The Republic of Korea, or South Korea, has a prominence in the academic and policy literatures all out of proportion to its weight in the world economy. From a starting point in the 1950s, when it was one of the poorest countries on the planet, more than four decades of rapid growth elevated South Korea to high-income status and membership in the Organization for Economic Cooperation and Development (OECD), the club of advanced industrial democracies. Despite being poor in natural resources and only midsize in terms of population, Korea has become an industrial powerhouse and the world’s seventh largest exporter. Its economic rise persisted through the transition from authoritarianism to democracy and in the face of chronic tensions with the Democratic People’s Republic of Korea, the country’s difficult neighbor to the north. For all these reasons, South Korea’s progression from agriculture to industry and its graduation from developing- to advanced-nation status have fascinated generations of scholars and policymakers.

At the same time, close observers of the Korean economy have always understood that its story is not one of unmitigated success. Korea has a history of financial crises interrupting the growth process. The disproportionate power of a handful of large family-controlled business groups, or chaebol, has created problems of political influence and hindered entry and competition for small firms and start-ups. Questions are increasingly raised about whether its education system, which rewards rote learning more than originality and favors the graduates of a handful of elite universities, can adequately serve the needs of the economy and society. Korea has an unusually large male-female earnings gap and a high poverty
rate among the elderly. Productivity in the service sector, where the majority of future employment growth will necessarily be located, is disappointing. Now that economy-wide growth appears to have slowed, some observers are asking whether the Korean miracle is over.

The earlier phases in the Korean growth story have been thoroughly studied. In the 1970s the Korea Development Institute (KDI), the country’s leading government-supported economic think tank, commissioned a series of book-length studies of the initial decades of high growth; the findings of this research project were summarized in an overview volume by the project organizers (Mason et al. 1980). In the wake of the Heavy and Chemical Industry Drive of the late 1970s and the transition to democracy in 1987, KDI commissioned an additional three studies designed to update the story (Haggard et al. 1994; Lindauer et al. 1997; Stern et al. 1995). This volume follows in that tradition. It synthesizes the findings of a KDI-supported research project culminating in a series of monographs that bring the story of Korean economic growth and development up to date. While any adequate analysis of Korean economic development must situate recent events in their historical context, our focus here is on the period subsequent to that covered in the earlier KDI projects.

**Political Democratization and Economic Liberalization**

A theme of this volume and the series as a whole is that the dual processes of democratization and economic transformation that have shaped the development of Korean economy and society over the past quarter century are profoundly linked. Democratization led initially to the election of governments that displayed considerable political and policy continuity with their predecessors. It is not surprising that voters did not immediately repudiate politicians tied to the prior authoritarian regime, given the success with which earlier governments had delivered the goods, and the priority attached by the electorate to continued economic growth.

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2. This is also the theme of the volume in this series by Mo and Weingast (2013). See also Mo and Moon (1998) and Kihl (2004). We elaborate on this further in Chapter 2.
3. While the Kim Young-sam government sought to distance itself from previous policies, in practice there was considerable personal and policy continuity with the earlier regime. For discussion, see Chapter 2.
And the first postdemocratization governments of Roh Tae-woo and Kim Young-sam succeeded in delivering high growth in the manner of their predecessors. But after the 1997–1998 Asian financial crisis disrupted the economic status quo, causing output to fall by nearly 10 percent, voters elected a series of left-of-center governments that promised to administer fundamental reforms to cure the ills bequeathed by the crisis and to root out the structural problems that had rendered the economy vulnerable to destabilization.

Again, this response is not surprising, given the social dislocations of the crisis and the urgency it engendered for pursuing structural reforms. What was surprising was that the subsequent governments of Kim Dae-jung and Roh Moon-hyun, while adopting populist rhetoric, pursued distinctly unpopulist policies. They offered carefully calibrated social welfare initiatives designed to level the distribution of income and provide support for the poor and unemployed, not radical reform with the goal of creating a European-style welfare state. Rather than opting for renationalization and re-regulation, they pushed through the most far-reaching economic liberalization in Korea’s history (although they may not have gone as far as some of their conservative rivals had hoped). They deregulated product and factor markets. They eased barriers to entry into legal and accounting services. They restructured the financial system. They stripped away barriers to foreign investment in the corporate sector. They introduced special economic zones and tax incentives for foreign investors. And while they cared deeply about basic welfare and balanced regional development, they relied not just on state intervention in the economy but also on market-friendly reforms, on the assumption that faster economic growth would ameliorate social problems in due course.

A first question addressed in this volume is thus why South Korea’s post-crisis populist governments pursued such unpopulist policies. The answer, in a nutshell, is that the post-crisis governments, no matter how radical their inclinations, had to contend with the objections of a conservative opposition and the conservative media. Korea, for reasons described further in Chapter 2, did not emerge from the period of authoritarian rule with a single charismatic leader or dominant political party. From the start, its political system was characterized by checks and balances—what political scientists refer to as “multiple veto points”—that worked to prevent sharp changes in the direction of policy, whether warranted or not.
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An additional factor was a binding external constraint. Foreign exchange reserves having been exhausted at the end of 1997, Korea was forced to appeal to the International Monetary Fund (IMF) for emergency assistance, requiring it to accept IMF-style policies of liberalization and limited redistribution. Of course, this observation only raises additional questions. Why did subsequent Korean governments not abandon those policies once the country was no longer dependent on the IMF? Korea paid off the last of its debt to the IMF in August 2001. Why did the government not advance a more populist agenda at that point?

It could be that the binding constraint was internal rather than external: that the government’s limited fiscal resources constrained its social-policy ambitions. The problem with this explanation is that countries poorer than South Korea have pursued more ambitious policies of redistribution. And even if tight fiscal constraints help to explain the limited extent of redistribution, they cannot explain the continuing commitment to deregulation and market liberalization.

A final possibility is that the rapid pace of economic and financial globalization convinced Korean politicians and their constituents that there was no choice but to restructure and liberalize, if the country was to compete in a globalized world. This hypothesis points, in turn, to the still more interesting question of how Korea, unlike many other crisis-stricken countries, managed to take advantage of the financial crisis to carry out structural reforms.

Recent Economic Growth

A second surprise was that these far-reaching post-crisis reforms did not more fully resuscitate economic growth. After having an average growth rate of 7 percent per annum in 1990–1997, growth in 2001–2008 decelerated to 4.6 percent per annum, less than two-thirds the previous pace. Following the global financial crisis of 2008–2010 it decelerated further, to 3.6 percent in 2011, 2.0 percent in 2012, and 2.6 percent in 2013.

Why did post-crisis reform fail to restore growth to pre-crisis levels? It may be that there still has not been enough time for firms to adapt to the

4. We omit the crisis and the immediate post-crisis recovery, since growth was exceptionally volatile in both periods.
new market and policy environment.\textsuperscript{5} Liberalization and deregulation that expose firms to entry and competition also squeeze profitability, production, and investment in the short run. In the long run, however, producers will either adapt or be forced to exit the market. After such adaptations—once Korean firms restructure their operations in ways better suited to a deregulated business environment—efficiency, production, and investment should recover. One can think of this as survival of the fittest: efficiency rises because the least efficient domestic competitors vanish from the scene. In this way reform eventually produces the hoped-for results. But patience is required—given the disruptions through which the world economy suffered in 2008–2009, unusual amounts of patience.

A different interpretation is that additional reforms will be needed in order to achieve faster growth. Korea, in this view, is stuck between the two banks of the river.\textsuperscript{6} There has been sufficient deregulation and market liberalization to disrupt old ways, but not enough for firms to restructure decisively. The most difficult reforms—deregulating the service sector, removing barriers to foreign acquisition of financial firms, relaxing restrictive labor market regulations—tend to be left for last, and because of this, uncertainty lingers about whether the commitment exists to follow through. In the absence of these remaining elements, reforms already in place may fail to produce the desired results, thus creating pressure to roll them back. And in the face of such uncertainty, firms are reluctant to restructure and invest. The implication is that pushing ahead with reform will help restore economic growth to earlier levels. But the political will must be there.

Yet a third interpretation, with entirely different implications, is that the presumption that the Korean economy is underperforming and that liberalization and restructuring have failed to deliver positive results is simply wrong. The fact that the rapid growth of the pre-1997 period culminated in a crisis may indicate that the period’s rapid growth was not, in fact, sustainable. Korea, in other words, is now doing as well as its circumstances can allow. A country far from the technological frontier can

\textsuperscript{5} These interpretations are elaborated in Chapter 3, drawing on the companion volume by Eichengreen, Perkins, and Shin (2012).

\textsuperscript{6} The phrase, along with the notion that partial reform may not deliver results or may even make things worse before it makes them better, is from Bertola and Ichino (1995).
achieve rapid growth by importing foreign technology, shifting labor from agriculture to industry, and otherwise making up lost ground. Eventually, however, easy gains will be exhausted and growth will slow to rates more typical of a country approaching the technological frontier. Rather than simply shifting workers from agriculture to manufacturing and services, Korea now has to raise productivity in those self-same manufacturing and service activities. Rather than simply licensing technology from abroad, Korea now must generate it. The country had already begun to experience this transition at the end of the 1980s, although this reality was disguised by a debt-financed boom during which large business groups engaged in breakneck capacity expansion. But the debt-financed investment boom was unsustainable, something that became clear in the crisis of 1997–1998.

As a result of these circumstances, growth downshifted abruptly rather than slowing gradually to lower levels as predicted by textbook models of catch-up and convergence. But while the shift may have been striking for its suddenness, Korea’s slower growth rate is not a sign of economic or political failure. It is simply the normal condition for what is now a relatively mature economy.

Finally, the slower growth of the Korean economy may be a corollary of a more difficult external environment. In 2008–2010 the world experienced the most serious global financial crisis in 80 years. The advanced countries dug themselves into a deep hole from which they now find it difficult to recover. Burdened with heavy public debts, they are growing more slowly than before. Deleveraging by foreign households promises to subdue the demand for consumer goods for an extended period, including the consumer goods produced and exported by Korean corporations. The continuing financial problems of the advanced economies, and the policies adopted in response, accentuate the volatility of international capital flows, making monetary and financial management more difficult for what remains a small open economy.

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8. The textbook model, with evidence, is laid out in Barro and Sala-i-Martin (1995).
9. We analyze this further in Chapter 7. The role of international transactions and the external environment in Korean economic growth feature in the volumes by Eichengreen, Perkins, and Shin (2012), which focuses on trade and foreign direct investment, and Park, Kim, and Park (forthcoming), which focuses on international finance.
Emerging markets, for their part, have driven up energy and raw material prices, creating an especially burdensome situation for an economy like Korea’s that is poor in natural resources. That said, it should be emphasized that emerging markets also create new opportunities for Korean producers: the non-OECD world now purchases 70 percent of South Korea’s exports.

But gaining and maintaining market share in the non-OECD world, as elsewhere, requires meeting the competition, most notably, China. China’s emergence has arguably been the single most important development reshaping the world economy at the outset of the twenty-first century. While there is a tendency in some circles to blame Chinese competition for whatever ails, Korea has special reason to ask how China’s rise has affected its economic performance. China and Korea are neighbors. They share many of the same natural markets, including each other’s. They have similar resource endowments in that both are more labor than land abundant and both rely heavily on imported energy and raw materials. China seems to be ascending the same industrial ladder that Korea climbed from the 1960s to the 1980s, moving from the production of labor-intensive exports like textiles and footwear to the assembly of consumer electronics and now the production of capital goods. This creates the impression that it is not just South Korea’s low-wage, labor-intensive industrial sector that is being squeezed by Chinese competition but the country’s manufacturing as a whole.

Still, is the rise of China really having a negative impact on Korean growth prospects and performance?\textsuperscript{10} Chinese competition has clearly accelerated the decline of South Korea’s labor-intensive industries. At the same time, however, capital- and skilled-labor-intensive industries, both those producing capital equipment and those producing relatively sophisticated parts and components going into Chinese assembly operations, have benefited from China’s emergence as the assembly platform for the Asian-Pacific region.

What is true of foreign trade is similarly true of foreign direct investment, or FDI. China’s emergence as a rival in the competition for FDI may have diverted some foreign investment away from Korea, but China also offers an attractive and profitable destination for Korea’s

\textsuperscript{10} Again, we draw here on the analysis of Eichengreen, Perkins, and Shin (2012), especially ch. 4.
own outward foreign investment. Korea is the fourth most important source of FDI in China. Setting up assembly plants and other operations is an important way in which Korean firms can maintain and enhance their international competitiveness.

The shift to more capital-intensive industrial production and the substitution of foreign for domestic investment is cold comfort for Korea’s unskilled workers, who must accept lower earnings in self-employment or small family-run businesses. To limit the impact on them, Korea will have to upgrade its institutions of skill formation and knowledge creation. To avoid being caught in China’s headlights, Korea also needs to continue graduating from assembly to product design. It needs to complement its success in manufacturing with more productive banking, insurance, communications, and health and business services.

Successive governments have offered initiatives to reform the national education system and transform Korea into a knowledge economy. South Korea has world-class researchers (in bioengineering, for instance) and technologically innovative firms (like Samsung, which is renowned for its leading-edge electronics). Korea is the most wired country in the world in terms of Internet connections per capita. Some progress has been made toward becoming a knowledge economy, in other words. But competition from China remains intense. Exports no longer create the same GDP and employment growth as before because of the growing imported-input component of Korean manufacturing. Productivity is also disappointing in the service sector, which already accounts for a majority of employment and, as in all mature economies, will account for an even larger share in the future.

Business, Government, and Finance

Why do commentators pay so much attention to the supposed “hollowing out” of Korean industry? The obvious answer is that the Korean growth story is fundamentally the story of industry. From a starting point where

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11. In its share of FDI in China, Korea follows only Hong Kong, Japan, and the Virgin Islands—and the figures for the Virgin Islands presumably reflect money originating in Hong Kong and perhaps the People’s Republic of China (PRC) itself. Attributing that money to Hong Kong and domestic investors raises Korea to number three on the list of source countries. At the same time, it is also possible that official PRC figures significantly understate Taiwan’s FDI in China.
industry produced little and exported less, manufacturing grew rapidly for four decades. The reallocation of labor from low-productivity agriculture to high-productivity manufacturing explains a substantial portion of the rise of labor productivity in Korea in the second half of the twentieth century and especially at the beginning of the high-growth period.\textsuperscript{12}

Initiating and sustaining industrial development, recent scholarship has emphasized, required Korean industrialists and their collaborators in government to solve a number of specific problems.\textsuperscript{13} Growing Korea’s industry required mobilizing finance for investment, given that manufacturing is more capital intensive than agriculture and services. In addition to using a relatively high ratio of capital to labor, industrial firms use large absolute amounts of capital. Capital requirements thus exceeded what any one individual or family could provide. Relatively high minimum efficient scale also meant that growth would be constrained by the size of the market unless firms succeeded in exporting. Finally, manufacturing requires specialized inputs that either the firm or its suppliers must provide. Here, too, the capital intensity of production comes into play, for a disruption of the reliable provision of those inputs can have debilitating costs if a capital stock is forced to sit idle.

These are not problems that arms-length markets—with transactions between otherwise unrelated agents—can necessarily be relied on to solve. Entrepreneurs, lacking reputation and collateral, may find it hard to obtain funding on the requisite scale. Outside investors, worried that their funds will be diverted by those in control, may hesitate to commit. Industrialists requiring specialized inputs may hesitate to rely on third parties, fearing that their own production will be held up. Producers lacking commercial contacts may find it hard to break into export markets. Not surprisingly, these problems are particularly pervasive in economies still on the cusp of modern economic growth.

A number of solutions suggest themselves. Government can directly mobilize the capital. It can substitute its own reputation and collateral, in the form of its power to tax, for the reputation and collateral of private

\textsuperscript{12} It makes sense that the Korean economy should have become a net exporter of manufactured goods, since the country is necessarily a net importer of agricultural goods and raw materials, reflecting its limited endowments of fertile land and resources.

\textsuperscript{13} Here we again draw on Mo and Weingast (2013).
borrowers, providing firms with external financing and insurance against risk. It can coordinate investments in complementary industries, all of which must get up and running in order for any of them to succeed. Bureaucrats can supplement other sources of managerial expertise. And government can provide consular and commercial services to help producers break into international markets. The Korean government took all these steps in the export push of the 1960s and the Heavy and Chemical Industry Drive of the 1970s.

Business groups offer another conceivable solution. As we describe in Chapter 5, business groups form through repeated contact or out of the simple fact that a controlling share of the ownership of each of the constituent firms is in the hands of the same economic or familial coalition. With family ties serving as a guarantee of good faith, cash-rich firms can provide finance for not-yet-profitable but potentially viable affiliates. The risks of doing business in sectors where capital requirements are high but finance is uncertain can be managed by within-group transfers. And when the firms in question are members of the same business group, they can outsource the production of specialized inputs without fear of being held up by suppliers. In Korea, these functions were carried out by the chaebol, which evolved out of the country’s family-owned trading companies.

Financial institutions offer a third possible response. Banks mobilize the capital of small savers. They also invest in specialized monitoring technologies to determine which loan applicants are reputable and possess attractive investment projects. Venture capital firms can combine specialized knowledge of technology with financial expertise to fund start-ups attempting to commercialize innovative products. Banks, as large investors, occupy seats and cast blocks of votes on corporate boards, enabling them to advocate on behalf of outside investors. Representatives of the same bank can sit on the boards of different companies in up- and downstream industries, easing coordination and hold-up problems. Korea was for many years the prototypical example of a late-developing country with a bank-based financial system engaged in these functions.

None of these solutions is perfect. Government bureaucrats lack the high-powered incentives of owner-managers, who stand to reap enormous returns from correct decisions. They do not obviously possess the specialized knowledge and talents of those who have risen to the top through the process of natural selection known as market competition. Those whose businesses they support may operate as if facing soft budget constraints,
expecting to be bailed out in the event of losses. They may make decisions on the basis of noneconomic objectives at odds with the pursuit of efficiency, be they social goals or outcomes in the interest of their political supporters and campaign contributors.

Business groups whose members interact mainly with other group members may similarly be insulated from the chill winds of competition. Groups with captive banks may be freed of having to compete for funds. In addition, business groups organized as pyramids, with the firm at the top owning a controlling interest in the next tier of firms, each of which owns a controlling interest in a next tier of firms, may have a wide gap between ownership and control, which can aggravate agency problems. The firms at the top of the pyramid, having become too big and politically well-connected to fail, may take excessive risks.

Financial institutions, too, are susceptible to agency and moral hazard problems. Outside investors can find it difficult to determine whether a bank’s managers are acting to advance their personal interest or that of the shareholders. Portfolio managers and loan officers will take excessive risks if they expect to be bailed out by the authorities. And if management feels pressure from government to lend, it will develop just such an expectation in the event that things go wrong.

Standard logic suggests that the benefits of these extramarket arrangements dominate their costs in the early stages of economic growth, when there is a need to jump-start industry and market mechanisms remain underdeveloped, as was the case in Korea in the 1960s and 1970s. But with growth and modernization come an improved information environment and stronger contract enforcement, at which point it is possible to rely more heavily on arms-length transactions. With the development of multiple suppliers of inputs, both domestic and foreign, hold-up problems become less severe. And with growth of the domestic market and penetration of foreign markets, adequate demand is assured. At this point the advantages of extramarket arrangements diminish and come to be outweighed by the costs.

The problem is that institutional substitutes for missing markets do not slip quietly into the night. While the phenomenon of “institutional overhang” is a concern everywhere, it has been especially serious in Korea because of the exceptional dependence of Korean businesses’ early growth on extramarket mechanisms and the telescoped nature of the country’s economic and market development. The challenge for the authorities
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overseeing the chaebol, for regulators responsible for supervision of the banking system, and for policymakers who determine the contours of Korea’s public-private risk-sharing partnership is to update this inherited dependence to better meet the needs of the twenty-first century. It is for them to do so in the face of resistance from entrenched stakeholders.

Labor and Social Development

In the early stages of the high-growth era, South Korea was a model of success in reconciling growth with low levels of inequality. One might expect this pattern to have been maintained with democratization and the end of government repression of unions, but a growing body of evidence points in the other direction. It suggests that Korea’s dualistic labor markets, in which a core of permanent workers receiving extensive training on the job coexists with an unstable fringe of temporary workers who provide employers with flexibility, give rise to undesirably high levels of wage and income inequality. While temporary workers have lower incomes in all economies, in Korea they account for twice as much of the labor force as the average share for OECD countries.

In addition there is growing evidence of persistent income inequality transmitted across generations. These differential outcomes can be traced, in turn, to differential access to early childhood education and, more generally, to the fact that children from disadvantaged families have inferior access to education in their formative years. The more limited access of such children to Korea’s distinctive system of after-school tutoring and instruction, known as hagwon, reinforces the problem. Tuition fees for tertiary education are also a burden for children of low-income families, something that may limit intergenerational mobility. Government could address this problem by more closely keying tuition payments to family

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14. This section draws on the companion volume in this series by Freeman, Choi, and Kim (forthcoming). We will elaborate on these points in Chapter 6.

15. Moreover, the prospect that one’s first job may be temporary and that this may make moving into permanent employment more difficult is one explanation for Korea’s unusually low rate of youth employment. Many employers offer a one- or two-year entry contract and then have a vetting process for permanent employment at the end of that time, based on job performance. Some observers point to the country’s unusually high rate of university enrollment as another explanation for youth unemployment, but the two stories are compatible—some young people avoid entering the labor market by extending their years of formal education.
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income. It could address the limited availability of high-quality university education and the superior employment prospects for graduates of the country’s elite universities by upgrading other institutions of higher education. It could strive for a better balance between investing in university education and developing vocational training for students for whom attending university is not appropriate.

Korea has the highest gender-based wage gap in the OECD. A corollary of the relatively low wages received by women is an unusually low female labor-force participation rate of around 60 percent. The participation rate of women with a tertiary education is especially low by international standards, reflecting the fact that the gender pay gap for university graduates is exceptionally high. These problems could be addressed by expanding public support for day care and education expenses, moving to full-day programs for school-age children, and legislating additional parental leave and more family-friendly workplace practices.

Recent data also point to a disturbingly high poverty rate among the elderly. As we describe in more detail in Chapter 6, 45 percent of Koreans of retirement age live in relative poverty, far in excess of the OECD average of 13 percent. Not only is this problem exceptional for an OECD economy, it is also likely to grow more serious as the Korean population continues to age. This highlights the importance of further developing the country’s National Pension Service. It also suggests rethinking the convention that workers should retire from their main job at the age of 60 (according to legislation passed by the National Assembly on 30 April 2013 that raised the minimum legal retirement age from 55), at which point many move into informal employment, often at a significantly reduced income.

Poverty rates are also high among households with no active worker. This demonstrates the urgency of expanding redistribution through the tax and transfer system with the goal of alleviating poverty. It highlights the underdevelopment of the National Basic Livelihood Security System, the country’s principal social welfare program, and the fact that social benefits more generally remain inadequately targeted at the needy.16

Identifying problems is easy; solving them is harder. Although weakening the generous job-security protections enjoyed by permanent workers

16. For more on the National Pension Service and the National Basic Livelihood Security System, see Chapter 6.
might help to reduce labor-market dualism by reducing the incentive for employers to rely on a rotating cast of temporary employees, such reforms will be resisted by the incumbent workers and those bargaining on their behalf. While it would be nice to boost spending on vocational training, this is likely to be resisted by the higher-education establishment. It would be desirable to provide greater access to the social safety net for temporary workers in order to provide for basic needs when they are between jobs, but doing so would be expensive; this reform will therefore have to compete with other priorities. Similarly, expanding the National Pension Service and Basic Livelihood Security System so they provide the same levels of support as services in other OECD economies, extending blanket reductions in tuition to university students, increasing state support for day care, and mandating paid parental leave would strain the resources of what is still a middle-income economy.

A Roadmap to What Follows

These are the issues around which we organize this volume. Chapter 2 begins with a review of the political economy of economic policymaking, focusing on the post-democratization period and the years following the financial crisis of 1997–1998. Chapter 3 then develops the natural-slowdown hypothesis, the idea that the observed deceleration is a predictable concomitant of the country’s increasing economic maturity. It contrasts that concept with the policy-failure hypothesis: that with a more concerted and coherent agenda, Korea could achieve faster rates of growth.

Financial liberalization and reform have been touted as promising a more efficient allocation of resources, better risk diversification, and faster economic growth. But as we show in Chapter 4, the evidence on the effects of financial liberalization is ambiguous. What is clear from Korea’s own history and from the experience of other countries is that financial deregulation does not guarantee improvements in economic efficiency and stability. An inadequately regulated financial system can be dangerously procyclical—that is, it can amplify business-cycle fluctuations. Korea has stumbled from crisis to crisis, from the investment and commercial bank crisis of 1997–1998 to the credit card crisis of 2003 and the savings bank crisis of 2010. For much of its history, financial stability has remained elusive. How to best secure it remains a prominent item on Korea’s public-policy agenda.
Another perennial issue is the role of the chaebol, which remain the leaders of the country’s industrial sector. Chapter 5 analyzes both the causes and consequences of this state of affairs. Among the consequences is a growing bifurcation of economic prospects for large versus small firms. More generally, there is concern in Korea and also in organizations like the OECD about issues of distribution and social cohesion and about the chaebol as a locus of concentrated power. There are questions about the labor market and the education system and whether they are well suited to the needs of an increasingly globalized Korean economy. There are questions about whether the social welfare system can be extended and redesigned to better reconcile the imperatives of efficiency and equity. We address these concerns in Chapter 6.17

Then there is Korea’s place in the world economy. This issue is of special concern to outside observers, given the prominent role of the external sector in the country’s economic growth and development. In Chapter 7 we review the importance of the external sector in the past and pose questions about its future. Prominent among those questions: What are the implications of Chinese competition, and should Korea continue to specialize in the cluster of heavy industries that have been the traditional basis for its industrial success, move up market into the production of high-tech products, or attempt develop a comparative advantage in tradable services?

An important future challenge and source of uncertainty is North Korea, in terms of the prospects for the North Korean economy and the possibility of reunification. Chapter 8 provides an overview of the state of the North Korean economy. It analyzes the different approaches taken by successive South Korean governments in managing relations with its difficult neighbor and embeds them in the larger geopolitical context, in which the United States, China, and Japan also play consequential roles.

In the concluding chapter we sketch a way forward for the Korean economy, drawing on our own analysis and the work of other contributors to the volumes in this series.

17. In doing so, we draw on the companion volumes by An and Bosworth (2013) and Freeman, Choi, and Kim (forthcoming).