

Reproduction Crisis and Alternative Fiscal Policy¹

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1. Introduction

Currently, Korean economy met major economic crisis. Accumulated disequilibrium such as polarization after the economic crisis in 1997 has threat economic stability as well as reproduction of labor forces.

Economic recession, begun from 3/4Q, 2000, had not been recovered and continues till now. It seems that depressed consumption by polarization played significant role for the prolonged recession. Rapidly declining total fertility rate would seriously affect future demographical change and economic performances.

Meeting economic crisis and class polarization, public finance policy proposed by each political party showed big differences. The Grand National Party, conservative opposition party, pushed ahead tax cut policy. Special consumption tax cut and 1% point cut of corporate income tax rate in 2001 was accomplished basically by the active promotion of The Grand National Party. They have argued that high economic growth and job creation can be fulfilled through raising firm's after tax profit. Government party and president Roh, basically conservative inspite of professing reform, preferred Public-Private Partnership (PPP) to restrict demand for

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fiscal expenditure to increase. Along side this policy line, the government fulfilled corporate tax cut and income tax cut twice. Conversely, Democratic Labor Party (DLP) proposed increasing tax and social security contributions. They argue that government must respond to increase of welfare demand by introducing Wealth Tax or raising tax on property income and property ownership.²

This article aims to suggest alternative fiscal policy to solve the problem of reproduction crisis in Korea. Section 2 reviews literatures and suggests theoretical viewpoint to approach the problems. Section 3 examines reproduction crisis such as prolonged recession and low fertility rate. Section 4 analyzes current situation and problems of the government tax-budget system. Section 5 proposes alternative fiscal policies. Especially, I try to stress the necessity of increasing social welfare expenditures through overall introduction of participatory budget system, and the necessity of introducing Net Wealth Tax.

2. Review of the Literatures

Some scholars propose active rolls of government to meet economic crisis. Kim argues that it is necessary for government to assume a supplementary role in dealing with market failure in order to reduce income inequality. She stressed that fiscal reform should cover a welfare model à

² Policy differentials between major political parties resemble party-specific policy composition of the United Kingdom. Major issue of the 2001 general election was how to solve deteriorating quality of public service, arisen by public investment shortage during 18 years' long rule of the Conservative Party. Labor Party proposed Public-Private Partnership as the policy promise. Electorates, who wanted improvement of the public service, recognized Conservative Party's tax-cut policy as cutting public expenditure and investment. Liberal Democrats promised tax increase to fund radical quality improvement of hospital and school. Charles Kennedy, candidate of the Liberal Democrats appealed to the electorates, "Let's all become honest." The election resulted in great success of Labor Party, which got 412 seats and failure of Conservative Party, which got at most 166 seats.

la Korea, construction of benefit system, raising efficiency and adjustment of government expenditure through the national consensus. Tax reform should include indirect increase of revenue through improvement and equity of taxation and reduction of tax expenditure in order to finance welfare expenditure (Kim, 2006). Yun searches remedies to solve bipolarization problem as follows: strengthening competitiveness of small and medium firms; developing knowledge economy; job creation; enhancing labor productivity; alleviation of inter-regional fiscal gap. He suggests government to focus to welfare of three fields: education welfare, job welfare and social safety net. During four years of carrying out, it was estimated to cost total 90.4-94.6 trillion won: 32.9 trillion won for education welfare; 57.5 Trillion won for job welfare; 4.2 trillion won for social safety net (Yun, 2006). He suggests several methods to raise the money for that: 17 trillion won by abolishing simplified taxation system; 9.3-14.5 trillion won by introducing stock transfer income tax; 26.4 trillion won by decreasing budget waste.

However, some Scholars are critical to expanding government expenditures. Na and Lee oppose to raise tax burden. They argues that actual tax burden ratio of Korea was higher than the optimal ratio since 1994, whereas the former was lower than the latter before 1994. However the actual social security contribution burden ratio has always been lower than the optimal ratio. National burden ratio was higher than optimal ratio after 1998 (Na and Lee, 2003). Researcher Kim of Korea Institute of Public Finance argues tax-cut policy would be better measures to boost the economy than expanding government expenditures. Analysing the effet of fiscal policies on real economy during 1970-2000, they insisted to find that tax-cut effect had last 20 quarters (5 years), but the effect of discretional expenditure expanding had last just 1 year and showed negative effect after 1year. It is because of the crowding-out effect, that is, expenditure expanding induces interest rate to rise and it dampens private consumption and investment. Evaluating each policy quantitatively, discretional tax-cut policy is 1.2-2.9 times more effective

than expenditure expanding for long term increase of income (Kim, Woochul, 2006). Song and Lee of KDI warn the possibility of worsening public finance situation. Factors encroaching financial soundness include rapid increase of national debt during overcoming foreign currency crisis, increase of demand for public expenditure of pension and medical care due to ageing society (Song and Lee, 2007).

Reproduction crisis can be categorized in two dimensions. The first is crisis in the circulation of national economy, and the other is crisis in the reproduction of labor forces. As for the roll of the state, industrial policy was important in the early industrialization period. However, meeting reproduction crisis of recent years, social security policy became more important. To understand the roll of public finance responding reproduction crisis, we hold the viewpoint of class relations and historical change. Firstly, to grasp the roll of public finance in capitalist state in general, we adopt Marxist welfare state theory and Keynesian macroeconomic theory. Furthermore we will approach characteristics of Korean welfare system by the concept of 'developmental welfare state' and 'the late industrialized'.

Generally, roll of public finance in modern capitalist state is allocation of resources, regulating business cycles and redistribution of wealth and income. O'Connor insisted that economic social conditions of reproduction lie in contradictory relations with successful capital accumulation capitalist development process. Because accumulation process is always in crisis, economic and social policy of the government cannot alleviate the crisis without transforming the ideological basis, which legitimate reproduction process, relations between the state and the society, state behavior(O'Connor, 1979).

Shaikh argues that subject which takes the burden of social welfare expenditure favorable to the workers is not the capital but the laborers themselves, that is net social wage is nearly zero level and in case of plus, the amount is negligible (Shaikh, 2003). Sheikh and Tonak calculated

net transfer, social welfare expenditure minus paid tax (tax and social security contributions) in the United States, 1952-85. The results were that net transfer was almost minus except several years as 1971, 1974-78, 1983. They argue that the workers give subsidies to the state in reality, so social income is only a myth (Shaikh and Tonak, 1987).

Espin-Anderson classified welfare states into three categories: liberal, corporatist and social democrat (Espin-Anderson, 1990a, 1990b). He argued that each categories accomplished welfare reform in various ways (Espin-Anderson, 1996).

As for the historical character of welfare reform by Kim daejung government after economic crisis, there were various argument that it was liberal, neo-liberal, conservative (Kim, Yonmyung, 2002). Welfare reform of Kim government can be categorised as neoliberal. It followed basically market principle, benefits compensated by contributions not by the needs, It did not establish any one of the welfare state principles ‘societal responsibility of poverty’, ‘loosening the qualifications for receiving benefits’, ‘approval of the right to receive public assistance’.

Kwon tried to explain changes and continuity of welfare system in Korea and Taiwan by the concept, ‘developmental welfare state’. He elaborates two strands of welfare developmentalism (selective versus inclusive) and argues that both Korea and Taiwan fell into the selective category of developmental welfare states before the Asian economic crisis of 1997–1998. The key principles of the selective strand of welfare developmentalism are productivism, selective social investment and authoritarianism; inclusive welfare development is based on productivism, universal social investment and democratic governance. He then argues that policy reform toward an inclusive welfare state in Korea and Taiwan was triggered by the need for structural reform in the economy. The need for economic reform, together with democratization, created institutional space in policy making for advocacy coalitions, which made successful advances

toward greater social rights. The paper argues that the experiences of Korea and Taiwan counter the neoliberal assertion that the role of social policy is minor in economic development, and emphasizes that the idea of an inclusive developmental welfare state should be explored in the wider context of economic and social development (Kwon, 2005).

Kuhnle and Hort sought lessons for developing countries from the experiences of Scandinavian welfare state. They show that a strong social role for the state was not incommensurate with economic development—economic growth and the institutionalization of comprehensive social security and welfare services programmes could develop hand in hand. The construction of the welfare state was gradual and a continuous balancing act between stimulating economic development and promoting social justice. During periods of economic down-turn and setbacks in the most recent decades, modifications were made to programmes and benefit structures, and some programmes were expanded. They argue that the Scandinavian historical experience cannot be copied, and the characteristics and goals of the Scandinavian welfare state may not be universal, but the Scandinavian route to a modern democratic welfare state does still offer some general lessons as to interrelationships between political, economic and social development (Kuhnle and Hort, 2005).

3. Reproduction Crisis and Its Causes

3.1. Prolonged economic recession

Current economic crisis had extended about seven years, from 3/4 quarter 2000 to now. It is too long compared to the past recessions ordinarily recovered after 18-24 months from the beginnings. Some researchers argue that recent business cycles in Korea continuously have gone

downward compared to trends and have become short-period. That is, expansion situations lasted 12 months during 198-2005 compared to 31months during 1970-2005, and contract situation lasted 16months compared to 18months during corresponding periods. The causes of short period cycles are pointed out as follows: worsening foreign environment after economic crisis in 1997; change of industrial structure to IT industries with high external dependency and volatility; depressed investment, etc (Ju, 2005; Nam, 2006). February 2006, Korea National Statistical Office revised Composite Index, adding two new indexes (service activity index (excluding wholesale and retail sale) and domestic shipment index and excluding export index. As shown in <figure 1>, the results are that previous composite index moves more sharply than the current one and composite index at peak Dec. 2002 was much lower level than that of peak Aug. 2000 in previous index but it was similar level in current index. So it can be argued that current recession has continued longer than 6 years after the peak Aug. 2000 viewed in previous composite index and, when estimated in current composite index, it continued at least 4 years after the recent peak Dec. 2002 announced by the government.

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Main reason of the prolonged recession is the contract of consumption resulting from worsening income distribution. Taiwan and Singapore experienced minus growth rate 1n 2001. But Korea could accomplish plus growth rate and it was by virtue of escaping contract of private consumption. Private consumption grew 9.5%, from 296 trillion won in 2000 to 324 trillion won in 2001. But economic growth was mainly backed by the borrowing, increase of household debt. Household debt balance increased 80 trillion won in one year, from 301 trillion won in March 2001 to 381 trillion won in March 2002. Consumption backed by borrowing could not continue

long period. 2001-2004 average growth rate of GDP was 4.9%, but that of private consumption was only 2.0%, and consumption decreased during 6 quarters after 2 quarter 2003. Stagnation of consumption was caused by the remarkable drop of propensity to consume.

The propensity to consume (real private consumption/GDP) had been stable mid 1990's, but began to decline after economic crisis in 1997 and dropped around 13% in 2004 compared to 1990's average. This fall of propensity to consume was mainly brought about by worsening income distribution as income polarization and poverty increase. Because the propensity of consumption is lower, the richer the class becomes, widening income differential will bring about the fall of propensity to consume. Actually, comparing income differential and change of after 1990's propensity to consume, it was found that the two have almost complete inverse correlation (correlation index: -0.92) (Kang, 2005). Study by the researchers of the Bank of Korea shows that household consumption exceptionally fell and ratio of household consumption to GDP dropped in 1998 and 2003-2004, when income differential widened, and household consumption increased in 2005, when income inequality was alleviated (Bae and Lee, 2006). Lee also insisted that worsening income distribution hurt economic growth (Lee, 2005).

3.2. Crisis in social reproduction

Fertility rate had fallen gradually during 1990's, but it declined dramatically, responding to neoliberal restructuring after economic crisis in 1997. Childbirth decreased from 1,007 thousands in 1970 to 865 thousands in 1980, 659 thousands in 1990, 637 thousands in 2000 and 438 thousands in 2005. Total fertility rate fell from 4.53 in 1970, 2.83 in 1980 to 1.59 in 1990, 1.47 in 2000 and 1.08 in 2005.

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What caused serious decline of child birth and fertility rate? Main cause of it was the rise of marriage age and evasion of childbirth between young generations, following the change of socio-economic environment and sense of values. Pregnancy period became short by high age marriage, and increasing burden of child care and education brought about shrinking of childbirth. Female average first marriage age rose to 27.5 years in 2004, 4.3 years higher than 1981. Ratio of the female with a mate between the age of 24-29 fell to 54.2% from 77.3% in 1990.

Rise of the female's economically active participation rate brought about the rise of marriage age and decline of fertility rate. Female's economically active participation rate rose 49.8% in 2004 from 42.8% in 1980. It rose most for the female between 24-29. Ratio of the female between the age of 18-21 in tertiary education rose from 15.2% in 1985 to 50.7% in 2004.

The rise of instability in income and employment after economic crisis, increase of burden of child education also caused decline of childbirth. Unemployment rate of 25-29 age male (female) rose to 7.5%(4.4%) from 3.6%(1.7%) in 1995. The ratio of contingent workers rose 35.4% in 2004 from 27.8% in 1995. Sense of views toward marriage and child changed sharply. Following the survey in 2005 by Korea Institute for Health and Social Affairs, only 71.4% of the unmarried male and 49.2% of unmarried female answered positively toward marriage.

4. Weak government's function for income redistribution

4. 1. Low redistribution effect

In Korea, the roll of public finance for income redistribution is very weak. Disposable income of a household is basically composed of market income and improved by government transfer payments. Tax system and social security system don't have meaningful income distribution effect. Following Yu's analysis using <Household consumption survey> data, jini coefficient of market income rose to 0.374 in 2000 from 0.302 in 1996 and jini coefficient of disposable income rose to 0.358 in 2000 from 0.298 in 1996. So, the redistribution effect was 1.3% in 1996, and 4.5% in 2000. In the case of United States (1986), having particularly weak redistribution effect, the effect was 22.7% (from 0.411 to 0.355), and in OECD average(mid 1980's), the effect was 41.6% (from Yu, 2003).

During 1990's, almost all OECD countries, being affected by trends of globalization and develoment of information technology, experienced worsening of income distribution calculated on market income (table 2). However, viewed on the gini coefficient of disposable including income tax and social security expenditure effect, income distribution situation was not worsened much. Under well established social safety net, worsening income distribution could be prevented by implementing various policies to share economic benefits by globalization and develoment of information technology.

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However, Korea is not the same case. Following Park et al.'s analysis on City Worker Household Survey by Korea National Statistical Office, redistribution effect by direct tax and income transfer is 10.5% based on gini coefficient. Excluding private transfer effect from this, net redistribution effect by public sector was 6.6%. Including consumption effect a little

retrogressive, it fell to 6.1%. Redistribution effect by payment in kind (2005 base) is 2.75%, 2.6%, 0.17% by health insurance, education and child care respectively (Park et al., 2006)

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Following recent study by the Ministry of Finance and Economy, analysing income inequality improvement (gini coefficient reduction) effect by social security and tax system of the Kim Daejoong government(1998-2002) and Roh Muhyun government(2003-2005), average improvement effect was 2.3% annual average during 5 years of Kim government and 3.2% average during 3years of Roh governmnet. In case of Sweden and Germany (in 2000), it was 35.5% and 30.8% respectively. OECD 15 countries average was 26.1%.³

4. 2. Meager social welfare expenditure

Low government redistribution effect is the result of meager social welfare expenditure by government. In Korea, the ratio of social welfare expenditure among government budget is very low compared to other OECD countries. In 2004, the share of education expenditure is 17.1% higher than other countries, but the ratio of social protection is only 10.4%, much lower than 30-40% of other OECD countries (table 4)

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³ Park, Hyun, "Roh Muhyun government, talk only high slogan", *The Hankyoreh*, January. 23, 2007.

In 2003, public social expenditure as percentage of GDP is 5.7%, strikingly low compared to 23.3% average of Europe 19 countries (table 5).

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Gross public expenditure can not be equal to Net social expenditure, which people enjoy in the end. There are some important factors which makes difference between gross public expenditure and net social expenditure. Tax on public social expenditure must be deducted from Gross expenditure. Tax Break with Social Purposes (TBSPs), and mandate and voluntary private social expenditure must be added to that. In the case of Sweden, tax deduction is high(7.0% of GDP), TBSPs are not existent, and private social expenditure is small, so net social expenditure(26.1% of GDP) is lower than gross public expenditure (31.3% of GDP). Denmark is the similar case. Contrastingly, United States shows peculiar case of substantially high level of net social expenditure(25.2% of GDP) compared to low level of gross public expenditure (16.2% of GDP). Interesting characteristics of United States' case is that TBSPs are high (1.4% of GDP) compared to other countries' small amount and voluntary private social expenditure is very high (8.9% of GDP) compared to OECD-24 average (1.8%). It can be argued that American rich donates large amount and it preserves the social solidarity inspite of weak roll of the government. In FRAnce and Germany, net social expenditure is almost the same level with gross public expenditure. In Korea, madated (compulsory) voluntary private expenditure is 1.8%, high compared to OECD-24 average 0.6%. Almost all of mandated voluntary social expenditure is retirement allowance or discharge allowance. Voluntary private social expenditure is very low. So net total social expenditure is lowest level with Mexico among OECD countries (table 6).

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Growth rate of social welfare expenditure under Roh government is higher than total budget growth rate, but lower than under Kim Daejoong government. Welfare budget (social welfare, health area) increased to 38 trillion won in 2002 from 21 trillion won in 1997, 17 trillion won increase in 5 years, average increase of 16.1% annually. Contrastingly, welfare budget under Roh government increased from 37 trillion won to 61.4 trillion won, 23.4 trillion won increase in 5 years and 12.4% increase annually.

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There are many group, who are excluded from weak social safety net. Among non standard workers, which is about 55% of total workers, only 33.6% join national pension, at most 34.5% join health insurance, 31.5% join employment insurance

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4. 3. Low burden of Income Tax and Social Security Contributions

Low public social expenditure is the result of low income tax and social security contributions. In 2004, ratio of national burden (tax plus social security contributions) as percentage of GDP was 24.6%, lowest level except 19.0% of Mexico (compared to 35.3% average of OECD). Ratio of social security contributions to GDP was 5.1%, about half of 9.4%, OECD average. Especially, social security contributions by the employers as percentage of GDP

was only 2.1%, under half of OECD average 5.1%. Ratio of personal income tax to GDP was 3.4%, one third of OECD average 9.1%.

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Especially, labor cost per worker in Korea, calculated by purchasing power parity (PPP), is 41,086\$, higher than OECD average 36,025\$, middle 14th among OECD countries. However total tax burden as % of of labor cost is 17.3%, under the half of OECD average 37.3%, lower than 18.2% of the Mexico. Ratio of income tax to GDP is 2.5%, much lower than 13.3% of OECD average, social security contributions by the employers

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Kim Daejung government reduced income tax rate from 10-40% (four grade) to 9-36%, and reduced corporate income tax rate from 16-28% (two grade) to 15-27% in 2001 (first cut). Roh government also pushed tax-cut policy, inspite of insiting distribution during election campaign period. In 2003, government cut corporate income tax 2% point to 13-25% (2nd cut) and reduced 1% point of personal income tax rate in 2004 (3rd cut). By Kim and Roh government's first tax rate reduction, it was estimated that government lost total 10 trillion won and 124.5 billion won during 2002-2005. And by 2nd and 3rd cut, it was estimated to lost 2.642 trillion won in 2005. And during 2006-2030, it was estimated to lost 241 trillion won, about half of necessary budget for <Vision 2030>.

Capitalists insited on that corporate tax cut would have investment promotion effect. However, it is not certain that corporate tax cut have investment promotion effect, because

actual investment would be affected by various factors. Kim Yoochul analysed the effect of corporate tax on investment and found that the effect shows minus sign, but not statistically meaningful (Kim, 2005). Following Kim Seung-Rae's study, the benefits of corporate tax cut are accrued only to capitalist class and big business. 10% tax rate cut would increase 2.6 trillion won of income, among them 1.93 trillion won would go to the capital and 0.22 trillion won to the labor. Big firm with the sale of above 10 billion won would occupy 98% of benefits from tax cut (Kim Seung-Rae, 2006).

4.4. Excessive burden of life insurance premium

Because public social welfare system is weak, people pay excessive life insurance premium to protect themselves from various risks. Following the survey⁴ by Korea Life Insurance Association, 53.8% of total respondents feel unest in daily life, higher than 47.7% in 2003 and 42.0% in 2000. Major objects of unrest were health problem of himself and the family (58.0%), life after retirement (56.7%), everyday living such as consumer price and business cycle (52.9%). The survey result showed that participation rate in life insurance is 89.2% (73.7% in 1997, 86.2% in 2000), each household joins average 4.4 insurances and pay annually 4,410 thousand won (12.2% of annual income).

Actually, total life insurance premium payed in 2004 was 60 trillion won and insurance received was 42 trillion won.⁵ Life insurance planners are about 120 thousands who raise around 4 trillion won total. Three giant insurance companies as Samsung, Kyobo and Korea occupy 75% of total net premium reserve (134 trillion won among 165 trillion won) in 2004.

⁴ "11th life insurance propensity survey" was conducted for 2000 households in May 2006.

⁵ Korea Life Insurance Association, "Current Situations of Life Insurance in 2004", 2005.

4.5. Over-education and excessive private tutoring cost

Meeting the trends of deepening polarization, without necessary welfare system, there are no other way except for rising the social ladder. To enter high level university is the key factor for that. Ratio of the student to enter university or college soared to 82.1% in 2005 from 68% in 2000. In 1990, it was only 33%.

So people try to educate their children as much as possible. In Korea, public expenditure for education is average level in primary and secondary school, but it is low in tertiary education (table 11, table 12).

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Responding to poor tertiary education and pressure of entrance to university, parents pay unbelievable amount of private tutoring cost. Following the survey by Korean Educational Development Institute, private tutoring cost was estimated 13 trillion won in 2003. Hyundai Research Institute, the private think tank affiliated with the Hyundai Group, announced the result of their recent survey. According to the Institute, parents were found to spend 19 percent of their monthly income on private tutoring for their children. The Institute said each household sets aside an average of 646,000 won for private tutoring, or 381,700 won per child. What's astonishing is that the total volume of South Korea's private tutoring market is estimated at 33.5 trillion won, accounting for 3.95 percent of the nation's GDP. The sum exceeds the government's entire education budget of 31 trillion won. The burden is much higher than that of

other countries belonging to OECD. In the end, the huge education costs have a negative effect on the economy, not only forcing households to cut down both consumption and savings, but also accelerating the ``double-income, no kids'' phenomenon.

5. Alternative Fiscal Policies

5.1. Expanding social expenditure

Firstly, to responding effectively to the reproduction crisis, budget size must be enlarged to the level of 35% of GDP from present 25% level as soon as possible. Workers with high income must also accept raising tax and social contributions. Employer must take the burden to pay social security contributions to 15.2% of total labor cost from 8.2% now.

Secondly, public social expenditure can be expanded through increasing social security contributions. Transforming huge amount of life insurance premium to health and pension related social security contributions not only can contribute to strengten the income redistribution function, but also can raise the efficiency of health care and pension system. In public health insurance system, lowest 1/20 class receive benefits 8.19 times of their contributions. Health insurance syetem of United States, mainly private insurance, is very inefficient: Ratio of Medical expenditure to GDP was 15% in 2003, compared to 10% in Europe OECD countries. But life expectancy was 77.2 age, low compared to about 80 age in other OECD countries. Recently, government have improved health care insurance system by raising benefits for heavy deseases as cancer. Peopple do not oppose to raise health insurance premium to support that. Because it is only transforming private insurance premium to public one.

Transforming private tutoring costs to public education tax can also contribute to enhance redistribution effect, to improve quality of tertiary education, and to lighten the heavy burden of university tuition for the parents.

To meet rapidly rising demand for social expenditures but with limited resources, government can accept budget deficit in the short run. At the end of 2005, national debt of Korea was 30.7% of GDP, low level compared to the 76.9% average of OECD countries. Korea is 5th lowest among OECD 30 countries.⁶

5.2. Tax reform

To support expanding social expenditure, government must raise capital tax. Net wealth tax, insisted by the Korea Democratic Labor Party in 2002 presidential campaign, is typical one of capital tax. It is necessary to raise tax basis of consolidated land tax, to strengthen taxing capital income tax. Stock transfer income tax must be introduced to allviate speculative transaction and to gather revenues for income redistribution.

Income tax rate and corporate tax rate must be raised to pre-tax cut reform level. Corporate tax rate is 13-25% now. Highest rate is 27.5% (including 2.5% provintially added rate), low compared to other OECD countries (39.3% in United States, 38.9% in Germany).

5.3. Enforcement of participatory budgeting

Participatory budgeting is a process of democratic deliberation and decision-making, in which ordinary city residents decide how to allocate part of a municipal or public budget.

⁶ OECD, *Economic Outlook*, 2005. 12

Participatory budgeting is usually characterized by several basic design features: identification of spending priorities by community members, election of budget delegates to represent different communities, facilitation and technical assistance by public employees, local and higher level assemblies to deliberate and vote on spending priorities, and the implementation of local direct-impact community projects. Various studies have suggested that participatory budgeting results in more equitable public spending, higher quality of life, increased satisfaction of basic needs, greater government transparency and accountability, increased levels of public participation (especially by marginalized residents), and democratic and citizenship learning.

Participatory budgeting was firstly introduced in 1989 in Porto Alegre, the capital city of Lio Grande state, Brazil and and succesfully enforced. Participatory budgeting in Porto Alegre is an annual process of deliberation and decision-making, in which thousands of city residents decide how to allocate part of the municipal budget. In a series of neighbourhood, regional, and citywide assemblies, residents and elected budget delegates identify spending priorities and vote on which priorities to implement. Partipatory budgeting spread to Lio Grande state in 1999. participatory budgeting has induced the municipal government to spend more in less favoured neighborhoods, inhabited by lower income families.

In Korea, participatory budgeting is just a begining. North district of Gwangju metropolitan city made regulations for participatory budgeting in 2004. In Ulsan city, a center of manufacturing cars and ships, East disrict and North district, KDLP held the reins of power of those, introduced participatory budgeting in 2004. Chungju city (Aug. 2004), Ansan city (Jan. 2005) and Daeduk district of Daejun metropolitan city also introduced participatory budgeting

When progressice party do not hold the power of provincial government, alternative budget strategy can contribute to raise social welfare expenditure. By making alternative budget, people

can figure out their demands more clearly and can extend solidarity between various socially weak groups.

6. Concluding Remarks

Korean economy is now on transitional period. Various disequilibria such as polarization were accumulated during high economic growth and economic crisis. If these were left as it is, let alone economic stability, economic and social reproduction for the future can not be secured. Rising unemployment and unstable employment created by long lasting economic recession weakened the capacity to provide the resources for fiscal burden for aging society. Polarization raised personal burden of child care and education costs. And it provoked the problem of rising marriage age and decreasing fertility rate. Polarization also widened education level-specific and vocation-specific income differentials, resulting in overabundance of university education, over-expansion of private tutoring costs.

To solve these reproduction crisis, there must be reform of fiscal expenditure, protecting the individual from the risks and strengthening income redistribution effect by expanding public social expenditure. And it is necessary to raise income tax rate and social security contributions by the employer to provide the revenues for increasing social expenditure.

The problem is that political power to implement these alternative progressive policies is weak. Many people, who experienced high economic growth, think they could get out of difficulties by individual effort. This give rise to high priority for economic growth and weakens political support for the welfare state. Thus it is more plausible for Korea to continue its neoliberal welfare system rather than to proceed to corporatist welfare state or social democrat welfare state in the near future

However, employment instability has extended to whole society after economic crisis, and demand and interest for social welfare services are rising. Labor class experienced frustrations to neoliberal Roh government which did not carry the promised policies into effect. They have tried to form the industrial union. So there is potential possibility that political support for welfare state would become strong.

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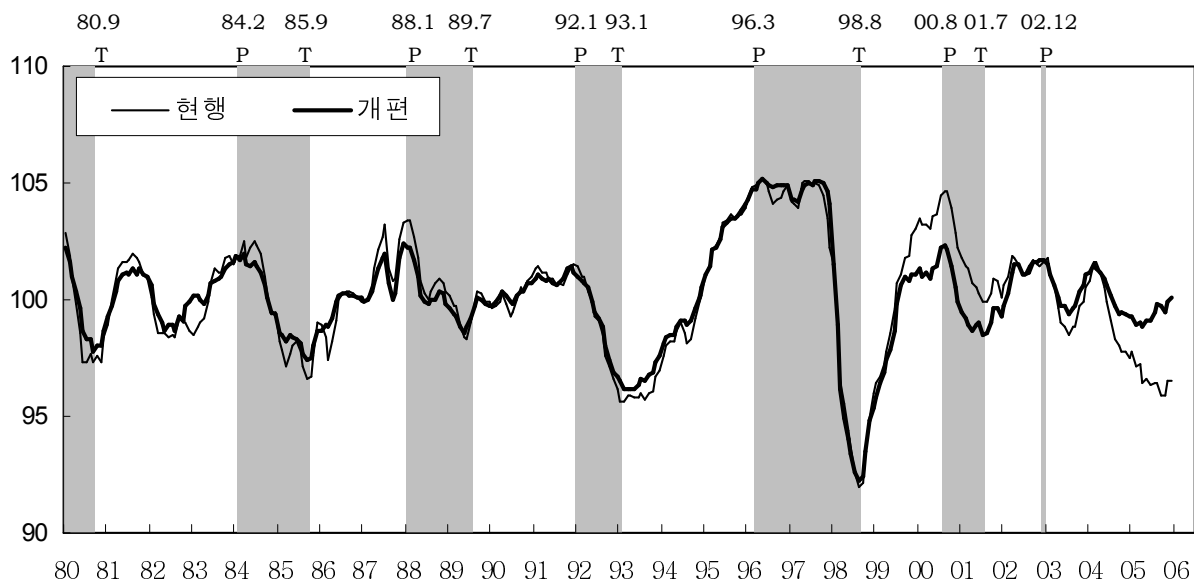
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Figure 1: Change of Cyclical Component of Coincident Composite Index



P: Peak, T: Trough.

Source: Korea National Statistical Office, Revise of Composite Index and Fixing Basis Business Cycle Day, February 2006.

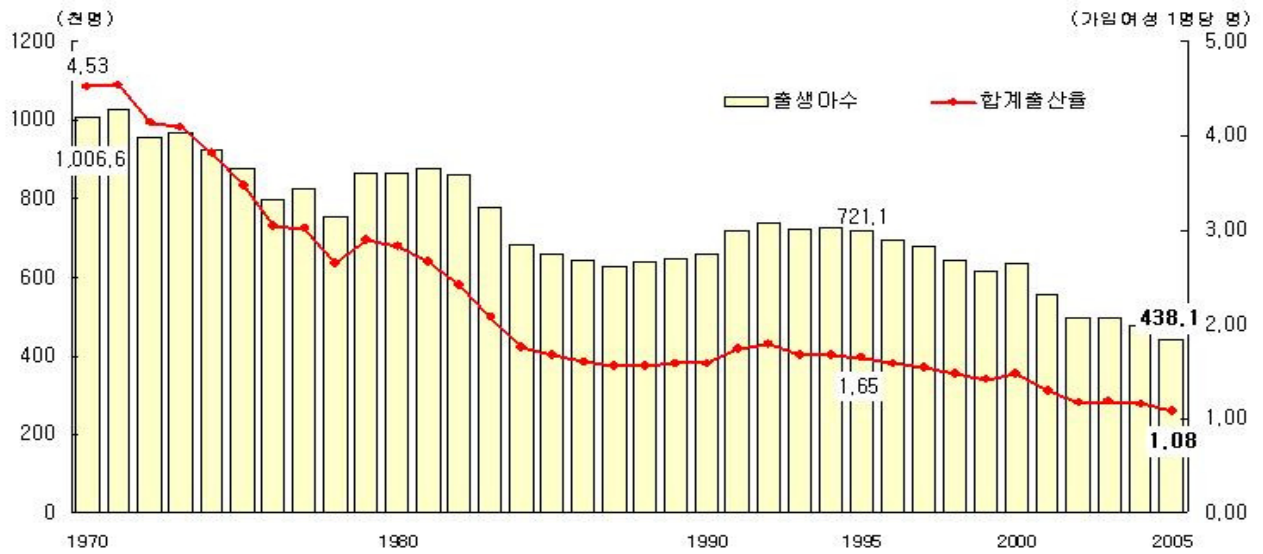
Table 1: Change of Birth and Death Rate

(Thousand heads, per thousand heads, per 1 pregnant woman)

	91	95	96	97	98	99	2000	2001	2002	2003	2004	2005
Live-births	718.3	721.1	695.8	678.4	643.0	616.3	636.8	557.2	494.6	493.7	476.1	438.1
Crude birth rate	16.6	16.0	15.3	14.8	13.8	13.2	13.4	11.6	10.3	10.2	9.8	9.0
Total fertility rate	1.74	1.65	1.58	1.54	1.47	1.42	1.47	1.30	1.17	1.16	1.16	1.08
Deaths	249.6	248.1	245.6	247.9	248.4	246.5	247.3	242.7	246.5	245.8	245.8	245.5
Crude death rate	5.8	5.4	5.3	5.3	5.3	5.2	5.2	5.1	5.1	5.1	5.1	5.0
Natural population growth	468.7	473.0	450.2	430.5	394.5	369.8	389.4	314.5	248.1	247.7	230.3	192.6
Natural rate of population growth	10.8	10.6	10.0	9.5	8.5	8.0	8.2	6.5	5.2	5.1	4.7	4.0

Source: National Statistical Office, [Birth and Death Rate Statistics]. various years.

Figure 2: Change of Live-births and Crude Birth Rate



Source: National Statistical Office, Birth and Death Rate Statistics, 2005, August 2006.

Table 2: Change of Gini Coefficient in Main OECD Countries

	Mid 1980's		Mid 1990's		2000	
	Market income	Disposable income	Market income	Disposable income	Market income	Disposable income
France	0.392	0.267	0.414	0.277	0.403	0.272
Germany	0.360	0.267	0.363	0.270	0.393	0.272
Japan	0.309	0.276	0.338	0.290	0.362	0.310
Norway	0.294	0.222	0.341	0.249	0.363	0.260
Sweden	0.347	0.224	0.416	0.247	0.375	0.242
U.K.	0.389	0.277	0.424	0.304	0.432	0.319
U.S.A.	0.376	0.326	0.417	0.351	0.420	0.346
OECD 15 average	0.357	0.266	0.395	0.284	0.394	0.291

Source: Förster, M and M. M. d'Ercole, "Income Distribution and Poverty in OECD Countries in the Second Half of the 1990s", OECD Social, Employment and Migration Working Paper No. 22. 2005.

<Table 3> Effect of Income Redistribution Policy in Korea

	1998	1999	2000	2001	2002	2003	2004	2005
Disposable income Gini Coefficient (A)	0.314	0.269	0.283	0.275	0.284	0.298	0.306	0.313
Disposable income Gini Coefficient (B)	0.303	0.257	0.270	0.261	0.270	0.270	0.276	0.281
Difference (B-A)	0.011	0.012	0.013	0.014	0.014	0.028	0.030	0.032
Rate of improvement ((B-A)/A)	2.6%	3.9%	3.7%	4.5%	3.9%	6.1%	6.4%	6.6%

Source: Park, Kibaek, et al. (2006).

<Table 4> Government Expenditure by Function in Main OECD Countries, 2004(%)

	Total	General public services	Defence	Public order and safety	Economic Affairs	Environment protection	Housing and community amenities	Health	Leisure, culture, religion	Education	Social protection
United States	100	12.9	11.6	5.6	10.1	0	1.7	20.5	0.8	17.3	19.4
Korea	100	12.1	8.8	4.8	24.1	3.1	5.4	11.4	2.7	17.1	10.4
Austria	100	14.1	1.7	2.8	10.2	0.7	1.2	13.4	2.0	4.4	42.6
Belgium	100	18.6	2.3	3.4	10.4	1.4	0.6	13.6	2.5	12.1	35.0
Czech Republic	100	10.8	2.9	5.0	16.8	2.6	1.7	14.2	2.6	11.4	31.9
Denmark	100	13.5	2.9	1.9	6.7	0.9	1.2	12.9	3.2	15.1	41.7
Finland	100	12.9	3.2	2.9	9.4	0.6	0.7	13.1	2.4	11.8	42.9
France	100	13.8	3.7	2.5	5.6	1.5	3.4	13.8	2.7	11.6	41.5
Germany	100	12.9	2.4	3.4	7.7	1.1	2.3	13	1.4	8.6	47.2
Iceland	100	5.4	0	3.5	13.5	n.a.	2.3	19	6.2	15.1	21.6
Ireland	100	10.4	1.6	4.1	14.8	n.a.	5.9	21.1	1.5	13.3	27.1
Luxembourg	100	11.4	0.6	2.4	10.9	2.5	1.9	12.0	4.6	11.9	41.7
Netherlands	100	17.5	3.2	3.8	10.1	1.8	2.5	9.7	3.1	11.2	37.2
Norway	100	9.4	4.0	2.4	8.9	1.4	1.7	17.0	2.5	13.6	39.0
Portugal	100	13.3	3.1	4.2	10.5	1.3	1.8	14.3	2.6	16.0	60.6
Slovak	100	12.4	2.5	3.2	16.4	1.3	3.1	10.3	2.9	9.0	39.0
Spain	100	12.5	2.9	4.7	12.5	2.3	2.6	14.2	3.6	11.2	33.5
Sweden	100	13.4	3.4	2.4	8.5	0.6	1.5	12.4	1.8	13.1	43.0
United Kindom	100	10.9	6.0	5.9	6.6	1.6	1.5	16.0	1.2	13.2	37.1

Source: OECD, General Government Accounts - Expenditure by function data, 2006.

Table 5: Public Social Expenditure in percentage of GDP

Year	1980	1985	1990	1995	2000	2001	2002	2003
Denmark	25.2	24.2	25.5	28.9	25.8	26.4	26.9	27.6
Finland	18.4	22.8	24.5	27.4	21.3	21.4	21.9	22.5
France	20.8	25.8	25.3	28.3	27.6	27.5	27.9	28.7
Germany	23.0	23.6	22.5	26.6	26.3	26.3	27.0	27.3
Ireland	16.8	21.8	15.5	16.3	13.6	14.4	15.5	15.9
Italy	18.0	20.8	19.9	19.8	23.2	23.3	23.8	24.2
Japan	10.3	11.2	11.2	13.9	16.1	16.8	17.5	17.7
Korea	0.0	0.0	3.0	3.5	5.1	5.4	5.4	5.7
Mexico	0.0	1.9	3.6	4.7	5.8	5.9	6.3	6.8
Netherlands	24.1	24.2	24.4	22.8	19.3	19.5	19.9	20.7
Spain	15.5	17.8	20.0	21.5	20.4	20.2	20.2	20.3
Sweden	28.6	29.7	30.5	32.5	28.8	29.3	30.4	31.3
United Kingdom	16.6	19.6	17.2	20.4	19.1	20.1	20.1	20.6
United States	13.3	12.9	13.4	15.4	14.6	15.2	16.0	16.2
OECD-Total	15.9	17.6	17.9	19.9	19.4	19.7	20.3	20.7

Source: OECD, 2006. Social Expenditure Database (SOCX, www.oecd.org/els/social/expenditure).

Table 6: From Gross Public to Total Net Social Spending, 2003

Social expenditure, in percentage of GDP at market prices

	Denmark	Sweden	France	Germany	Netherlands	United Kingdom	United States	Japan	Korea	Mexico	OECD-24
1. Gross public social expenditure	27.6	31.3	28.7	27.3	20.7	20.6	16.2	17.7	5.7	6.8	20.7
- Direct and indirect tax	7.3	7.0	4.0	3.3	3.5	1.8	1.1	0.8	0.3	0.2	1.2
+ Net TBSPs similar to cash benefits	0.0	0.0	0.9	1.5	0.3	0.3	0.7	0.7	0.6	0.7	
+TBSPs towards current private benefits(T2)	0.0	0.0	0.0	0.4	0.3	0.1	1.4	0.0	0.0	0.2	0.2
2. Net current public social expenditure	20.3	24.3	25.5	25.8	17.9	19.3	17.3	17.6	5.9	7.6	18.2
3. Net current mand. private soc. Exp.	0.1	0.3	0.3	0.6	0.4	0.6	0.4	0.6	1.8	0.0	0.6
4. Net publicly mandated soc. exp.(2+3)	20.4	24.6	25.8	26.4	18.3	19.9	17.6	18.2	7.8	7.6	18.9
5. Net current voluntary private soc. exp	1.2	1.5	2.2	1.6	5.1	4.8	8.9	2.4	0.2	0.2	1.8
6. Net current private soc. exp. (3+5)	1.2	1.8	2.5	2.2	5.6	5.4	9.2	3.0	2.1	0.2	
7. Net total social expenditure(2+6-T2)	21.6	26.1	28.0	27.6	23.1	24.6	25.2	20.6	8.0	7.5	20.5

Source: OECD, 2006. Social Expenditure Da26.1tabase (SOCX, www.oecd.org/els/social/expenditure).

Table 7: Annual Budget Expenditure of Central Government by Function (Billion won, %)

	Expenditure	Net Defence	Education	Social Development	Economic Development	General Administration	Grants to Local Gov't	Repayment of Debt & Others	Ratio of Expenditure to GNP
1977	2,739	34.6	16.6	4.6	22.7	11.0	6.7	3.7	14.9
1980	6,486	35.6	16.9	7.2	21.5	9.7	6.3	2.7	16.7
1985	12,406	30.6	20.1	6.8	21.3	10.1	8.1	4.1	14.8
1987	15,794	30.4	19.8	8.2	19.4	9.9	10.2	2.0	13.7
1991	31,283	25.4	17.7	10.2	16.4	11.2	11.0	8.0	14.6
1995	51,498	22.1	18.8	8.1	22.3	10.6	10.6	7.4	13.6
1996	58,490	22.1	18.9	8.6	22.4	10.7	10.9	6.4	14.0
1997	63,962	21.3	18.9	9.2	25.4	10.7	10.7	3.8	14.1
1998	73,225	19.3	16.6	9.8	30.3	10.0	9.6	4.4	16.4
1999	80,509	17.3	14.2	11.4	29.2	9.7	8.3	9.9	16.6
2000	87,464	17.7	14.5	12.1	27.3	9.3	9.5	9.6	15.1
2001	98,668	16.4	18.1	13.8	25.8	9.3	12.5	4.1	15.9
2002	108,918	16.0	17.2	12.7	29.4	9.3	11.3	4.2	15.9
2003	117,222	15.8	17.7	13.1	27.7	10.8	12.6	2.3	16.3
2004	118,236	16.9	18.7	14.0	26.0	10.1	12.2	2.1	15.2
2005	135,215	16.3	20.3	13.1	20.8	10.8	14.9	3.8	16.6
2006	144,807	16.2	19.7	13.4	19.5	11.8	14.8	4.6	16.5

Source: Editing Committee, *40 Years' History of Korean Fiscal Policy*, Vol. 5, Fiscal Statistics (2), Korea Development Institute, 1991. Ministry of Planning and Budget, "Annual Budget Expenditures FY 1996-2006", 2006.

Table 8: Application Rate of Social Insurance and Working Condition for Employment Type (%)

	Standard worker						Non standard worker					
	01	02	03	04	05	06	01	02	03	04	05	06
National pension	92.7	92.3	94.8	96.6	98.0	98.2	19.3	21.6	25.4	30.3	32.8	33.6
Health insurance	94.8	94.6	95.8	97.3	98.3	98.4	22.2	24.9	27.8	33.0	33.4	34.5
Employment insurance	80.0	79.1	78.0	80.5	81.6	82.9	20.7	23.2	25.0	29.7	30.7	31.5
Retirement allowance	94.3	93.2	96.9	99.1	98.2	98.0	13.6	13.9	15.3	18.6	19.6	19.1
Bonus	93.1	92.5	95.3	96.2	96.3	95.8	14.0	14.0	13.9	16.5	17.5	18.7
After-hours allowance	75.6	76.8	75.2	81.0	80.6	77.0	9.7	10.1	10.4	13.7	14.6	14.0
Leave allowance				83.6	82.3	77.2				16.0	15.9	16.3
5 day work week					47.1	51.7					17.1	21.3
Documentation of work contract			15.6	49.1	50.2	53.6			15.7	27.8	29.3	31.3

Source: Kim, Yousun, 2006. "Size and Conditions of Non Standard Workers: Result of Added Survey for Economically Active Population Survey", *Labor Society Bulletin*, November, Korea Labor and Society Institute.

Table 9: Tax Level and Structures in Main OECD Countries, 2004

Main tax categories as percentage of GDP

	Total tax revenue	Personal income tax	Corporate income tax	Social security contributions			consumption tax	Property tax
				subtotal	employee	employer		
United States	25.5	8.9	2.2	6.7	3.0	3.4	4.0	3.1
United Kingdom	36.0	10.3	2.9	6.8	2.8	3.7	11.1	4.3
Japan	26.4	4.7	3.8	10.0	4.3	4.5	4.7	2.6
Korea	24.6	3.4	3.5	5.1	3.0	2.1	8.7	2.8
Denmark	48.8	24.7	3.2	1.2	1.1	0.0	15.1	1.8
Finland	44.2	13.5	3.6	11.9	2.1	9.0	13.6	1.1
France	43.4	7.4	2.8	16.1	4.0	11.0	10.8	3.3
Germany	34.7	7.9	1.6	14.1	6.1	6.9	9.8	0.9
Sweden	50.4	15.8	3.2	14.3	2.8	11.3	12.6	1.6
OECD Total	35.9	9.1	3.4	9.4	3.0	5.5	10.8	1.9
OECD America	26.0	10.3	2.8	5.0	2.5	3.1	7.5	2.3
OECD Pacific	29.4	8.8	4.6	3.8	1.8	1.7	8.2	2.5
OECD Europe	38.3	9.1	3.3	10.9	3.3	6.5	11.7	1.8
EU-19	38.8	8.9	3.1	11.7	3.5	7.0	11.6	1.8
EU-15	39.7	10.1	3.2	11.3	3.6	6.6	11.4	2.1

EU-15 area countries are: Austria, Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, Netherlands, Portugal, Spain, Sweden, and United Kingdom.

EU 19 countries are: EU-15 countries plus Czech Republic, Hungary, Poland, and Slovak Republic.

Source: OECD, *Revenue Statistics 1965-2005*, 2006.

Table 10: Income Tax plus Employees' and Employers' Social Security Contributions

(as % of labor costs) 2005¹⁾

Country ²⁾	Total Tax Wedge (1)	Income Tax (2)	Social Security Contributions		Labour costs ²⁾ (5)
			employee (3)	employer ³⁾ (4)	
Germany	51.8	17.3	17.3	17.3	53,278
United Kingdom	33.5	15.7	8.2	9.6	50,982
France	50.1	10.8	9.6	29.7	47,824
Sweden	47.9	18.1	5.3	24.5	43,916
Norway	37.3	18.8	6.9	11.6	43,554
Finland	44.6	20.1	5.1	19.4	43,443
Denmark	41.4	30.2	10.6	0.5	38,664
Japan	27.7	5.9	10.5	11.3	43,122
Korea	17.3	2.5	6.5	8.2	41,086
United States	29.1	14.6	7.3	7.3	34,144
Mexico	18.2	5.6	1.4	11.2	12,031
OECD average	37.3	13.3	8.8	15.2	36,205
EU-15	42.1	14.2	10.0	17.8	42,317
EU-19	42.5	13.1	10.6	18.8	37,325

Note: EU-15 area countries are: Austria, Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, Netherlands, Portugal, Spain, Sweden and United Kingdom.

EU-19 area countries are: EU-15 countries plus Czech Republic, Hungary, Poland and Slovak Republic.

1. Single persons without children at the income level of the average worker.

2. Countries are ranked by decreasing labour costs (US dollars using PPP).

3. Payroll taxes only in the case of Australia and employees social contributions plus payroll taxes for Austria, Hungary and Sweden.

Source: OECD, *Taxing Wages: 2004-2005*, 2006. OECD calculations based on country submissions and OECD, *Economic Outlook*, No. 77, June 2005.

<Table 11> Public and Private Education Expenditure, 2003

as percentage of GDP

	Total			Primary and secondary			Tertiary		
	public	private	subtotal	public	private	subtotal	public	private	subtotal
Australia	4.3	1.5	5.8	3.4	0.7	4.1	0.8	0.8	1.5
United States	5.4	2.1	7.5	3.9	0.3	4.2	1.2	1.6	2.9
United Kingdom	5.1	1.0	6.1	4.0	0.6	4.8	0.8	0.3	1.1
Japan	3.5	1.2	4.8	2.7	0.3	3.0	0.5	0.8	1.3
France	5.8	0.5	6.3	4.0	0.3	4.2	1.7	0.1	1.8
Germany	4.4	0.9	5.3	2.9	0.5	3.5	1.0	0.1	1.1
Denmark	6.7	0.3	7.0	4.1	0.1	4.2	1.7	0.1	1.8
Finland	6.0	0.1	6.1	3.9	-	4.0	1.7	0.1	1.8
Sweden	6.5	0.2	6.7	4.5	-	4.5	1.6	0.2	1.8
Spain	4.2	0.5	4.7	2.8	0.2	3.0	0.9	0.3	1.2
Korea	4.6	2.9	7.5	3.5	0.9	4.4	0.6	2.0	2.6
OECD average	5.2	0.7	5.9	3.6	0.3	3.9	1.1	0.4	1.4

Source: OECD, Education at a Glance, 2006.

<Table 12> Public education expenditure per student, 2003

US dollars using PPP

	Elementary	Secondary	Tertiary (excluding R&D)	Tertiary (including R&D)	Tertiary R&D
Australia	5,494	7,788	8,645	12,406	3,761
United States	8,305	9,590	21,566	24,074	2,508
United Kingdom	5,851	7,290	9,130	11,866	2,735
Japan	6,350	7,283	-	11,556	-
France	4,939	8,653	7,330	10,704	3,374
Germany	4,624	7,173	7,282	11,594	4,311
Denmark	7,814	8,183	10,190	14,014	3,824
Finland	5,321	7,402	7,506	12,047	4,530
Sweden	7,291	7,662	8,278	16,073	7,795
Spain	4,829	6,418	6,563	8,943	2,379
Korea	4,098	6,410	6,213	7,089	876
OECD average	5,450	6,962	8,093	11,254	3,254

Source: OECD, *Education at a Glance*, 2006.