



LABOR MARKET RIGIDITIES AND SOCIAL INEQUALITY IN KOREA: THE ROLE OF LEGAL, ECONOMIC AND SOCIAL GOVERNANCE

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Abstract

This study explores the organization of the Korean labor market, systemic faults in it leading to undesirable outcomes and their determinants, and consequences for workers and employers. Long-term implications for the arrangement and cohesion of society at large are discussed. The study has three specific objectives: 1) to describe the present labor relations, structure and governance of the Korean labor market through the prism of imperfect/regulated competition theory, with a focus on rigidities and systemic faults in the present organization; 2) to identify structural determinants of the faults, and their intermediate- and long-term consequences; and 3) to inform regulatory and legal reforms in order to achieve superior modes of governance and market organization.

The study focuses on understanding of the role of social, structural and regulatory constraints on effective matching of workers and jobs – their sources, manifestations, and consequences. Implications of market rigidities are evaluated vis-à-vis workers' skill-acquisition decisions and outcomes, their social and intergenerational mobility, and firms' long-term prospects. Existing policies and policy proposals are reviewed in regard to their impacts. The ultimate aim is to identify opportunities for economic regulation, legal governance and market norms to help overcome the existing faults in labor relations and market organization, and to transition to a more flexible, transparent, equitable, and sustainable form of market organization.

Key Words: *Labor market organization, dual markets, Korea*

Introduction

Korea faces the challenges of low and stagnating factor productivity, rising social inequality, and unsustainable demographic change while striving to maintain economic growth. Until the 1997 financial crisis, Korea experienced rapid growth with a modest level of economic inequality and healthy population growth. In the 1990s and 2000s, the Korean manufacturing sector expanded its production, exporting capability, and factor productivity. The services sector followed its lead in the 2000s when financial and technology firms joined the international market for high value-added services. Korean firms' success is to a large degree due to rapid upskilling and high motivation of the Korean workforce.¹ Correspondingly, workers' earnings and working conditions have improved dramatically in the past two decades.² These positive trends have not, however, been equally distributed across economic sectors and groups of workers. Notable pockets of systematically underutilized workers have arisen, through a mismatch between their skills and jobs. This affects labor productivity as well as – through workers' skill-acquisition and family-planning decisions – long-term demographic trends.

The gap between the rich and the poor in Korea has risen, and the relative poverty rate doubled during the 2000s and has stagnated since.³ Deprivation among marginalized workers – such as the elderly, youth and women – is stubbornly high, and social mobility is low. Moreover, over the past decade, the Korean population has rapidly aged as the baby-boom generation reach retirement age and the fertility rate drops to all-time lows following years of government family-control policies and various

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constraints that child-bearing women faced in the labor market. An aging population stands to negatively impact economic growth, labor-market productivity and social inequality in the decades to come, as the economy fails to adapt and integrate the elderly, childbearing women, and other nontraditional workers effectively.⁴

This lack of effective labor integration is partly due to patchy laws and structural barriers in the labor market that prevent workers from effectively demonstrating their skills or negotiating their working conditions, and limit firms' human resource management (HRM) to options made available to them by sector-specific regulations and norms. The labor market is not sufficiently flexible to assign all workers to best-fitting jobs, or to guide them to invest in the needed sets of skills. Women who get married or return from maternity leave are relegated to non-regular jobs, rather than being put on an alternative schedule or being retrained. Elderly workers whose utility to employers may potentially diminish or increase non-pay costs face similar circumstances.⁵

In general, workers are trapped in particular industrial sectors and career paths, with predetermined working conditions, not because of their existing skills and potential, but because of HRM constraints and path dependency. Workers have been effectively divided between a *primary* and a *secondary* labor market, and offered regular or non-regular working status.⁶ The primary market consists of too-large-to-fail shareholder-owned employers and firms with a government stake in them, known as the *chaebol*, which remain at the forefront with access to the best business opportunities by being innovative and dynamic, but also operate under the spotlight of regulation. The secondary market is populated by small and medium-sized enterprises (SMEs) that rely much less on innovation and compete more on cost than on value of their product, and are regulated much more loosely. Jobs in the primary sector are secure, carry generous benefits and opportunities for professional growth, and are subject to strong protection of labor standards and equal opportunity laws. Secondary sector jobs, on the other hand, are insecure, largely without benefits, and are regulated much more loosely. They offer workers wages, but little longer-term income security or social protection. Workers from disadvantaged backgrounds, childbearing-age women, the disabled, and the elderly are largely excluded from participating in the primary labor

market, and have consequently lagged behind in their earnings, non-pay benefits and various opportunities for advancement. This in turn reduces their incentives for skill acquisition in the first place.

Such a state of segmentation, or dualism, endures in many sectors of the Korean economy. Markets for factors of production, intermediate goods and final goods – and particularly labor markets – are fragmented into segments that do not compete directly with one another, and that effectively trap resources from flowing across market segments and from finding their best uses. This study therefore starts by observing that it is the systemic faults in the organization of labor market and rigidities in labor relations that cause the market outcome to exhibit duality and persistent inequality. The study concentrates on understanding the role of social, structural, and regulatory constraints on effective matching of workers and jobs – their sources, manifestations, and consequences. It reviews workers' and firms' objectives in labor relations, and constraints and information asymmetries that prevent them from achieving mutually more desirable, socially beneficial, and sustainable outcomes. The study then catalogs manifestations of rigidities in labor relations, including chronic un- and under-employment among marginal workers, cases of skills–jobs mismatches, strategic adjustments to firms' and workers' practices, the distortionary role of third-party recruiters, skill certification agencies and trade unions, and other impediments. Implications of these conditions are evaluated vis-à-vis workers' skill-acquisition decisions and outcomes, their social and intergenerational mobility, and firms' long-term performance. Existing policies and recent policy proposals are reviewed in regard to their impacts. The ultimate aim is to identify opportunities for economic regulation, legal governance and norms prevailing in markets to help overcome the existing faults in labor relations and social organization, and to transition to a simpler, more flexible, equitable, and sustainable form of labor market organization.

Present Labor Market Organization and Its Faults

Labor markets are typically not paragons of perfectly competitive markets that would be predicted to produce welfare-maximizing outcomes. In Korea, the imperfections are accentuated by a unique interdependence between business conglomerates (*chaebol*), SMEs, and the government; by a system of inconsistent unevenly-enforced laws; and by inadequate social protections.



Several features of the present organization of Korean labor markets cause particular rigidity in labor relations, prevent effective coordination of the supply and demand of skills, and yield inequitable and inefficient outcomes for workers and employers. This section reviews these faults.

Chaebol vs. SMEs

First, as has been widely documented in existing studies, a state of dualism exists in the business climate faced by firms, namely between the *chaebol* and SMEs. The *chaebol* are capital-intensive, export-oriented, typically manufacturing firms that remain at the forefront by investing in innovation and dynamism. The *chaebol*, thanks to their formal qualifications and perceived reliability, have access to the best corporate and government tenders, credit lines, retail space, and other factors of production. By their nature they have a holdout (monopsony) power over their suppliers. They also operate under the spotlight of regulation and customer scrutiny, and for the most part comply with equal opportunity laws and government-mandated or recommended labor standards. Their position hinges on their ability to avoid government crackdowns and customer backlashes.

SMEs rely much less on dynamism and reputation, and compete more on cost and output than on value of their product. They are to a large extent labor-intensive service firms, whose typical customers are local residents and the *chaebol*. One problem is that service firms face heavy product-market regulation relative to manufacturing, which adversely affects their earning capacity and costs.⁷ At the same time, their HRM is regulated much more loosely, in part due to their numerousness, and in part because regulators and disgruntled workers know that it is not worth filing complaints. Bankruptcy and reorganization rates are high. Workers at SMEs are typically barred from associating, receive significantly lower non-pay benefits, and face insecure employment.

The *chaebol* and SMEs face systematically different distributions of skills in their applicant pools, and different incentives and constraints on the procurement and management of human capital. Workers clearly prefer being hired by the *chaebol*, and only consider SMEs once they fail with the former group of employers. In this respect, one may distinguish primary and secondary labor markets, in which employers and workers compete within their segments but not across the fault lines. Once workers join the secondary labor market, they face an uphill battle switching to the primary sector later in their career. Given their working conditions and prospects for advancement, many secondary market workers can be categorized as engaging in informal employment.⁸

As with workers, firm mobility across the fault line is virtually nonexistent, because of the established system of exclusive access to tenders, suppliers and infrastructure, and reputation with workers. Essentially all small firms remain small (if they survive at all), and all medium-sized firms remain medium-sized. Primary and secondary market firms end up with chronically different workforce composition and hierarchy.^{9,10}

Regular vs. Non-Regular Workers

Another fracture in the Korean labor market is the distinction between regular and non-regular workers. Approximately 60 percent of Korean workers are classified as non-regular. Moreover, temporary workers – fixed-term, on-call, and temporary agency workers – account for more than one-third of that, near the top among OECD countries (Figure 1). The persistently high number of non-regular workers and their unstable economic conditions represent a problem in the Korean society. They earn only about 60 percent of the average hourly wages of regular employees, and are often excluded from benefits such as medical insurance, severance pay, welfare subsidies, and training opportunities available to regular employees.¹¹

The dualistic state came into existence in the labor market in the late 1990s after the financial crisis. Companies started using non-regular workers for non-core positions in the organization with the aim to preserve labor flexibility and cost advantage in the face of rising global competition.¹² They took advantage of an exception in the strict employment-protection legislation that applied to permanent workers only. In years since the 1997 crisis, non-regular employment arrangements spread throughout the economy, particularly in the service sector and at SMEs where workers do not have to undertake intensive firm-specific training and are easier to replace.

The problem with the non-regular work scheme is that it places a discrete wedge between the cost of regular and non-regular workers, even though productivity is distributed continuously across workers. Under the scheme employers have the prospect of earning economic rents from the labor-cost differential across different categories of workers, all with similar productivities.¹³ They can hold out on hiring regular workers or on filling non-regular positions with less productive applicants. Combined with the requirement that non-regular workers be converted to regular status after two years of service, the scheme most gravely affects the working conditions and employment stability of marginal and unproven workers such as fresh graduates, women returning from maternity leave, and the elderly. Youth under- and un-employment have become entrenched. Relatedly, growth of temporary and part-time employment



diminishes firms' incentives – and workers' own capability – to invest in workers' human capital.^{14,15} Finally, growth of non-regular employment leads to an enduring dispersion in incomes and working conditions in the economy. This is exacerbated by the erosion of disadvantaged workers' skills and by the consequences for the opportunities of workers' families and children.

Unresolved Uncertainty Over Workers' Productivity

Another typical failure of labor markets – causing particular rifts in Korea under existing market norms and regulations, as this section will argue – is the inability of firms and workers to effectively resolve the uncertainty over workers' productivity. In recruitment and in the ensuing employer-worker relationships (in granting promotions or other career-advancing opportunities), employers cannot rid themselves of the risk of making wrong selections and HRM decisions. While firm performance depends crucially on their ability to select the best-qualified people and manage them through the workers' tenure with the firm, the employers' ability to assess, select, and nurture talent is limited by patchy anti-discrimination regulations and imprecision of the available signals for workers' skills. Employers are prohibited from using some types of personal information for workers in their HRM decisions, but enforcement is uneven across various types of information collected, and across employers in the primary versus secondary labor markets, regular versus non-regular workers, and employers versus recruiting agencies. Screening a candidate's personal characteristics is prohibited, but looking into their family background is tolerated. Legal loopholes and special concessions also breed duality in the labor markets, whereby some firms and workers have better opportunities than others. Regular or unionized workers are protected at the expense of non-regular workers or job applicants. Typically only primary-sector employers are inspected by regulators. If firms face significant restrictions on their practices, they outsource to HRM companies that are largely unregulated.

Employers' problems are compounded by workers' self-selection, whereby only workers with the best observable signals – but possibly mediocre productivity – apply for positions where those signals are screened, and moral hazard, whereby workers' behavior or usable skills change once they are hired. This represents a particularly large risk if workers' effort and skills are difficult to assess, and if workers are shielded from repercussions such as termination by their permanent-employment contracts. An inadequate conflict resolution system between employees and firms prevents the parties from fully agreeing to terms

of employment before hiring, or settling disputes efficiently. Corporate norms and regulations provide for limited arbitration, and impose limited civil damages for law violations and contract breaches. Coupled with the lack of systematic enforcement of anti-discrimination laws, this leaves employers with only non-transparent informal ways – reliance on a set of imprecise signals or costly bypasses – to ensure hiring productive workers. Employers rely on third-party certifications, internal or external references, or family background such as parents' work history as signals for uncertain skills and personality traits of workers. These practices are costly to employers and/or amount to worker profiling and discrimination. Although they are effectively sanctioned by the state of regulation, they are socially costly and unfair toward some workers and firms.

Inefficient and fragmented markets typically create opportunities for intermediaries such as recruiting agencies or trade unions. They are involved in matching workers to jobs, but by internalizing only some of the consequences of hiring choices (e.g., employer's short-term satisfaction) and externalizing others (e.g., worker's long-term performance, career growth, and dedication to employer) recruiting agencies make different recommendations than well-informed employers might. Similarly, unions have a stake in getting only particular types of workers hired, thus performing their own profiling and discrimination. If workers become whistleblowers or cause other trouble to employers or unions, they may be blacklisted from working in the industry.

Cultural acceptance of the status quo exists among employers, workers and regulators. Employers have no means to unilaterally change their practices if their competitors continue using them and workers act under rational expectations that the practices will prevail. Workers are also powerless, given that whistleblowing could lead them to be fired or black-listed in the industry.¹⁶ Regulators accept the lack of formality and transparency in the face of a needed overhaul that would be met with strong opposition from business and labor groups.

There is presently no private market or government solution for the uncertainty over workers' skills. Compensation policy and employment contracts are typically not subject to negotiation. Employers thus cannot negotiate with workers effectively. They cannot offer inferior benefits or working conditions to less productive or unproven workers beside what the regular/non-regular worker system allows for. Employers also cannot insure themselves against the hiring of undesirable workers, cannot defer payments until workers demonstrate their skills, and are unable to terminate at will regular workers if proved undesirable.



The government, which should help employers and workers to get matched, does not provide reliable information on workers or guarantees for them. In fact, the current regulatory regime contributes to the uncertainty. Enforcement of equal-opportunities laws is lax, and penalties for non-compliance are limited to non-criminal charges. There are no provisions for compensation of discriminated workers. Industry and human rights watchdogs lack the authority to prosecute.¹⁷ Government efforts to usher in more flexible labor relations have also failed to bring transparency and fluidity to the labor markets. By promoting the categories of non-regular and temporary workers, the government has caused a schism in the labor market. By prohibiting worker discrimination, but enforcing it selectively across sectors and worker types, the government has distorted employers' behavior in harmful ways.

The implications of uncertain worker productivity are that even equally skilled and qualified workers may end up with vastly different careers and lifetime earnings, as workers are not matched efficiently to jobs in which their productivity is highest. Employers may not hire the correct number and type of workers, consequently failing to minimize their operating costs.¹⁸ Workers' incentives regarding skill acquisition are distorted, as they cannot demonstrate their qualities effectively and instead invest in qualities that are easily observable by employers (e.g., physical appearance, certifications of aptitude with computer programs or languages), even if these have little bearing on workers' ultimate productivity at particular firms. The problems due to the lack of opportunities for workers to prove themselves accumulate throughout workers' lives, and even across generations. Fresh graduates with an inferior set of signals such as disadvantaged backgrounds are not in the pool for best starting jobs, which will limit their career paths throughout their lives. These workers thus lack motivation to invest in skills most highly valued by primary-sector employers – regardless of the workers' ability to learn.

Inadequate Social Safety Net and (Re)education Policy

Another source of inequality and polarization in the Korean labor market is the inadequate system of care and support for disadvantaged workers. Workers trapped in wrong jobs or sectors, as well as workers with interrupted careers, those with children to take care of, and the long-term unemployed presently lack opportunities to be matched to jobs making use of their best potential. Workers who stray off the appropriate career path (considering their true potential skills) are not given a second chance to join it.¹⁹

Since private markets are traditionally not the best sources of support for unproven workers, and nongovernmental organizations cannot fill that role consistently enough and adequately given their limited budgets and authority, it is the role of legislation and public welfare policy to provide for deprivation-trapped workers, and to facilitate a second chance to workers in order to make use of their potential skills and to match them to best-fitting jobs.

Employment-assistance and (re)education policy: Non-regular workers, workers at small businesses, the unemployed and the self-employed, among others, have limited access to skill-improvement opportunities. Mothers returning from maternity leaves fall behind their cohort of coworkers. This contributes to growing polarization in the society, as these workers fail to adapt to skill-biased changes in the labor market, and lag more and more behind other workers in their qualifications. Policies that offer retraining to these marginalized workers, or policies that condition collection of public assistance on participation in retraining, help to improve the outcomes of marginalized workers and combat this polarization.

Formal education: Formal education plays a problematic role in relation to inequality in the labor market. University education is expensive, and the availability of public funding for credit-constrained students from disadvantaged backgrounds and later-life students is limited. Moreover, admission to high-quality secondary, tertiary and post-tertiary schools requires extensive preparation in private after-school academies (*hakwon*).²⁰ This suggests that students from poor families are limited in their educational opportunities, and the cross-family inequality accumulates at each subsequent educational level.

Educational inequalities are compounded by wage inequalities in the sense that generationally transmitted inequalities in higher education are positively associated with inequalities in wages. Thus, highly educated high-income parents usually seek better education programs for their children. To the extent that this type of skill investment is closely related to future labor market success, early-life opportunities to move up the socio-economic hierarchy diverge between workers from advantaged versus disadvantaged families.²¹ Indeed, the Gini index of inequality among Korean urban families with two or more members – one group of interest in the discussion of educational opportunities – rose by nearly four percentage points during the 1997 crisis, and has risen even from that level since then.²²



While education is often seen as a social equalizer, in a competitive environment where the vast majority of students go to college, even small differences in academic performance – acquired at nontrivial expense – can translate into vastly different career outcomes. Rather than reflecting on the quality of skills obtained, worker's *alma mater* provides a signal of their motivation, of sunk investment vouching for workers' commitment to primary-sector jobs – and of parents' wealth. Income gaps between graduates from top-ranking versus other universities have increased since the 1997 crisis. Employers care about a worker's *alma mater* in what may be thought of as educational elitism.²³ Employers also often prefer workers from the same *alma mater* as themselves, to promote workforce cohesion in a workplace where all colleagues have the same background, or to discriminate based on idiosyncratic tastes.^{24,25}

Policy Recommendations

Given the various conditions preventing employers and workers from achieving their best potential and trapping them on predetermined paths, an active public policy is needed to break market barriers for firms and disenfranchised workers, encourage hiring and labor mobility across sectors and career paths, and promote transparent and formal market practices. Since the 1997 crisis the government has enacted a number of laws, market regulations, and social welfare programs to facilitate more equitable and efficient labor market outcomes.²⁶ Despite these efforts, little equalization across workers has occurred, because laws are poorly enforced using weak sanctions, have loopholes or have unintended consequences. Even today, the climate in which employers and workers interact is permeated with obstacles, as the previous sections outlined, and further policy reforms are warranted. This section reviews recent steps at correcting labor-market faults and outlines promising directions for further policy action. Table 1 provides a brief summary of the problems, existing policy responses, and recommendations for further policy reform.

Chaebol vs. SMEs

The government has introduced initiatives to increase productivity at SMEs, and to help un-trap SMEs from stagnation by providing financial support and preferential opportunities to them, but the preferential arrangements have for the most part encouraged SMEs to remain SMEs.²⁷ The government has also promoted cooperation between SMEs and large firms (including publicly-owned organizations) with subsidies and preferential treatment, but these have limited effects on long-term coexistence and relations among firms.²⁸

Less attention has been paid to the transition of small firms into medium-sized ones, and their expansion across sectors.²⁹ The government should work more on leveling the competitive field among different types of firms by removing preferential access to tenders and credit (that the *chaebol* traditionally enjoyed and that SMEs have now received access to), and regulatory exceptions that SMEs operate under. The government has taken steps to encourage competition and equalize opportunities across industries and firm types, by removing product-market regulation and cross-sector regulatory burdens. The Framework Act on Administrative Regulations (amended 2013) and a *cost-in, cost-out* system were implemented under which the overall burden of regulation should not increase, and for any new regulation at least one equally burdensome existing regulation should be struck down.³⁰ This deregulatory measure is expected to benefit all firms. It is unclear, however, whether SMEs or large firms stand to gain more, and how the relative position of SMEs and their long-term prospects for expansion will be affected.

The government has also provided some support for entrepreneurship and consolidation through encouragement of venture-capital investment and of mergers and acquisitions among small and medium-sized firms. Specifically in relation to high value-added services, the consulting and legal markets have opened up to foreign competition and capital, and medical and educational service markets are on the path to be opened up.³¹

Regular vs. Non-Regular Workers

In 2007 the government reformed the Fixed-Term Employment Act and the Act on the Protection of Temporary Workers to prevent discrimination against part-time, fixed-term and temporary workers.³² These acts aimed to address unjustified discrimination against fixed-term and part-time employees and reinforce the protection of their working conditions.³³ Under the revised laws, the length of non-regular employment was limited to two years, with some exceptions, to avoid excessive use of non-regular workers.³⁴ Labor inspectors were instructed to encourage employers to correct any discrimination they find, even in the absence of worker complaints. The regulation was not effective. While the share of non-regular workers among all workers fell, their absolute number rose. As some fixed-term workers were converted to regular status, companies created a third, essentially overlapping category of employment that did not provide the benefits or the wages of regular workers, while allowing firms to retain workers indefinitely. The rise of regular employment in recent years thus paints an overly rosy picture of the conditions faced by workers in the labor market.



The increased shift to regular status for some fixed-term employees also came at the cost of greater job instability for a larger share of fixed-term workers.³⁵ Moreover, the contracts of many temporary workers are canceled after two years due to the limits under the 2007 reform, rather than changed to regular status. Thus, the 2007 reforms did not resolve job instability for a large number of non-regular workers.³⁶

In 2011, the Comprehensive Non-Regular Workers Initiative was enacted to improve social safety net, social insurance coverage, vocational training, and other working conditions of non-regular workers, primarily at SMEs. In 2014, Comprehensive Measures for Non-Regular Workers were put forth to promote the conversion of non-regular workers at SMEs into regular status. Two-year term on temporary workers was extended for some workers to four years to offer more stability to these workers and employers. Trade unions were empowered to act on discrimination cases against non-regular workers. However, these measures are unlikely to solve non-regular workers' underlying problems. By extending the legally sanctioned temporary status, the measures merely postpone the timing of workers' termination or status change, meanwhile lowering the burden on employers of relying on non-regular workers, keeping non-regular workers with unsustainable working conditions and unresolved job insecurity, and hardening the dualism between regular and non-regular sectors. Empowering labor representatives or regulatory bodies will not yield improvement in working conditions in the presence of patchy audits, low enforcement and sanctions, and inhibition on worker input.

Instead of adjusting the time limits on temporary or non-regular employment, policy focus should be on reducing the gap in working conditions, job security, and training opportunities between regular and non-regular workers. This will facilitate labor mobility across sectors and jobs, and improve dedication and qualifications among non-regular workers, in turn benefiting employers themselves. Intra-firm differences between regular and non-regular workers should be narrowed by streamlining the switching of non-regular workers into regular positions.³⁷ This should involve some relaxation of employment protection for regular workers while strengthening the protection and enforcing the rights of non-regular workers.³⁸

Uncertainty Over Workers' Productivity

In recent years the government has made various strides toward limiting discrimination by employers and contracting agencies, improving skills of disadvantaged workers, offering subsidies

to employers for hiring them, and cleaning up its own act by recruiting workers with nontraditional backgrounds. However, more needs to be done.

The degree of job security of regular workers needs to be reduced to make hiring regular workers a less weighty decision, and to bring the standards closer to those for non-regular workers. The government should educate and encourage firms to introduce negotiable employment contracts under which compensation and working conditions could be up for agreement between employers and individual workers. This will allow employers to offer tentative terms to workers who have not proved themselves, and will allow workers to be open about their own needs, such as receiving time off to take care of dependents.

While discrimination in labor relations has been made illegal, and various channels have been established to identify cases of discrimination, more needs to be done to systematically and meaningfully punish wrongdoers, protect whistleblowers, and empower workers to respond to discriminatory practices in ways that will not disadvantage them and without incriminating themselves (e.g., lie to discriminatory questions during interviews without fearing subsequent termination). Enforcement of equal-opportunities laws should lie with industry and human rights watchdogs (such as the National Human Rights Commission), be systematic and cover all employers and all types of workers, and penalties for non-compliance should include criminal charges and compensatory damages to victims.

Social Safety Net and (Re)education Policy

The area in which the government is arguably bringing reforms most actively is welfare protection. This section reviews the main existing public programs for the promotion of employment, workers' human capital, and the application of that human capital to the most appropriate uses.

Employment-assistance services: In response to soaring unemployment following the 1997 crisis, the government created a nationwide job-information network and expanded a system of Employment Security Centers (ESCs). ESCs provide job seekers with many forms of information and services, from vocational training to information about vacancies.^{39,40} However, ESCs have shown poor organizational effectiveness and quality of administrative services. ESCs presently lack employment-assistance, in-depth counseling and job-placement services tailored to individual job seekers. The (re)training services they provide are too rudimentary to improve workers' skills, in part because ESCs are understaffed, under-supported by the central



government in terms of autonomy, manpower and budget, and insufficiently connected with employers and other relevant organizations.⁴¹ Due to their weak capacity, only a fraction of middle-aged workers, married women, and the disabled in need of urgent support actually use the centers.

The national Employment Insurance System (EIS) was launched in 1995 to reduce the social cost of unemployment, and to improve the country's employment structure. The EIS strives to provide employment information and guidance enabling a more efficient redistribution and utilization of national manpower.⁴² The EIS was designed with three key components: the Employment Stabilization Program (ESP), the Job Skill Development Program (JSDP), and the Unemployment Benefits Program (UBP).⁴³

The ESP assists job-seekers at finding jobs according to their aptitude and competency. Through the ESP, the government provides financial support to companies to ease the burden on them and to prevent unemployment in times of short-lived economic downturns.⁴⁴ The ESP offers economic incentives to employers who have averted mass layoffs; maintained the same level of employment by retraining and relocating workers or reducing work hours; or employed marginal displaced workers. It also seeks to promote job placement by administering vocational counseling and guidance, and providing accurate information on the labor market. To improve job matching, the ESP supports job placement services. However, the ESP has not produced sufficient improvements in job opportunities, employment stability and efficiency of firms' labor adjustments, due to low utilization of the services.^{45,46} More investment should be made to develop the service offering of the ESP in line with the needs of today's labor market, and to improve the convenience for beneficiaries.⁴⁷

The JSDP aims to strengthen firms' competitiveness by providing training opportunities throughout workers' careers. The program provides an institutional framework for the support of lifetime, post formal-education vocational training and job skill development.⁴⁸ It offers firms financial incentives to invest in employee training, thereby improving employment stability, marketability of workers, and firm competitiveness and factor productivity. The JSDP also offers vocational training for the unemployed and low-income workers, including initial training at public training centers and follow-up training at firms.⁴⁹ Limitations of this program have included insufficient capacity to provide training, staffing shortages, high turnover rates among clients, and unequal services offered to different groups of workers.

The UBP aims to improve efficiency of the national labor distribution by enhancing the quality of reemployment. It serves as the primary social safety net for the unemployed, granting allowances to those unemployable due to illness, injury, or mass layoffs.⁵⁰ Limitations of the UBP are that the legally prescribed duration of benefits and the duration of actual benefit payment are short (up to 210 days, and 110 days, respectively) and eligibility criteria are strict.⁵¹ As a result, many unemployed people are ineligible, and the long-term unemployed receive inadequate support.

Assistance to the working poor and the self-employed: Support for the working poor in the secondary labor market, particularly the self-employed in the service sector, is presently insufficient.⁵² The self-employed presently lack access to training opportunities because existing programs are not best suitable for them, or because they are ineligible until they become unemployed. Policy solutions for the low-income self-employed would include creation of new middle-income jobs in social services, assisting low-income self-employed workers to build collaborative support networks, providing them with access to re-education, retraining and other safety net features, and improving their access to capital and credit to allow them to grow into medium-size businesses. The JSDP aims to improve the qualifications of marginalized workers, but has not entirely succeeded at bridging the opportunity gap.⁵³

The Basic Livelihood Security Program (BLSP) was expanded in 2014, and the eligibility criteria for unemployment benefits have been relaxed. The government plans expanding Employment Security Centers as hubs of employment services in local communities providing counseling and job-placement services. To encourage job seekers to search actively and to participate in available skill-improvement opportunities, the government plans to lower unemployment benefits.

Childcare assistance: Working parents face particular hurdles managing their professional and family lives. This is mostly the case of mothers, for cultural reasons and since paternal leave is effectively nonexistent. Working mothers require access to childcare, and shorter work days or flexible working conditions to take care of their children. Mothers re-entering the labor market also face the hurdle of catching up with their cohort of coworkers – and proving their value to their employers given attrition of their skills and gap in experience.⁵⁴



To improve their access to childcare services, in order to lighten the burden on parents and the public, available resources should be consolidated and put into a more effective use through closer cooperation between national and local government levels, and greater initiative and control at the local community level.⁵⁵ Possibilities include granting powers to local authorities to raise taxes for social welfare programs supplementing the national funding; and empowering civil organizations to pool community resources. More active partnerships with employers and the private sector are also warranted, such as urging employers and business groups to purchase childcare on behalf of their employees. More flexible choices for childcare programs are currently being rolled out to support parents working on alternative schedules. The government is also revising conditions for maternal and paternal leave, increasing welfare spending, and expanding welfare net and retraining programs for those re-entering employment market.

Industry-labor-government cooperation: An initial Tripartite Agreement on structural reforms of the labor market was reached between labor representatives, business groups, and the administration in 2015 to promote labor flexibility and to combat market dualism. This should be achieved through: cooperation between small and large firms, and primary contractors and their subcontractors; improving working conditions and prevention of discrimination of non-regular workers; promotion of employment of marginal workers and youth; clarification of employment standards; expansion of the social safety net and unemployment-benefit coverage; support for work-family balance; support of vocational learning and re-training programs, and others.⁵⁶ However, the effort in its current state has several limitations. The lack of technical detail, to be agreed over time, and the voluntary nature of the majority of existing articles in the agreement put into question its effectiveness. The uneven roles of the three groups of signatories in complying with and enforcing the agreement puts into question the negotiating power of each party, and the agreement's power and sustainability. In fact, the country's second largest labor union did not participate in the drafting of the agreement. Since signing, cracks have appeared between the signatories, with the remaining labor union threatening to pull out. The negotiating process has stalled. Time will tell how effective this flagship agreement will be.

Conclusion

The problem of structural faults in the Korean labor market has various dimensions and involves a number of parties who have a role in it and who must be engaged to identify and reach solutions. Over the past decade the Korean government has taken the problem seriously and attempted to tackle it on multiple fronts, using fiscal incentives, legislative action, regulatory directives, and brokering with business and labor groups. More work clearly needs to be done, since there are as yet unaddressed areas, and some policy responses have proved to be toothless, slow or misguided. Nevertheless, the concerted efforts of various government institutes to tackling a common problem, and the ongoing tripartite negotiation over the equitable and efficient organization of the future labor market, are a good sign of future improvements to come. The hope is that the voluntary, open-ended, all-parties-inclusive deliberation process itself will help to clarify all positions and stakes, and through the created knowledge-exchange and goodwill will help to heal the deepest faults of labor market structure.

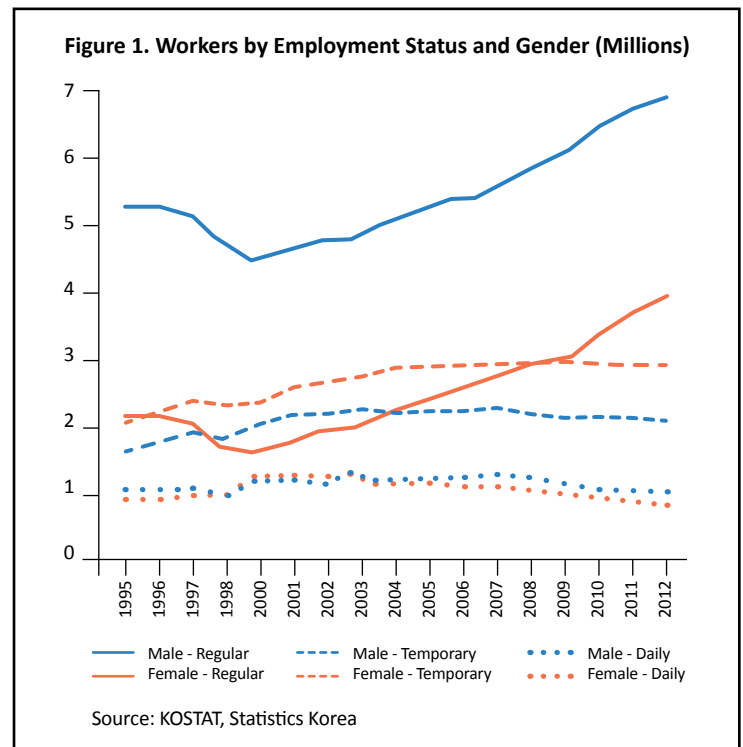




Table 1. Summary of structural problems, proposed solutions and further recommendations

Structural Problems	Existing/proposed policy	Recommended further action
Chaebol vs. SMEs	<ul style="list-style-type: none"> Promote competition in manufacturing Cut red tape using cost-in, cost-out framework Financial support for SMEs Preferential treatment for SMEs Incentives for SME innovation Support for chaebol-SME cooperation 	<ul style="list-style-type: none"> Promote competition in services Leveling of the competitive field across sectors End to regulatory exceptions for SMEs Neutral support system for innovation, and employment expansion Incentives for SME expansion
Regular vs. non-regular employment	<ul style="list-style-type: none"> Protect temporary and non-regular workers from discrimination Extend allowed duration of non-regular employment to 2 years, 4 years for some workers Provide re-training opportunities for disadvantaged workers 	<ul style="list-style-type: none"> Narrow the gap in working conditions between regular & non-regular workers Improve job security and job-training opportunities of non-regular workers Streamline intra-firm switching of non-regular to regular positions
Uncertainty over worker productivity	<ul style="list-style-type: none"> Pass laws prohibiting discriminatory HRM practices, extend their applicability to non-regular workers Educate employers regarding recommended practices Provide re-training opportunities for disadvantaged workers 	<ul style="list-style-type: none"> Enforce laws effectively through systematic audits, referrals to prosecutors, public shaming of wrong-doers Equalize standards and enforcement across sectors & types of labor Empower regulatory & human-rights agencies to prosecute Introduce criminal charges & high compensatory damages Empower workers to tackle discrimination without facing repercussions Prohibit industry-blacklisting of outspoken workers, and enforce it Educate employers and workers about their rights & about sanctions Encourage flexible negotiation of working conditions
(Re) education policy and social safety net	<ul style="list-style-type: none"> Provide employment assistance Provide support for employment stabilization, hiring expansion, work sharing Provide re-training opportunities for disadvantaged workers Expand childcare services Support reentry of career-interrupted women Increase incentives of the unemployed to find jobs (by lowering unemployment benefits) Expand eligibility coverage for unemployment benefits Extend allowed duration of benefit collection Encourage dialogue between government, business & labor groups 	<ul style="list-style-type: none"> Improve funding & quality of services Improve convenience for beneficiaries Improve access to & quality of services Improve provision of childcare without stretching public resources, by engaging local governments & NGOs Promote paternal leave effectively Guide the tripartite reform process by stressing technical benchmarks & timeline, formal commitments of all parties, sanctions

Endnotes

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- ⁵ There are significant differences in training opportunities across genders, age groups and education backgrounds. For example, women lack opportunities for promotion and raises due to employers’ lower expectations over their skills or dedication. This makes it difficult for women to advance in their careers, and yields higher turnover rates among women. In response, employers offer women even fewer training opportunities, leading to a vicious cycle and an ‘opportunity poverty’ trap as discussed in Kim, 2005. Similarly, workers with less education who are most in need of training receive fewer training opportunities than highly educated and skilled employees. This is because the training decisions are made by employers rather than workers themselves, and the decisions are derailed by employers’ imperfect information, expectations, and possibly even personal biases. See Keum et al. 2006.
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- ⁷ Park, J., et al., “The Effects of Korea’s Service Industry Reform and Its Direction,” KJET research report, 2014-702.
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- ¹¹ Koo, Hagen, “The Changing Faces of Inequality in South Korea in the Age of Globalization,” *Korean Studies* 31(1) (2007): pp 1-18. Project MUSE, May 9, 2013, <https://muse.jhu.edu/article/233528>.
- ¹² The economic crises of 1997 and of 2009 have simply aggravated the problem. See Shin Donggyun “Bipolarization of the Income Distribution after the Recent Financial Crisis: Trends, Causes, and Policy Implications,” *Study of Economics*, 2007 and Chang, 2009. During the 1997 crisis, the fall in the number of employed persons consisted mostly of regular workers. Compared to temporary and self-employed workers, the drop in the number of regular workers was not brief, but persisted for a long period, see Kwon, 2010. Even after 1999, when the economy began to recover, the decrease in the number of regular workers continued, while the number of temporary workers continued to rise. Employment of regular workers recovered only after 2000 when the economy stabilized. Source: Lee, Byung-Hee, Hye-Won Kim, Jin-Ho Jeong, and Seong Jae Cho, *Labor in Korea 1987-2006: Looking through the Statistical Lens* (Seoul: Korea Labor Institute, 2009).
- ¹³ Grubb, David, Jae-Kap Lee, and Peter Tergeist, “Addressing Labour Market Duality in Korea,” OECD Social Employment and Migration Working Paper #61, OECD Publishing (2007), <http://dx.doi.org/10.1787/058184274204>.
- ¹⁴ Nam, Jaeryang, Keunkwan Ryu, and Hyomi Choi, *Situation of Employment Instability and Employment Policy Tasks* (Seoul: Korea Labor Institute, 2005).
- ¹⁵ Of course, temporary employment and other flexible work arrangements have benefits too. They increase demand for labor by enhancing firms’ flexibility in labor management. They may also increase labor supply of workers who desire non-regular positions – because they permit them to combine work with other activities.
- ¹⁶ Yoo, Gyeongjoon, Daeil Kim, Changhui Kang, Yong-seong Kim, Jaehoon Kim, and Chunghoon Lee, *Studies on Non-regular workers*, KDI Research Monograph 2009-03, www.kdi.re.kr/kdi_eng/publication/publication_view.jsp?pub_no=11370.
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- ²¹ The relationship between the importance of education and the changing nature of social inequality is evident from the rise in average family expenditures on formal and after-school education, and the growing disparity in these expenditures across social groups, see Yoo et al. 2009. Families with higher incomes and particularly higher wealth have channeled higher resources to their children’s private education, and the disparity grows over time. The differences in educational opportunities across social classes are perhaps most clearly discernible geographically: Seoul’s Gangnam (south of the Han River) district where the wealthy reside is also home to top-ranking private tutoring institutes, whereas Gangbuk (north of the Han River) has been falling behind in terms of the provision of private as well as public educational opportunities, see Koo, 2007. Availability of educational opportunities and expenditures on education are also much higher in Seoul and the surrounding Kyonggi Province than in poorer regions such as the southern-most Jeolla Province. As Korean educational system becomes more internationalized, wealthy Korean families are increasingly looking for superior educational opportunities overseas while poor income families cannot afford them, see Yoo et al. 2009. Also see Lee, Y., M. Moon, M. Kim and S. Yang, “A Survey on the Current Status of Hakwons (private academies) for Young Children in Korea,” Research Project-05, Korea Institute of Child Care and Education, Seoul (2009).
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²² Data from KOSTAT, Statistics Korea.

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²⁴ Hlasny, Vladimir, “Economic Determinants of Applicant Screening Practices: An Empirical Analysis of the Human Capital Corporate Panel,” Proceedings of the 4th HCCP Conference, Seoul, September 2012; Ewha Womans University working paper. See also Hlasny, Vladimir, “High Stakes in Education: A Public Policy Failure,” *Korea Herald*, Feature & Analysis (April 2, 2012).

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²⁹ A few existing laws include the Act on special measures for the promotion of venture businesses (1997, amended 2010); Special act on the promotion of business conversion in small and medium enterprises (2006, amended 2012); Support for small and medium enterprise establishment act (2007, amended 2012).

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³¹ Foreign Legal Consultant Act (2009, amended 2011); Certified Public Accountant Act (amended 2008, 2011).

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