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Human capital and productivity for Korea's sustained economic growth

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Abstract

This paper assesses Korea's growth experience and its prospects based on methods of 'level accounting' and 'growth accounting'. The level accounting method shows that the gap of output per worker between Korea and the US has rapidly decreased over the past three decades. However, this swift 'catch-up' process is attributed to physical and human capital accumulation for the most part, rather than to the total factor productivity (TFP) growth. Growth accounting shows that the productivity growth of the Korean economy, particularly the manufacturing industry, has accelerated in recent years. But, poor productivity performance in the service industries, including finance, insurance, and real estate, construction, and wholesale and retail trade sectors, hampers overall productivity growth. For sustained productivity growth, Korea needs to stimulate technological investment, and upgrade the quality of human capital.

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1. Introduction

South Korea has shown a remarkable economic performance during the past four decades. The GDP grew extremely rapidly at an average of 7.0% a year between 1960 and

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Table 1
Economic growth in selected countries, 1960–2000

	GDP per capita			Average annual GDP growth per capita					
	1960	2000	2000/ 1960	1960– 1970	1970– 1980	1980– 1990	1990– 2000	1960– 2000	1970– 2000
Korea	1495	15881	10.62	5.97	5.68	7.32	4.67	5.91	5.89
Japan	4545	24672	5.43	9.27	3.09	3.53	1.05	4.23	2.55
USA	12273	33308	2.71	2.87	2.66	2.16	2.30	2.50	2.37
Canada	10384	26905	2.59	3.06	2.97	1.63	1.85	2.38	2.15
Finland	7491	23792	3.18	4.21	3.09	2.65	1.60	2.89	2.45
France	7825	22358	2.86	4.55	2.74	2.11	1.10	2.62	1.98
Ireland	5136	26381	5.14	3.46	3.16	3.51	6.22	4.09	4.30
Australia	10699	25559	2.39	3.26	1.44	1.59	2.42	2.18	1.82
China	682	3747	5.50	1.79	2.72	5.14	7.41	4.26	5.09
Hong Kong	3090	26703	8.64	7.45	6.59	5.04	2.48	5.39	4.70
Malaysia	2119	9937	4.69	3.08	5.26	2.92	4.19	3.86	4.12
Philippines	2015	3424	1.70	1.73	3.17	−0.89	1.30	1.33	1.19
Singapore	2161	27186	12.58	8.93	7.76	4.48	4.16	6.33	5.47
Taiwan	1430	18718	13.09	6.68	7.44	6.27	5.36	6.44	6.35
Argentina	7371	10995	1.49	2.29	1.38	−3.87	4.22	1.00	0.57
Brazil	2371	7185	3.03	4.23	5.67	−0.26	1.46	2.77	2.29
Chile	3853	9920	2.57	2.19	1.22	1.28	4.79	2.37	2.43

Note: The per capita GDP levels and growth rates are based on the international (purchasing power parity adjusted) prices of 1996, which are based on the Penn-World Tables 6.1. *Source:* Heston, Summers, and Aten (2002).

2000, and the per capita income has increased almost 11 times over the past four decades (see Table 1). Although the economy was devastated suddenly by the financial crisis in 1997–1998, by 2000 it had managed to recover quickly.

The crisis has passed now in Korea but the economy's recent growth performance has been rather disappointing when compared with its historical record. From 2001 to 2004, the GDP growth averaged 4.6%.

The startling performance of the Korean economy and its subsequent setback leads to challenging questions of what the fundamental factors that explain Korea's growth performance are. It is also questionable as to whether the current depression is merely a cyclical phenomenon, or an indication of a permanent drop in Korea's growth potentials. Some argue that Korea's recession will be further aggravated, eventually leading to a state comparable to Japan's 'lost decade'. Others say that the dynamic forces that have enabled Korea's fast growth still remain intact, and thus with the appropriate development strategies can resume the pre-crisis growth rates.

The purpose of this paper is to assess Korea's growth experience, as well as its prospects. Empirical methods called 'level accounting' and 'growth accounting' will be used in order to analyze the sources of output growth in the Korean economy over the last three decades. First to be examined is the evolution of the gap in output per worker between Korea and the United States over time, as well as a comparison of Korea's experience and that of other countries. The 'level accounting' results show that although Korea has experienced a very rapid catch-up in output per worker over time, the gap reduction of

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