

Assessing Economic Dynamism in Korea

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Economic dynamism can be defined as the pace or scale of creative destruction and innovation, occurring as the manifestation of entrepreneurship, that work towards enhancing the allocational efficiency and productivity. While Korea had received considerable attention in the past as one of the most dynamic economy in the world, growing concerns have been raised in recent years about the country's diminishing economic dynamism as its low growth appears entrenched among others. Against this backdrop, this paper examines how Korea's economic dynamism has evolved over the past fifteen years from various angles based on major macroeconomic indicators, firm dynamics, industrial structure, and innovative capacity.

First, Korea's macroeconomic indicators signify that the country's overall economic vitality has steadily weakened, with its growth decelerating, growth gap vis-à-vis advanced economies narrowing, growth potential lowered, productivity growth slowing, and population aging. Second, firm dynamics in Korea reveal that there have been delays in the exit of inefficient firms, declines in the entry of new firms and in the number of jobs newly created as a consequence, and a decrease in the likelihood of scale-up of small- and medium-sized enterprises due to a falling mobility across firm sizes. Third, Korea's industry dynamism appears to have declined, as the speed of change in industrial structure has slowed down, the productivity gap among industries has widened, and the country's export has heavily resorted to only a few products with little changes to the product mix. Fourth, Korea's innovative capacity too appears to have deteriorated, as manifested by the poor R&D efficiency and an increasing dependence on the import of technology from advanced economies due to the lack of technological innovation. Lastly, in an attempt to make an overall assessment, the above-mentioned features are collectively used in developing an economic dynamism index, showing a secular decline in Korea's economic dynamism for the past fifteen years.

To revive the dynamism of the Korean economy, it is essential above all to strengthen economic fundamentals through structural reforms and to create an

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environment conducive to incessant creative destruction and innovation so as for entrepreneurship to manifest itself. Specifically, regulatory reforms should be carried out to ease such regulations that unduly limit competition and discourage innovative entrepreneurs from starting a new business; and an environment conducive to promoting fair competition needs to be created by improving corporate governance and prohibiting unfair business practices for instance. Also, a complete overhaul of corporate restructuring system is necessary to facilitate non-viable zombie firms to exit the market in a timely fashion so as to promote a more efficient allocation of scarce resources. These efforts then could contribute to creating more jobs as well.

***Disclaimer:** The views expressed in this paper are those of the authors and do not necessarily represent the official views of the Bank of Korea. Any citation of this paper therefore should specify the names of the authors.*

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