Structural Reform in Korea: its Process and Consequences

by

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On the 21st of November 1997, Korea turned to the International Monetary Fund (IMF), as the rollover ratio of short-term external borrowings by domestic financial institutions kept decreasing and the country’s usable foreign exchange reserves plummeted to US$ 7.3 billion, from US$ 22.3 billion only a month earlier. On the 3rd of December 1997, Korea and the IMF signed an agreement on a financial aid package totalling US$ 58.3 billion. The IMF Stand-By Arrangement was subject to a broad range of conditions, including macroeconomic stabilisation and structural reform.

As emergency measures, the Korean government was required to implement tight monetary policy, fiscal austerity and the immediate closure of insolvent financial institutions. In the longer term, the Korean government was required to pursue economic reform programs in the financial sector, the corporate sector, and the labour market. Because the Korean crisis had its roots in the weakened fundamentals of the Korean economy, attempting to stabilise only the financial market without an emphasis on structural reforms is like treating symptoms without addressing the cause. Thus, since the onset of the financial crisis in 1997, the Korean government has pursued structural reforms in the areas that the IMF required. In addition, the Korean government has pursued public sector reform to achieve the efficiency necessary to keep up with other sectors’ reforms.

This chapter aims to evaluate the post-crisis performance of the Korean economy with a special emphasis on the Korean government’s structural reform efforts under the IMF program. Having done this, this chapter identifies potential dangers and challenges lying ahead, and further discusses the prospects of the Korean economy. The remainder is as follows. Section 2 presents the structural reform programs of the financial sector, the corporate sector, the labour market and the public sector. In section 3, economic developments after the crisis are presented. Section 4 discusses the problems associated with the structural reforms and the challenges that the Korean economy has to overcome so as to attain full recovery from the crisis and a sustainable growth. Section 5 concludes.