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Why Cannot One of the Asian Tigers (Korea) Jump over the Threshold of Advanced Countries?

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Abstract. This paper attempts to investigate the unpropitious prospects of the Korean economy from a cultural perspective, introducing the concept of transaction costs as an intermediary between culture and economic development. Under this model, culture affects the level of social trust which in turn has an effect on transaction costs, thereby on economic development. This paper examines a variety of recent cultural changes in Korea, which raise transaction costs. This assessment of Koran culture is reinforced by comparing relevant cultural features to those of advanced countries. Therefore, even if all else remains the same, Korean economic prospects will be weakened by its cultural influence.

Keywords: Korea, Culture, Transaction Cost, Economic Development.

1. Introduction

In spite of a high expectation that Korea would maintain its rapid growth and soon join the rank of advanced economies, it has entered a low growth phase from the dawn of the 21st century, and has been concerned with the dimming prospect of crossing the threshold to advanced economy status. Economic development is a complex phenomenon influenced by capital, labour, technology and formal and informal (culture) institutions. Culture has important bearings on the economy through its effects (a) on the behavioural patterns of individual economic actors, (b) on economic relations among citizens, and (c) on the performance of formal institutions. Recognizing the complementarity of the multiple factors for economic development, this paper explores the role of culture as one of the important development factors to better assess Korean economic prospects.

The traditional Confucian model, focusing on cultural effects on individuals' behaviours, argues that Confucian cultural features such as thriftiness, diligence and educational zeal, have been one of the key development factors for East Asian economies. Different from the traditional Confucian model, this paper explores cultural effects on commercial relations among economic agents, on the performance of formal institutions, and on creative capacity of citizens. In doing so, this paper examines a variety of recent cultural changes in Korea, such as a declining social trust, law observance, and future orientation. Finally, Koreans' cultural features, relevant to this model, are compared to those of advanced countries to reinforce cultural effects on Korean economic prospects.

2. Literature Review

Conventional economists had traditionally shied away from analysing culture in economic development. It was then Max Weber (1950) who has at first considered different cultural influences on economic development. Weber argued that the Protestant work ethic was the basis of Western economic development, and that the absence of this ethic in Asia was the reason for the region's lower level of development. Swift and unprecedented economic development in East Asia during the 1970's and the 1980s has inclined scholars to argue that Confucian culture, shared by East Asian countries, is the key to East Asian economic success (Pye 1990, Adams et al 2007). They point to specific characteristics of Confucian culture, including

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hierarchical collectivism, loyalty toward authority, emphasis on education, diligence, frugality and discipline as factors for economic development. However, the Confucian model is limited in that it explores a parochial aspect of cultural effects on an economy.

A number of Korean scholars (Nam 1994) have embraced the Confucian model and argued that national culture contributed significantly to economic development over the three decades from the early 1960s. However, the Confucian model cannot explain recent sluggishness of the Korean economy, as Confucian behavioural characteristics such as frugality, diligence and educational zeal have remained more or less unchanged in Korea. This paper therefore explores cultural effects on commercial relations among economic agents, on formal institutional performances and on creativity of citizens. This is done by introducing the concept of transaction costs between culture and economic development.

Transaction costs arise through the processes of negotiation between economic agents, valuation of goods and services to be exchanged, and enforcement of contracts (North 1990). Culture affects the level of social trust (or social capital), which in turn affects the level of transaction costs. Not only do transaction costs affect the economy directly as part of economic costs, but they also work as an important factor for how well markets function, as the degree of specialisation, division of labour and productivity depends on transaction costs.

Harrison (1985), drawing from his extensive study of economic development in South American countries over two decades, argues that differences in economic development among countries or ethnic groups arise primarily due to cultural differences. He argues that culture shapes the radius of trust and identification among people and the rigour of a society's system of ethics, thereby affecting the level of transaction costs. Harrison also argues that culture affects economic development through its impact on the creative capacity of all citizens – a critical factor for the future Korean economic development. He identifies cultural traits that foster creative capacity as 'future orientation, rationality and equality'. This new approach with the concepts of transaction cost and creative capacity is employed in investigating the role of culture for future prospects of the Korean economy.

3. Recent Cultural Changes and Their Effects on the Korean Economy

While cultural change is usually slow, a raft of institutional and legal reforms introduced in response to the 1997 crisis has induced relatively swift cultural changes in Korea, resulting in declines in trust or increases in social discontent. First, the 1998 change in the labour law has opened the way for private companies to dismiss their staff, thereby diminishing the concept of lifetime employment. Companies have also introduced performance-based compensation, replacing the seniority system. These changes in human resource management create uncertainty for workers and inevitably reduce the level of trust between employers and employees and aggravate labour relations. All this is reflected in high labour disputes in Korea (Table 1).

Second, trust has declined from the rising disparity between regular and non-regular workers. Since the 1997 crisis, many employers have changed employment from regular to non-regular workers to reduce labour costs and to improve employment flexibility (Table 1). Non-regular workers are treated substantially worse than regular workers in terms of remuneration and social and statutory benefits. In response to perceived injustice particularly toward non-regular employees, the appeal of such approaches as cooperation and compromise has declined in Korean society. Third, as Harrison (1985) argues, increasing inequality in income distribution reduces social capital. Inequality in income distribution, measured by the Gini coefficient, has increased in Korea (Table 1).

Fourth, Fukuyama (1995) argues that the rise of crime and litigation indicates the decline of social trust. In Korea today, the rule of law appears to be losing its regulatory power, as does the prerequisite underlay of trust and ethics that enables, sustains and reinforces the rule of law. The numbers of penal code criminal cases and the judicial processing of civil cases have both increased substantially over the 2000-2008 period

(Table 1). Perceptions of social injustice in a variety of forms are reflected in low social trust, on which Korea ranked 24th out of 29 OECD member countries (Lee 2009). Finally, relatively strong nationalism in Korea, as compared to other national examples, helps to explain why many observers from overseas still regard Korean people as xenophobic (Dodgson 2009). Xenophobic attitudes of some Koreans reduce the radius of identification and raise transaction costs in international commercial dealings.

The future orientation also appears to be declining in Korea in recent years. Uncertainty perceived by workers after 1997 and uncertainty and instability generated by inconsistent government policy measures in the recent past would have hindered the future orientation of citizens. Declining savings and investment rates may reflect the decline in future orientation (Table 1). As imbedded in hierarchical collectivism with social stratification based on education and ranks in organisation, Korean society is lacking equality, impeding productivity, innovation and entrepreneurship in Korea.

Table 1: Korea's Social and Economic Indicators

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
GDP growth (%)	8.8	4.0	7.2	2.8	4.6	4.0	5.2	5.1	2.0	0.2
Saving rate (%)	33.0	31.1	30.5	31.9	34.0	32.1	30.8	30.8	30.5	30.0
Investment rate (%)	30.7	29.3	29.3	30.0	29.9	29.8	29.7	29.5	31.0	25.8
Labor disputes	250	235	322	320	462	287	138	115	108	121
% of non-regular workers	n.a	n.a.	27.4	32.6	37.0	36.6	35.5	35.9	33.8	34.9
Gini coefficient	0.296	0.303	0.298	0.298	0.301	0301	0.299	0.304	0.303	0.301
Penal code criminal cases(000)	523	554	797	857	827	826	828	845	898	993
Judicial processing of civil cases	2757	2740	3146	4410	4094	3663	3603	3932	4246	n.a

Sources: KOSTAT (Korea Statistics) (2010), KLI (Korea Labor Institute) (2010), KOSTAT (2011), KIHASA (Korea Institute for Health and Social Affairs) (2011).

4. Comparative Analysis of Recent Cultural Trends in Korea

So far the wide-ranging cultural changes within Korean society have been analysed. This is augmented by an analysis of a variety of Korean cultural features, compared to those of advanced countries. This is done by comparing pertinent social indicators between Korea and other countries, developed by a number of well-known international organisations.

Obviously trust has declined in the Korean labour market markedly more than other countries (Table 2). Over the period 2000-2010, Korea belonged to the worst 95 percentile in labour relations, thereby Korea being one of the countries that had most industrial disputes.

Korean society's view of individual firms' behaviours is quite low, as indicated by Korea's relatively poor rankings in corporate social responsibility and ethical behaviour. The low level of trust in companies together with poor labour relations would be reflected in a relatively low level of worker motivation.

The levels of ethics and law observance are remarkably lower in Korea. This is indicated by Korea's poor ranking on the Corruption Perceptions Index (CPI), perception of justice, favouritism in official decisions and judicial independence, ranging from 34.3rd to 47.5th (Table 2). Finally, Koreans' mindsets have remained quite closed, as indicated by its relatively poor ranking on national culture. This vindicates the arguments that xenophobia is still prevalent in Korea.

Table 2: Comparative stances of Korean Social Indicators

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	Avge (2000-10)
1) Labour market												
Labour relations (IMD)	44	46	47	30*	60	60	61	55	55	56	56	54.0 (53)#
Worker motivation (IMD)	33	32	19	16*	42	37	32	33	30	38	28	32.4
Industrial dispute (IMD)	38	25*	44	45	43	37	38	36	38	n.a.	n.a.	39.9
Worker motivation (IMD)	33	32	19	16*	42	37	32	33	30	38	28	32.4
2) Society's view of firms												
Social responsibility (IMD)	39	40	24	18*	30	30	34	41	2	15	13	26.8
Ethical behaviour (WEF)	n.a.	n.a.	38	33	61	35	38	25	27	48	57	40.2
3) Observance of ethics and laws												
CPI (TI)	48	42	40	50	47	40	42	43	40	39	39	42.7 (180)
Justice (IMD)	32	32	35	18*	41	35	42	30	31	32	33	34.3
Favouritism in official Decisions (WEF)	27	35	30	18	49	26	46	15	22	65	84	37.9
Judicial independence (WEF)	44	47	41	49	48	45	51	35	45	58	60	47.5
4) Social attitudes to globalisation												
National culture (IMD)	47	48	44	30*	49	53	55	55	55	56	52	51.4

Sources: IMD Sources: IMD International Institute for Management Development) International) (2000-2010).
WEF (World Economic Forum) (2000-2011), TI (Transparency International) (2000-2010).

5. Conclusion

Unlike the Confucian economic development model that focuses on economic behaviour of individual economic agents, this paper has explored cultural effects on social trust (social capital), which in turn affects transaction costs, and on creative capacity of citizens. It has found that a variety of cultural changes in the recent past have decreased the level of trust in Korean society, raising transaction costs and socio-economic instability. It has also been found that future orientation of citizens has been fading. A comparative analysis of relevant Korean cultural features, as compared to those of other countries, reinforces recent adversarial cultural changes in Korean society.

In conclusion, the complex and wide-ranging changes in Korean culture in the recent past are serving to raise transaction costs and curtail the Korean people's creative capacity. These cultural effects are likely to be negative on its future economic development. Even if all else remains the same, the prospects of the Korean economy will be weakened by the influence of culture. Therefore, to achieve the nation's aspiration of crossing over the threshold of advanced countries, government, business and society as a whole need to work together to redirect what appear to be deleterious cultural changes in the recent past to a direction conducive to economic development.

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