scheme, the budget of which have entered in deficit since 1995 and present rule of contribution and benefit will entail 995 billion deficit in 2000 in addition to depletion of the fund. The Government passed a revised law the main content of which raises the contribution rate from 15% to 17% and reduces pension benefit by changing salary base for calculation of benefits from final one year's salary before retirement to final three years' salaries before retirement. This proposal was severely challenged by civil servants at the end of 2000 in Pusan, the second largest city in Korea.

The fund of military pension scheme was already dried and required government assistance of 565 billion won in 1999, which amounts to 56.3% of total payment. Private teachers pension scheme is expected to meet budget deficit in 2007.

Under the previous National pension scheme with 9% contribution rate and 70% replacement rate, the fund would begin to run deficits by 2048 and will be depleted by around 2037. Therefore, the National Pension Act amended in December 1998 reduces the replacement rate for an average worker to 60%. And the government planned to raise gradually contribution rate until it reaches 17.25% in 2033, which would preclude deficits until at least 2070 but was not legislated yet in the Congress.

The National Pension Scheme (NPS) also confronts inefficient management of surplus fund. The NPS has accumulated pension reserves to about 60 trillion won and 11.7% of GDP in 2000 and positive reserve will continue during next 30 years. And the expected plan of raising contribution rate would accumulate more its fund to the level of GDP before first deficit starts. However, the accumulated fund has been made use of by the government for public interest. The public sector borrows 57.9% of total fund at the end of November 2000 with

hich has been allocated to special fiscal account and management fund of public money. The loan for assisting welfare service occupies only 1.2% to build nurseries and welfare facilities for the aged and support livelihood for the unemployed poor. The portfolio investment in financial market holds 40.9%. The rates of return are very different among sectors, The rate of return was highest, 24.5%, in financial sector in 1999 because of booming stock price, while it was 8.5% and 8.0% in public and welfare sectors respectively. The low rate of return will damage more financial instability of National Pension Scheme.

The NPS is suffered by many more problems related to illegal avoidance of participation in pension insurance program, especially in urban resident. Non-participation rate is assumed to reach almost 50% of total mainly because of difficulty finding out real income level. The urban pension insurance scheme exempted the burden of contribution for 54.5% of total target because of their low reported level of income in 1999, the inception year of the urban pension program. Even 28.5% of target population do not report income at that time. The majority of them are thought to be workers who unemployed or engaged in small petty shop management, and so on.

Four kinds of public pension programs have different contribution rates and replacement rates where the national pension program has the lowest replacement rate. Other pension schemes including Civil servants pension program provide higher benefits for longer retirement periods because the base years to decide benefits are different between NPS and other public pension schemes and because NPS only requires 60 years old to get pension after retirement while other pensions in the just period of retirement.

Furthermore, the national pension scheme could not provide minimum living expenses for two and three person households while the richest person here would have more benefit than the contribution he would pay at the immature stage of pension scheme. The benefit rule is installed redistributive mechanism in favor of the lower income attendants. Under the current scheme, income replacement rate (pension benefit / individual lifetime average income) are estimated 0.900 for the person with 20 years contribution and 20% of average income of total participants and 0.193 for the person with 350% of the average income, and the rates increase to 1.000 and 0.386 when contribution period is 40 years (refer to Yoon). Nonetheless, the person whose income is just 20% of average income will receive one third of benefit of average recipients even after 30 and 40 years contribution, which amounts 18% of average workers income. This benefit is much lower than minimum living cost. Even the person who earns 50% of average workers' income will receive 45% of average payroll, which might be almost similar to the minimum living cost.

Therefore, the government has made several major reforms of the whole pension scheme in 2998. First, the age receiving pension benefit is delayed from 60 to 61 in 2013 and 65 in 2033 by increasing one year every 5 years. Second, income replacement rate is lowered from 70% to 60%. Third, the financial accounting system is introduced to stabilize finance. Fourth, member of the National Pension Fund Management commission increases from 15

to 20, raising number of representatives of the insured from 3 to 12. Furthermore, the government plans to increase contribution rate from 9% to about 18% and to seek ways to enhance ability of finding income sources, and so on.

And pension model is also in the process of discussion in two broad categories of internal parametric and structural reform. The latter includes the multi pillar scheme recommended by the World bank which divides basic pension, income-proportional and compulsory pension and voluntary private pension. However, the government prefer the parametric adjustment within the present system which could not eradicate upcoming fiscal instability. The prevailing discussion can be as follows.

The World Bank advocated a three-pillar pension system composed of basic pension as the first pillar, occupational and individual pensions operated by the private sector on a fully funded scheme as the second pillar, and voluntary private pensions as the third pillar. Hence, the first is only redistributive. ILO has suggested its own version, criticizing that the World Bank model would fail to provide effective pension for the poor group. The ILO proposal insists three pillars but much different contents. The first pillar requires guarantee a minimum income financed fully by the general budget and means test to be beneficiaries. The second pillar is a mandatory public pension aiming at basic protection with defined benefit based on contribution. The supplementary private pension belongs to third pillar operated as a defined contribution scheme under strict supervision by the Government.

The multi-pillar system has an advantage to provide various levels of pension appropriate to individual economic situation as well as basic protection, especially for developed countries. However, Korea is still at the immature stage of pension and the expected benefit level seems to be low to keep minimum livings for the poor. The separation of basic pension and income proportional pension has a very high possibility to bring a shortage of fund to protect basic livelihood for the most participants and the rich would attempt to escape obligation to participate in the system or have strong disincentive to report real income. The ILO proposal has an advantage to protect basic livings after retirement because it requires basic protection for the second pillar in addition to the first pillar. However, the scheme needs more contribution of the wealthy so that they would be more hostile to pay higher contribution to the pension in recent difficult economic environment.

Therefore, a more feasible reform would be to preserve the current pension scheme by restructuring benefit levels and contribution rate. First, benefit rule could be structured to strengthen basic livings within current consolidated system, by raising minimum pension to the level of minimum livings, and by lowering benefits for the wealthy who are able to depend on private pension insurance for higher levels of retirement life. Second, the need for private pension to secure better life and fiscal stability of NPS is crucial because Korea will struggle with matters of aged society. The proportion of the aged over 65 is 7.1% in 2000 and will reach to 10% in 2010 in Korea. And the rate of the aged to population in 14 – 64 years has risen rapidly from 5.6% in 1970 to 9.6% in 1999 and will rise to 14% in 2010 and 3

0% in 2030.

Third, we have to do also utmost effort to restore long term financial sustainability in other public pension systems than NPS. The excessive burden of government budget to support them will eventually meet opposition if benefit levels do not reduce to similar levels to benefit of the NPS. Either the benefits enjoyed in the public pension other than NPS should accompany higher contribution, or the benefits should be adjusted to the levels within their own financial capacity, even though a gradual and stepwise adjustment is necessary to avoid resistance of the civil and military servants due to a drastic change.

III. Social protection programs

1. Counter-acting labor market policies against the Economic Crisis

In May 1998, the Government launched new big projects to protect massive unemployment and poured huge amounts of budget into several major programs. The public works was the biggest project to stabilize the unemployed poor. The number of persons or workplaces the project employed at the end of 1998 was 439,000 with 925.5 billion won and increased to 1,515,000 in 1999 and 886,000 in 2000. It was very instrumental not only to reduce unemployment incidence and assist poor households but also to increase effective demand in market.

Public work still takes a chief role when the index of unemployment rate shows a risk of rising greatly as in early 2001. However, many criticisms have arisen on the effectiveness of public works in reducing unemployment. One nationwide survey conducted in 1998 (Bark, 1998, p. 306) revealed that only 38.9% of targeted unemployed persons was absorbed in Sep. 1998 and most of participants were the aged persons below sixties who had been once economically inactive but applied officially to job-seeking program to satisfy requirement of participation in public works.

The active labor market policies were also intensified to provide opportunities of improving abilities of the unemployed and poor households to find jobs and complement their depressed household income. The Government Budget of occupational retraining programs in 1998 was expanded about three times the budget in 1997 and it rose to seven to eight times in 1999 when the program of the employment insurance included. Number of the trained jobs is planned to be only 16,000 in 1998. It increased to 320,000 in 1999 but attained more achievement of 356,000 trained with budgets of 493.9 billion won in 1999. The outcome expected for 2000 is 216,000 trained persons with 358.6 billion won. The program delivered knowledge-based skills such as computer programming and internet in addition to traditional low skilled techniques like brick and painting works and simple labor works like just cleaning walls and sweeping street. This program had also severe loopholes to misappropriate public money since private suppliers of retraining service seized a large portion of training budget by reporting disguised or false number of trainees and institutional arrangements.

ts was very incomplete to promote sufficient and effective training in short term.

The employment service has been speedily enlarged by increasing employment service center from 0 in 1997 to 99 and 126 in 1998 and 2000 respectively. The experts including counselors and administrative personnel also have increased to 2633 persons in 2000. This program is also criticized to succeed to match only about 16% of unemployed to work-places. Another big project was to subsidize employers not to fire workers. The project looks more promising to bring incentives to preserve their workers in production. The budget of the program was allotted in large amount, for instance 122.4 billion won in 1998 and 491.5 billion won in 1999 to assist 10.2 million persons. This program also faced false reports. For instance, some companies committed frauds to get public subsidy by reporting as if some of their workers were in state to be laid off.

(Table 10) The budget expansion of main labor market policies (billion won)

	1997	1998	1999	2000
Occupational training	125.8	305.6(449.7)	384.9(570.3)	2289
Employment service	19.7	79.0(108.2)	584.6(491.5)	440.9
Public works	-	1,004.4	2,492.6	1,100.0

Source : The Summary of Government Budget, 1998, 1999, 2000, Ministry of Planning and Budget

Note : () in Occupational training represents budgets of the Employment Insurance Fund and

() in Employment service represent budget for construction of employment service center.

2. Responding to the Economic Crisis through Unemployment Insurance

The existing social insurance programs have been strengthened since 1998. The fund of Unemployment Insurance became the most important means to complement insufficient government budget needed to react to massively generated unemployment and poverty. In order to expand coverage of insurance and ability to pay benefit, the Government implemented the program to most workplaces merely within one year. As the result, the payment of the employment insurance in 1999 rose 9.9 times the level of 1997 and recipients also increased 5.4 times in the same period. The most rapid increase in payment occurred in employment service program, 15.2 times, and then the unemployment benefit and occupational retraining was respectively 11.9 and 6.4 times. The rate of increase in number of beneficiaries was the fastest in order of the unemployment benefit, the employment service, and retraining. The number of beneficiaries of unemployment benefit inclined 6.5 times from 368,203 persons in 1997 to 1,973,967 persons in 1999 which are acquired by summing monthly data. And the beneficiaries of the employment service and retraining program increased respectively 5.7 and 4.9 times the numbers of which were 184,233 and 977,952 in 1999. The insurance is composed of three main programs. Among them, unemployment benefit program used 60.6% of total payment in 1999 and occupational training and employment stability service occupied 27.5% and 11.9%.²

² Yoo Gil-sang (2000), p.77

Despite great contribution of the Employment Insurance to stabilize the unemployed households, its benefit level is still short to satisfy even basic needs of the poor unemployed. The average recipients of job-seeking benefit, major unemployment benefit, are paid only 2,278,000 won for average benefit period, 98.1 days in 1998 and 2,389,000 won for 103.3 days in 1999. The benefit period is relatively short while wage replacement rate was 45% in latter half of 1999, almost similar to the level of the USA.

Second the coverage is still so limited that its function of social safety-net is narrow, because it excludes daily workers and part-time (less than 18 hours a week) workers who employed under contracts less than one month. In addition, there are 34.5% of total target population in the end of 1999 who are not absorbed in the Employment Insurance, mainly because the employers of petty workplaces are inclined not to report correct state of employment to avoid to pay the insurance premium imposed on them, 1.0-1.5% of payroll of their employees.

Third, the infra-structure in labor market is not efficient enough to support job and personnel seeking activities. The experts are very short of in both number and quality of service. The number of experts should increase many times, if compared with European countries in spite of recent rapid increase of public employment service institution from 53 in 1997 to 158 in 1999. And the counselors employed recently had been just trained for only two weeks before starting their jobs and information-collecting ability could not follow changes in demand and supplies in labor market because of frequent structural adjustment in business and labor mobility.

The delivery service inclines also to be decided in convenience of suppliers especially in application, modification of state, extinction in activities with respect to the Employment Insurance. Since internet service is only partially utilized, consumers of employment service have to visit relevant offices, which exhaust much time for both visitors and administrators

3. Strengthening Social Assistance Programs

The most important change in social assistance programs is the legislation of the Minimum Living Standards Security Act enacted in August 1999 and implemented October 2000. Before this act, the Government introduced various temporary policy measures to respond many social problems taken place during the economic crisis. Among them, the temporary Livelihood Protection program was the largest in budget size. The temporary livelihood protection program was introduced in April 1998 with the budget of 216 billion, 15.7% of budget of the existing livelihood protection program and further increased to 497.3 billion in 1998, occupying 34.2% of the latter budget. The cash assistance program particularly expanded budget and recipients with a staggering pace as much as 3.0 and 3.6 times respectively from 1997 to 2000. The budget for medical protection rose by almost the same rate.

This could be appraised as a great leap in the history of social assistance policy with the enactment of Minimum Living Standards Security Act. This new policy transforms the former

Living Protection Act by changing the direction of welfare policies from a policy of simple giving of alms to a policy stressing both national responsibility based on the rights of welfare recipients and the responsibility of the beneficiaries to do work who have work abilities. For example, low-wage earners with the ability to work who receive welfare benefits must also participate in job-training programs or other programs that contribute to the public good, such as public works. Providing these benefits, as an incentive to participate in the labor market, aims at reinforcing the independence of the Korean people and restoring their desire to work.

The new act contains more comprehensive benefit structure including food, clothing, housing, education, and healthcare, in addition to cash aids for the poor households whose per capita income are below about \$7/day (980,000won for 4 persons household) in 2000. In other words, all households, whose incomes do not meet the minimum cost of living, will receive welfare benefits from the Government that equal the difference. Housing benefits were also established to elevate housing assistance for the underprivileged.

A number of other programs have been implemented to solve economic difficulties of the unemployed poor. Medical Insurance was temporarily arranged for the unemployed to keep their insured state for two years. The fund of Employment Insurance and National Pension Scheme were mobilized to loans to help stability of livings for the poor unemployed. Other special assistance programs were also implemented for the unemployed women, daily construction workers, and new comers in the labor market.

(Table 11) Trend in Budget, Expenditure and the Number of Recipients by type of social protection (unit: billion won, 1000 persons)

		Years							
		1990	1995	1997		1998		2000	
				Budget	Number	Budget	Number	budget	Number
Total		8,073	19,717	30,146		49,267			
Public assistance	Sum	861	1,524	2,077		2,512			
	Live. Prot.	821	1,490	2,069	488	2,449		2,407	
	(cash)	(167)	(286)	(457)	(266)	(516)	(271)	(1371)	(952)
	(medical)	(151)	(292)	(478)	(1640)	(546)	(1390)	(1036)	(1379)
	Disast. Prot.	40	33	7		62			
	Others	-	1	1		Public work			
Social Welfare Service	Sum	1,103	2,935	4,446		5,799			
	Facil. Prot.	52	138	216		216		261	
	Home Prot	104	424	797		840		852	
	Work fare	100	418	793		2,049			
	(active la.)	(113)	(267)	(552)		()			
	Health	846	1,956	2,626		2,694			
Social Insurance	Sum	3,687	8,596	12,071		16,674			
	Pension	1,235	3,769	4,717	8,608	7,419	7,804		11937('99)
	Medical Ins.	1,913	4,079	5,680	44,925	6,696	44,472	8,789	55,895
	Ind. Dis.	539	1,134	1,556		1,451		1,456	
	Unemp. In	-	2	118	4,280	1,110	5,268	981	6,747
	(Un. Bene.t)	(-)	(-)	(78.7)	(51)	(85.0)	(440)	(471)?	(260)
Industrial Benefit	Sum	2,422	6,662	11,551		24,279			
	Leg. Retir.	1,797	4,922	9,358		21,131			
	Retir. Allo	-	791	794		1,526			
	Birth Ben	-	-	85		94			
	Disease Be	625	948	1,315		1,529			

Source: Koh, K. H., 1999, pp.63-64

4. Reform of Budget Structure and Development of ‘Productive Welfare Policies’

Last several years, we made an epoch-making stride in building social safety net in reaction to confrontation of various challenges cast by the threat of globalization. Especially, the budget for social safety-net policies reached to a new horizon level at the end of century. Social security expenditure has increased 2.5 times from 1995, one of the years of highest per capita GNP, to 1998, the most serious recession year, as shown in Table 11. The budget for social safety net policies of the Government, which includes livelihood protection, Government assistance to Medical Insurance, social welfare service and unemployment policies, has also demonstrated remarkable increases from 2,571 billion won in 1997 to 8,301 in 1998 and 13,310 billion won in 1999, while reducing a little to 10,510 billion won in 2000.

Social Insurance was a major source of social security expenditure the proportion of which was 39.4% in 1997, compared to 27.5% for tax revenue and 33.1% for private sector. Public pension is the fastest growing part in social insurance expenditure. In particular, the size of National Pension Scheme has grown from 1,485 billion won in 1997 to 3,872 billion won in 1999 and 7.4 million recipients in 1997 to 10.7 million in 1999. However, the private sector also displayed a big jump with the highest rate of increase, 28.2% during 1990 to 1997. Taking the mass unemployment in the structural adjustment period into account, the rate will be higher in near future.

(Table 12) Public and Private Source of Social Security Expenditure (unit, %)

	Public sector			Social insurance	Private Sector				Total
	Government				Sum	Retirement benefit	Retirement allowance	Benefit for birth leave	
	sum	Central	local						
Proportion in '97	27.5	17.1	10.4	39.4	33.1	30.3	2.6	0.3	100.0
Growth rate'90-97	16.9	13.8	23.9	19.1	28.2	26.6	87.9	-	20.8

Source: Koh, K. H., 1999, p.65

Since poverty incidence was still very high after the recovery of economies and unemployment rate was also still far higher than that of the pre-crisis period, the Government has consolidated the existing projects into 'productive welfare' concept in 1999, one of three main political ideologies of the current DJ government including 'democracy and market economy'. The productive welfare incorporates broader conception than welfare used in European countries because the productive welfare encompasses the provision of enabling environment for the vulnerable households to attend in labor market as well as the protection of basic living.

Productive welfare begins with securing the minimum standard of living for all people. If the minimum conditions necessary for the realization of a higher quality of life are not met due to social impediments including poverty, disease, unemployment, and inadequate housing, then promoting productive welfare policies of self-support through voluntary human development efforts and labor is impossible. There are several policy goals that are required to be achieved in any attempt to provide a national standard of living. First, minimum standard of living should be secured to ensure that no one lives below the poverty line. Assistan

ce will be provided to enable people without ability to work to meet the minimum standard of living, while those with the ability to work will be assisted to become more independent through various forms of vocational training. Second, despite the expansion and strengthening of the social insurance system, a substantial part of population has yet to be covered by the social insurance system and the level of benefits are still insufficient. Thus, the social security system will be enhanced in order to provide greater stability in the face of unavoidable changes, such as those associated with the rapid socioeconomic reconfigurations. Third, self-support plans will be diversified to assist the underprivileged. Self-support will be encouraged through various assistance programs, such as education, development of skills, and the provision of information. Diversified assistance will not only increase the degree of self-sufficiency, but will also enable a more stable participation in the economy by the underprivileged, thereby contributing to greater social integration.

IV. Major Issues To Be More Emphasized

1. Insufficient coverage of policy targets

While a great advancement has been made in the area of social safety net during last several years since the economic crisis, there is a wide blind spot to be eliminated in social insurance and assistance programs. The poverty incidence is estimated to be almost 9% in 2000 and the unemployment incidence is released to be 4.6% in January 2001 which leaps much from 3.9% last October. Despite the efforts to extend the minimum living standard protection program, the coverage remains only 3% of the general population. It would not exceed 5% even if beneficiaries of other social assistance are taken into account. Hence, almost half of the poor are still excluded from any social protection. Social insurance system could not cover all persons designated by the compulsory system because of intentional avoidance of contribution levied to both employers of petty workplaces and the lower income class insured in the regional insurance programs. Even Medical Insurance Scheme still leaves 2-3% of population excluded, who do not pay their premium. And unemployment benefit are only provided to 7.9% of the whole unemployed in the first half of 2000.

And, social assistance programs are not systematically linked to social insurance system and other workfare programs. Some beneficiaries are paid by several programs that may cause undue overlapped protection. Incorrect targeting is also impeding attaining goals of the programs. The cash benefits by National livelihood Protection were given to the non-poor, about 18% of all recipients as surveyed in 1998(Bark, 1999, p.306). And the rate of participants whose income were above minimum living cost amounted to 46% for public works, 35% for loan assistance, and 60.6% for unemployment benefit in the same period(Bark, 1999, p.268). Therefore, The coverage has still not a little blind portion of population to be protected more.

2. Insufficient Benefit Level and Necessities of Enlarging The role of In-kind Benefit

Benefit levels provided actually by most programs are far below welfare needs, for instance, minimum living cost. The cash aid, the assistance program emphasized by the Government, does not fully supplement the gap between minimum living cost and actual income as declared by The Minimum Living Standards Security Act when the old Livelihood Protection Act was revised. The new program only secured 476,000won for four person households whose income were below 4,000 won. It is only 51.1% of the Minimum Living Cost. The aid divided by four person is just 14.0% of per capita Gross National Income, which is far below the rate of western developed countries, for example, around 20% for the USA and United Kingdom in the early 1990s.

Public works as a main public assistance program constrains participation period to three to six months with lower wage levels than market wage. Unemployment benefit replaces 45% of previous wages with short period (average benefit and period were respectively 2,389,000 won and 103.3 days in 1999). The benefit levels of other assistance programs are, needless to say, lower. Therefore, Korean social security system is waiting another renovation to protect adequately basic livings for correctly targeted persons who need assistance.

Furthermore, benefit system is focused on the extension of cash benefit. On the other hand, the provision of in-kind service is particularly insufficient for the vulnerable groups. Many of the aged and chronically ill have no capabilities to pay high cost of treatments and hospitalization where self-burden amounts to 50-60% of total medical cost in current Medical Insurance system. The unemployed heavily depends on friends and relatives, newspaper, and other private sources to find jobs, while merely 10.1% of them visited public employment service office (Bark, 2000(1)). Personal care is scarcely provided to the disadvantaged households such as the disabled and aged. Nursery facilities are still highly insufficient to help mother-headed families despite the large loans with low interest by National Pension fund last 6 years. Rent subsidy is only partially implemented to a very small number of poor households.

Therefore, focus of welfare policy should be more concentrated to the extension of in-kind service than cash assistance in future.

3. Improvement of Labor-oriented Policies

While the Government is emphasizing productive welfare, there remain several important issues to be addressed. First, welfare policy has no systematic relationship with labor market policy. The Ministry of Health and Social Welfare has promoted self support program to the poor who have work ability and which would give cash aid conditional on participation in occupational training or work imposed, but without any close cooperation with Ministry of Labor, which are more specialized in work programs. A survey shows 40.1% of beneficiaries of the Livelihood Protection Program to want work as well as cash aid and 17.4% of them desire only cash aid (Bark, 2000(1)). Other public services, including personal and m

medical care, are also demanded simultaneously for some targeted households. Therefore, it is necessary to provide integrated welfare service under a systematic relationship of several different institutions both in central and local organizations.

Second, The major reasons of aggravated income distribution turns out to be joblessness and instability of employment in an analysis (Bark, 2000(3)). And, the economic crisis strike a heavier blow on younger generation, especially the households whose ages of the head are thirties and twenties, compared to forties and fifties, and even sixties. Both cohorts of ages are assumed to be laid-off more because they might engage in the industries of construction and other physical workplaces which are more damaged by the economic crisis. And, they are likely to accumulate less assets which can be appropriated in economic hardship, and they are more likely losers in recent submerged stock market.

Therefore, income and asset policies are necessary to enhance economic state of households plunged from middle class on the one hand. On the other hand, occupational retraining and transformation into leading industries including information technology are more stressed especially for the younger generations.

Third, implicit tax rate on supplementary benefit of the National Livelihood Basic Protection is so high, 1, as it would have a very strong work disincentive effect for normal and able poor workers. Social assistance policies have grown much beyond aiding simply cash to the aged and disabled and substantial part of cash assistance are now imputed to the able-bodied. Therefore, work disincentives provoked by cash benefit should be controlled by efficient design of the program to stimulate self-supported activities.

4. Restructuring Delivery System

We have seen a lot of inefficiencies in delivery of welfare service, especially during last several years. Despite the unprecedented investment in welfare improvement, welfare services are not being effectively allotted to right persons with adequate contents and levels. A large portion of budget prepared for the massive unemployed have gone to the non-poor and the employed in the programs of public works, assistance loans, cash aids, and subsidies for retraining and keeping employment.

To solve these problems would, first of all, require more number of service deliverers, which are quite lower than developed countries and more specialties to identify correct targeting and to evaluate adequate levels and contents of benefit. Second, private resources should involve in delivering service, decision process of selection of beneficiaries and benefit levels, and evaluating outcome of programs. Private partners might have more affection to the disadvantaged group and more information than the bureaucratic civil servants. The Government has allowed more participation of NGO to react to the crisis than the previous Government in procedures of promoting unemployment policies. But the scope of private bodies has been very narrow and its participation has been severely constrained by incredibility of the local government to civil bodies the major executives of which compose of previous le

ft-wingers. The participation should be strengthened to increase effectiveness of welfare programs, especially in evaluation and decision process.

Donation is not popular in Korea, but we have a large source of private fund in religious bodies. We need more efforts to raise welfare fund from private sector. And, integrated service is urgent to increase effectiveness of welfare provided and to curtail wasteful expenditure of welfare fund.

5. Need To Expand Welfare Budget and Seeking for Optimal Welfare Cost

Social expenditure has increased remarkably for the last several years, but the proportion of it with respect to GDP is still very low. The rate, 6.7% in Korea in 1999, which includes retirement benefit and allowances, is less than one third of United Kingdom and less than half of United States in 1990, and less than one fourth of Germany in 1990. Since the cause of insufficient welfare in Korea is mainly attributed to budget constraint rather than inefficient governance, welfare budget of the Government has to be expanded more.

However, the recent pace of expansion of social insurance expenditure looks formidable and the rate of social insurance to GDP would reach 10-15% within next 20-30 years. Furthermore, financial shortage particularly in pension and medical insurance would raise payroll tax rate for preserving current social insurance benefit to almost 30% of average salaries and will entail in large disincentive effect to our economy. In the wake of these kind of fear, hot discussions have been followed for long time and are still on going in relevant research institutions and Government. Privatization is one of main topics. Another attempt is to find ways to increase containment of medical costs and pension benefit levels to the level that enables adequate contribution to social insurance fund to coexist with adequate rate of economic growth, i.e., a sustainable growth, for example, 15-20% of GDP.

Appendix

Table -1. Changes in the Real Values of the Minimum Cost of Living of 1994 by Year and the Minimum Cost of Living and 50% of Average Income in 1999 (unit, 1000won)

Classification	2 persons	3 persons	4 persons	5 persons	6 persons	7 persons
The Minimum Cost of	402	547	669	768	846	903
The Real Value of	462	629	769	883	973	1038
The Real Value of	487	662	810	930	1025	1094
The Real Value of	516	702	859	986	1086	1159
The Minimum Cost of Living Estimated in	521	717	901	1025	1156	1156
50% of Average	659	894	1091	1253	1380	1474

Note: 50% of average income in 1999 is cited from Lee, Hyun Joo, Poverty and Next Poor Class, Health and Welfare Forum Policy, KIHASA, 2000

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