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**Employment Sector  
Employment Working Paper No. 148**

**2013**

# **Dual dimensions of non-regular work and SMEs in the Republic of Korea**

**Country case study on labour market segmentation**

Byung-jin Ha, Sangheon Lee



Employment  
Analysis and  
Research Unit

Economic and  
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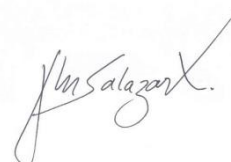
## Preface

The primary goal of the ILO is to contribute, with member States, to achieve full and productive employment and decent work for all, including women and young people, a goal embedded in the ILO Declaration on Social Justice for a Fair Globalization (2008),<sup>1</sup> and which has now been widely adopted by the international community. The integrated approach to do this was further reaffirmed by the 2010 Resolution concerning employment policies for social justice and a fair globalization.<sup>2</sup>

In order to support member States and the social partners to reach this goal, the ILO pursues a Decent Work Agenda which comprises four interrelated areas: Respect for fundamental worker's rights and international labour standards, employment promotion, social protection and social dialogue. Explanations and elaborations of this integrated approach and related challenges are contained in a number of key documents: in those explaining the concept of decent work,<sup>3</sup> in the Employment Policy Convention, 1964 (No. 122), in the Global Employment Agenda and, as applied to crisis response, in the Global Jobs Pact adopted by the 2009 International Labour Conference in the aftermath of the 2008 global economic crisis.

The Employment Sector is fully engaged in supporting countries placing employment at the centre of their economic and social policies, using these complementary frameworks, and is doing so through a large range of technical support and capacity building activities, policy advisory services and policy research. As part of its research and publications programme, the Employment Sector promotes knowledge-generation around key policy issues and topics conforming to the core elements of the Global Employment Agenda and the Decent Work Agenda. The Sector's publications consist of books, monographs, working papers, employment reports and policy briefs.

The Employment Working Papers series is designed to disseminate the main findings of research initiatives undertaken by the various departments and programmes of the Sector. The working papers are intended to encourage exchange of ideas and to stimulate debate. The views expressed are the responsibility of the author(s) and do not necessarily represent those of the ILO.



José Manuel Salazar-Xirinachs  
Executive Director  
Employment Sector

<sup>1</sup> See [http://www.ilo.org/public/english/bureau/dgo/download/dg\\_announce\\_en.pdf](http://www.ilo.org/public/english/bureau/dgo/download/dg_announce_en.pdf).

<sup>2</sup> See [http://www.ilo.org/public/libdoc/ilo/2010/110B09\\_108\\_engl.pdf](http://www.ilo.org/public/libdoc/ilo/2010/110B09_108_engl.pdf).

<sup>3</sup> See the successive Reports of the Director-General to the International Labour Conference: *Decent work* (1999); *Reducing the decent work deficit: A global challenge* (2001); *Working out of poverty* (2003).



## Foreword

One of the key features of the labour market developments observed during the past decades throughout the world relates to a phenomenon of labour market segmentation, e.g. the division of the labour market into separate submarkets or segments, distinguished by different characteristics and behavioural rules. To a large extent, these attributes depend on the specific environment in which workers operate. Segmentation may arise from particularities of labour market institutions, such as contractual arrangements (permanent versus temporary employment), their enforcement (and the resulting informality), as well as types of workers concerned (such as migrant, domestic, or dispatch workers).

While the phenomenon is not new, the job crisis has brought an increasing attention to the segmentation/duality issue, especially in Europe. The implications and costs of segmentation are multiple, in both economic and social terms: they include wage gaps between segments, differences in access to training and social security, as well as in working conditions or tenure. Moreover, segmentation implies limited transitions to better jobs. The consequences of segmentation also have macroeconomic implications, such as lower productivity and higher employment volatility.

In this context, and as part of its objective of promoting decent work, the ILO launched, in 2012, a research programme to better understand how labour market institutions affect employment outcomes in both quantitative and qualitative terms. One of the main motivations of the research project is to put job quality at the forefront of the policy debates, informing the main stakeholders in the world of work of the extent of labour market segmentation and its implications for job quality in selected countries. Fourteen country studies on labour market segmentation and job quality were provided by external country experts, as well as thematic papers on job quality in segmented labour markets and the role of labour law, collective bargaining, and improved enforcement. These studies were discussed in a scientific Workshop held at the ILO in December 2012 and used as thematic inputs in a policy-oriented Workshop held at the ILO in April 2013.

The current paper is one in the series of such country studies. It makes an important contribution to the discussion on contractual segmentation of labour markets, providing an overview of the institutional setup as well as empirical evidence on the extent of segmentation and its implications for various aspects of job quality. The paper also offers a policy perspective on the ways to alleviate the negative consequences of segmentation.

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## 1. Introduction<sup>4</sup>

The notion of labour market segmentation is back to research and policy debates in the Republic of Korea (hereafter Korea) after decades-long silence or disinterest. Previous generation of research on labour market segmentation began with industrialization in the 1960s when dualism between rural and urban labour market in the presence of massive labour surplus was the cause of concern for both researchers and policy makers. As the economy picked up and moved into the impressively high growth route which absorbed surplus labour, the focus shifted to dualism within the urban sector, especially on contrasting fortunes of formal and informal workers. Such issues, although remaining significant, lost momentum soon with the beginning of “full-employment” economy in the 1980s and 1990s. This is also when the Korean economy began to be seen as achieving a “miracle” of “equitable growth” which effectively combined both high growth and lower inequality through a more integrated labour market.

However, the Asian financial crisis in 1997 marked an abrupt end of the “golden age of capitalism” in Korea. Although the economy recovered surprisingly quickly from the crisis, the growth never got back to the pre-crisis level. The recovery of employment was strong, but the structure of employment began to change significantly. Particularly influenced by policy shifts towards labour market flexibilization (imposed by World Bank and International Monetary Fund (IMF) as part of their rescue packages). Inequality in major aspects of job quality (e.g., wages and benefits) began to widen. For this reason, there has been a growing body of statistics and research on labour market segmentation in recent years in Korea, and debates on the causes and the consequences continue.

This paper aims to review these recent developments in the labour market in Korea, from the perspective of labour market segmentation. Based on our own analysis of national statistics and the review of numerous empirical studies which are already available on the topic. We show that the widening inequality in job quality is a combined result of structural changes in economy and employment as well as policy shifts, which has created an increasing proportion of highly vulnerable workers at the bottom of the labour market.

Another important contribution of the paper is to explain the key characteristics of Korea’s labour market segmentation (which can potentially distinguish the Korean experience from others) by identifying dual dimensions of segmentation (i.e., non-regular work and small and medium-sized enterprises (SMEs)) and how they interlock each other into an increasingly fragmented labour market. We document what “penalty” is imposed on workers when they are working with non-regular contracts and/or for SMEs. It also shows the scale of “double penalty” for non-regular workers in SMEs.

Our emphasis on SMEs is very important. Workers in small enterprises are often not covered by the existing labour laws, and thus legal changes to “re-regulate” non-regular work would not provide effective protection to these non-regular workers who account for the majority of non-regular work in Korea. In addition, it is argued that at the heart of the segmentation lie their increasing share of employment and their disadvantageous position *vis-à-vis* large enterprises. We will show that the financial capacity of SMEs to

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offer better quality jobs has been deteriorating over years. This means that the issue of labour market segmentation cannot be fully addressed by labour market policies alone but requires a radical change in the economy.

The rest of the paper is organized as follows. Section 2 provides a statistical overview of labour market outcomes in terms of both quantity and quality of employment since the Asian financial crisis and the subsequent labour market reforms over the past decade. Sections 3 and 4 examine dual dimensions of labour market segmentation, non-regular work and SMEs. Finally, Section 5 concludes with summary and policy implications.

## **2. Changes in the labour market: the end of “equitable growth” in Korea?**

Three-decade long period of “equitable growth” in Korea came to an unexpected end during the Asian financial crisis of 1997. The resulting changes have turned out to be structural in that the potentially cyclical changes relating to the crisis were combined with policy shifts towards labour market deregulation to induce structural transformation to the labour market in Korea. This sector reviews these changes in both policies and actual labour market outcomes.

### **2.1. Major changes in labour market outcomes: sluggish employment growth with deepening segmentation**

Before the financial crisis, the Korean economy recorded a high annual growth rate of over 7 per cent and maintained almost full employment from the late 1960s. However, the post-crisis growth became lower and more unstable, never returning to the pre-crisis levels (Table 1). The latest crisis, aka Great Recession, has accelerated this declining trend in recent years.

Interestingly, when looking at gross employment statistics, the deterioration of economic performance appears to have surprisingly modest impact on the labour market. For instance, the unemployment rate increased rapidly during the Asian financial crisis but decreased quickly and stabilized around 2-3 per cent. This means just about 1 per cent point increase in unemployment rate compared to the pre-crisis level, which is relatively a small change. Other employment figures suggest similar stability. Both employment ratio and labour market participation ratio have been stable, although with about 1 per cent point decrease in both cases. This overall modest but declining trend is in contrast with increasing trends in women employment.

**Table 1 Trends in major economic and social indicators**

|      | Real GDP growth rate (percentages) | Unemployment rate (percentages) |       | Employment (thousand) | Employment to population ratio (percentages) |       | Labour participation rate (percentages) |       |
|------|------------------------------------|---------------------------------|-------|-----------------------|----------------------------------------------|-------|-----------------------------------------|-------|
|      |                                    | Total                           | Women |                       | Total                                        | Women | Total                                   | Women |
| 1994 | 8.8                                | 2.5                             | 2.0   | 19,848                | 60.1                                         | 46.9  | 61.6                                    | 47.8  |
| 1995 | 8.9                                | 2.1                             | 1.7   | 20,414                | 60.6                                         | 47.6  | 61.9                                    | 48.4  |
| 1996 | 7.2                                | 2.0                             | 1.6   | 20,853                | 60.8                                         | 48.1  | 62.1                                    | 48.9  |
| 1997 | 5.8                                | 2.6                             | 2.3   | 21,214                | 60.9                                         | 48.6  | 62.5                                    | 49.8  |
| 1998 | -5.7                               | 7.0                             | 5.7   | 19,938                | 56.4                                         | 44.4  | 60.6                                    | 47.1  |
| 1999 | 10.7                               | 6.3                             | 5.1   | 20,291                | 56.7                                         | 45.2  | 60.6                                    | 47.6  |
| 2000 | 8.8                                | 4.1                             | 3.3   | 21,156                | 58.5                                         | 47.0  | 61.0                                    | 48.6  |
| 2001 | 4.0                                | 3.8                             | 3.1   | 21,572                | 59.0                                         | 47.7  | 61.3                                    | 49.2  |
| 2002 | 7.2                                | 3.1                             | 2.5   | 22,169                | 60.0                                         | 48.4  | 61.9                                    | 49.7  |
| 2003 | 2.8                                | 3.4                             | 3.1   | 22,139                | 59.3                                         | 47.4  | 61.4                                    | 48.9  |
| 2004 | 4.6                                | 3.5                             | 3.1   | 22,557                | 59.8                                         | 48.3  | 62.0                                    | 49.8  |
| 2005 | 4.0                                | 3.5                             | 3.1   | 22,856                | 59.7                                         | 48.4  | 61.9                                    | 50.0  |
| 2006 | 5.2                                | 3.3                             | 2.8   | 23,151                | 59.7                                         | 48.8  | 61.7                                    | 50.2  |
| 2007 | 5.1                                | 3.0                             | 2.4   | 23,433                | 59.8                                         | 48.9  | 61.7                                    | 50.1  |
| 2008 | 2.3                                | 3.0                             | 2.4   | 23,577                | 59.5                                         | 48.7  | 61.4                                    | 49.9  |
| 2009 | 0.3                                | 3.4                             | 2.7   | 23,506                | 58.6                                         | 47.7  | 60.7                                    | 49.0  |
| 2010 | 6.3                                | 3.4                             | 2.9   | 23,829                | 58.7                                         | 47.8  | 60.8                                    | 49.2  |
| 2011 | 3.6                                | 3.0                             | 2.7   | 24,244                | 59.1                                         | 48.1  | 60.9                                    | 49.4  |

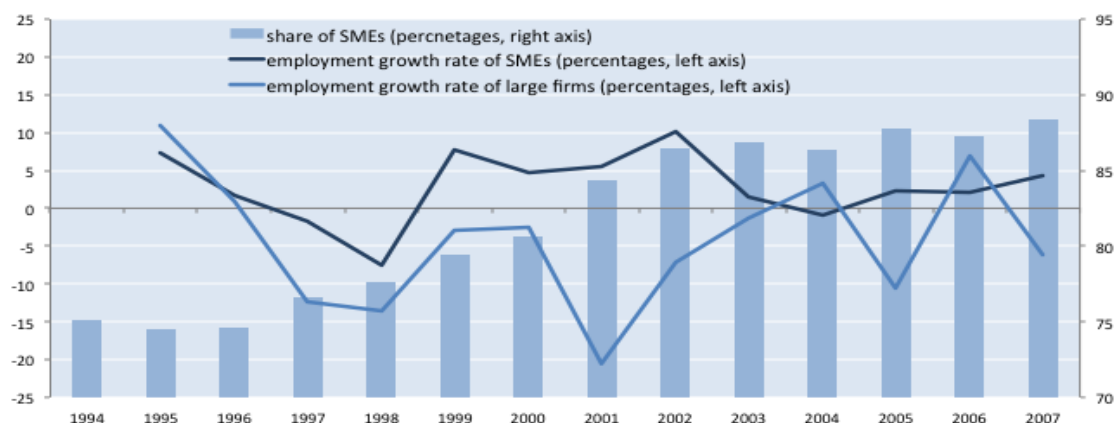
Source: Korea National Statistical Office, Economically Active Population Survey; Bank of Korea, Economic Statistic System.

However, these macro trends in employment hide significant changes in the structure of employment towards further fragmentation of employment along multiple and complex dimensions.

### 2.1.1. Employment structure – the growing importance of SMEs, service sector and non-regular employment

One critical change in employment structure is the growing importance of SMEs in their share of employment (Figure 1). Traditionally, large firms, in particular the affiliates of *Chaebol*, were the source of job creation, but the 1997 crisis marked the end of this pattern, as their contributions to job creation have been negative. Then, the “engine of job creation” has since shifted gradually to SMEs, and as a result, the share of employment in large firms was reduced from 25 per cent in 1996 to only 12 per cent in 2007.

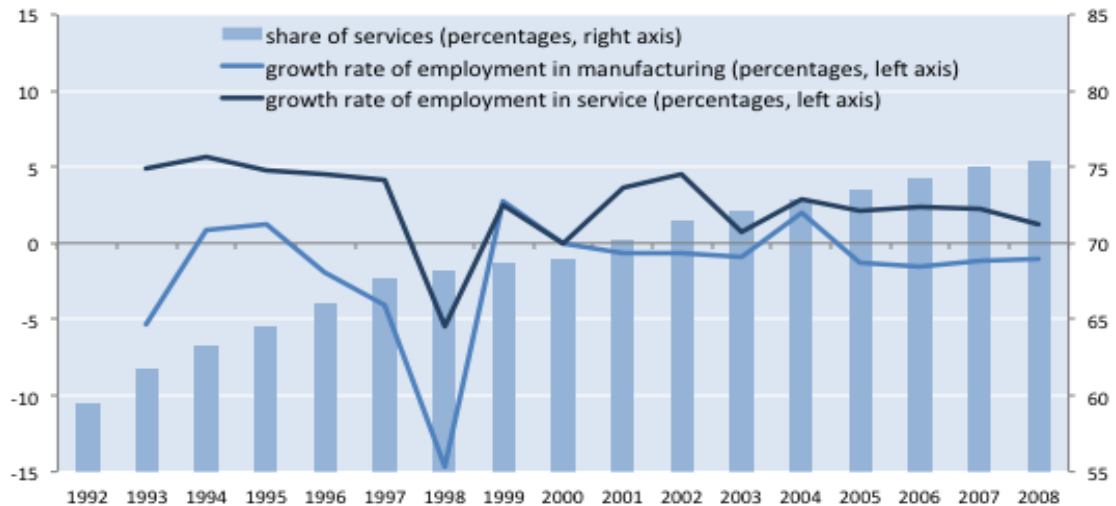
**Figure 1 Who is the engine of job creation? : Employment creation by large enterprises and SMEs, 1994-2007**



Source: Korea Federation of Small and Medium Business, Statistics of Small and Medium Enterprises.

Another notable change in employment structure is the expansion of the services sector, or “de-industrialization”. As the manufacturing sector has lost its status of “engine of employment creation” (e.g., during the developmental period of the 1960s to the early 1990s), the share of service industries in total employment increased substantially from about 60 per cent in 1992 to almost 75 per cent of the total employment in 2008 (Figure 2).

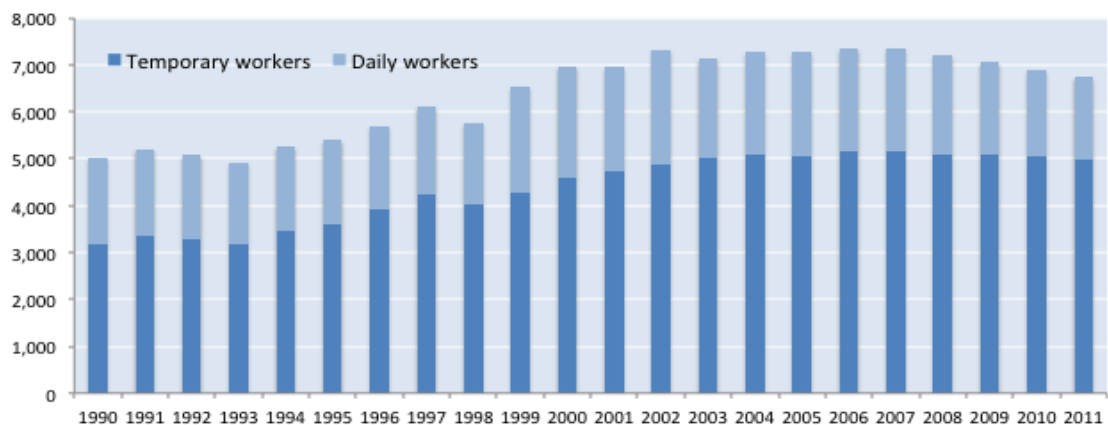
**Figure 2 Who is the engine of job creation? Employment creation by sector, 1993-2008**



Source: Korea National Statistical Office, Economically Active Population Survey.

Finally, these structural shifts in employment have been accompanied by increase in number of non-regular workers, notably temporary and daily workers in Korea (Figure 3).<sup>5</sup> According to the Economically Active Population Survey (EAPS), the growing trend accelerated after the 1997 financial crisis. Despite some reduction in the number of these workers in recent years, it still remains much higher than the pre-crisis level. We will discuss this issue in greater detail in the next section.

**Figure 3 Trends in temporary and daily workers, 1990-2011 (thousand)**



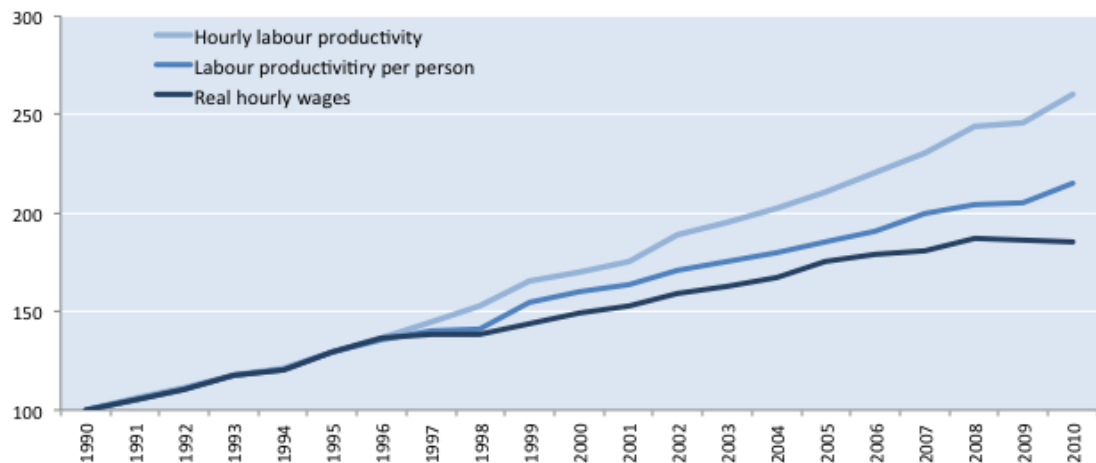
Source: Korea National Statistics Office, Economically Active Population Survey.

<sup>5</sup> As the data for the non-regular workers classified by type of employment, which are provided by the Economically Active Population Survey, Supplements, are available only from 2002, the classification by employment status from the Economically Active Population Survey is used here to capture the long-term trend of non-regular type of workers.

### 2.1.2. Labour earnings: lower growth and widening inequality

These changes in employment structure have had serious impacts on both the level and distribution of labour earnings. In fact, it is the quality of employment that the structural changes since the 1997 financial crisis have impacted most dramatically. With the growing employment share of SMEs and the service sector which tend to offer relatively low wages, wage growth has been much slower than before. More importantly, the close linkage between wage growth and labour productivity growth which characterized the pre-crisis period have been broken so that there has been a consistent and growing gap between the two (Figure 4). These discrepancies, which imply the strong tendency of wage moderation in the post-crisis period, have shifted functional income distribution in favour of capital, thereby reducing the labour income share quite considerably.

**Figure 4 Productivity-wage gaps in Korea (Base year = 1990)**



Source: Authors' calculation based on data of the Korea National Statistics office.

The shift in the functional income distribution (i.e. falling labour income share) was accompanied by increases in personal income distributions in terms of both wages and income, hence, widening inequality in both types of income distribution.

As regards wage inequality, the incidence of low pay (defined as the proportion of employees who are earning less than two thirds of the median wages) is a useful indicator (see Lee and Sobeck, 2012). Until the 1997 crisis, the low-pay incidence had been declining significantly, thanks to the strengthening of workers' bargaining power in the massive drive to unionization and collective bargaining, combined with the introduction of statutory minimum wages (Hwang and Lee, 2012). However, this trend was reversed during the 1997 crisis and an increasing trend continued afterwards. As of 2010, low pay affected 26.3 per cent of wage earners, which is one of highest among Organisation for Economic Co-operation and Development (OECD) countries (Figure 5) (ILO, 2010; OECD, 2010).

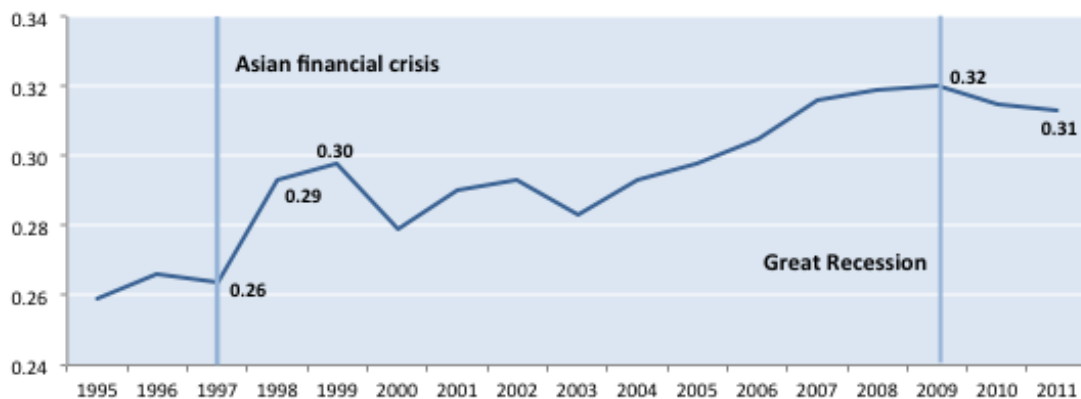
**Figure 5 Trends in the incident of low pay in Korea, 1986-2010 (percentages)**



Source: Hwang & Lee (2012), based on data of Korea National Statistics office and Ministry of Employment and Labor.

Trends are quite similar in income distribution. The 1997 financial crisis affected low-income households disproportionately and their relative income situation did not improve much in the post-crisis period. Income disparity among the Korean urban households (measured in Gini coefficients) has widened dramatically since the 1997 financial crisis and was not reduced during the post-crisis period, except for a very short period of re-adjustment (Figure 6). Of course, these trends in inequality in Korea are the outcome of a wide range of factors, including skill-based technological changes and globalization (Ahn et al., 2007; Ok et al., 2007; Seo et al., 2008). However, as will be discussed later, policy shifts towards labour market deregulation since the 1997 crisis have been a key factor.

**Figure 6 Gini coefficients for the Korean economy, 1995-2011**



Source: Bank of Korea, Economic Statistic System.

## 2.2. Policy shifts toward labour market deregulation: Legislative and policy changes since the 1997 financial crisis

So far we have shown that the labour market has seen further segmentation since the 1997 financial crisis, particularly along SMEs (versus large enterprises) and non-regular employment (versus regular employment), which has created higher vulnerability and widening inequality. However, these labour market outcomes need to be understood in the context of a series of policy shifts which started with the crisis.

### 2.2.1. Labour market flexibilization

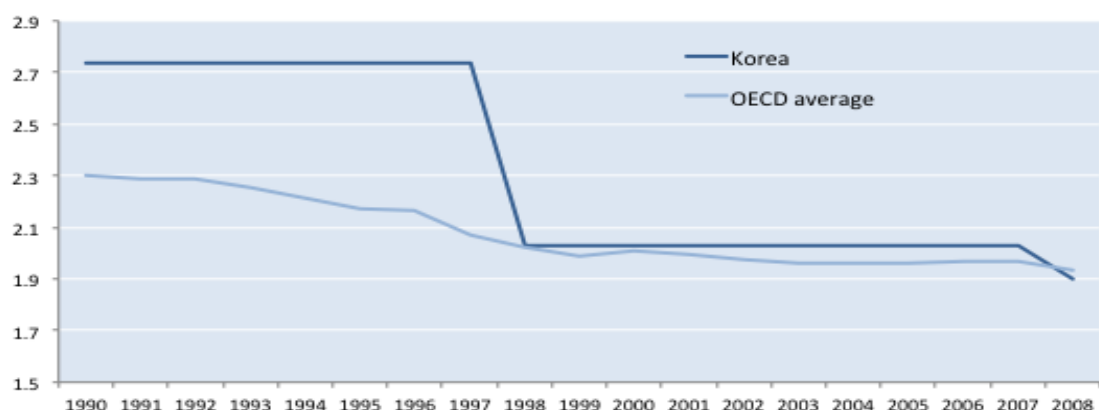
The need for economic restructuring after the crisis, under the pressure from international financial institutions, placed labour market flexibility on top of the policy agenda. Thus, when the Tripartite Commission was set up for the first time in the history of Korea in order to develop a social pact, its discussion was heavily focussed on the issue of collective dismissal and dispatched workers. The labour laws were revised accordingly.

Collective dismissal was recognized by the revised labour law in case there are “urgent managerial needs”. According to the law, the “urgent managerial needs” include the transfer, merger and acquisition aiming at preventing the aggravation of financial difficulties.<sup>6</sup> Some safeguards were also specified, including: the selection of employees for layoff by fair and rational criterion (in particular, any gender discrimination is prohibited); the notice period of the minimum of 60 days; the requirement of companies to make all possible efforts to re-employ the laid-off when new demand for hiring arises.

The practice of dispatching workers also got legal recognition. The ‘Act relating to Protection, etc., for Dispatched Workers’ (adopted in February 1998) provided a legal basis to the already widespread business practice of using dispatched workers, in allowing firms the worker dispatch undertaking for tasks that require specialized knowledge, techniques or experiences (except direct production tasks in the manufacturing), in cases of vacancies due to child birth, diseases or injuries, or of needs for supplement of personnel on the temporary and non-regular basis excluding specific activities. On the other hand, the law provided measures to protect dispatched workers and to prevent abuse of such employments, by prohibiting use of replacement workers for tasks interrupted by the industrial disputes and discrimination of this type of worker from others undertaking the same tasks.

These reforms, in particular the revision of the labour law regarding with the collective dismissals, had an immediate and significant impact on the level of employment protection. For instance, OECD’s Employment Protection Legislation (EPL) indicator for Korea used to be much higher than the OECD average but the legal revisions removed such gap completely (Figure 7).

Figure 7 EPL indicators for Korea: overall, 1990-2008



Source: OECD Employment Protection Legislation Indicators.

<sup>6</sup> The old labour law allowed collective dismissals when there are “urgent managerial needs”. However, as there were not any precision about these latter, the legal justification of collected dismissals had been earned on the basis of the judicial precedents.

While the legislation in 1998 was somewhat restrictive by allowing temporary agencies to operate in only 26 specified occupational areas, it remained liberal for fixed-term contracts by not specifying the maximum duration of fixed-term contracts and restrictions of contract renewal. Therefore, it remained legal until 2007 to hire workers on fixed-term contracts for an indefinite duration. As a result, the share of non-regular workers among total waged workers rose consistently over the long term.

### 2.2.2. Re-regulating non-regular worker, but only partially

Over the 2000s, there have been discussions on how to restrain the prevalence of non-regular workers and protect their working conditions. Eventually, two bills on non-regular employment (*the Act on the Protection, etc., of Fixed-term and Part-time Employees* and *the Act on the Protection, etc., of Dispatched Employees*) were passed in December 2006. They were put into effect eight months afterward from July 2007. The primary change introduced in the 2007 reform was to limit the employment period for fixed-term workers from an indefinite duration to two years.<sup>7</sup> If an employer uses fixed-term workers for more than two years, the workers shall be considered, in principle, as regular workers. New fixed-term contracts signed in July 2007 and onward are subject to the new regulation of two-year maximum duration, while the contracts formed earlier are regarded as signed on July 2007. These two acts, together with the revised *Labour Relations Commission Act*, are commonly called non-regular workers protection law (Box 1).

#### Box 1: Main features of the non-regular workers protection law in Korea

- *Act on the Protection, etc., of Fixed-term and Part-time Employees* prohibits undue discrimination against non-regular workers (fixed-term, part-time or temporary agency workers). The law has also put in place the procedures for seeking a remedy for discrimination through the Labour Relations Commission. If employers fail to comply with a confirmed remedial order, they are punished by a fine for negligence not exceeding KRW 100 million, and in this case, the burden of proof is imposed on the employers.
- *Act on the Protection, etc., of Fixed-term and Part-time Employees* limits the employment period for fixed-term workers to a maximum of two years. If an employer uses fixed-term workers for more than two years, the workers shall be considered, in principle, as regular workers.
- On the issue of part-time workers, *Labour Standards Act* limits the overtime work for part-time workers up to a maximum of 12 hours per week in an effort to regulate the use of part-time workers for long-hour.
- In the case of dispatched workers, *Act on the Protection, etc., of Dispatched Workers* regulates the scope of occupations in which employers are allowed to employ temporary agency workers. The law permits 197 occupations based on the Korean Standard Classification of Occupations.
- *Act on the Protection, etc., of Dispatched Workers* also stipulates that the period in which an employer can use a dispatched worker is limited to less than two years, whereas when the duration of employment exceeds two years, the employer is obliged to acquire him/her as an employee. Employers that do not fulfill this obligation can be subject to a fine of up to KRW 30 million per dispatched worker.

<sup>7</sup> There are a few exceptions of fixed-term contracts to which the two-year maximum period does not apply. They include cases of employing workers aged 55 or older at the time of signing a fixed-term contract, workers holding doctoral degrees or other highly technical and professional qualifications, part-time instructors in tertiary education institutions, workers subject to contract durations specified by other special laws, etc.

Limitations on the period of retainment and prohibition of discriminatory practices have been applied to companies or work sites that have at least five workers. Such rules are to be implemented in stages according to the size of the business and the nature of the business (whether it is public or private). Provisions on limitations on the service period of fixed-term workers have been applied to employment contracts established after implementation of the law and have been effective since July 2009. Provisions on prohibition of discrimination have been effective immediately upon implementation of the law for business sites of 300 or more workers, as well as the public sector. For business sites with at least 100 and less than 300 workers, the provisions have been effective since July 2008, while for business sites with at least 5 and less than 100 workers, the provisions have been effective since July 2009.

However, the non-regular workers protection law seems to have limitations to effectively protect the non-regular workers at the small companies because of the following reasons:

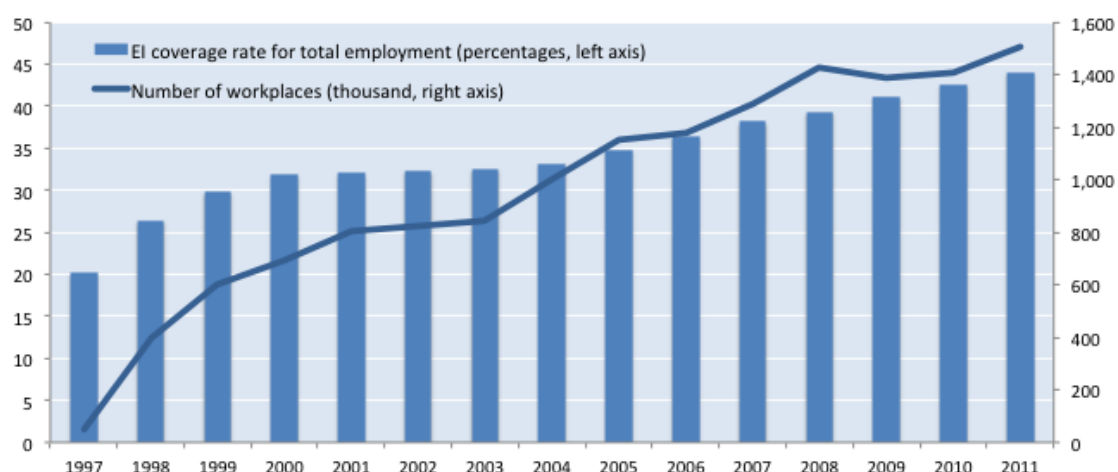
- (1) the law is applied only to business sites of at least 5 workers, meaning that non-regular workers at business sites of 1-4 workers, where there are the highest portion of non-regular workers, are excluded; and
- (2) among non-regular work, only a certain type is applicable, meaning that workers by independent contract workers (673 thousand workers), workers in special types of employment (614 thousand workers), at-home workers (75 thousand workers), and daily (on-call) workers (962 workers) are excluded.

### *2.2.3. Improving social safety net: Growing coverage with loopholes*

Given the potentially damaging impacts of labour market flexibilization on income security of workers, the government had taken a balancing act by improving social safety net. Indeed, one positive development since the 1997 financial crisis is that it provided a turning point for social security system in Korea. This system, which had gradually improved with the economic growth before the crisis, swiftly expanded because of the urgent need to secure social safety net during the crisis (Hur 2002). The expansion of the social safety net maintained momentum in the post-crisis period.

Arguably, the most significant development in this regard is the expansion of the employment insurance system (EIS) which includes the unemployment benefits system and active labour market policies (also maternity protection since 2002). EIS was limited to large and medium-sized enterprises before the crisis but was quickly extended to all enterprises in 1998, just one year after the crisis broke out. As Figure 8 shows, the coverage of EIS witnessed rapid and massive increases, from a mere 50 thousand workplaces in 1997 to more than 1.5 million in 2011.

**Figure 8 Expansion in the coverage of employment insurance**



Source: Ministry of Employment and Labor (2012).

Yet there are serious limitations with EIS, which have created another layer of labour market segmentation in Korea. First, the coverage was confined to regular workers. Although, since 2004, EIS has been applicable to non-regular workers (such as temporary and part-time employees working for more than 60 hours a month), most temporary and part-time workers still remain uninsured. Second, self-employed workers are effectively excluded, although participation on a voluntary basis is a possibility. Note that self-employment accounts for more than 30 per cent of total employment and the incidence of working poverty is exceptionally high among the self-employed (Yee 2007). Thus, the capacity for EIS to provide safety net for most vulnerable workers has been significantly compromised. Thirdly, the level and duration of benefits is also relatively restrictive. As Table 2 shows, the duration of benefits depend on age and the period of service (tenure), ranging from the minimum of 90 days to the maximum of 240 days. Also, the replacement rate is relatively low at 50 per cent of average income for the preceding 12 months.

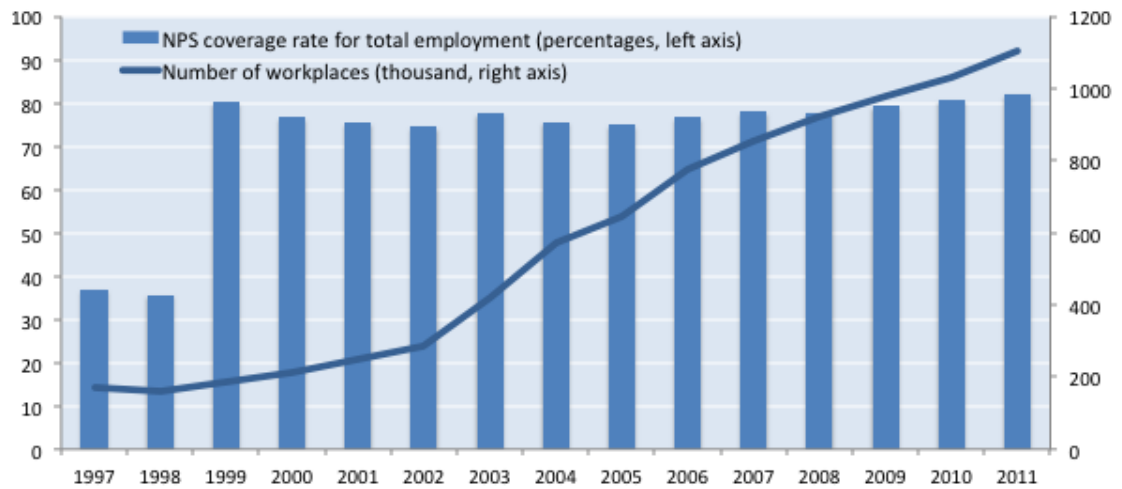
**Table 2 Benefit duration by employment periods and workers' age (days)**

| Period of service<br>Tenure<br>(year) |         |       |       |        |         |
|---------------------------------------|---------|-------|-------|--------|---------|
|                                       | Under 1 | 1 - 3 | 3 - 5 | 5 - 10 | Over 10 |
| Workers' Age                          |         |       |       |        |         |
| Under 30                              | 90      | 90    | 120   | 150    | 180     |
| 30 - 50                               | 90      | 120   | 150   | 180    | 210     |
| Over 50                               | 90      | 150   | 180   | 210    | 240     |

Source: Ministry of Employment and Labor (2012.)

Another important pillar of the social security system in Korea is the National Pension Scheme (NPS) in Korea which has also seen massive expansion since the crisis (see Figure 9). It was initially established in 1960 for the civil service and armed forces, extended its coverage gradually over the years. As of 2011, a total of 19,885,911 workers, accounting for 82 per cent of total employment, and 1,103,570 workplaces were covered by the national pension scheme. Yet this system has the constraints similar to the EIS as discussed above. Non-regular workers tend to be excluded as they are often not qualified as an “employee” due to their high turnover in the labour market. The coverage of self-employment is also very low. As of 2011, 33.1 per cent of self-employed workers, temporary and daily workers, and workers in small firms with less than five employees did not contribute to the pension scheme. In addition, daily workers and part-timers working less than 80 hours a month are not covered. As a result, the NPS fails to provide a safety net for those who are most in need of income security.

Figure 9 The coverage of the National Pension Scheme by employment and workplaces



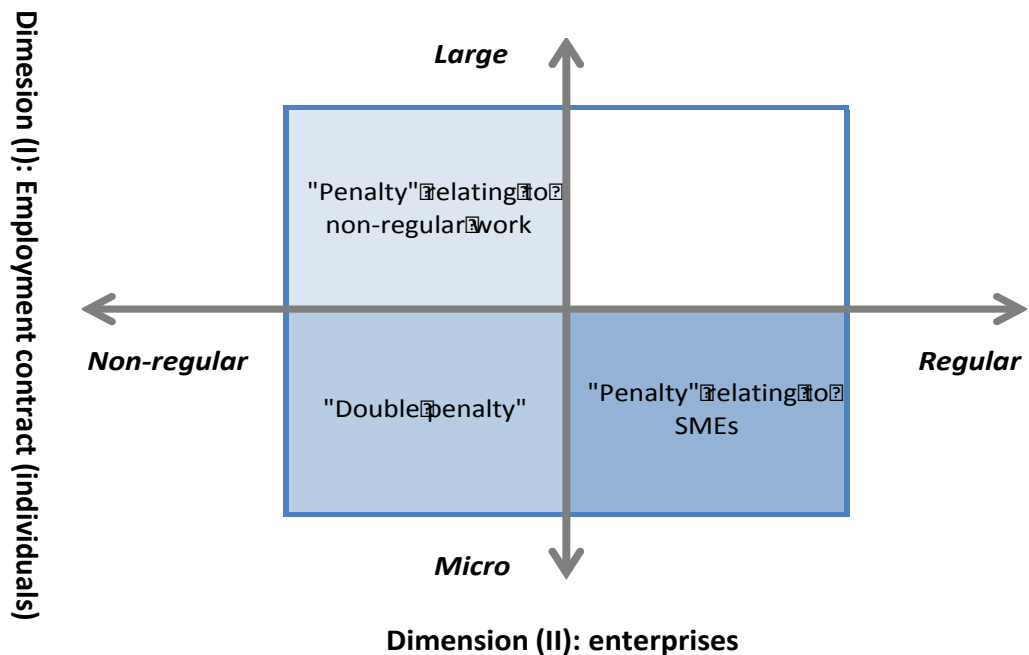
Source: National Pension Service (2012).

### 3. Dual dimensions (I): non-regular work

The analysis so far suggests that the increasingly important dimensions of labour market segmentation particularly since the 1997 financial crisis are non-regular employment and SMEs. This section will examine non regular employment, while the dimension of SMEs will be analysed in the next section. As will be clear in our analysis, these dual dimensions are strongly interlinked, as the expansion of SMEs in recent year has contributed to increases in non-regular employment.

Our conceptual framework concerning dual dimensions is illustrated below (Figure 10).

Figure 10 Dual dimensions and double penalty



### 3.1. Definition, trends and determinants

#### 3.1.1. Two definitions and different estimates

There is no commonly accepted definition of non-standard employment, and in fact it varies considerably across countries, reflecting specific circumstances of their labour markets. Generally speaking, non-standard employment refers to types of employment which differ significantly from the standard employment which is defined as full-time, permanent salaried employment. Thus, non-standard employment typically includes part-time work, work of a fixed duration (temporary or agency-related employment), self-employment and non-remunerated domestic work. A number of other terms, including *atypical*, *non-regular* and *contingent* are used to describe “non-standard” forms of employment.

In Korea, the term non-regular worker has been used mostly commonly. It used to be defined rather loosely, mainly capturing marginalized workers, including temporary workers and daily workers. This classification focused on formal “employment status”, without considering different treatments within each category of workers. As is shown earlier, the share of non-regular workers rose drastically since the financial crisis, exceeding half of total paid workers from 1999 (see Figure 3). Not surprisingly, debates were intensive over the causes of this rapid increase in non-regular work and possible policy remedies. Through these debates, it became evident that the current definition needed to be further articulated for meaningful policy discussion and development.

In 2002, a tripartite agreement was reached on the new definition of non-regular work which reflects the reality better (see Box 2). According to the new definition (which is called classification according to “employment type”), non-regular workers are classified in three categories: contingent workers, part-time workers, and atypical workers (see

Table 3). Under atypical workers, a number of subcategories of workers are identified to capture complex employment relationships (e.g., dispatched workers, subcontract workers, independent contract workers, at-home workers, and daily (on-call) workers. They are mostly new types of workers who increased rapidly after the Asian financial crisis.

### Box 2: Agreement on definition of non-regular workers by tripartite committee

To resolve the dispute over the different criteria used in defining the scope of non-regular workers, in July 2002, the tripartite committee agreed on a definition of non-regular workers.

The definition was established primarily according to employment type in consideration of employment contract period, method of service provision, continuity of employment, and working hours, as follows (1) “contingent workers”, (2) “part time workers”, (3) “atypical workers” (temporary agency workers, independent contract workers, workers in special types of employment, at-home workers, and daily (on-call) workers). In addition, the group of workers, which do not belong in the above three categories, with an insecure employment status and excluded from protection by the Labour Standards Act and various social security benefits (most often the point of controversy when calculating the size of the non-regular workforce) were defined as “disadvantaged workers”.

Table 3: Employment classifications in Korea

|                   | Classification | Criteria                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                    |
|-------------------|----------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Employment status | Regular        | <ul style="list-style-type: none"><li>• Employee with contract of at least one year.</li><li>• Hired according to company HR regulations and subject to severance and bonus payments.</li></ul>                                                                                                                                                                                                                                                                                                                                                                                                             |
|                   | Temporary      | <ul style="list-style-type: none"><li>• Employee with contract of at least one month, less than one year.</li><li>• Company employee regulations are not applied, and severance and bonus payments are not made.</li></ul>                                                                                                                                                                                                                                                                                                                                                                                  |
|                   | Daily          | <ul style="list-style-type: none"><li>• Employee with contract of less than one month.</li><li>• Company employee regulations are not applied, and severance and bonus payments are not made.</li></ul>                                                                                                                                                                                                                                                                                                                                                                                                     |
| Employment type   | Regular        | <ul style="list-style-type: none"><li>• Full-time worker with no prescribed contract period.</li></ul>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                      |
|                   | Contingent     | <ul style="list-style-type: none"><li>• Worker with prescribed contract period.</li></ul>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                   |
|                   | Part-time      | <ul style="list-style-type: none"><li>• Worker with shorter working hours than other workers performing the same task.</li></ul>                                                                                                                                                                                                                                                                                                                                                                                                                                                                            |
|                   | Atypical       | <ul style="list-style-type: none"><li>• Dispatched workers: workers who are employed by an employment agency to provide services to a third party.</li><li>• Subcontract workers: workers who work in other workplaces although they are compensated by employers.</li><li>• Independent contract workers: workers who work dependently but not hired.</li><li>• At-home workers: workers who work in their own house, but the nature of work is the same as that of workers in factory.</li><li>• Daily (on-call) workers: workers who work according to the demands of work without a contract.</li></ul> |

With the adoption of the new definition, a series of special surveys on non-regular workers were implemented and then gradually regularized as part of the standard labour force survey (i.e., Economically Active Population Survey). The “Supplement Survey by Employment Type”, which was pilot tested in 2002, is the key result of this statistical endeavour. It provides solid statistical basis for detailed analysis of the status and size of

workers in various employment forms according to the new definition of non-regular work. Since 2007, this survey has been conducted twice a year (March and August).

However, the issues were not entirely resolved, and various and competing analysis and estimates have been put forward. In particular, some proposed a matrix approach which estimates the size of non-regular work considering both employment type and status. In this approach, some of regular workers (under the classification by the employment type) are considered to be a de facto non-regular worker if they are not subject to the company's employee regulations and do not receive in-house benefits (Kim, 2011). This approach received strong support from academics and policy circles. As of August 2011, the size of the non-regular workers purely by formal employment status (known as the government's official estimate) was around 6 million or 34.0 per cent of total paid workers, but the new innovative matrix approach produced a much higher estimate at 8.7 million or 49.4 per cent of total paid workers (Table 4).

**Table 4: Size of non-regular workers according to the different classifications, 2011 (thousand, percentage)**

|                                                    |                     | <b>Classification by employment type</b> |                                                     |                      |
|----------------------------------------------------|---------------------|------------------------------------------|-----------------------------------------------------|----------------------|
|                                                    |                     | Regular                                  | Non-regular<br>(Contingent, part-time,<br>atypical) | <b>Total</b>         |
| <b>Classification<br/>by employment<br/>status</b> | Regular             | 8,857 (50.6)                             | 1,853 (10.6)                                        | <b>10,710 (61.2)</b> |
|                                                    | Temporary,<br>daily | 2,701 (15.4)                             | 4,099 (23.4)                                        | <b>6,800 (38.8)</b>  |
|                                                    | <b>Total</b>        | <b>11,558 (66.0)</b>                     | <b>5,952 (34.0)</b>                                 | <b>1,7510 (100)</b>  |

Source: Kim (2011), based on data of Korea National Statistics Office, Economically Active Population Survey (EAPS) Supplement.

### *3.1.2. Trends in non-regular employment*

Then, what has been the overall trend in non-regular work in Korea? Whatever definition and estimation method is used, the overall trend is obvious: Significant increase since the 1997 financial crisis. Massive restructuring during the crisis period affected regular workers and also led to a growing use of non-regular workers (such as temporary and part-time workers) for making hiring and firing easier in case of workforce adjustment. For instance, the proportion of non-regular work under the classification by "employment status" rose from 27.4 per cent in 2002 to 34.2 per cent in 2011 (Figure 11). The period of 2002 to 2004 in particular witnessed a surge in non-regular workers due to another round of comprehensive restructuring of the economy with downsizing, merging, and acquisition of firms (Shin, 2012).

Figure 11: Trends in non-regular work by employment status classification, August 2001-2011



Source: Korea National Statistics Office, Economically Active Population Survey (EAPS) Supplement

It is also important to note that the trend has been stabilized in recent year, with some sign of reversal since 2007. The causes of this possibly reversing trend is still very much in debate in Korea, but some attributed it to the new act on non-regular workers enacted in December 2006 which limits the maximum period of fixed-term contract to two years (Keum, 2012). According to this law, workers who are working more than two years on a temporary contract shall be considered as working on an ‘unlimited contract’ and be thus granted the standard job protection measures.

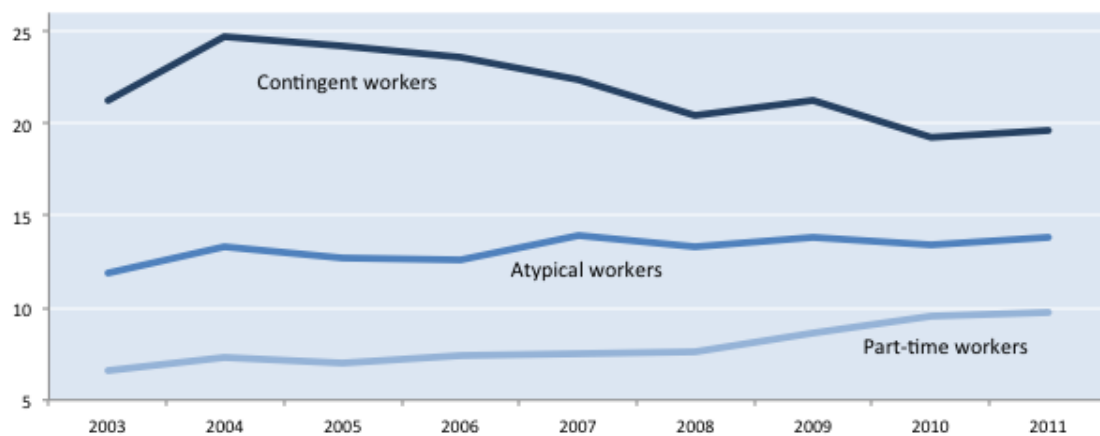
The proportion of the part-time workers is small compared to other types of non-regular employment, but it grew more than two-fold in respect to the entire percentage of non-regular employment, with a relatively steeper rise in 2009 and 2010. In 2011, part-time workers amounted to 1.7 million, which was 0.5 million more as compared to 1.2 million of 2008. Considering the very high rate of non-regular workers in Korea, the low rate of part-time workers indicate that the most of non-regular workers are working as full-time non-regular workers (Shin, 2012).

Moreover, the percentage of involuntary part-time worker is climbing. Among part-time workers, the share of involuntary part-time workers rose from 52.9 per cent in 2006 to 55.3 per cent in 2011.<sup>8</sup> This implies that the increase of non-regular workers since 2007 has occurred mostly due to the growing number of part-time workers.

A similar trend can be found if we use the classification by “employment type”. In the case of contingent workers, they increased considerably until early 2000s and then decreased in recent years. Yet, other types of non-regular workers continued to increase. The proportion of atypical workers, including dispatched workers, subcontracting workers, independent contract workers, workers in special types of employment, at-home workers, and daily (on-call) workers, has seen a steady growth (Figure 12). Subcontract workers in particular doubled from 332,000 in 2002 to 672,000 in 2011. Large companies in manufacturing sector mostly used these subcontract workers. In the manufacturing industry, 54.6 per cent of firms with more than 300 employees used in-house subcontracting workers in 2008 (Eun, 2012). Most recently, part-time workers have been on increase, especially since the Great Recession.

<sup>8</sup> Korea National Statistical Office, Economically Active Population Survey (EAPS).

Figure 12: Trends in non-regular work by employment type, 2003-2011 (percentages)



Source: Korea National Statistics Office, Economically Active Population Survey (EAPS) Supplement.

### 3.1.3. Who are non-regular workers?

Then, who are non-regular workers? As is in other countries, non-regular work tends to be concentrated among certain demographic groups and occupations/industries in Korea. First, non-regular work is highly gendered. The incidence of non-regular work for women (42.8 per cent in 2011) is far higher than that for men (27.8 per cent) (Table 5). Recent increases in non-regular work for women are associated with rapid increases in part-time work, as mentioned above.

**Table 5 Incidence of non-regular worker by employment status classification: EAPS Supplements, 2001-2012**

|                         |                                 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 |
|-------------------------|---------------------------------|------|------|------|------|------|------|------|------|------|------|------|
| Gender                  | Men                             | 21.8 | 23.5 | 27.6 | 32.2 | 31.5 | 30.4 | 31.5 | 28.8 | 28.2 | 27.1 | 27.8 |
|                         | Women                           | 35.4 | 33.4 | 39.5 | 43.7 | 43.7 | 42.7 | 42.1 | 40.8 | 44.1 | 41.8 | 42.8 |
| Age group               | 15-24                           |      |      | 39.8 | 40.3 | 44.2 | 42.2 | 43.4 | 44.8 | 47.5 | 48.7 | 48.7 |
|                         | 25-54                           |      |      | 28.4 | 33.7 | 32.7 | 31.4 | 31.6 | 29.2 | 29.2 | 27.5 | 28.4 |
|                         | 55-64                           |      |      | 51.3 | 54.6 | 54.9 | 54.3 | 55.4 | 52.5 | 54.9 | 51.7 | 50.7 |
|                         | 65 and over                     |      |      | 72.1 | 74.0 | 69.1 | 75.3 | 69.8 | 70.9 | 78.9 | 77.7 | 77.2 |
| Occupation <sup>a</sup> | White-collar                    |      |      |      | 25.7 | 24.1 | 24.5 | 24.6 | 22.0 | 20.8 | 20.9 | 22.1 |
|                         | Pink-collar                     |      |      |      | 43.9 | 45.5 | 42.3 | 43.1 | 42.1 | 43.0 | 42.8 | 44.4 |
|                         | Blue-collar                     |      |      |      | 34.0 | 32.2 | 31.4 | 31.9 | 29.9 | 29.9 | 27.5 | 28.5 |
|                         | Unskilled                       |      |      |      | 62.9 | 64.9 | 62.8 | 62.5 | 62.7 | 68.0 | 63.5 | 63.7 |
| Industry                | Agriculture, forestry & fishing |      |      |      | 75.5 | 78.1 | 77.6 | 67.8 | 67.8 | 67.3 | 70.6 | 69.5 |
|                         | Mining & quarrying              |      |      |      | 18.2 | 14.3 | 15.4 | 18.8 | 13.6 | 15.0 | 15.8 | 9.1  |
|                         | Manufacturing                   |      |      |      | 23.3 | 20.7 | 20.1 | 20.5 | 16.6 | 16.2 | 14.9 | 15.6 |
|                         | Construction                    |      |      |      | 63.2 | 63.1 | 58.1 | 57.9 | 54.9 | 54.9 | 51.8 | 51.4 |
|                         | Service                         |      |      |      | 37.8 | 38.0 | 37.1 | 37.4 | 36.0 | 37.4 | 36.1 | 37.0 |
| Education <sup>b</sup>  | Low                             |      |      | 51.2 | 55.6 | 56.8 | 55.5 | 56.7 | 55.4 | 60.9 | 57.3 | 58.3 |
|                         | Medium                          |      |      | 33.5 | 37.7 | 38.2 | 36.5 | 37.5 | 36.8 | 38.1 | 36.4 | 37.9 |
|                         | High                            |      |      | 21.4 | 27.0 | 25.5 | 25.7 | 25.9 | 23.1 | 22.6 | 22.2 | 23.2 |
| Firm size               | SMEs                            |      | 29.0 | 35.1 | 39.3 | 39.1 | 37.7 | 38.0 | 36.0 | 37.4 | 35.6 | 36.4 |
|                         | Large companies                 |      | 14.8 | 14.7 | 20.4 | 19.7 | 20.1 | 19.5 | 17.3 | 17.1 | 15.4 | 17.2 |

a) White-collar occupations include legislators, senior officials and managers; professionals; technicians and associate professionals. Pink-collar occupations include clerks; service workers; sales workers. Blue-collar occupations include skilled agricultural and fishery workers; craft and related trades workers; and plant and machine operators and assemblers. Unskilled occupations correspond to elementary occupations.

b) Low refers to under lower secondary education; medium refers to upper secondary education; and high refers to over post-secondary education.

Source: Korea National Statistics Office, Economically Active Population Survey (EAPS) Supplement; Korea Labor Institute (KLI).

In addition, young and older workers are more vulnerable to non-regular workers. This may imply that the non-regular jobs serve as entry ports into the labour market for the young workers and as a way of remaining in the labour market for the aged workers after mandatory retirement. According to a study observing the composition of regular and non-regular workers by both age and gender in Korea (Seong, 2011), in the case of men, the highest incidence of regular workers was displayed in their 30s, and the incidence of non-regular workers exceeded in their 50s or older. This was due to the fact that early retirement leads most men to engage in non-regular work at old age. On the other hand, the incidence of regular workers among women in their 20s, when they first enter the job market, was similar to that of men, but this rate dropped in their 40s, when they marry, give birth and raise children.

Non-regular workers are typically unskilled, working in agriculture, construction and the service industry (e.g. finance and insurance, business services and household services). More importantly, non-regular workers are concentrated in SMEs.<sup>9</sup> SMEs account for more than 90 per cent of non-regular employment so that the issue of non-

<sup>9</sup> SMEs in Korea typically refer to businesses with less than 300 employees.

regular work is effectively the issue of SMEs. Moreover, the incidence of non-regular workers in the small companies with less than 5 employees was 46.1 per cent in 2011, and almost half of non-regular workers are in the small companies with less than 10 employees, which have inferior working conditions (KLI, 2012).

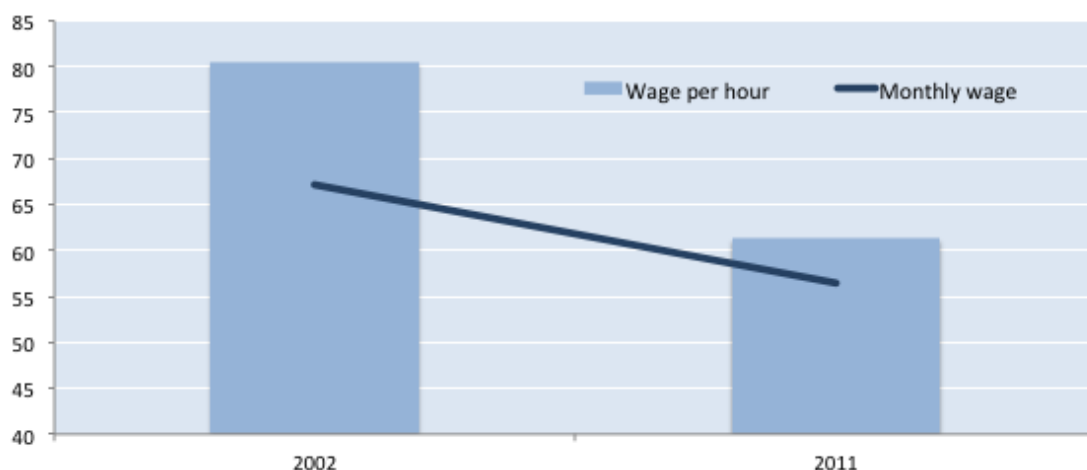
### 3.2. Non-regular employment and job quality

Given the sheer scale of non-regular workers in Korea, then, what exactly does non-regular work mean for workers and what kinds of “penalty” (or potentially, discrimination) are associated with it? Expectedly, non-regular employment is largely characterized by low pay and few benefits, few prospects for advancement, and considerable risk in terms of employment security. Non-standard workers who are lower-skilled, who may suffer from discrimination in the labour market, or who face other constraints (e.g., family responsibilities; inability to finance training that would enhance skills) may have limited economic opportunities and be restricted in their choices in the labour market. Moreover, they may not have access to union or other forms of representation. These types of “penalty” have been well observed in other countries, but their scale and extent appear to be larger in Korea.

#### 3.2.1. Employment income

Let us start with wages. Figure 13 shows that the average monthly wage of non-regular workers is only 56 per cent of that for regular workers, and average hourly wage rates for non-regular workers were only 61 per cent the level of that for regular workers in 2011. This wage gap between non-regular and regular workers has been widening over time. The ratio of average hourly wages for non-regular jobs to regular jobs decreased from 80 per cent in 2002 to 61 per cent in 2011, with most of the change taking place from 2002-03.

**Figure 13** Relative level of the average wage of the non-regular workers, 2002-2011 (regular workers = 100, percentages)



Source: Eun et al. (2008); Korea National Statistics Office, Economically Active Population Survey (EAPS) Supplement.

However, the wage gap between regular and non-regular workers might reflect other characteristics of workers and of the firms where the workers are employed, such as age, tenure, as level of education, size of firm, unionization etc. The existing studies on this issue report ambiguous results: some studies found a significant wage gap (Ahn, 2001, 2004), while others conclude a less significant and smaller wage gap (Nam, 2009). According to a survey result released by the Ministry of Employment and Labour in

2010, the hourly wage gap between regular and non-regular workers was estimated to be 12.6 per cent, controlling for these variables.

### *3.2.2. Career progression*

Some argue that non-standard employment may be a useful means for initial entry into the labour market and can speed up the transition to standard employment. Even if non-standard employment fails to generate an offer of standard employment, it may still provide relatively continuous work and may also allow individuals to acquire additional human capital, which makes them more attractive to future employers.

But others point out the risk of non-standard workers becoming trapped in a cycle of precarious and low-paid work, with potentially long-term negative effects, including poverty, lack of training and career progression, or stress caused by insecurity (Tucker, 2002).

In Korea, there has been a significant amount of research on this issue that provided different results. According to empirical research (Nam 2009), the transition rate from non-regular employment to regular employment in Korea takes up between 33 and 38 per cent, and in 2006 33.7 per cent of non-regular workers had moved into regular employment after one year. However, 48.8 per cent stayed in non-regular employment and 15.6 per cent became economically inactive or unemployed. 15.4 per cent of regular workers moved into non-regular employment or unemployment. The same study shows that the transition from non-regular to regular work is more probable in case of young, male and highly educated workers with a longer tenure in the unionized workplace, which implies that there is a high degree of heterogeneity even amongst the non-regular workers.

However, other studies are more pessimistic on this issue. According to Lee and Eun (2011), only 23.4 per cent of non-regular workers in private sector companies with more than 5 employees in 2005 became regular workers in 2006, and after the implementation of the Non-Regular Workforce Protection Act in 2009, the transition rate to regular employment increased to 26.7 per cent. Moreover, the transition usually took place in the large firms.

Although workers who have worked for longer than one year are classified as regular workers and often employed for longer by constantly renewing the contract, they are not free from dismissal.

### *3.2.3. Employment-related benefits*

Non-regular workers are not only at a relative disadvantage in terms of wages but also in terms of corporate-provided benefits, such as retirement pay, bonuses, overtime pay and paid leave. Although overtime pay should be applied to all workers, regardless of the type of employment, the actual coverage of non-regular workers remains low. According to EAPS Supplement conducted in 2011, only 38.4 per cent of non-regular workers benefit from retirement pay, compared to 78.4 per cent for regular workers. 35.5 per cent of non-regular workers get bonuses, while 80.4 per cent of regular workers benefit from bonuses in addition to their regular wage (Figure 14).

Figure 14 Coverage rate of firm-provided benefits by employment status, 2011 (percentages)



Source: Korea National Statistics Office, Economically Active Population Survey (EAPS) Supplement.

### 3.2.4. Access to social insurance

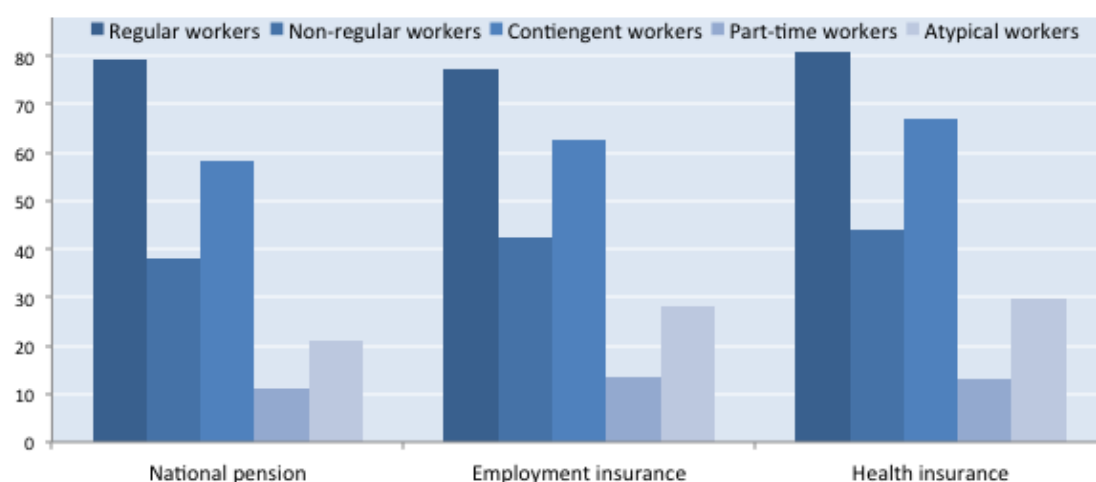
Numerous workers, particularly those in non-regular employment, are in the blind spot of the social protection system. Only 38 per cent of non-regular workers are subscribed to the national pension system, while the corresponding number is 79 per cent for regular workers. The same pattern can be found in the Employment Insurance system, where only 42 per cent of non-regular workers are subscribed compared to 77 per cent for regular workers (Figure 15).

When observing coverage rates of social insurance by employment type, the subscription rates are significantly low for part-time and atypical workers. It reveals that part-time and atypical types of employment find it difficult to access social insurance, due to the limitations of the social insurance system.<sup>10</sup>

In addition, independent workers are classified as ‘self-employed’ and are therefore legally excluded from the social insurance system, although their *de facto* status is that they are workers who would otherwise be entitled to these insurances. In the case of construction workers, multi-layered subcontracting is an impediment to implementation of social insurance. The Korean social security system has not caught up with the changes in employment practices (Yun, 2007).

<sup>10</sup> The national pension and health insurance schemes legally exclude workers that work less than 80 hours a month, and less than one month from workplace insurance programmes. Moreover, in the case of employment insurance, workers that work less than 60 hours a month and domestic workers are not eligible for the subscription.

Figure 15 Coverage rate of firm-provided benefits by employment type, 2011 (percentages)



Source: Korea National Statistics Office, Economically Active Population Survey (EAPS) Supplement.

This implies that saving social insurance contribution and costs for other firm-provided benefits constitute an important motivation for employers to hire non-regular workers.

## 4. Dual dimension (II): SMEs employment

Another important dimension of labour market segmentation is the size of enterprises. As pointed out earlier, most of non-regular workers are working for SMEs. Yet, as the situation between large enterprises and SMEs has become polarized in many respects, even regular workers in SMEs suffer from ever growing gaps in job quality. The relative deterioration of SMEs is also in a sharp contrast with their increasing proportion of employment (see Figure 1 in Section II). This section examines how labour market segmentation along with the size of enterprises has evolved and how this evolution has compounded the issue of non-regular work in Korea.

### 4.1. Chaebol-centred economic growth and polarization between large enterprises and SMEs

During the times of high economic development, Korea's industries grew in an imbalanced manner, with the *chaebols* leading the core areas of development. The growth pattern began with *chaebols'* preemptive investments in new industries, followed by SMEs. It resulted in high growth of the leading industries, such as export industries and *chaebol*-led industries, which promoted domestic demand and the growth of SMEs. In this growth model, the growth foundation of SMEs was provided through subcontracts with *chaebols*, and as the volume of such subcontract transactions increased, SMEs continued to grow within a relationship of vertical specialization.

This model began to change since the Asian financial crisis. Large companies have adopted a strategy of pursuing short term profit by reducing cost, and have increased the use of non-regular workers and expanded outsourcing. Moreover, based on market power strengthened through restructuring process, large companies have increased R&D, sought innovation, and aimed to convert from quantitative growth to qualitative growth. In contrast, SMEs with weak capacity for technological development and investment were subject to dual pressure, with stronger demands from domestic large companies to reduce

cost and global competition resulting from open markets and increased imports from low-wage countries. SMEs resorted to subcontracting to other sub-tier entities, resulting in greater dependence on low wage workers. Thus, the vertical integration between large enterprises and SMEs which used to be to a large extent mutually beneficial became more unfavourable for SMEs.

This structural shift is reflected in employment and labour productivity. As mentioned earlier, SMEs' share of employment increased rapidly, the trend which can be observed irrespective of size of SMEs (see Figure 16). However, the productivity gap between large companies and SMEs remained substantive. In the case of small enterprises (20-49 employees), their productivity was less than 40 per cent of that of the average large enterprise. Indeed, a recent study by UNESCAP (2012) shows that Korea has one of the largest productivity gaps in Asian countries.

**Figure 16 Employment and labour productivity (value added per employee) in SMEs manufacturing, 1999-2006 (large firms = 100)**

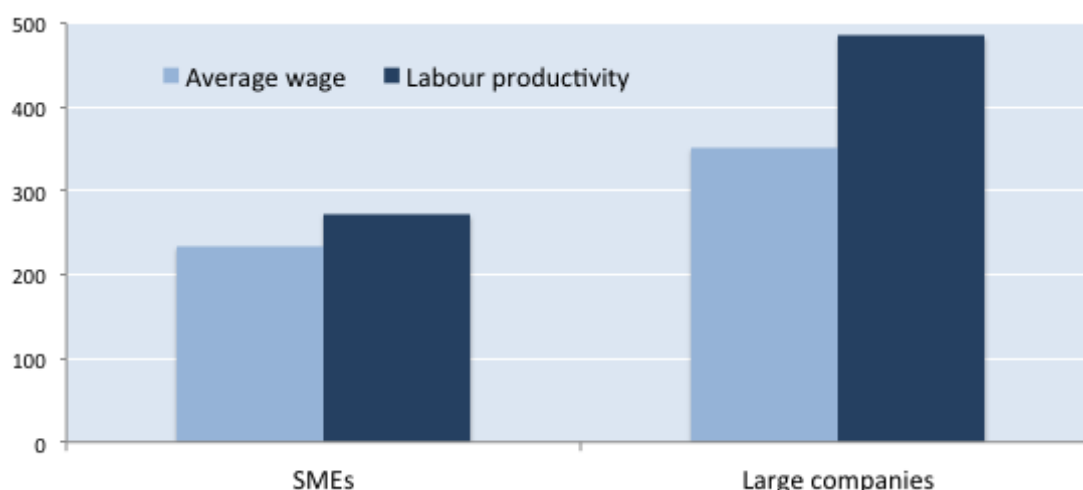


Source: Korea National Statistics Office, Mining and Manufacturing Survey.

Substantive gaps are also observed in the growth rate of labour productivity. Between 1991 and 2007, labour productivity in large enterprises increased almost five times, but the growth rate was less than three times in SMEs.

Interestingly, both types of enterprises saw wage growth lag behind labour productivity growth, but the gaps between the two were much larger in large enterprises. In other words, the wage gap between large companies and SMEs has increased consistently, yet SMEs' burden of labour cost has not been relieved, while ironically that for large companies has been reduced.

**Figure 17 Increase of average wage and labour productivity from 1991 to 2007 (percentages)**



Source: Korea National Statistics Office, Economically Active Population Survey (EAPS); Bank of Korea, Economic Statistic System; Korea Federation of Small and Medium Business, Statistics of Small and Medium Enterprises.

Such large gaps in labour productivity between large enterprises and SMEs come from a wide range of factors such as investment, technological changes, and management practices. However, one important factor is the immense pressure of cost cutting from large enterprises, especially in the case of vertical integration through subcontracting or outsourcing. In fact, the burden of labour cost of large companies could drop extensively not only because of the rapid rise in labour productivity, but also the great increase in product outsourcing, which led to a reduced number of employees (Cho & Yang, 2010). The cost of outsourced processing over total labour costs of large companies grew considerably from 32.3 per cent in 1991 to 66.5 per cent in 2007. Thus, large companies increased outsourced production to reduce the number of employees, and succeeded in reducing the burden of labour cost despite high wages.

The scale of “cost-shifting” from large enterprises to SMEs is illustrated in Table 6. Despite its increasing reliance on non-regular workers, SMEs saw significant wage increases of 56 per cent between 2001 and 2007. At the same time, the prices of raw materials for their production grew even faster by 83 per cent. This means large increases in production costs as a whole. By contrast, supply prices which SMEs offered to large enterprises dropped by 2.4 per cent and 2.3 per cent for single components and intermediate components respectively. Even for finished goods, the increase was a mere 1.6 per cent. This reveals that the pressure to lower supply costs in subcontracts was severe and prevalent. When considering the fact that SMEs’ dependence on subcontracts is high, such chronic pressure to lower supply costs damaged profits in SMEs and also eventually translated into low wages and worsening working conditions (Cho & Yang, 2010).

**Table 6 Supply prices, wages, and raw materials price in SME subcontractors, 2001-2007 (base year = 2001)**

|                                         | Supply prices for large enterprises |                         |                | Wage      | Raw materials price index |
|-----------------------------------------|-------------------------------------|-------------------------|----------------|-----------|---------------------------|
|                                         | Single components                   | Intermediate components | Finished goods |           |                           |
| <b>2001</b>                             | 100                                 | 100                     | 100            | 100       | 100                       |
| <b>2002</b>                             | 96.0                                | 96.2                    | 97.5           | 109       | 101                       |
| <b>2003</b>                             | 96.8                                | 96.9                    | 97.5           | 118       | 108                       |
| <b>2004</b>                             | 98.0                                | 96.3                    | 98.6           | 127       | 129                       |
| <b>2005</b>                             | 97.1                                | 96.4                    | 98.6           | 138       | 152                       |
| <b>2006</b>                             | 95.5                                | 96.7                    | 98.1           | 147       | 172                       |
| <b>2007</b>                             | 97.6                                | 97.7                    | 101.6          | 156       | 183                       |
| Changes from 2001 to 2007 (percentages) | <b>-2.4</b>                         | <b>-2.3</b>             | <b>1.6</b>     | <b>56</b> | <b>83</b>                 |

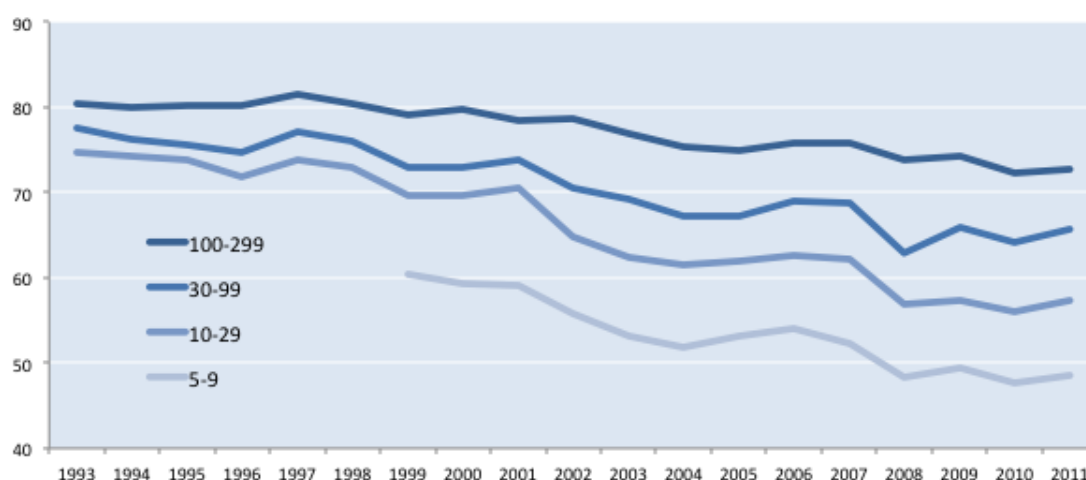
Source: Korea National Statistics Office; Bank of Korea, Economic Statistic System; Korea Federation of Small and Medium Business, Statistics of Small and Medium Enterprises.

## 4.2. Job quality in SMEs: a free fall?

### 4.2.1. Overall situation in SMEs

Then, how is the polarization between large enterprises and SMEs reflected in job quality? First, wage differentials between them have been increasing. As Figure 18 shows, all sizes of SMEs have witnessed their relative wages to continue to fall. For example, in 1993, workers employed in the firms with 100-299 employees received about 81 per cent of the average wages in large firms, but the ratio was reduced to 73 per cent in 2011. Similar scales of reduction are observed for other smaller enterprises. In 2011, the average wages of micro-enterprises (5-9 employees) were less than the half of those in large enterprises.

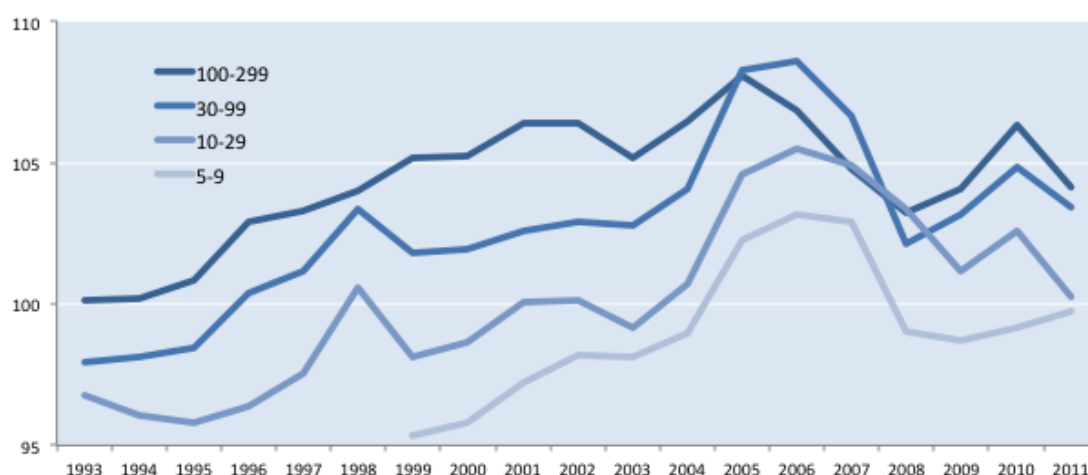
**Figure 18 Relative monthly wage per employee according to firm size, 1993-2007 (large firms = 100)**



Source: Korea National Statistics Office, Monthly Labour Survey, various years.

However, these growing wage differentials should be seen in the context of relatively longer working hours in SMEs. As Figure 19 shows, average working hours in the beginning of the 1990s, average working hours were shorter in SMEs. However, as working hours became shorter in large enterprises thanks to collective bargaining and the new statutory standard of 40 hours (which had been gradually implemented by the size of enterprises), the relative length of working time in SMEs increased in the 2000s (see Lee & McCann, 2011). In other words, without relatively long working hours in SMEs (or if hourly rather than monthly wages are estimated), the wage differentials between the two types of enterprises would be much larger.

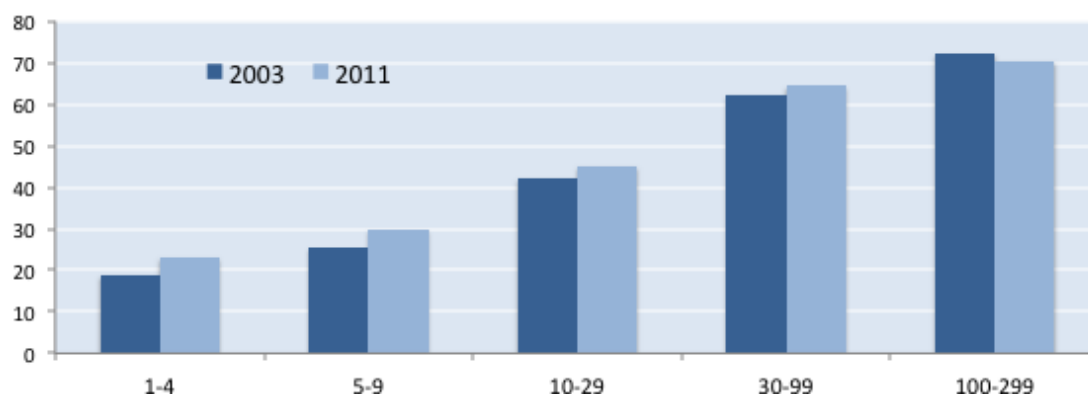
**Figure 19 Relative monthly working hours per employee according to firm size, 1993-2011 (large firms = 100)**



Source: Korea National Statistics Office, Monthly Labour Survey, various years.

As can be easily anticipated, jobs created in SMEs are less stable than those in large firms. On the one hand, on average, the entry and exit rates for SMEs are higher than large firms, so that the average job tenure tends to be shorter. On the other hand, the SMEs tend to rely more intensively on the fixed-term contracts, which allow the firms not only to secure a higher degree of flexibility but also to save part of labour costs. In Korea, the length of the average job tenure for the workers working in the firms with 100-299 employees is only two-thirds of that for larger firms (Figure 20). The workers in the smaller sizes of firms have shorter average job tenure, the average job tenure for workers in firms with less than 5 employees being only 20 per cent of that for the workers in large firms.

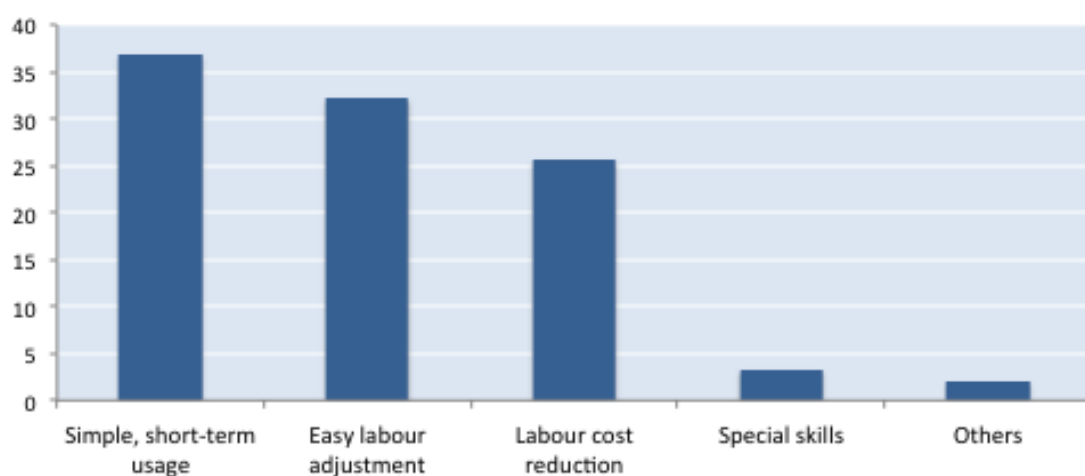
**Figure 20 Relative job tenure of the SME workers, 2003, 2011 (large firm workers = 100)**



Source: KLI Labour Statistics based on National Statistics Office, Economically Active Population Survey (EAPS).

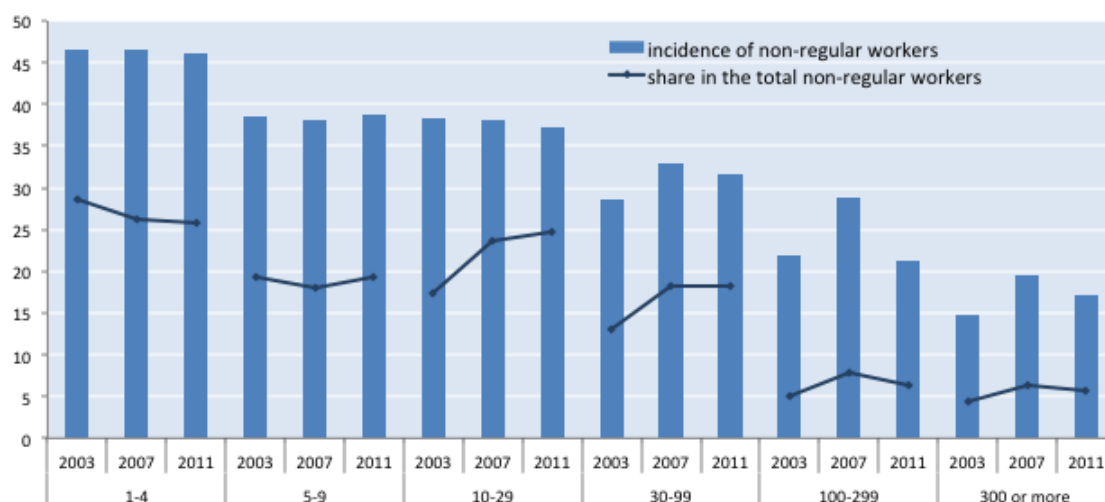
Finally, SMEs tend to rely on non-regular (and cheap) employment to address the cost pressures (see Figure 21), and indeed, most of non-regular workers are employed in the SME sector (Figure 22). In 2011, only 6 per cent of the non-regular workers are employed by firms with more than 300 employees, and a proportionally larger share of non-regular workers are employed in the smaller sized firms. Similarly, the incidence of non-regular workers is higher in smaller firms. In firms with less than 5 employees, almost half of wage workers have non-regular labour contacts, while in firms with more than 300 employees the corresponding figure is only 17 per cent. The share of non-regular workers in businesses increased and began to decline after 2007. In particular, there was a considerable drop in the share of non-regular workers in firms with more than 100 persons. Approximately 90 per cent of all non-regular workers work at businesses with less than 100 persons. Among total non-regular workers, in 2011 only 5.6 per cent worked in large companies of more than 300 persons, while only 6.3 per cent worked in businesses of 100 to 299 persons.

**Figure 21 Reasons for SME retainment of non-regular workers (2004)**



Source: Reorganized the results of the panel data, KLI (2005)

**Figure 22 Incidence and share of non-regular workers according to firm size, 2003-2011 (percentages)**



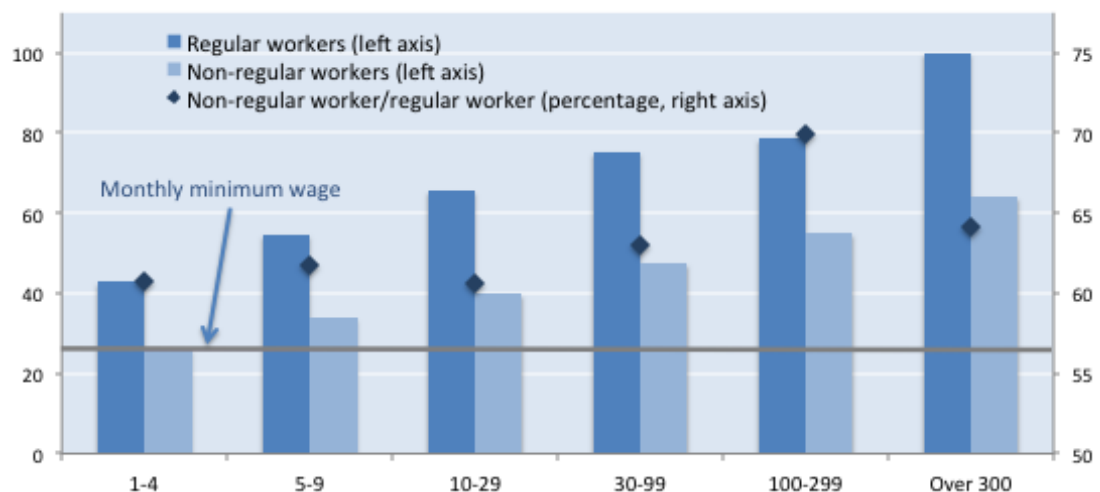
Source: KLI Labour Statistics based on National Statistics Office, Economically Active Population Survey (EAPS).

#### 4.2.2. Non-regular workers in SMEs: double penalty

We have argued that labour market segmentation in Korea has been deepened along with two key dimensions of non-regular work and SMEs. Thus, the cost of the segmentation is particularly high for non-regular workers in SMEs. They suffer “double” penalty.

Figure 10 shows how non-regular workers in SMEs are penalized twice. As discussed, the wage differentials with large enterprises tend to be larger for smaller enterprises. Yet workers in SMEs are now the same. With each type of SMEs, the differences in average wages between regular and non-regular workers are considerable, ranging from 30 to 40 per cent. It is also interesting to note that the average wages of non-regular workers in micro firms (1-4 employees) are exactly the same as the monthly minimum wages (Figure 23). According Hwang and Lee (2012), about 12 per cent of employees earn less than minimum wages,<sup>11</sup> and the non-regular workers in these firms seem to fall into this group of workers.

**Figure 23 Monthly wages according to employment type and firm size, 2011 (regular workers at large firms = 100)**

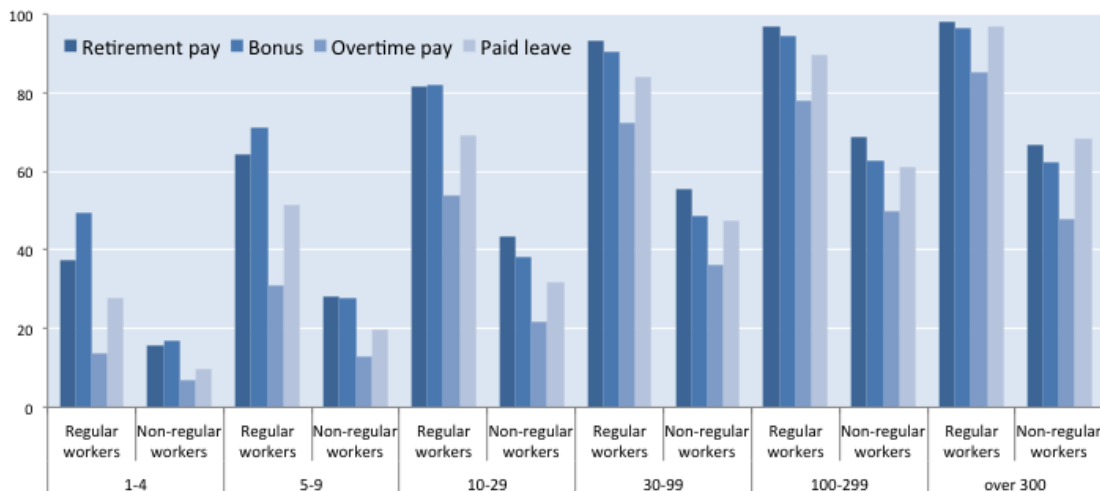


Source: KLI Labour Statistics based on National Statistics Office, Economically Active Population Survey (EAPS).

Similar patterns are applied to benefits. In the case of corporate benefits, such as severance pay, bonuses, overtime allowance and leave payments, the company size is also important, other than the employment type. The probability of non-regular workers receiving benefits at firms with over 100 employees is higher than that of regular workers at firms with less than 10 workers (Figure 24).

<sup>11</sup> Currently, Korea’s minimum wage is at 25-29 per cent of average wages.

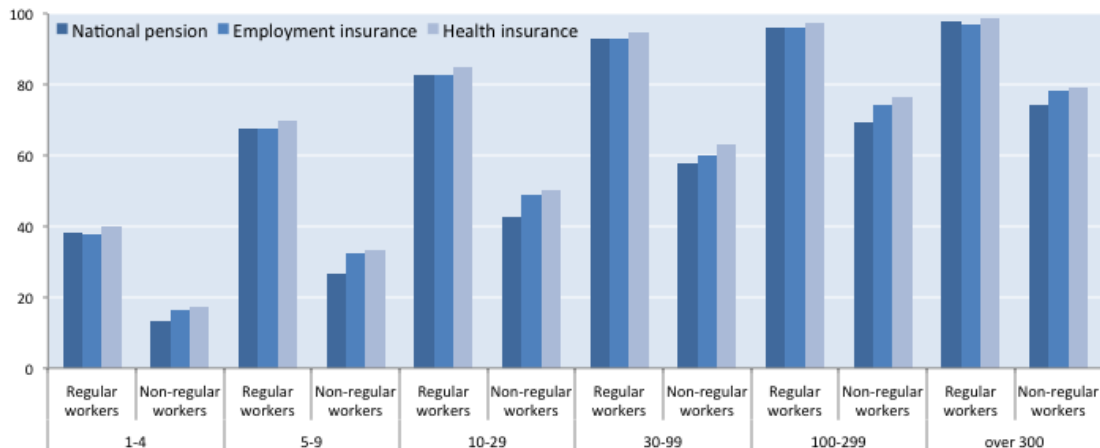
**Figure 24 Coverage rate of firm-provided benefits according to employment type firm size, 2011 (percentages)**



Source: KLI Labour Statistics based on National Statistics Office, Economically Active Population Survey (EAPS).

Most non-regular workers are excluded from social insurance, and employee subscription to social insurance programme differs greatly according to the company size. The larger the company, the higher the rate of subscription to social insurance for both regular and non-regular workers. The smaller the business, the relatively greater the gap in subscription rates between regular and non-regular workers. When looking at the coverage rate of employment insurance for firms with 1-4 employees, the rate for regular workers is more than double the rate of non-regular workers, while for firms with 10-29 and 300 or more employees, the difference drops to 1.7 times and 1.2 times, respectively. Similar phenomenon can be observed for health insurance and national pension schemes (Figure 25).

**Figure 25 Social insurance coverage rate according to employment type and business size**



Source: KLI Labour Statistics based on National Statistics Office, Economically Active Population Survey (EAPS).

However, even regular workers at firms with less than 10 employees have lower coverage rates of social insurances, such as employment insurance, health insurance and national pension, than that of non-regular workers at firms with more than 100. It implies that the blind spot in social insurance is a problem not only for non-regular workers, but for small companies in general.

In addition, there are a large number of workers who are not covered by employment insurance nor the basic livelihood security system. Although those workers are currently employed, in most cases their companies are too unstable to maintain their employees and have severely weak payment abilities. It seems to be pointless being a

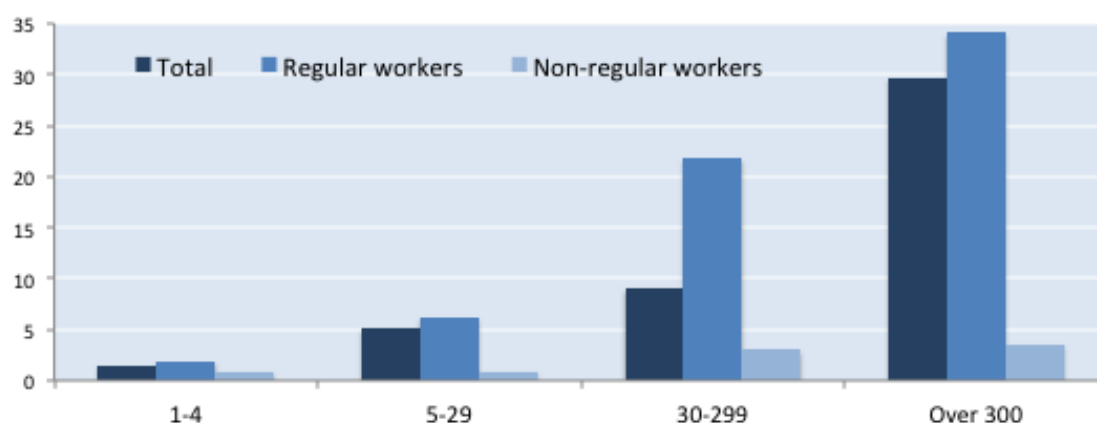
regular worker compared to being a non-regular worker within such companies where all workers are exposed to on-going precarious situations, such as job instability and poverty.

The double penalty for non-regular workers in SMEs is revealed in the lack of (or insufficient) coverage of legal protection. Workers at firms with less than 5 workers are not subject to protection by certain provisions of the labour standards act and the non-regular worker protection law. For example, provisions as per the labour standards act including 40-hour, 5-day work week, and restrictions in terminating employees are not applied to these workers. Provisions as per the non-regular worker protection law on restricting the retention period of temporary workers and restricting overtime work of part-time workers are not applied either. In effect, workers under the worst working conditions are left neglected, outside legal protection.

#### 4.2.3. Limited trade union's role

If, as discussed, the laws do not offer much protection to SMEs workers (especially in micro enterprises), can trade unions provide “functionally equivalent” protection to them? The role and functions of the Korean trade unions are limited and declining in protecting the SMEs and non-regular workers due to their low unionization rate (Figure 26). Here again, non-regular workers in SMEs are subject to double penalty. According to Kim (2009), the number of union members is 2 million, including 1.8 million regular workers and 0.2 million non-regular workers. Considering that non-regular workers occupy 35.0 per cent of total wage workers, their unionization rate is very low in total union membership. In addition, SMEs with the high incidence of non-regular workers usually do not have organized trade unions, which is why the likelihood of formation of labour union for non-regular workers is rather low.

**Figure 26 Unionization rate by company size among regular and non-regular workers (2010)**



Source: KLI Labour Statistics based on National Statistics Office, Economically Active Population Survey (EAPS).

The Korean labour movement has attempted to open trade union membership to all wage workers including non-regular workers and to increase unions' political activities. Potential membership in national, industrial and sectoral unions is open to all employed workers, regardless of whether they are in regular or non-regular employment. However, most of the enterprise-based unions in Korea limit their membership base to employed workers who are regular employees of the given company. It is quite common for union constitutions to limit the membership eligibility to regular employees. Even if this is not the case, most unions pay less attention to organizing those workers engaged in non-regular employment.

The fragmented interest representation of enterprise unions has contributed to the growing polarization between organized labour of large firms and unorganized labour in the SMEs and non-regular employment (Kim, 2009). The unionization rates are severely dispersed according to employment type and company size. The polarized Korean trade union enables the protection of regular workers in large companies but is not strong enough to protect non-regular workers.

## 5. Conclusions: summary and policy implications

The 1997 Asian financial crisis was a major turning point for Korea's socio-economic paradigm which had been much touted as the "champion of equitable growth" with an increasingly inclusive labour market. The structural changes which followed the crisis have been particularly strongly felt in the labour market and revealed in the deepening segmentation of the labour market.

Our analysis in this paper has shown that while the overall employment performance has not deteriorated much in the post-1997 crisis, the quality of employment has become increasingly polarized, with increasing number of non-regular and precarious workers and widening inequality in wages and income. These developments are also the results of many factors, but we highlighted changes in economic and employment structure as well as policy changes. First, structural changes towards the service sector and SMEs played a critical role, as both tended to offer lower job quality. In addition, the gaps between large enterprises and SMEs have been growing. Second, we have also argued that policy shifts toward deregulation since the crisis contributed much to these developments and that recent attempts to alleviate the worsening trends (especially in the area of social security) were of limited success. The recent "re-regulation" of non-regular work appears to have been successful in preventing further increases in non-regular workers but largely failed to reduce them.

Based on these observations, we have investigated dual dimensions of labour market segmentation in which two-related increasingly important dimensions tend to overlap with each other. First is concerned with non-regular work. In Korea, non-regular work is an invitation to lower quality of work in numerous areas, ranging from wages, job security, social security and voice at work. The second dimension is related to SMEs. Despite their growing importance in employment, SMEs' relative position *vis-à-vis* large enterprise has been worsened. The productivity-gaps between the two have been on increase and cost pressures on SMEs (imposed by large enterprises) are more intense. For this reason, the differences in job quality among regular workers between large and SMEs are widening. Regular workers in SMEs are *de facto* non-regular workers in terms of their job quality. This also means that non-regular workers in SMEs are exposed to "double penalty" which comes from types of both enterprise and employment contract.

What do all of these mean, especially for policies? In Korea, there appears to be a consensus that labour market segmentation has gone too far and counter-measures are needed to alleviate it. Then, the question is how. Some may suggest workers' collective actions to improve the situation. This is certainly important and helpful, but, as our analysis has shown, the roles of trade unions are severely limited in SMEs and non-regular workers. For non-regular workers in SMEs, trade unions are a remote (if not non-existent) possibility. In this case, re-regulation through legal revisions would be a more promising option. As mentioned earlier, this is what the Korean government pursued in recent year with limited success. In Korea, the introduction of a multiple-layered and complex regulatory framework in which non-regular work is legally recognized and controlled is like "shooting a moving target", as innovative employment practices tend to emerge in response to new regulations. However, more importantly, most of labour laws,

including the Labour Standard Act, do not provide effective protection to most vulnerable workers: non-regular workers in very small enterprises who account for the majority of non-regular work in Korea. Therefore, the focus of legal revision should be placed on removing such loopholes in the current laws by effectively embracing all workers of all types of enterprises within their scope, rather than undertaking a series of patchwork on some limited aspects of non-regular work.

There is one important (possibly, more fundamental) issue for policies. Our analysis indicates that the current status of labour market regulation is highly economic-natured in the sense that the economic polarization between large enterprises and SMEs (through problematic business practices such as unilateral price cutting by large enterprises) has limited resources in SMEs for improving job quality. Without reducing these gaps and preventing “unfair” business practices, regulatory changes alone would have only modest impacts on the labour market. In other words, the transformation of the socio-economic model is a necessary condition for making the labour market less fragmented and more inclusive.

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