

Inequality in South Korea, and how to fight against it.

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Introduction

- The question of inequality and distribution is at the center of political conflicts/debates.
 - The traditional left-right distinction is, *largely*, about the matters of distribution.
- The left-right conflicts about distribution are partly due to different *principles of justice*, but also to different *analyses of the economic and social mechanisms* engendering inequality.
- The latter appears to become more important than the former.
- There is a certain consensus regarding the principles of justice.
 - If inequality is due to factors that individuals are not responsible for, such as inequality owing to inheritance, capital gains, or discrimination based upon race/gender, then justice requires that the society seek to improve the lot of the worse-off.
- I focus more on the inequality generating economic and social mechanisms in S. Korea.

S. Korean miracle

- Modern history of Korea was a drama, both economically and politically.
- Before 1860, Korea (*Chosun* at that time) was a backward agrarian society.
 - It was annexed to Japan in 1910.
- It was liberated in 1945, divided into two Koreas in 1948, and had civil war during 1950-1953.
 - Only ashes remain on both sides after the ceasefire.
 - The two Koreas were the poorest countries in the world circa 1960.
- From the mid 1960s, South Korea grew, with relatively equitable distribution of income and wealth accompanied, at least until 1997.
 - GDP per capita has risen from \$156 in 1960 to \$29,743 in 2017, while that of the world average rose from \$450 to \$11,755.
 - As of 2017, it became the 12th largest economy in terms of total GDP.

What brought about the miracle?

- What contributed to the S. Korean economic success?
 - Relatively equal distribution of initial wealth (Land reform in 1948 and massive destruction of wealth and consequent collapse of the landed class during war contributed to this)
 - High quality of human resources (both skilled and unskilled workers, well-educated bureaucrats)
 - Hard-working and patient laborers, who indeed overworked with low wages (relative to their high productivity);
 - Trust and solidarity among citizens, which results in a good combination of competition and cooperation
 - A high rate of savings, pipelined into a high rate of investment and fast capital accumulation
- Were these factors absent, good coordination between markets and states, often mentioned as a source of the Korean success, would not have been possible. Oft-cited leadership of developmental dictators is rather marginal.
- Many of these virtues were rapidly eradicated since 1997.

The rise of market fundamentalism in South Korea

- Since the early 1990s, market fundamentalists in Korea in politics, bureaucracy, and academia made strong voice, calling for deregulation of industries, flexible labor markets, liberalization of financial sectors, and privatization of public firms and public assets.
- They hold that market forces and productivity growth are the sole determinants of the distribution of income, wealth, and well-being.
 - Efforts to redistribute income and wealth are largely futile, and if unavoidable, we should use instruments least interfering with virtuous mechanism of the market.
 - Lucas (2004): “Of the tendencies that are harmful to sound economics, the most seductive, and in my opinion the most poisonous, is to focus on questions of distribution.”
- After 1997, market-oriented policies were more strongly demanded in the name of ‘structural reform,’ from both outside and inside.
 - further strengthened during the conservative era (2008-2017).

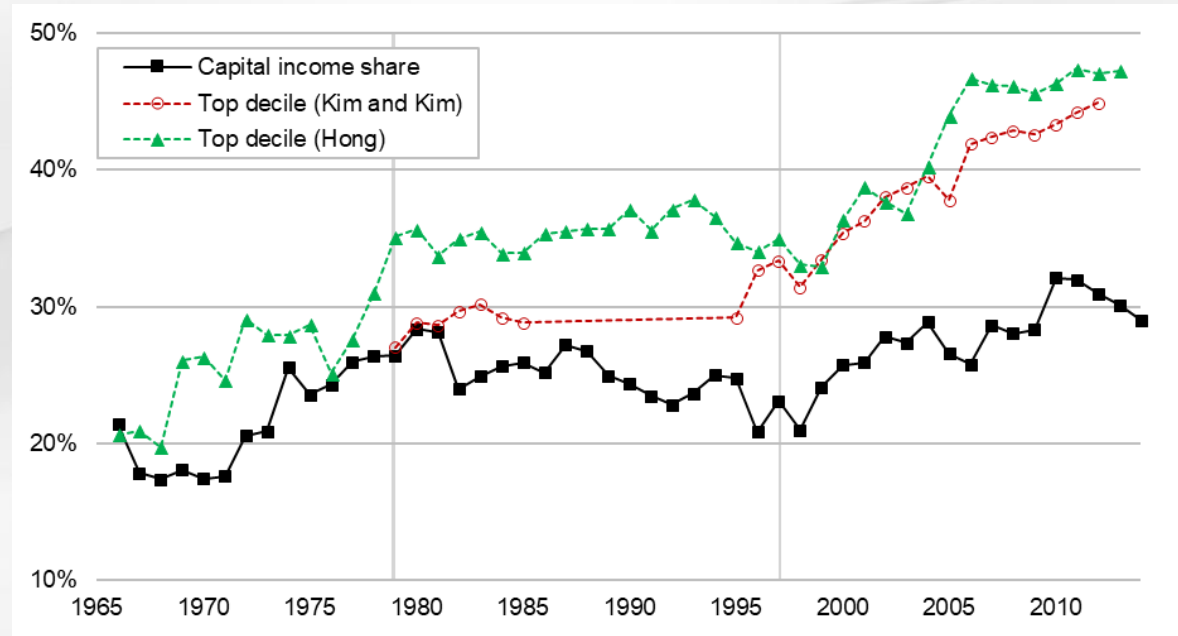
What happened over the last 20 years?

- The consequences of following the abracadabras of the market fundamentalism for the last 20 years are:
 - Growth rate and productivity declined significantly. Economy lost its vigor.
 - Bargaining power of workers and have-nots became significantly weaker; labor income share has been declining.
 - Workers are easily laid-off, and early retirement is forced.
 - Income gaps among workers have been widened, between regular and irregular workers, big- versus small-size firm employees, etc.
 - Bottom incomes declined, middle incomes stagnated, and top incomes soared.
 - Wealth was concentrated to the fewer, and plutocracy became stronger.
 - Wealth accumulation due to inheritance, price manipulation/speculation, and capital gains becomes more important than savings from earnings.
 - Due to uncertainty towards future, people become extremely frugal. The savings are not pipelined into investment, only reducing consumption (paradox of thrift)
 - Many good state apparatuses and policies were quickly dismantled in the name of 'business-friendly' reforms and of fixing the problems of dictatorship.

Growth performance (1966-2014)

	Real growth rate of national income	Population growth rate	Real growth rate of per capita national income	Net private savings rate (personal + corporate) (% of national income)
South Korea				
1966-2014	7.16%	1.13%	5.96%	13.9%
1966-1979	10.46%	1.89%	8.41%	12.2%
1980-1997	7.95%	1.13%	6.74%	20.4%
1998-2014	3.90%	0.55%	3.33%	11.4%
Japan 1970-2010	2.5%	0.5%	2.0%	14.6%
USA 1970-2010	2.8%	1.0%	1.8%	7.7%
UK 1970-2010	2.2%	0.3%	1.9%	7.3%
France 1970-2010	2.2%	0.6%	1.6%	11.1%
Germany 1970-2010	2.0%	0.2%	1.8%	12.2%
Italy 1970-2010	1.9%	0.3%	1.6%	15.0%

Macro-level income distribution (1966-2014)

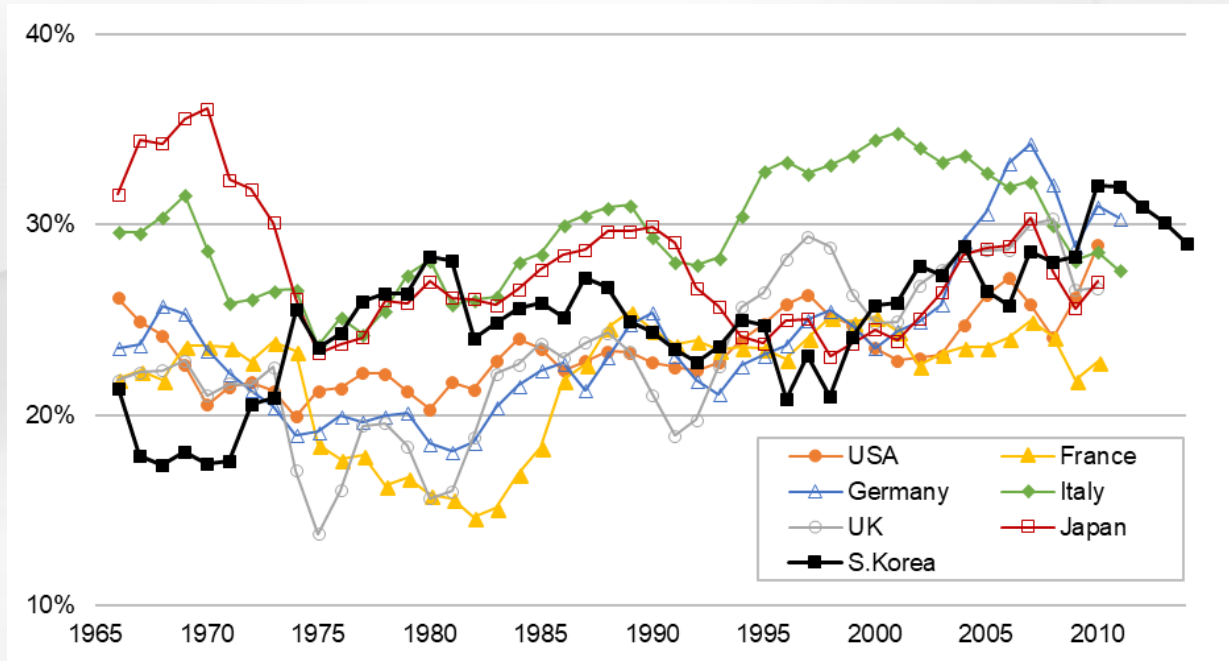


Source: Woojin Lee and Younghoon Yoon (2017)

Rising capital income share = declining labor income share after 1997

Top decile income share also has been increasing.

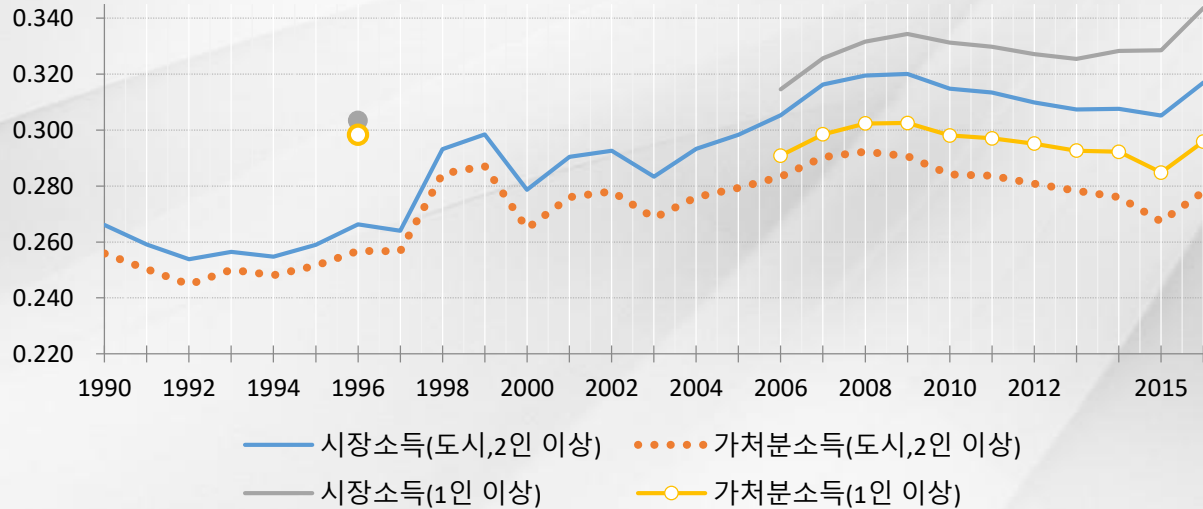
Capital income share: int'l comparison



Source: Woojin Lee and Younghoon Yoon (2017)

Micro-level income distribution (1990-2016)

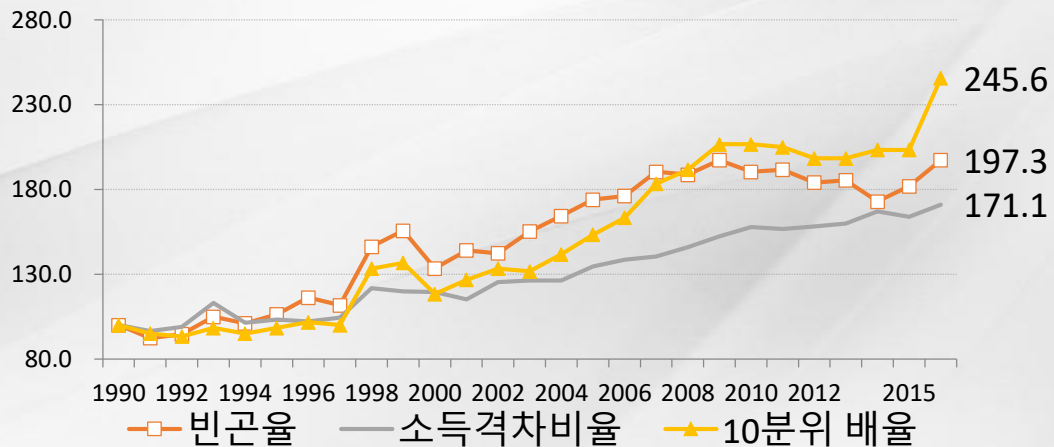
Changes in Gini of family income (1990-2016)



Source: Shinwook Kang and Minki Hong (2018)

Micro-level income distribution (1990-2016)

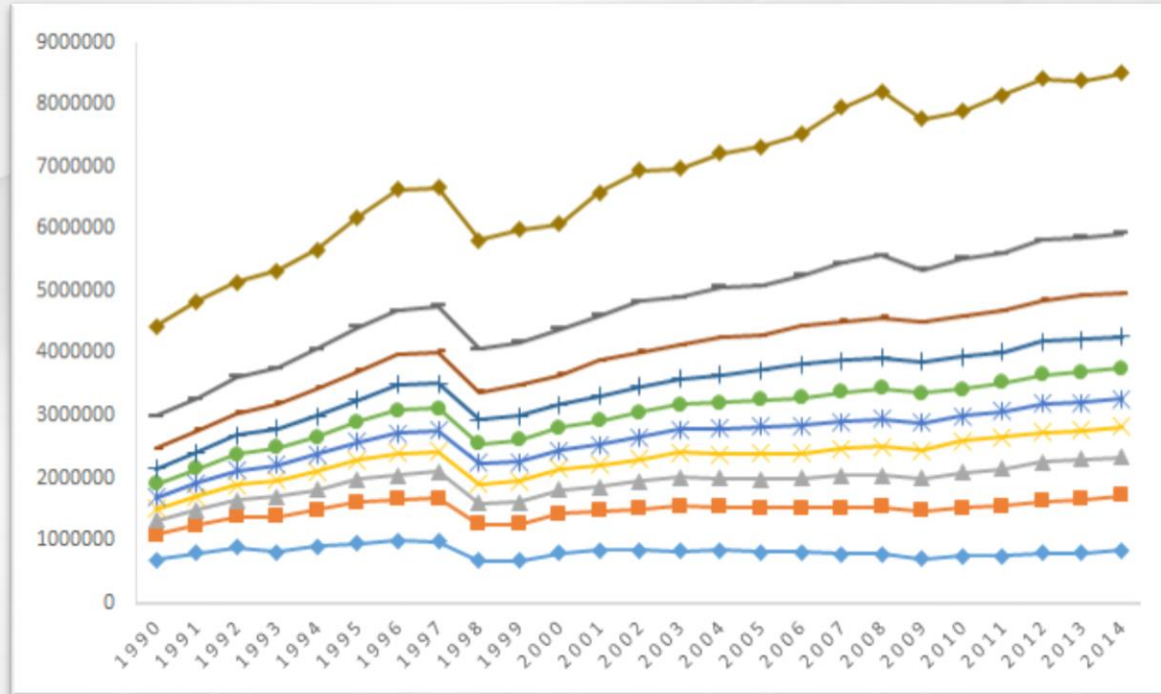
Other measures (1990=100)



Source: Shinwook Kang and Minki Hong (2018)

Stagnation of low income

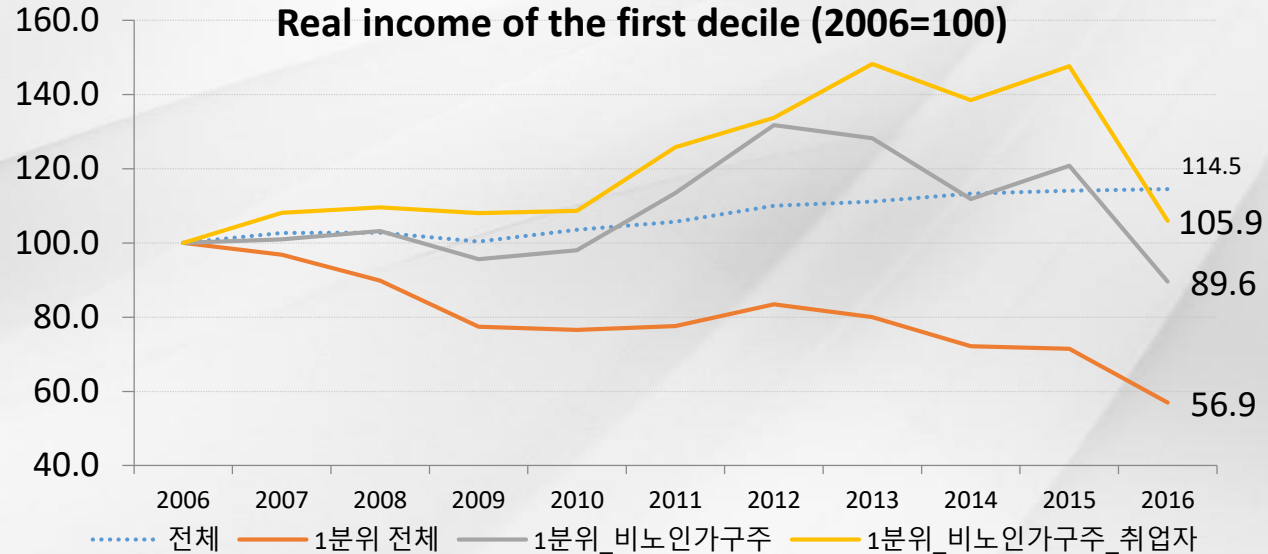
Growth of real monthly income by decile



Source: Author's calculation

Income distribution

Stagnation of low income families



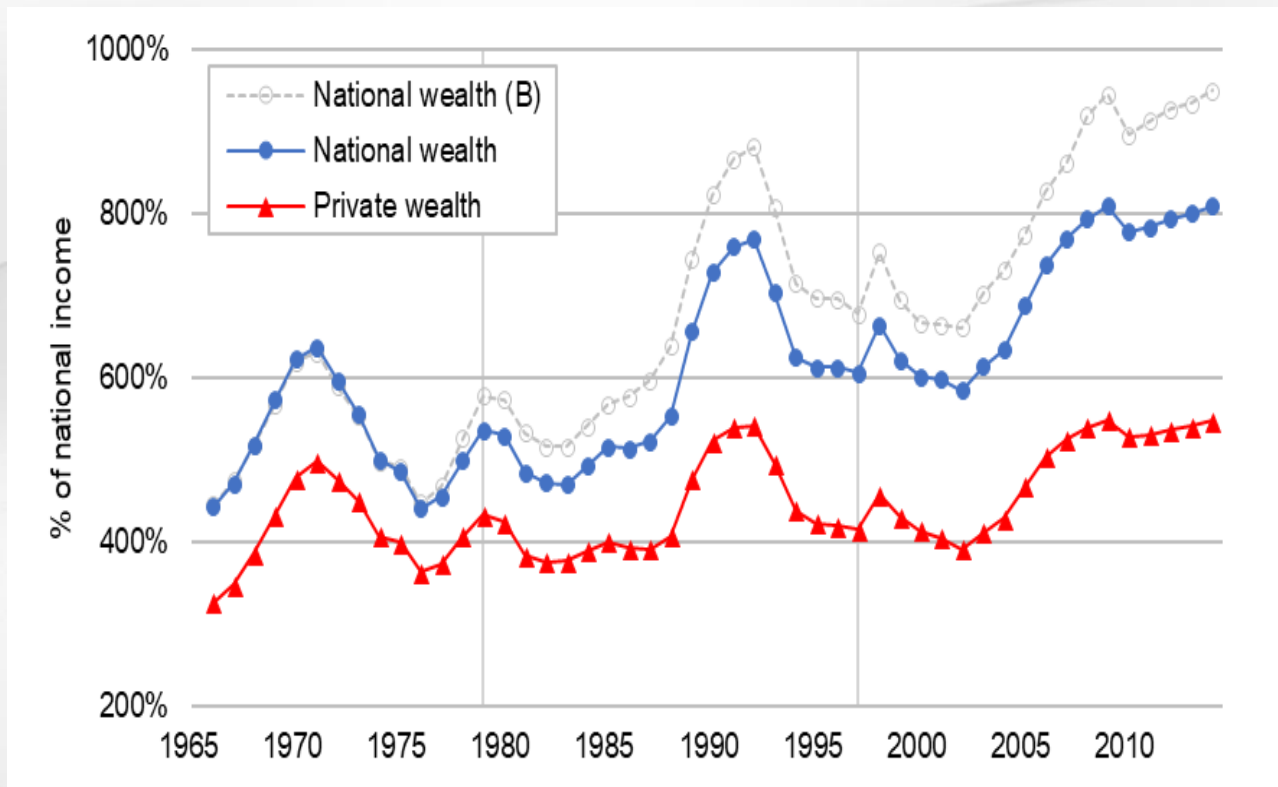
Source: Shinwook Kang and Minki Hong (2018)

- Real income of the first decile has been declining over a decade.

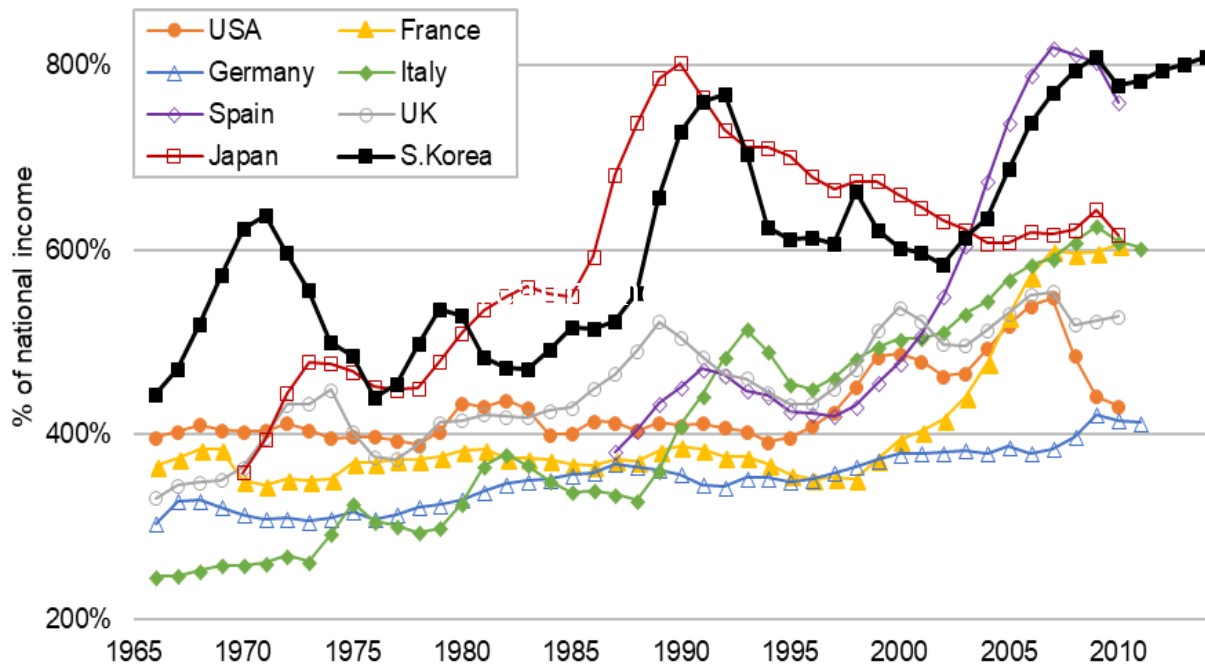
Concentration of wealth

- Real estate takes up about 80% of individual wealth in South Korea.
 - Over the last 20 years, prices of house and land soared, and their price differentials across regions have been widened.
 - House Price/Income Ratio in Seoul in 2018 is 18.9. (LA=8.42, SF=12.3, NY=12.34, Tokyo=13.8, Stockholm=15.56, Paris=17.7, London=22.2)
 - This contributed to wealth inequality significantly.
- Old age people are polarized economically. Some asset-rich elderly enjoyed windfalls from the soaring house and land prices, bequeathing some of them to their children, while many elderly, deprived of assets and traditional family-level protection, were driven to extreme poverty.
- Household debt/income has been increased due mainly to expensive housing cost and partly to heavy expenditure on education, reaching 186% in 2017.

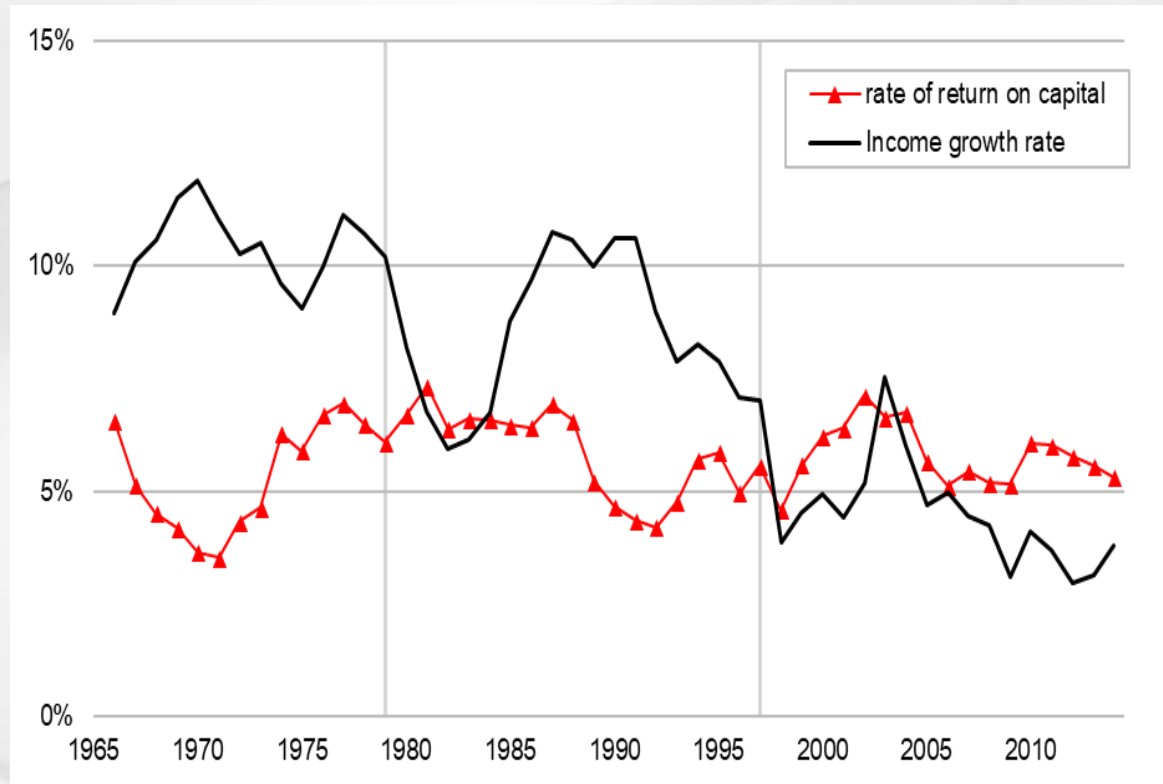
Evolution of wealth-income ratios (1965-2014)



Wealth-income ratios: int'l comparison



R.O.R on capital and growth rate



Wealth accumulation is largely due to capital gains.

	Wealth-income ratio (b)			Income growth rate (g)	Decomposition of wealth growth rate			Share of total wealth accumulation coming from		
	1966	1970	2010		Real growth rate of wealth (g_w)	Savings-induced wealth growth rate (g_{ws})	Capital gains-induced wealth growth rate (q)	Initial wealth	Savings	Capital gains
South Korea	326%	478%	529%	7.2%	7.4%	3.5% 48%	3.8% 52%	6%	45%	49%
Japan	-	299%	601%	2.5%	4.3%	3.4% 78%	0.9% 22%	18%	64%	18%
USA	348%	342%	410%	2.8%	3.3%	3.0% 90%	0.3% 10%	28%	65%	7%
UK	311%	306%	522%	2.2%	3.6%	1.9% 55%	1.6% 45%	25%	41%	34%
France	287%	310%	575%	2.2%	3.8%	3.4% 90%	0.4% 10%	23%	70%	8%
Germany	216%	225%	412%	2.0%	3.5%	4.3% 121%	-0.8% -21%	25%	91%	-16%
Italy	222%	239%	676%	1.9%	4.6%	4.2% 92%	0.4% 8%	17%	76%	7%

Unequal Opportunity

- Social mobility, both intergenerational and intragenerational, has declined.
 - Few Koreans believe that their society is providing equal opportunity to them.
 - Many believe that the type of spoons that an individual has at birth determines his/her economic prospects, not his/her efforts.
- Total fertility rate has been declining, reaching 1.05 in 2017, ranking bottom 4-5th in the world. (World=2.42, US=1.87, UK=1.88, France=2.07)
- Jinsoon Cho and Woojin Lee (2017) find that the circumstance variables account for a large portion of the inequality of education and income.
 - In education inequality, family background (measured by father's education) contributes the most (about 31% of inequality) and the gender(7%), birth year(4%), the number of siblings(3%), and grown-up region(2%).
 - In income inequality, gender contributes the most (39%) and family background (12%).

Enough is enough...

- Wrapping up:
 - Growth rate and productivity declined significantly.
 - Labor income share has been declining.
 - Income gaps among workers have been widened, between regular and irregular workers, big- versus small-size firm employees, etc.
 - Bottom incomes declined, middle incomes stagnated, and top incomes increased.
 - Wealth accumulation due to inheritance, price manipulation/speculation, and capital gains becomes more important than savings from earnings.
 - Savings are not pipelined into investment, only reducing consumption.
- The market fundamentalists still argue that market forces and productivity growth are the only way to foster growth and improve distribution.
 - “The definition of insanity is doing the same thing over and over again and expecting different results.” (Albert Einstein?)
 - **If you want different results than what you’re getting, you have to try different approaches.**

What is to be done?

- I am not arguing that “inequality is always bad, or unjustifiable.” Nor do I argue that we need to reduce every kind of inequality.
 - There may be a certain level of ‘fair’ inequality, such as inequality due to differential efforts. There also may be inequality created by innovative minds making great fortune.
 - I am concerning more about the inequality due to factors that individuals are not responsible for, and inequality due to unfair institutional and legal factors.
 - Fighting against only this kind of inequality requires a huge amount of effort and a dramatic change in the way of thinking.
- Since 2017, the new government is implementing policies that are very different from those of the market fundamentalists.
 - Demand-led growth strategies, including raising the minimum wage, more expansionary fiscal policies, encouraging innovation by small- and medium- size enterprises.
 - An increase in the public-sector employment
 - Fixing unfair competition and corporate governance of chaebols

What is to be done?

- Justice, not efficiency, in the labor markets must be restored.
 - Regarding a recent increase in the minimum wage (7530 KRW=\$6.85, 16.4% increase), conservatives bombarded its advocates with the argument that labor demand (employment) is decreased because of that.
 - It is too early to properly assess the effect of the increase in the minimum wage on employment.
- Wealth inequality must be reduced. People are worrying about the emergence of the new landed class, replacing the old landed class collapsed during the Korean war.
 - Taxes on properties, which take a large portion of individual wealth, and taxes on inheritance and gift must be increased.
 - Effective tax rates of the comprehensive real-estate tax (central government taxes imposed on the top 1.5% property holders) must be increased.
- Incomes from capital (rental income, dividend income) and those from capital gains must be more heavily taxed.

What is to be done?

- Some might argue that poverty reduction is more important than inequality reduction.
 - As Atkinson (2015) argues, we need to recognize that there are important interconnections between top and bottom; what happens at the top affects those at the bottom, and vice versa.
 - “What thoughtful rich people call the problem of poverty, thoughtful poor people call, with equal justice, a problem of riches.” (Richard Tawney, English historian, quoted from Atkinson (2015))
- “Inequality/equality is a choice,” not a destiny (J. Stiglitz, 2013)
 - We can either make the choice of creating shared prosperity or let inequality go amok.
 - Sharing also restores solidarity among people:
 - Not only competition but also solidarity is important for creating national prosperity and well being of the people.
 - “We must all hang together, or we shall each hang separately.” (often credited to Benjamin Franklin, quoted from Roemer (2017).)