

**FROM POST-WAR FLEDGLING EXPERIMENTATION
TO KOREAN-VERSION NEW DEAL:**

Where is the End of Mudding Through in Korean Housing Policy?

**Housing Policy GSD 5473
SPRING 2005
KWAN OK LEE**

TABLE OF CONTENTS

<i>Section</i>	<i>Page</i>
Executive Summary	1
I. Introduction	9
II. Housing Market	12
1. Expansion of Housing Demand	13
2. Chronic Housing Shortage	14
3. Consequences of Demand-Supply Mismatch	15
III. Review of the Housing Policies	18
1. Major Policy Measures	19
2. Evolution of Housing Policy	24
3. Gains and Losses from the Housing Policies	28
IV. Changing Directions in the Housing Policies	35
1. Ensuing Changes	36
2. Current Issues in Housing Policy	41
3. Korean Version of “New Deal”	45
V. Concluding Remarks	49
References	53

TABLES

<i>Table</i>	<i>Page</i>
1 Demand-Supply Mismatch: Causes and Results	3
2 Summary of Housing Policy Objectives and Measures	4
2.1 Changes of Population and Households	13
2.2 Housing Tenure Comparison	17
3.1 Types of Public Rental Housing	23
3.2 Numerical Achievement of the Two Million Houses Project	29
3.3 Housing Supply Ratio Comparison	30
3.4 Housing Investment Trend	31
3.5 Factors Limiting Private Sectors' Participation	33
4.1 Key Indicators of Primary and Secondary Mortgage Markets	39
4.2 Changing Pattern of Rental Type	43
4.3 Rate of <i>Jeonse</i> Deposit Increase	43
4.4 <i>Jeonse</i> Deposit Increase by Unit Size	43
4.5 Stocks of Rental Housing	44

FIGURES

<i>Figure</i>	<i>Page</i>
1 Evolution of Housing Policy and with Milestones	5
2 Impacts of Financial Crisis	6
2.1 Urbanization in South Korea	14
2.2 Changes in Housing Tenure	17
3.1 National Housing Supply Ratio Changes	30

EXECUTIVE SUMMARY

Korea experienced a remarkably rapid economic growth since the 1960's and the per capita GNP peaked in 1996 with over US\$ 11,380. With the fruits of such economic growth, the housing situation also has substantially improved: the national census of 2000 indicates that the number of housing units per one hundred households was 96 units and the average size of housing unit, about 82m². The figures look quite encouraging; nevertheless, the country has yet to solve its housing problems.

Demand-Supply Mismatch in the Housing Market

The most serious one has been the mismatch between housing demand and supply in the major metropolitan areas, particularly in Seoul, where the increase in housing stock fell short of the household increase due to continuing in-migration. As a result of accelerated urbanization with growing manufacturing industries, urban population rose from 39.1% in 1960 to 87.2% in 1997. More than four out of every five Koreans now live in urban centers of 20,000 people and more. Urbanization also brought about various problems including inadequate sewerage and transportation systems and urban poverty. The gap between housing units and households was further aggravated by the changes in the family structure and the increase of personal income in the 1970s and 1980s.

In spite of the continual increase in housing demand, housing production, until the Two Million Houses Construction Project¹ that started in 1988, could not catch up with the increase in households. During the early state of economic development, housing was viewed as a low-return sector relative to manufacturing and export industries. Therefore, government tried to discourage the nation's scarce capital from flowing into residential housing. Moreover, the continual tension between north and south necessitated enormous resources for national defense leaving little room for social investment. As a result, housing was not given great priority and there developed a worsening housing shortage. Shortage of residential land in urban areas has also been the primary factor that causes housing supply to be inelastic.

The ensuing mismatch between housing demand and housing supply led inevitably to a

¹ It was not until 1988 when government realized that the problem of housing shortages could not be resolved without a massive increase in supply. Such a change in housing policy was materialized as a drive to build two million new dwellings over the 1989-92 periods. Consequently, housing production per year increased by more than 100 % from 227,000 for the 1977-86 period to 550,000 for the 1987-96 period. The important point is that the level of residential investment was a policy variable to a large extent.

rise in housing prices. This weakened housing affordability and increased housing insecurity for urban dwellers. The sustained housing price increases brought about housing speculation and some segments of society enjoyed large capital gains. On the other hand, housing speculation meant enormous capital gains for specific groups thus widening household income distribution and inviting social problems. The following matrix summarizes causes and results of demand-supply mismatch in Korean Housing Market.

Table 1 Demand-Supply Mismatch: Causes and Results

	<i>Causes</i>		<i>Results</i>
	Expanded Demand	Insufficient Supply	
1950	North to South Migration after the Korean War	Wartime Destruction of Housing	No Acute Housing Shortage
1960	Population Growth	Limited Investment on Housing from “Economic Growth First” Principle of the Government	Beginning of Housing Shortage
1970	Urbanization and Formation of Nuclear family		Shortage of Residential Land in Urban Areas
1980	Personal Income Growth	Housing Speculation	

Review of the Housing Policies

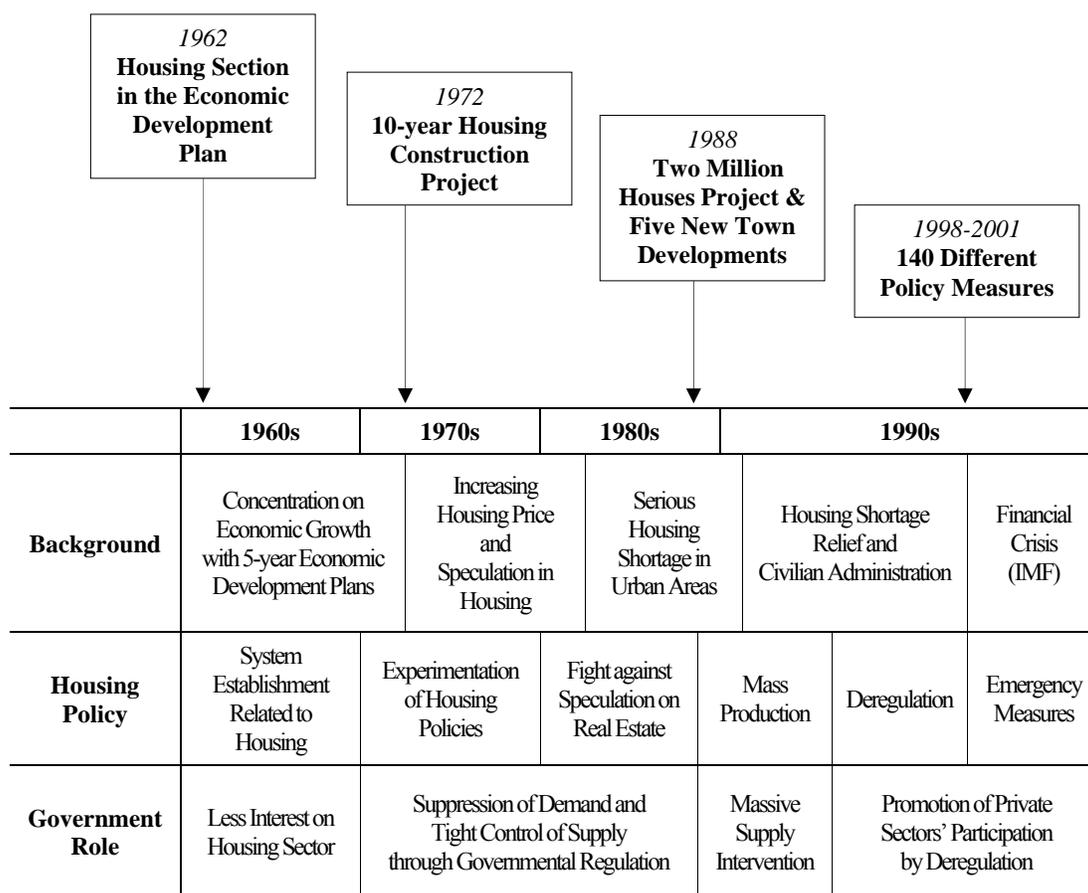
Against the consequences of demand-supply mismatch in the housing market, the primary objectives of Korea’s housing policy can be seen to be the reduction of house prices, the balance between supply and demand, and the ending of speculation in housing. In order to tackle the demand-supply mismatch problem and its related problems such as price increases and housing speculation, Korean government took a series of policy measures. These policy measures can be grouped under three headings: supply measures; anti-speculation measures through the stabilization of housing price; and policies for low income households. Key measures of housing policy are presented below (*Table 2*).

Table 2 Summary of Housing Policy Objectives and Measures

Objectives	Policy Measures		Implementation
Balance between Demand and Supply	Supply Expansion	Supply of Residential Land	Public Sector's Development and Provision of Land for Massive Housing Construction
		Expansion of Supply-Side Housing Fund	Expansion of Public Investment and Private Sector Funds for Housing Supply
		Favorable Legislature	Privileges of Residential Developers in Loans and Land Allocation
Ending of Speculation in Housing	Anti-Speculation/ Housing-Price Stabilization	Housing Price Regulation	Upper Ceiling on the Price of New Dwellings (<i>Expired in 1998</i>)
		Controlled Allocation of New Houses	Requirement of Applicants' Subscription of the Housing Contractual Savings to Get the First Priority for House Purchase
		Social Recovery of Speculative Gains	Capital Gains Tax System and Housing Bond Bidding System
Reduction of Housing Burden of Low-Income Families	Housing Policy for Low-Income Families	Housing Allowance System Governed by the Ministry of Public Health and Social Welfare	Cash Assistance (US\$ 250 – 500 / mo.) Based on Income, Asset, and Number of Family Members
		Low-Income Housing Program Governed by the Ministry of Construction and Transportation	Provision of Public Rental Housing Units and Supply-Side Subsidies
			Demand-Side Rental and Home Loan Assistance and Tax Deduction
			Size-Based Construction Quota System to Compel Small-Units' Supply (<i>Expired in 1998</i>)
Residential Environment Improvement and Minimum Housing Standard (<i>Only in Seoul City</i>)			

The first five-year housing plan in Korea began in 1962 in parallel with the five-year Economic Development Plan, but the housing issues were only marginally dealt with. As the Korean economy improved and the income of households gradually increased, absolute housing shortages and high prices were perceived as the major housing problems in the 1970s. Therefore, after 1970s, massive housing production was initiated and several regulations were imposed on the housing sector. However, only ten years ago, such an effort of expanding housing production and provision of low-income housing was materialized by the Two Million Houses Construction Project and Five New Town Developments around Seoul Metropolitan Area of 1988-1992. More recently, after the financial crisis of 1997-1998, the country went through severe economic restructuring processes and various emergency measures were put into effect to revitalize the housing market, including those which resulted in housing speculation. This evolution of Korean housing policy is summarized with key milestones in *Figure 1*.

Figure 1 Evolution of Housing Policy and with Milestones

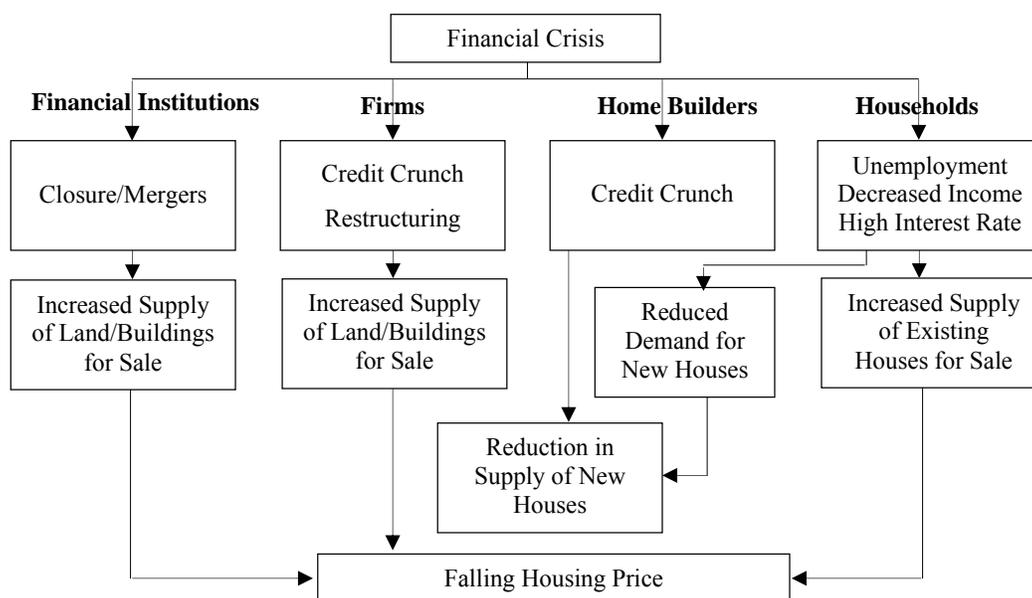


Thanks to those government efforts, there has been a tangible improvement in the housing sector, but the problem of inter-regional discrepancy in housing consumption level has remained as serious as ever. The anti-speculation measures were basically intended to discourage “speculative minds,” but there was little evidence that they had been effective in controlling speculative behavior. The issue of low-income housing has been brought up over the last 30 years, but the solution is not satisfactory because most of the low income housing programs are proven to be very costly to implement. In terms of the role of government, one recognizes that tight market control policy would not work when the demand for housing rapidly increase. Equally undesirable is any drastic measure to expand the housing stock through new construction within a short period of time without due consideration of the input market constraints.

Changing Direction in the Housing Policies

More recently, after the financial crisis of 1997-1998, the country went through severe economic restructuring processes under the International Monetary Funds. The crisis started with a shortage of foreign exchange reserve. Demand for homes and land fell drastically as a result of extremely high rate of interest and of reduction in bank credit. Housing production declined substantially and consequently, almost three quarters of homebuilders went bankrupt, and the housing industry experienced bubble to bust. The figure below shows the impact of financial crisis on the housing sectors.

Figure 2 Impacts of Financial Crisis



Various emergency measures were put into effect to revitalize the housing market, including those which resulted in housing speculation. These measures were effective in raising housing prices and thus, attracting idle funds into the market. The recovery of the housing market contributed to that of the nation's economy because the housing industry created almost a million jobs a year. It also had very high-income multiplier effect. But equally serious were continuously rising price and also increasing number of households who could not afford to purchase adequate housing. Coupled with increasing unemployment rate, inequality in income and asset distribution was getting worse and there has been a gradual reduction of the middle class, for which both the housing speculation and consumption-oriented economy are primarily responsible.

All these social issues following the financial crisis have suggested that more appropriate and effective housing policies should be pursued for correcting the past mistakes and easing unequal housing consumption between social classes. Reflecting the inequality situation, emerging issues have focused on the housing welfare policies, addressing inadequate rental housing system and poor living environment of low-income households. Housing security for low-income people came to be one of the social issues due to the rapid increase of *Jeonse*² deposit and transferring *Jeonse* to monthly rental with high interest rate applied. To make the rental housing market more worse, the stock of long-term public rental housing in Korea is at a mere 2.4 percent of total housing stock, significantly lower than in advanced countries. In addition, 3.34 million households, that is, 23.4% of the total, are still living in substandard housing units and suffering from poor living conditions and excessive housing prices.

Based on this background, the government has established a comprehensive housing policy plan in 2003, which will guide housing policy for Korea for the next 10 years. This plan aims to improve housing welfare and to curb social and regional inequality in terms of housing allocation and access. In 2004, the government also designated Korean Version of "New Deal" policy, as a stimulus measure focused mainly on rescuing the struggling construction industry through a series of large development projects such as provision of one million public rental housing and the development of new towns around Seoul Metropolitan Area. This "New Deal" project is expected to serve as a catalyst of domestic economic development as well as a housing welfare measure for

² As a unique lease system in Korea, the tenant makes a lump sum deposit with the landlord to rent housing and the deposit is refunded when contract expires. He does not pay a monthly rental fee and instead gives up the interest on the deposit.

low-income households through broad public projects. It would be interesting to watch whether or not South Korea's ambitious "New Deal" policy could be a two-bird-one-stone solution as the U.S. government pulled itself out of the Great Depression 75 years ago.

Taking all those previous policies and current issues into account, the following suggestions are made for the future housing policy directions. They are basically of the four types; deregulation consistent with market oriented economic and financial policy, promotion of housing industry, improvement of policy instruments; housing finance and housing related taxation in particular, and equitable distribution of housing welfare.

I. INTRODUCTION

Korea has experienced remarkably rapid economic growth since the 1970s and the per capita GNP peaked in 1995 with over US\$ 10,000, but fell down to US\$ 9,770 in 2000 due to the financial crisis of 1997-1998. With the fruit of such economic growth, housing situation also has substantially improved: according to the census of 2000 the number of housing units per one hundred households was 96 units and the average size of housing unit, about 82m².

One of the key problems of housing in Korea was housing shortage, being measured in terms of the number of housing stock over that of the households. Accordingly, government efforts had been concentrated on the expansion of housing production and provision of low-income housing. Only ten years ago, such an effort of expanding housing production and provision of low-income housing was materialized by the Two Million Houses Construction Project of 1988-1992. Shortage of residential land was the primary factor that caused housing supply to be inelastic. The key strategy was to supply a large amount of residential land through new town developments. Another important program was provision of 190 thousand units of low-rent public rental housing, primarily geared to the lowest 10 percentile of the nation's population.

More recently, after the financial crisis of 1997-1998, the country went through severe economic restructuring processes under the International Monetary Funds. The crisis started with a shortage of foreign exchange reserve. Demand for homes and land fell drastically as a result of extremely high rate of interest and of reduction in bank credit. Housing production declined substantially and consequently, almost three quarters of homebuilders went bankrupt, and the housing industry experienced bubble to bust.

Various emergency measures were put into effect to revitalize the housing market, including those which resulted in housing speculation. These measures were effective in raising housing prices and thus, attracting idle funds into the market. Thanks to such market promotion measures the market revived very quickly since 1999 and recovered its price level comparable with that of 1996-1997, i.e., prior to the financial crisis. The recovery of the housing market contributed to that of the nation's economy because the housing industry created almost a million jobs a year. It also had very high-income multiplier effect. But equally serious were continuously rising price and also increasing number of households who could not afford to purchase adequate housing. It is very likely that the vicious circle will go on and easy solutions are not in sight.

This paper seeks to show a general picture of Korean housing policies in the past and at present. Next section examines the demand-supply mismatch in the housing market by the reciprocal analysis of demand expansion and supply limitation. After that, it draws the consequential problems from the mismatch in the housing market. Section III reviews major policy measures to solve those problems and the evolution of Korea's housing policy since 1960s. It also analyzes what are the gains and losses from the housing policy measures and how the roles of the public and private sector in the housing sector changed over time as the governmental policies evolved. Section IV presents the ensuing changes in the housing market and industry after financial crisis and current issues in housing policy evolved from those changes. In addition, the brand-new housing policy – what is called “Korean-Version of New-Deal” – emerged by new administration is briefly discussed. And finally, Section V suggests the direction for future housing policies.

II. HOUSING MARKET

1. EXPANSION OF HOUSING DEMAND

In general, housing demand increases with the increase in the number of households, which increases with population increase and the formation of nuclear households (Murphy 1990). In turn, population increase depends on natural increase and migration, which includes rural to urban migration. Coupled with these demographic phenomena, the increase of personal income causes housing demand to drastically expand as well.

The population in 1960, the year when the first population census took place, was 25 million, rising by 2000 to 46.1 million, or 1.85 times. The annual rate of population increase of 2.69% in 1960 had slowed down to 0.62% by the 1990-2000 period. The number of households rose more rapidly than population because of the rise of nuclear households. Rapid industrialization combined with urbanization destroyed the traditional system of extended families resulting in a rapid rise in the number of households. Thus while over the period 1960 to 2000 population increased by 85%, the number of households increased by 174% with the average number of persons per household decreasing from 5.6 to 3.2 (*Table 2.1*).

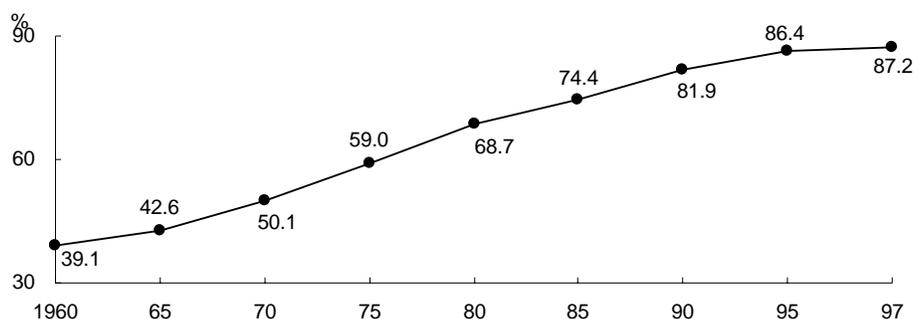
Table 2.1 Changes of Population and Households

	1960	1970	1980	1990	2000	Change: 1960 to 2000
Population (000)	24,989	31,466	37,436	43,411	46,136	1.85
Household (000)	4,361	5,576	7,969	11,355	11,928	2.74
Persons per Household	5.6	5.4	4.6	3.7	3.2	0.57

Source: National Statistical Office (2000)

There were large differences in population increase by region. The urban population, which was 9.8 million in 1960, increased by more than 4 times to 40.8 million in 1997, representing 87.2 percent of the total population. The excessive urbanization led to a concentration of households in major cities that was beyond the capacity of their housing markets to cope with (Lee 1996b). In contrast, the rural population that numbered 15.2 million in 1960 radically shrank to 5.9 million in 1997. *Figure 2.1* shows the rapidity of the urbanization taking place especially in the 1960-80 period. After 1980, the speed of urbanization slowed down.

Figure 2.1 Urbanization in South Korea



Source: Ministry of Construction & Transportation (2000)

Housing demand depends also on income (Charles 1977; Lim et al.1980). With the exception of the early 1970s, marked by the first oil crisis, and the early 1980s, marked by the second oil crisis, the Korean economy maintained an annual growth rate of 9 percent or more. As a result, GNP per capita increased from US\$ 87 in 1962, the first year of the first Five-year Economic Development Plan (EDP)³, to US\$ 11,380 in 1996, the last year of the seventh Five-year EDP. Such an increase in income has inevitably strengthened housing demand.

2. CHRONIC HOUSING SHORTAGE

In spite of the continual increase in housing demand, housing production, until the Two Million Houses Construction Project that started in 1988, could not catch up with the increase in households. Therefore, the most significant characteristics of the Korean housing was housing shortage, defined as the number of dwelling units that must be constructed if every household were to have exclusive use of a dwelling. The housing shortage rate increased from 15.8 percent in 1960 to 27.6 percent in 1990 until the government launched the Two Million Houses Construction Project.

³ Until the 1960s, Korea was a largely agricultural country, with a lopsided trade imbalance and relatively few exports. With the launching of the First Five-Year Development Plan in 1962, Korean economy began a rapid transformation that placed South Korea twelfth among the world's trading nations by the mid-1980s. As one would expect, Korea's highest annual GNP growth rates were recorded in the earlier stages of development. But even in the 1980s, Korea's GNP growth rates have been among the highest in the world, reaching 12.3 percent in 1986.

The shortage had its roots in the wartime destruction of a major portion of the existing stock and the north to south migration of over a million people during and after the Korean War. The large initial gap between housing units and households was further aggravated by the huge expansion of housing demand driven by the high population growth in the 1960s, rural-to-urban migration, and changes in the family structure in the 1970s and 1980s. Another principal reason was insufficient housing investment from the fact that the housing industry was treated as a ‘nonproductive’ or ‘consumption’ sector. Housing investments were considered as counter-productive to economic growth (Donnison and Ungerson 1982).

In fact, the housing shortage crisis was aggravated by economic development policies. Right from the first Five-year Economic Development Plan (EDP), which ran from 1962, Korea’s economic development policy was based on the “Growth First” principle and most of the available resources were allocated to economic growth. For example, during the first four Five-year EDPs, the priority was escape from poverty, and housing investment constituted no more than 3 percent of GNP.⁴ Moreover, the continual tension between north and south necessitated enormous resources for national defense leaving little room for social investment. As a result, housing was not given great priority and there developed a worsening housing shortage.

Shortage of residential land has also been the primary factor that causes housing supply to be inelastic. Rapid urbanization was precipitated by a massive rural to urban migration and rapid industrialization. Naturally, demand for urban land increased. But urban land could not be supplied timely. The chronic shortage of urban land impacted on the housing market simultaneously.

3. CONSEQUENCES OF DEMAND-SUPPLY MISMATCH

The basic source of problems in Korean housing market was a mismatch between the

⁴ During the first Five-year EDP (1962-66), housing investment was a mere 1.6 per cent of GNP and the five-year housing production was no more than 325,000 units. From 84.2 percent in 1960, the housing supply ratio dropped to 81.2 percent in 1965. The housing investment ratio during the second Five-year EDP (1967-71) was 2.6 percent, which was considerably higher than it was during the previous period. Although about 540,000 units were built, a little more than the number in the plan, the housing supply ratio dropped by 1970 to 78.2 percent.

demand and supply of housing. Housing demand was expanded rapidly by the high population growth in the 1960s, rural-to-urban migration and changes in the family structure in the 1970s and 1980s. Nevertheless, if housing production was increased adequately and timely, then the problems might be mitigated. But because of several reasons including limited investment on housing industry and inelastic land supply, housing was not sufficiently provided. As a result, until the end of the period of the Two Million Houses Construction Project, supply could not catch up with demand.

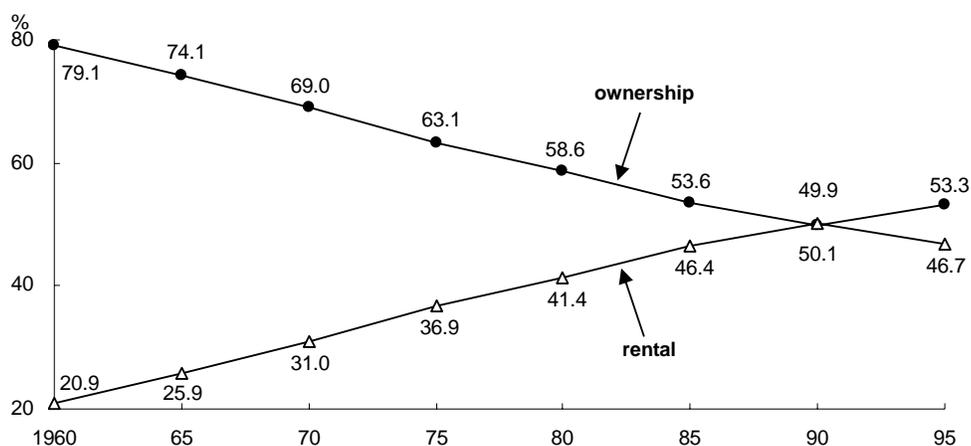
In the meantime house prices continued to rise rapidly. In the period 1975-90, incomes rose by 3.5 times, the consumer price index by 4.1 times but house prices by 6.5 times (Lee and Yang 1992). In particular, during the middle of the 1970s and the construction boom in the Middle East, a huge amount of foreign currency flowed into Korea and housing prices skyrocketed. Moreover, this construction boom provoked serious shortages of cement, steel and other construction materials, which added fuel to price inflation in the domestic market. The excess demand for apartments was so great that the ratio of applicants to apartments constructed by the Sam-Ik Company was 55 to 1 (Ministry of Construction and Transportation 1987).

In 1979, the second oil shock brought about economic recession. The Korean economy experienced negative growth for the first time and housing construction also experienced a slump. The government adopted housing construction recovery measures in 1980. After the latter part of 1980, the balance of payments was especially favorable allowing increased liquid funds to flow into housing. The economy recovered and began to experience rapid growth in 1981 and house prices began to rise again (Korea Research Institute for Human Settlement 1992). This rise in housing prices invited housing speculation and was seen to undermine the desire to work of the workers (Van Vliet and Hirayama 1994). Moreover, house price rise worsened housing affordability and the price to income ratio increased from 5.63 in 1988 to 9.38 in 1991 (Kim 1993).

The increasing house price affected the housing tenure pattern as well. Korea had long been a nation predominantly of homeowners, as indicated in *Figure 2.2*. In 1960, 79.1 percent of the housing units were owner occupied; whereas 20.9 percent were of rental status. In the last 30 years the ratio of home ownership decreased substantially to 49.9 percent. While the pattern of change was pervasive, there were substantial geographic variations in home ownership. As shown in Table 1.3, less than half of urban households (46.2 percent) owned homes, a sharp decrease from 85.8 percent in 1970;

whereas still more than 77 percent of the rural households were owner occupied in 1995 (Table 2.2). This indicates the problem of inter-regional discrepancy in housing consumption level has remained as serious as ever.

Figure 2.2 Changes in Housing Tenure



Source: Ministry of Construction & Transportation (2000).

Table 2.2 Housing Tenure Comparison

	1970		1980		1990		1995	
	Number	Percent	Number	Percent	Number	Percent	Number	Percent
Urban Areas								
Total Units	1,398	100.0	4,669	100.0	8,462	100.0	10,032	100.0
Owner Occupied	718	51.3	2,007	43.0	3,429	40.5	4,641	46.2
Renter Occupied	680	48.7	2,662	57.0	5,033	59.5	5,391	53.7
Rural Areas								
Total Units	2,962	100.0	3,300	100.0	2,892	100.0	2,926	100.0
Owner Occupied	2,516	84.9	2,664	80.7	2,238	77.4	2,268	77.6
Renter Occupied	446	15.1	636	19.3	654	22.1	658	22.4

Source: Census of Population and Housing, each year

III. REVIEW OF THE HOUSING POLICIES

1. MAJOR POLICY MEASURES

Against the consequences of demand-supply mismatch in the housing market, as described in the previous chapter, the primary objectives of Korea's housing policy can be seen to be the reduction of house prices, the balance between supply and demand, and the ending of speculation in housing. In order to tackle the demand-supply mismatch problem and its related problems such as price increases and housing speculation, Korean government took a series of policy measures (Lee 1990). These policy measures can be grouped under three headings: supply measures; anti-speculation measures through the stabilization of housing price; and policies for low income households.

Policy to Expand Housing Supply

In view of the chronic housing shortage and demand-supply mismatch, the government adopted several strategies to expand housing supply from early days through the Two Million Houses Construction Project of 1998-1992. The key strategies to encourage housing supply have been through the supply of residential land, the expansion of supply-side housing fund, and some favorable legislature.

Various techniques have been introduced and applied to develop and provide land for massive housing construction. The Land Readjustment Project by land owners' cooperation and the National Housing Land Development Project under the Act of Housing Construction Promotion were executed in the 1970s. The Act of the Housing Site Development Promotion was enacted to correspond to the large increase in the demand for land in the 1980s. The Public Housing Site Development Project, which allows public organizations to purchase private lands by compulsion, was introduced. However, as the viewpoints on the housing problem and housing site development changed in the middle of 1990s, the Public housing Site Development Project began to be varied. In 1994, public organizations, which enjoyed a monopoly in acquiring land for development, had to compete with private constructors through the easing of the development restrictions on semi-farm land. They also have more trouble in purchasing land by force because the local self-government system has been established.

It was given a low priority in early days and the expansion of housing funds, especially private sector funds, became a major issue. To address this issue, in 1969, the Korea

Housing Bank⁵ was established. Until the Korea Housing Bank became privatized in 1998, it had been making loans for housing construction, purchase, land development and other related activities. The National Housing Fund (NHF)⁶ was also established in 1981 in order to support long-term and low rate loans for housing construction. Especially, during Two Million Houses Construction Project, the government decided to provide one trillion Won (about US\$ 0.8 billion) of budgetary assistance and the loan to value ratios for the National Housing Fund loans and the Korea Housing Bank loans increased from 30-40 percent to 40-50 percent. As a result, the supply of housing funds quadrupled in less than four years from US\$ 1.08 billion in 1987 to US\$ 4.43 billion in 1990.

To encourage private sectors' construction of housing, the government has enacted some favorable regulations and removed various regulations restricting residential developments. By adoption of the Housing Construction Promotion Law (HCPL), house builders were distinguished from general builders. Among the registered residential builders, those which had superior capacity were chosen as the 'designated builders' which made them eligible to some privileges in construction loans, residential sales loans and land allocation. This resulted in the active participation of large industrial conglomerates in housing construction (Kim W. J. 1997). Meanwhile, for the success of Two Million Houses Construction Project, the previous system of price control for new housing was made more flexible by indexing the controlled price to the general price increase. In addition, the floor ratio and land coverage ratio was eased so that low income housing such as low rise collective dwellings could be produced more easily.

Anti-Speculation/Stabilization of Housing Price

Between the 1960s when Korea's economic take off began and the early 1990s when the Two Million Houses Construction Project started to give results, housing speculation was always active and considered a social problem. The government reaction to this took three forms: housing price regulation; controlled allocation of new

⁵ As of the end of 1996, the Korea Housing Bank accounted for 32.2 percent of the total housing loans, while the National Housing Fund accounted for 48.1 percent.

⁶ The National Housing Fund was established in July 1981 to provide long term housing funds at low cost. The funds are raised from types of loans, such as the issue of national housing bonds, fiscal loans, housing deposits, mortgages, etc. The net amount, excluding repayments from total revenue in one year, is used to support long-term and low rate loans for housing construction, housing purchase, and rental housing. The National Housing Fund was raised to total of US\$ 33 billion during 1981~1999, and it supported the construction of a total of 2,913,000 houses.

houses; and social recovery of speculative gains.

Housing price regulation is based on the rationale that the sustained housing price increase has brought about, on the one hand, a widening gap between the poor and the well-to-do and, on the other, increased the housing burden of the poor. In response, in 1977 the government imposed an upper ceiling on the price of new dwellings. Since 1989, the regulated housing price has been indexed as a function of construction cost, measured as the cost of land acquisition added to the standardized construction cost per floor area that varies by year. This system of housing regulation had several shortcomings. The system is applied uniformly throughout the country without allowing for local housing market conditions. One result has been to contribute to the poor quality of housing construction in high cost areas. To make matters worse, the enormous gap between the regulated price and the market price of similar, existing dwellings has led to active speculative activities (Kim J. H. 1991; Kim K. H. 1991; Yoo 1995).

The regulations related to housing allocation were established as administrative measures in August 1977. The price gap between new and existing dwellings has meant that large capital gains accrue to those who are selected to be the buyer of a new dwelling. The regulations require applicants to subscribe to the housing contractual savings with the Korea Housing Bank for a prescribed time period before they are given the first priority for house purchase. The regulations had a number of other stipulations. First, new housing should be allocated first to the homeless-defined as those households that are currently sharing a dwelling with another household. Second, having acquired a new unit, the person is not eligible for selection for a given period of time. Those who have been selected to buy a public sector dwelling lose the eligibility for good. In the case of private housing, the house buyer loses the eligibility for five years. Moreover, in order to prevent speculative gains, the buyer of a public sector dwelling is prohibited from selling the house for five years. If the dwelling is sold within five years, capital gains are taxed away (Korea Housing Institute 1999).

The government has adopted two measures in order to recover speculative gains: a capital gains tax and a housing bond bidding system. The capital gains tax was introduced by the Income Tax Law and levied on capital gains. It was known as an anti speculation tax and made a significant contribution to house price stabilization in the 1960s and 1970s when severe housing shortage caused violent speculative activities. On

the other hand, the capital gains tax has some difficulties regarding its impact on equity. Capital gains tax is not levied in the case where one household owns one house, regardless of the amount of capital gains attained from its transaction. This is liable to favor the well-to-do. If someone owns more than five units for rental purpose, the capital gains are also not taxed away. This creates inequity since those who can afford to invest in no more than four dwellings are not eligible.

The second device was the housing bond bidding system, whereby the house is allocated to whoever offers the highest amount for the housing bond. This system was established in May 1983 in order to reduce speculative activities in the housing market and stabilize house prices. It comes into operation when the amount of potential capital gains, the difference between the controlled price and the market price, was above a pre-established level, i.e. 30 percent or more. The receipts of the bonds were expected to be added to the National Housing Fund and help low income housing. However, in fact the housing bond bidding system resulted in the acceleration of house prices and in response, in November 1989, the bidding was given an upper ceiling.

Low-Income Housing Policy

In Korea, housing policy to the low income households for their stable living condition composes of two parts. One is the housing allowance system governed by the Ministry of Public Health and Social Welfare, and the other is low-income housing program governed by the Ministry of Construction and Transportation including three major forms: the provision of public housing units; demand-side assistances and tax policy; supply-side compulsion, and policies to improve low-income housing condition.

The housing allowance system is not separately operated, but included in the living allowance system. Living allowance is based on the criteria of income, asset, and condition of supporting family members. In 2002, housing allowance was paid with the range from US\$ 250 for 1-person households to US\$ 500 for over 6-person households per month. Beneficiaries were 0.69 million households that reached 5% of total population. Budget expenditure was US\$ 200 million in 2002.

The current public housing programs have started since 1988 when the Korean government announced 'the Plan of Permanent Rental Housing Supply' for securing low-income people's housing. In Korea, public housing units are defined to be those, which are being finance in part by public funds – e.g. government fund or the National

Housing Fund, even though those are owned and operated by private sector.⁷ This public rental housing is classified into two types as shown in the *Table 3.1*: national rental housing with the government's financial assistance and other rental housing which receives subsidies from the National Housing Fund without the government's financial assistance.

Table 3.1 Types of Public Rental Housing

Division	National Rental Housing	Rental Housing with National Housing Fund
Fund Assistance	Finance (30%) National Housing Fund (40%) Korea National Housing Corporation (10%)	National Housing Fund -below 60m ² : \$22,500 per unit (40% of construction cost), 3% interest rate -60-85m ² : \$27,000-45,000 per unit (50% of construction cost), 5.5% interest rate
Occupiers	Income in the lowest 25%	Heads of homes without homes
Occupiers' Share -Rental Deposit -Rental Fee	Criterion : 39.67m ² of net area 10,116,000 Won (\$9,105) 156,000 Won (\$140.4)	Criterion: 59.50m ² of net area 26,100,000 Won (\$23,492) 266,000 Won (\$239.4)

Source: Ministry of Construction and Transportation

The National Housing Fund also provides demand-side assistance for rent and purchasing homes. When a low-income family without a home purchases a small home, the government provides various kinds of assistance in finance and taxation. People with an annual income of less than US\$ 30,000 can borrow upto 70% of the total house price with lower interest rate. A family without a home is also exempted from the acquisition tax and registration tax when buying a house below 40m² and pays only 50% of those taxes when buying a house of 40-60m². The loan programs for the low-income people in urban areas and for low-income laborers without homes were executed after the foreign exchange crisis happened, to support the system of *Jeonse*⁸ for the purpose of stabilizing the *Jeonse* market and reducing the burden of the low-income tenant's residential expenses.

⁷ One should note that the concept of public housing in Korea is not the same as that used in western countries where public housing units are owned and operated by public sector.

⁸ A tenure system in Korea, whereby the tenant makes a lump sum deposit with the landlord to rent housing and the deposit is refunded when contract expires. He does not pay a monthly rental fee and instead gives up the interest on the deposit.

The government adopted another measure for low income housing: the compulsory building of small sized houses for low income households. Private builders tended to maximize their profit by producing middle sized or large sized dwellings for which the effective demand was greater. Unfortunately, this meant that fewer resources were made available for small dwellings for low income people. The government has, since 1978, made it compulsory to allocate at least 40 percent of residential land developed by public agencies to the production of dwellings with a floor area of less than 85m². As the housing shortage became worse, that was raised to 50 percent in 1981, 70 per cent in 1991 and 75 percent in 1992. However, this policy has now led to the oversupply of small dwellings, while larger houses became relatively scarce thus experiencing additional price increases (Korea Housing Institute 1998). As a result, since 1996, in those regions where the housing supply ratio is more than 90 percent, the compulsory allocation regulation was removed. In 1998, it was removed throughout the country.

To improve the housing condition of low-income families, the government introduced the renewal project for low income housing areas. And local governments are responsible to improve the urban infrastructures including roads, water-supply and the drainage systems in the areas designated as the objects of the residential environment improvement project under “the Act on Temporary Measures for the Improvement of Dwelling and Other Living Conditions for Low-Income Urban Residents” enacted in 1989. It also passed special regulations related to the management of designated buildings designed to legalize the squatter housing. More recently, the Seoul Metropolitan Government, for the first time in Korea, adopted the minimum housing standard system by enacting Housing Ordinance in 1998.

2. EVOLUTION OF HOUSING POLICY

The first five-year housing plan in Korea began in 1962 in parallel with the five-year Economic Development Plan, but the housing issues were only marginally dealt with. As the Korean economy improved and the income of households gradually increased, absolute housing shortages and high prices were perceived as the major housing problems in the 1970s. Therefore, after 1970s, massive housing production was initiated and several regulations were imposed on the housing sector. However, only ten years ago, such an effort of expanding housing production and provision of low-income

housing was materialized by the Two Million Houses Project and Five New Town Developments of 1988-1992. More recently, after the financial crisis of 1997-1998, the country went through severe economic restructuring processes and various emergency measures were put into effect to revitalize the housing market, including those which resulted in housing speculation. This evolution of housing policy with key milestones since 1960 is presented below.

Building of Housing-Related Institutions, 1962

In the 1960s, a housing policy began to be established as a part of the governmental planning. The 1st 5-Year Economic Development Plan, started in 1962, contained the housing section. However, as the priority of investment was given to economic growth and the construction of the industrial infrastructure, the investment for housing gave way to them. The plan focused on the arrangement of systems and institutions related to housing. Various housing delivery organizations came into being in the 1960's, including the Korea National Housing Corporation (1962) and Korea Housing Bank (1967).

Housing policy division was instituted at the Ministry of Construction and relevant laws and regulations were either newly enacted or substantially modified. In this period the Building Act (1962), the Act of Urban Planning (1962), the Act of the Korea National Housing Corporation (1962), the Act of Public Housing (1962) and the Act of Korea Housing and Commercial Bank (1969) were enacted. Furthermore, the government revised the Housing Bank Law to set up home mortgage system. In fact, most of the institution building works were completed in this period, which helped formulate more effective housing policies in the ensuing years.

Experimentation of Housing Policy, 1972

The country went through rapid industrialization and urbanization throughout the 1970s, and consequently, household income rose quite rapidly, which pushed housing demand up to the extent that demand increased by almost 10 percent a year. Housing shortage became critical, particularly in large metropolitan areas like Seoul and Busan. The housing supply ratio drastically fell even to below 60 percent in large cities down from 80 percent in the 1960s. Government enacted the Housing Construction Promotion Law in 1972 in order to meet the increasing demand for housing. It mandated the government to develop massive housing construction plan and to draw upon a set of regulations for effectively implementing the plan and promoting the housing industry.

10-Year Housing Construction Project was intended to produce up to 2.5 million housing units over a ten-year period of 1972-81. However, the plan did not move forward; for one thing, government did not make any investment into housing while most of its investment funds were put into the heavy industries. The other reason was housing speculation. As home price skyrocketingly rose, the government's immediate at that time was to stabilize the speculative market.

Emergence of Mass Production Policy, 1977

As the national economy developed, and urbanization progressed rapidly with the farming population rushing into the cities, the housing shortages in the urban areas became a new social problem in the 1970s. On the other hand, housing prices sharply increased in the end of the 1970s. The stability of housing prices became the most important goal of the housing policy.

According to the 4th five-year housing plan (1977-1981), mass production of housing began in the late 1970s with a policy goal of one dwelling per household. The public sector devoted its available resources to public housing construction, encouragement of self-help construction, and initiation of redevelopment policies. The Korea National Housing Corporation, the Korea Land Corporation, the Korea Housing Bank, and many city governments were actively involved in housing construction activities. Several government regulations were imposed on the housing market to achieve this goal. Two measures, a price ceiling system on new units and a size-based construction quota system, were introduced in order to restrain the increase of housing prices to a certain level at this time.

Fight against Housing Speculation, 1983

The housing business cycle had a ten-year peak in the late 1970s, but it suddenly receded as a result of strong anti-speculation measures. The industry suffered from severe recession. Thus, housing policy of the early 1980s started with various incentive measures to promote housing construction industry. Government also relaxed the anti-speculation measures, e.g., lowering the real estate transfer income tax rate. These measures, combined with the recovery of overall economy, ignited another round of home building business cycle. The market became heated up a few months later, but government had to cool it down again by reinstating the strong anti-speculation measures. This Catch-22 situation repeated almost every three years.

The government introduced the "bond-bidding" system in 1983 as a device to discourage speculative motives in housing purchase on the one hand, and to "tax away" a large portion of the windfall gains from both real and potential speculators on the other. The other important measure was the sale price system. It was basically designed to control the price of the newly built condominium unit and thus, to stabilize the housing price.

The Drive to Build Two Million New Units, 1987

It was under the 6th five-year housing plan (1987-1991) that two million units construction plan was initiated to relieve the housing shortage and stabilize the ever-increasing housing prices. The house price index for all city areas increased from 65.0 in 1986 to 109.3 in 1990; Housing price increased by about 68% in those five years and about 13% per annum. These figures are very noteworthy, because the general price level (consumer price index) increased by 26.7% for the same period and just 5.4% per annum.

The ratio of total investment on housing sector to GNP has sharply increased from 4.9% in the 5th plan to 7.1% in the 6th plan. A significant amount of loans were made to construction firms and to households in order to promote housing construction and homeownership. Five new towns, accommodating a population of about 1.5 million, were developed around Seoul to alleviate housing problems in the capital region. The Two Million Houses Construction Project was successful in stabilizing house prices and in increasing the housing supply ratio; the house price index for all city areas has decreased from 109.3 in 1990 to 100.0 in 1995, an 8.5% decrease for five years. In the same period, Five New Towns adjacent to Seoul were constructed to relieve housing shortage in Seoul.

Deregulation and Emphasis on the Role of the Private Sector, 1993

Kim Young-Sam's administration started with a strong "civilian" image in 1993. It developed the new and "ambitious" Five-Year Socio-Economic Plan, advocating minimum intervention of government into the competitive and free market. The housing sector plan was considered as an integral part of the plan and emphasized deregulation and elimination of government controls over the housing market, including price control.

In the 7th housing plan (1993-1997), the primary role of the public sector was confined to improving housing conditions of lower income households. Many of the regulations

imposed on the private sector were recognized as inefficient, for they distorted the housing market mechanism. Especially under the price ceiling system and the size construction quota system, the profitability of construction firms was very much limited; Firm had to sell their units at the below-market price and also had to construct small-sized units which provided lower profits than medium and large units. The price ceiling was lifted in 1998, right after the financial crisis in order to alleviate bankruptcy of construction firms, which have struggled with a considerable amount of unsold units, which were mostly smaller than 60m². Currently, the price ceiling system is not in effect. The size based construction quota system was also eliminated in 1998.

Emergency Policy Measures, 1998

The government policy toward housing dramatically changed after the financial crisis. Most of the government controls over the market were either loosened, or readjusted, or completely eliminated. Over 140 measures were announced between May 1998 and July 2001, and almost 100 of them were intended to revitalize the housing market by activating housing investment demand. From the government's point of view what was urgent was to create jobs as the unemployment rate went up as high as 16%. The rate was particularly high among the blue-collar workers and manual laborers. And an easy way to do so was to help the home building industry recover quickly from the recession because the industry was highly labor intensive. Accordingly the government policies were primarily focused on attracting investment monies into the market and making home purchases more secure and profitable. The rich were allowed to own a large number of homes as long as they registered as home rental businessmen. In old days those who owned two or more homes were penalized and forced to pay higher taxes. And right before the crisis apartment purchasers were not allowed to sell the units within 3 years after signing the purchase contract, but this clause was taken away from the tax code.

3. GAINS AND LOSSES FROM THE HOUSING POLICIES

Thus far, some of the key policy measures and evolutions have been highlighted. Evidently, some of them brought positive impacts on the housing industry and the others were adversely affecting the housing market, thus, leading eventually to “market failure.” A few lessons can be drawn from the Korean housing policy efforts

experimented with various measures through its evolution for over 40 years. In terms of the role of government, one recognizes that tight market control policy would not work when the demand for housing rapidly increase. Equally undesirable is any drastic measure to expand the housing stock through new construction within a short period of time without due consideration of the input market constraints.

How Did the Housing Policy Measures Work?

Government efforts had been concentrated on the expansion of housing production since one of the key problems of housing in Korea was housing shortage. Such an effort of expanding housing production was mainly materialized the Two Million Houses Construction Project of 1988-1992. The project was very successful in promoting housing construction in a massive scale. As shown in *Table 3.2*, housing completions doubled within a two-year period from 287,000 units in 1988 to 572,000 in 1990. This was quite remarkable, given the fact that the total number of housing units produced up until 1987 averaged less than 240,000 a year.

Table 3.2 Numerical Achievement of the Two Million Houses Project

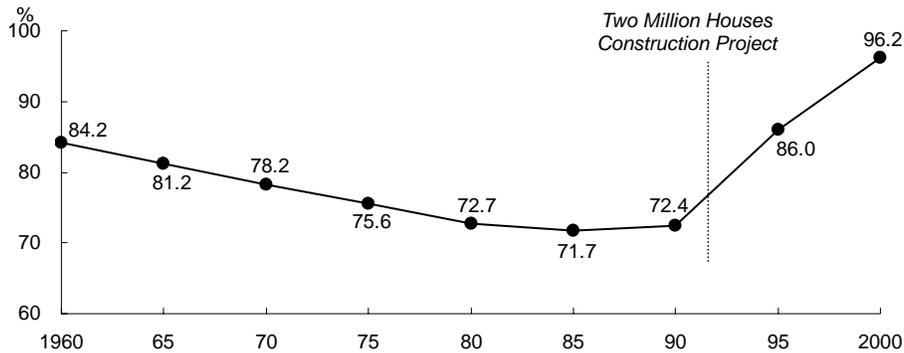
	88	89	90	91	92	88-91	88-92
Permit Based							
Total	317	462	750	648	600	2,177	2,777
-Public	115	161	270	220	250	766	1,016
-Private	202	301	480	428	350	1,411	1,761
Completion Based							
Total	287	353	572	695	631	191	2,538

Source: Ministry of Construction and Transportation

Expansion of housing stock obviously helped reduce the housing shortage ratio. As shown in the *Figure 3.1*, the housing supply ratio reached 79.1 percent by the end of 1994, up almost by 10 percent from 69 percent in 1987 when the plan was drawn up. The geographic variation was large, however; in 1990, for example, the housing shortage in urban areas was 38.9 percent; whereas in rural areas it was only 1.9 percent. With a substantial increase in housing stock as a result of the housing construction plan housing shortage rate in urban areas fell down to 11.3 percent in 2000 (*Table 3.3*). Massive housing construction also helped stabilize home price and rent. In fact, house price gradually declined at a rate of 0.3 to 1 percentage point per month since May 1991 according to a monthly housing market survey conducted by the Korea Housing Bank.

The same survey found rent falling between 0.7 percent and 1.6 percent over the same period.

Figure 3.1 National Housing Supply Ratio Changes



Source: Census of Population and Housing, each year

Table 3.3 Housing Supply Ratio Comparison

	1960	1970	1980	1990	2000
Urban Areas					
Households (A)	1,209	2,377	4,362	7,604	9,459
Housing Units (B)	805	1,398	2,468	4,646	8,393
Housing Supply Ratio (B / A (%))	66.5	58.8	56.6	61.1	88.7
Rural Areas					
Households (A)	2,989	3,199	3,109	2,563	2,469
Housing Units (B)	2,659	2,962	2,850	2,514	3,079
Housing Supply Ratio (B / A (%))	88.9	92.6	91.7	98.1	124.7

Source: Census of Population and Housing, each year

Two Million Houses Construction Project also contributes to the national economy in terms of fixed capital formation. In 1990 somewhere near the peak of the housing construction cycle, gross housing investment was 21 percent of the total fixed capital investment and contributed 8.4 percent to the nation's GNP, far above the desirable level of 6 to 6.5 percent. As shown in Table 3.2 below, the ratio rose as high as 9.7 percent in 1991. One recent study, using 1989 real figures, pointed out that a ten percent increase in housing investment induced 0.6 percent increase in imports and increased overall

balance of payment deficit by US \$ 93 million.⁹ Such impact does not seem to be quite substantial, given the size of the nation's economy, but the cumulative effects would be enormous in the long run. Excessive investment in housing was hard-pressing various input markets; land, capital, construction material and labor market in particular. In somewhat sense, the housing sector was overly invested to the extent that it almost jeopardized the normal operation of the national economy. This problem seemed to have occurred primarily because policy and planning efforts in housing area had been pursued in isolation from the macroeconomic perspective.

Table 3.4 Housing Investment Trend

	88	89	90	91	92	Total
Housing Inv.	5,968	7,867	14,660	19,060	18,515	66,070
Ratio to GNP	4.7	5.5	8.7	9.7	8.2	

Source: Ministry of Construction and Transportation

The anti-speculation measures were basically intended to discourage “speculative minds,” but there was little evidence that they had been effective in controlling speculative behavior. Some worked, but only temporarily, and none of them provided permanent solution. Besides, most of the anti-speculation measures cost a lot of tax money to enforce. Furthermore, since almost all of them were taken remedially, i.e., after the facts, those who had earned speculative profits already left the market, and thus, the preventive functions of them were constraining the land supply, and hence, raising the housing price in the long run. For example, the strengthening of the real estate transfer income tax was often accompanied by “lock-in effects,” and therefore, it substantially reduced the supply of residential land.

The issue of low-income housing has been brought up over the last 30 years, but the solution has not been very satisfactory because most of the low income housing programs are proven to be very costly to implement. One of the important program as a part of Two Million Houses Construction Project was provision of 190 thousand units of low-rent public rental housing, primarily geared to the lowest 10 percentile of the nation's population. However, that first and most primary public rental housing program discontinued because it was too costly and instead, publicly subsidized rental housing program was established, but again the program did not succeed to provide housing for

⁹ These figures were derived from the parameters estimated by Professor Suh Seong-Hwan of the Yonsei University, using a recently developed macro-economic model.

very low-income households. As of the end of 2003, the stock of long-term public rental housing in Korea was at a mere 2.4 percent of total housing stock, significantly lower than in advanced countries. In addition, the current housing welfare program for low-income households shows inefficiency and problems under the dual operation by the two Ministries. If someone is not selected as a beneficiary or disqualified for benefits due to a little higher income or property value, he cannot receive any of the social benefits including living allowance in the current scheme. As a result, the “all or nothing” policy makes beneficiaries remain helpless and stay in poverty trap. The current housing allowance system does not respond to the needs of low-income households adequately, and the marginalized groups can be even poorer than the beneficiary class.

Roles of Public and Private Sectors

The Korean government has constantly intervened with the market in many ways the demand side, the supply side, and even the pricing mechanism. And government policies have played a major role in determining the level of housing investments in Korea. During the early state of development, housing was viewed as a low-return sector relative to manufacturing and export industries. Therefore, government tried to discourage the nation's scarce capital from flowing into residential housing. Government has had a very tight control over land development through which it was able to control the volume of new housing supply. At the same time, government suppressed demand for housing through counter-speculative measures. It was not until 1988 when government realized that the problem of housing shortages could not be resolved without a massive increase in supply.

The important point is that the level of residential investment in Korea was a policy variable to a large extent. Various governmental regulations on the supply side of the market as well as direct control on “speculative” transactions have made housing supply response to changing market demand very inelastic. Such inelastic supply may have been an important factor in explaining volatility of house prices in Korea (Kim 2003, Renaud 1993, Malpezzi and Wachter 2002). Another problem with the Korean government was that it did for a wrong cause, i.e., simply to stimulate the market without due considerations of such a stimulative policy on income and asset distributions.

During the Two Million Houses Project, the government promoted massive housing

production through the diverse deregulation of land use control including the easement of density control, the relaxation of design review, and easier process for the land use conversion. Although this project was opened to both the public and the private sector, many private sectors could not participate, because many conditions related with the new development limited the participation of private sectors. The preceding developers were limited within the public sectors such as the nation, local governments, and public corporations. Also in funds, the lack of governmental financial support resulted in the lack in financing capabilities of private developers. The various factors limiting private sectors' participation are shown in the table below.

Table 3.5 Factors Limiting Private Sectors' Participation

	Factors
DEVELOPER (MAIN BODY)	<ul style="list-style-type: none"> ·Mainly promoted by the central government, that the participation of local government and private is passive ·Conflict between public corps (corps-corps, local governments-corps) ·Excluding residents' participation in planning and object establishment
FUND	<ul style="list-style-type: none"> ·Over-charged responsibility on infrastructure of executers ·Lack in financing capabilities of developers ·Lack in inducing private capital ·Lack of financial support on the new development
PROPERTY ACQUISITION	<ul style="list-style-type: none"> ·Delay of execution for whole-purchase ·Weak in objective compensation standards and theoretical basis/ ·Lack in countermeasures of migrants and functions and activities of compensation deliberation committee
SERVICED LAND & SALE	<ul style="list-style-type: none"> ·Preferences of real demand residents are not rationally reflected in land supply ·Lack of redeeming development profits for subdivision-oriented land supply
DEVELOPING ENVIRONMENT	<ul style="list-style-type: none"> ·Dullness of development from standardized planning ·Inconvenient habitat environment from hasty development planning ·Inferiority of infrastructure from little investment in public sector

After the Two Million Houses Construction Project, the following civilian administration relied heavily on the private sector for the expansion of the housing stock. With the deregulation on price and unit size, the supply of small-sized units less than 60m2 has decreased considerably after the financial crisis in 1997 as construction companies concentrated on a supply of larger units for secure demand. In the meantime public sector's role became obscure. Even though the primary role of the public sector was confined to improving housing conditions of lower income households, the

improvement of housing welfare among the low-income families turned out to be never fulfilled. And little effort was made to modernize the housing finance system either, even though the government strongly advocated elimination of various rules and regulations which prevented the housing industry from open and fair competition.

IV. CHANGING DIRECTIONS IN HOUSING POLICY

At the end of 1997 Korea was granted International Monetary Fund (IMF) loans on condition that it undertook structural readjustment in financial, business and other sectors in addition to tight economic policies. This led to high interest rates, high price levels, high foreign exchange rates and a mounting unemployment rate. The high interest rates combined with grave unemployment caused housing demand to fall sharply and a great number of house builders went bankrupt. Moreover, the fact that the Bank for International Settlements (BIS) requires at least 8 percent of reserve rate for the banks meant the end of construction loans. The Korean economy is recovering from the crisis; the income of the middle class is increasing and interest rates are falling. Owing to the sustained trend of producing about 600,000 units per year, Korea's overall housing supply ratio has attained over 100 percent in 2002. However, the Korean economy may never repeat a two digit growth rate and, at the time of writing, it seems unlikely that the violent price hikes of the past will be repeated. This section presents the ensuing changes in the housing market and industry after financial crisis and current issues in housing policy evolved from those changes. Finally, the brand-new housing policy – what is called “Korean-Version of New-Deal” – emerged by new administration is briefly discussed.

1. ENSUING CHANGES

Changes in the Housing Market

As the housing supply ratio increased and house prices stabilized, by the 1990s the gap between the regulated new housing price and the market price disappeared. Consumers tended to choose houses not for capital gains but for their usefulness including location and other qualities. Meanwhile, increases in income induced the consumer to ask for a greater variety and better quality of housing in terms of design, construction materials and construction techniques (Lee 1996b; Korea Housing Institute 1999). The housing market evolved from a seller's market to a buyer's market. Housing demand in Korea has thus been changing steadily and requires a greater variety in products (Lee 1996b). The monolithic supply characteristic of earlier decades failed to satisfy the new trend of housing demand and this was one of main causes of the increasing unsold inventories (Lee 1995). Some of the houses that had once been so popular now became unsold and the number of unsold inventories of dwellings began to increase from 10,000 units in 1991 to 160,000 units in 1995.

The housing sector has also been most severely hit by the financial crisis. Demand for housing has been shrinking due to reduced incomes and increasing unemployment. High interest rates and the decrease in the supply of mortgages, as well as the pessimistic expectations about housing prices in the near future suppressed the demand for owner-occupied housing even further. The market for owner-occupied housing in Korea was driven by the expected capital gains, but the fall in housing prices since the financial crisis began has changed the perception of many home-buyers. In addition, financial products guaranteeing high returns diminished the attractiveness of housing as an investment. As a result of the sluggish demand, the number of unsold new apartments has been rising to a level that is equivalent to almost 30 percent of the annual production.

On the other hand, stabilization of housing prices resulted in an increase in demand for rental housing. Even though interest rates dropped significantly to encourage individuals to purchase houses with lower borrowing cost, rental housing was preferred over purchasing a house, since the modest increase in housing price was not likely to be large enough to reap any capital gains. Besides, the amount of acquisition and registration taxes during the transaction process is still high, accounting for about 10 percent of the total purchase price.

In addition, the Korean population is ageing and, with the continued decline of the extended family system, this requires housing to meet the specific needs of older people. The population has also become more mobile because of the increasing importance of service sectors. This means greater demand for monthly rental dwellings. The increasing desire of consumers to live in ecology-friendly environments could signify the increasing popularity of suburban low density housing (Chung and Lee 1998). The declining popularity of apartments is being reflected in the increasing preference for single family dwellings. Thus, housing demand in Korea is shifting from monolithic apartment living to single family dwellings, elderly housing, monthly rental dwellings and suburban housing. There are some changes also in the supply behavior. The housing industry is supplying a wider mix of dwellings by type, size and design. The recent increase in house prices could be said to reflect not so much an excess demand as an improvement in housing quality.

Changes in the Housing Industry

Despite rigid regulations, the housing industry has continued to evolve. Whereas the

rate of growth varies greatly between builders, in general the industry has been able to overcome the lack of construction funds through the pre-sale system, by which the house buyer pays a substantial part of the construction costs earlier than actual progress of construction. However, the increasing amount of unsold inventories has caused many builders to go bankrupt. In 1995, because of the slow down of housing market, more than 150,000 units of housing were unsold. This put heavy pressure on the builder's financial position that was further accentuated by the structural readjustment recommended by the IMF, involving the premature repayment of bank loans combined with the stoppage of new bank loan. The number of bankruptcies rose from 60 companies in 1960 to 168 in 1995. Up until November 1997, the monthly number of bankruptcies was 15 companies but after 1997, it went up to 50.

The elimination of loan companies that were the principal source of funding for the house builder made their financial position even more precarious. To make matters worse, numerous sub-contractors closed their businesses thus making it impossible to continue housing production. The builders tried to sell their assets, especially real properties, but few buyers appeared. The only alternative was the issuing of high cost debentures in the secondary financial market. Prior to the IMF crisis, the interest rate on construction loan was 15 percent per year, after the crisis, it soared to 30-40 percent. Moreover, after the crisis, the cost of construction materials rose 20-30 percent and the solvability of the builder became further compromised. As a result the number of registered house builders dropped from 9000 in 1991 to 3000 in 1999, resulting in the closing of numerous construction sites. It is interesting to point out that between 1990 and 1996 the regulated housing price was between 14 and 32 percent below the actual construction cost (Korea Housing Institute 1997). In 1998, the standardized construction cost, that is the basis for the regulated sales price, increased only by 4.5 percent whereas the consumer price index had risen by 6.6 percent in 1997. The burden of the continual increase in construction cost was squarely placed on the builder.

Changes in the Housing Finance

The system of housing finance in Korea has a number of important characteristics. Firstly, the National Housing Fund and the Korea Housing Bank account for as much as 85 per cent of total formal housing loans; secondly, virtually all housing loans are for new dwellings; and, thirdly, the house price to income ratio is high, which ensures a heavy constraint on the ability of borrowers to repay.

Market-based housing finance is only a recent phenomenon in Korea. The primary mortgage market used to be dominated by the National Housing Fund (NHF) providing below market loans to low- to moderate-income households, and the Korea Housing Bank (KHB) serving a somewhat higher income group with amortizing mortgages at a low loan-to-value ratio below 30%. Following the financial deregulation and privatization of KHB in 1997, competition among financial institutions intensified in the primary market. More diverse products were marketed and loan-to-value ratio has gone up. The size of the primary market also increased substantially. The housing finance system has become more closely integrated with the capital market since a secondary mortgage market was created. The MBS Company Act was legislated in 1999 and the Korea Mortgage Corporation (KoMoCo) was established.

Table 4.1 Key Indicators of Primary and Secondary Mortgage Markets

(US\$ in Billion)

	1997	1998	1999	2000	2001	2002
Outstanding Balance (A)	53.0	55.5	61.3	67.6	72.9	n.a.
New Originations (B)	13.4	12.1	17.1	21.4	29.7	n.a.
GDP (C)	453.3	444.4	482.7	522.0	545.0	596.4
A/C	11.7%	12.5%	12.7%	13.0%	13.4%	n.a.
B/C	3.0%	2.7%	3.5%	4.1%	5.4%	n.a.
Share of KB Loans with Maturity of 3 years or less		4.1	55.4	62.6	70.8	75.6
MBS issues (D)	-	-	-	1.38	0.84	0.95
D/B				6.4%	2.8%	n.a.

Source: Adapted from Lee (2003: pp.24-27)

Table 4-1 presents some key indicators of the formal mortgage market. First of all, the size of the primary market measured by total loans outstanding increased substantially in recent years. In fact, the 2000 and 2001 figures underestimate the total because the portions held by insurance companies and mortgage companies are not included. In any case, outstanding mortgage balances amounted to 11.7% of GDP in 1997 but the figure rose to 13.4% by 2001.¹⁰ Nevertheless, the current level is much lower than those of the

¹⁰ Statistics on housing finance that are comparable with those prior to 2001 are not available since 2002. The Bank of Korea publishes data on only the housing loans made to consumers but not those made to developers. Many lenders under-report housing loans as they declare loans with housing collateral as consumer loans. This makes it difficult to get a full picture of the size of the primary mortgage market. Lee estimates the mortgage loans outstanding in 2001 to be 139 trillion won, almost twice as large as the available figure reported in the table.

developed economies.¹¹ Secondly, the vast majority of housing loans are short-term bullet mortgages with a maturity of three years. The short-term mortgages have become a norm in the market since Kookmin Bank (KB), the predominant lender in the primary market, merged the former Korea Housing Bank that had been privatized in 1997. In August 2002, short-term loans represented 76% of new originations.

Thirdly, the spread between mortgage lending rate and the yield on three-year government bonds was negative in 1997, rose to 6.14% in 1998 as a consequence of the financial crisis, and then narrowed to 1-2 percentage points since 1999. The reversal of the sign of the spread has made it possible to introduce the secondary mortgage market. Since its creation in 1999, KoMoCo issued a total of 2.55 trillion won in MBS between 2000 and 2002, while additional 619 billion won was issued in ABS under the separate Asset-Backed Securities (ABS) Law. However, the volume of MBS issued represents a very small fraction of new mortgage originations, 3-6% for 2001 and 2002.¹²

In addition to the formal housing finance system, Korea has an unorganized housing finance segment called *Jeonse*. It emerged naturally from the environment of high inflation, financial repression and housing shortages. Under this arrangement, the tenant gives the landlord a lump sum deposit up front in lieu of monthly payments on the rented premise. The deposit is fully refunded at the end of the lease although complications can arise in weak rental markets in which the landlord cannot find the new tenant in time for the departure of the exiting tenant. In some cases, *Jeonse* deposit is becomes a source of financing the purchase of a house by the would-be landlord. The total claims on *Jeonse* deposit in 1997 were estimated to be twice as large as the total mortgage loans outstanding (Kim and Suh 2002, p.231). Although its importance as housing finance is declining in recent years as monthly rental contracts become more popular, the existence of *Jeonse* tends to under-estimate the size of the primary market.

Since the IMF crisis, financial institutions have had to observe the BIS asset ratio of 8 percent and lenders have become much more cautious in making loans. Because loan to value ratios have generally been low, housing loans presented relatively low risks and this has led to a reasonable increase in housing loans. The trend of falling interest rates is likely to increase the amount of loans to the housing sector. Privatization of housing

¹¹ The average for EU in 2001 is 39 % (European Central Bank 2003: p.9).

¹² And the vast majority of the loans securitized were those originated by the National Housing Fund.

loans and establishment of secondary market are also new factors favoring the development of housing finance. The loan to value ratio that is now at 30 percent may be increased, thus diminishing the burden of the down payment. This will strengthen demand for housing loans.

2. CURRENT ISSUES IN HOUSING POLICY

The deep changes Korea has experienced since 1997 in housing, finance, businesses and civilian administration have made it necessary to look for new policy paradigms in housing. The government policy toward housing dramatically changed after the financial crisis. All the actions taken by the government during the recovery period might have been necessary to help the market recover quickly, but they also had some serious negative side effects. Home prices have gone up so rapidly over the last three years that an ordinary household can't afford to buy home. The price to income ratio (PIR) used to be 4 to 5 once in 1995-97 periods, but now it rises to 6 and as high as to 12, depending on location. Good quality housing with good location is almost out of reach for most of the ordinary people in Seoul. Even more serious in the long run is the fact that the rich get richer, and the poor get poorer. In other words a small number of the well-to-do dominate the market, leaving the majority almost inaccessible to the market. This looks pretty critical and must be corrected, but policy instruments are hard to find. But if the situation goes on, one can't expect "an integrated society," that the new administration hopes to achieve. Furthermore, housing price spiral, if unchecked sooner or later, will eventually lead to inflation and very skewed distribution of income.

Most critical of all is gradual reduction of the middle class, for which both the housing speculation and consumption-oriented economy are primarily responsible. The fundamental problem is that too much money is floating around, which is estimated to be almost US\$ 217 billion. And the interest rate has been too low; nonetheless, private firms hesitate to invest in business expansion because they think that the economy is not quite promising at least in a short term. The previous DJ administration¹³ totally failed

¹³ Most of the government controls over the market were either loosened, or readjusted, or completely eliminated during DJ administration. Over 140 measures were announced between May 1998 and July 2001, and almost 100 of them were intended to revitalize the housing market by activating housing investment demand.

to perceive these problems in advance. It was shortsighted! All it was concerned about was to stimulate the economy in an easy way so that it could solve the unemployment problem. In a way the housing sector became an instrument of such economic policy. Housing boom can easily take place; the past experience suggests that once ignited, the market is quickly heated up.

Inequality in income and asset distribution is getting worse; a recent estimate of GINI index demonstrates that the index for asset is as high as 0.915, almost 100% unequal while that of income is 0.312, which is not bad at all, as compared with those of the advanced economies: 0.408 of the U.S., 0.360 of the UK and 0.327 of France. In reality the income gap is not as critical as the asset gap, which often causes socio-political unrest in any society. All these social issues following the financial crisis have suggested that more appropriate and effective housing policies should be pursued for correcting the past mistakes and easing unequal housing consumption between social classes. Reflecting the inequality situation, emerging issues have focused on the housing welfare policies, addressing inadequate rental housing system for low- and moderate-income households and poor living environment of low-income housing.

Inadequate Rental Housing System

*Jeonse*¹⁴ – which is a kind of payment unique only in Korea – has been the prevalent rental system in Korea for more than a hundred years since WW II. It derived from the circumstances that few people used the banking loan system, as discussed in the last chapter. As the interest rates exceeded 10 percent most investors preferred a lump sum, rather than a high monthly rent. However, the recent low interest rate policy has brought significant changes in the housing market. The rental system has been influenced most seriously: monthly rental housing stocks increased, while *Jeonse* rental housing stock decreased significantly. This is because, due to low interest, interest incoming generated from *Jeonse* deposit amounts to less than monthly rental income, and has induced landlords to switch their rental housing from *Jeonse* to monthly rent. Monthly rent has been determined to be approximately 1.5 times the interest income from *Jeonse* deposit. The landlords' preference for the monthly rental system and the tenants' preference for *Jeonse* resulted in a shortage *Jeonse* stocks and a rapid increase in *Jeonse* deposit. *Jeonse* deposit has increased by almost 20% annually since 1999 and has been highest for apartments and units less than 85m².

¹⁴ For the detail definition of *Jeonse*, see page 40 in this paper.

On the other hand, the monthly rental system implies a higher economic burden to most rental households compared to the *Jeonse* system, which is a deposit-only system. There is a concern that rent payment will reduce total household spending for most rental households in the future, and this may cause an economic depression. This is because the money which would have normally been put aside in bank accounts for children's education, housing, and retirement is apparently being used for monthly payment. The continued increase in rent has resulted in the rent to income ratio recently becoming more than 30 percent for middle to low-income households, and the ratio is even higher for lower-income households. Consequently, a system of monthly rent payment plus deposit has recently started to increase as a compromise between house owner and renters, and this is most likely remain as the prevalent rent type for a considerable period of time.

Table 4.2 Changing Pattern of Rental Type (Unit%)

	<i>Jeonse</i>	Monthly Rent with Deposit	Monthly Rent
2000.10	66.3	29.7	4.0
2001. 8	53.6	42.7	3.7
2001.12	58.0	39.1	3.0

Source: Lee (2001), R114

Table 4.3 Rate of *Jeonse* Deposit Increase (Unit%)

	Average	Apartment	Row Housing	Detached Housing
1999	22.2	32.5	19.7	10.7
2000	13.8	12.1	15.8	15.0
2001	18.3	22.2	16.0	13.9

Source: Lee (2001), R114

Table 4.4 *Jeonse* Deposit Increase by Unit Size (Unit%)

	Average	Less than 66.1 m ²	66.2- 99.2 m ²	99.3- 132.5 m ²	More than 132.5 m ²
Rate of <i>Jeonse</i> Deposit Increase	21.0	20.0	23.9	22.6	15.1
<i>Jeonse</i> Deposit to Sales Price Ratio	62.4	71.1	69.6	63.1	54.2

Source: Lee (2001), R114

Notes: Rates are for the year 2001.

At the same time, these problems of the private rental housing system drew issues of public rental housing system. Korean government has escaped the construction of public rental housings for the low-income group by making full use of the unique private house lease system – *Jeonse*. Even though public-funded housing units have been built since 1984, when The Rental Housing Act was established, that public rental housing system was mainly targeting non-homeowners who have a Housing Subscription Savings Deposit. In addition, after five years of the lease hold started, the tenants were scheduled to buy their flats. It shows that the government encouraged the middle classes to construct or purchase their own dwellings, making little account of low-income rental housing. As a result, as of the end of 2003, the stock of long-term public rental housing in Korea was at a mere 2.4 percent of total housing stock, significantly lower than in advanced countries.¹⁵ (Table 4.5)

Table 4.5 Stocks of Rental Housing

(Unit: No. of housing units)

	1997	1998	1999	2000	2001
Total of Legal Rental Housing	584,439 (5.5%)	592,830 (5.5%)	659,830 (5.9%)	753,512 (6.5%)	919,721 (7.7%)
*Net Public Rental Housing	256,224 (2.4%)	267,635 (2.5%)	254,891 (2.3%)	269,116 (2.3%)	279,118 (2.3%)
Total Housing Stock (1,000 housing units)	10,627 (100%)	10,867 (100%)	11,181 (100%)	11,578 (100%)	11,892 (100%)

Source : Ministry of Construction and Transportation

Note: *Net public rental housing includes long-term public housing – permanent, 50-year, and national rental housing.

Poor Living Environment of Low-Income Housing

Housing quality issues have not been properly addressed during the course of massive housing production and have often been neglected in policy implementation until the late 1990s. As a result, while overall housing conditions have been improving due to the

¹⁵ The proportion of public housing in total housing stocks seems to vary from country to county. It makes up about 20-30% in European countries and 14% in middle-income countries. This is because the importance of public housing has long been recognized in many European countries as a basic right of the people. The public housing stock also reveals absolutely low level, comparing with neighboring Japan of 37% and Hong Kong of 35%.

government's mass housing provision policy, efforts to resolve the severe shortage of small-size housing and rental housing for the low-income family have not been satisfactory. In 1995, 1,590,000 households, or 12.3% of the nation's households, were one-room units, and a considerable number of people without homes were living in slums such as a *Moon Village*¹⁶ or in vinyl houses. According to a survey¹⁷ in 2000, 3.34 million households, that is, 23.4% of the total, are still living in substandard housing units and suffering from poor living conditions and excessive housing prices. This indicates that one out of five households fall into the category of housing poverty.

3. KOREAN VERSION OF “NEW DEAL”

With the red-hot exports showing signs of slowing down and record-high oil prices, many economists warned that the Korean economy would not be able to achieve the government target of 5 percent growth for 2005 unless the depressed domestic consumption and investments improve significantly. Recognizing the seriousness of the macroeconomic situation, in 2004, a current administration of President Roh, “Participatory Government,” decided to carry out various stimulus measures focused mainly on rescuing the struggling construction industry through a series of large development projects such as the free economic zones and new cities. The government described its large-scale stimulus package to jumpstart economic growth as a Korean Version of the “New Deal” policies, referring to the public project implemented by the U.S. government to pull itself out of the Great Depression 75 years ago. This “New Deal” project aimed at creating more than 400,000 jobs, boosting consumption and mobilizing outdated industrial facilities. The project allowed the government to funnel pension funds, including the Civil Servant Pension Fund and the National Housing Fund, into social overhead capital projects in the second half of 2005.

The Korean Version of “New Deal” is estimated to be worth some US\$ 10 billion for this year, including US\$ 7 billion from private investors and US\$ 3 billion from the

¹⁶ Moon village is a more recent and more poetic term for the informal settlements which came into the city with the flood of rural migrants in the 1960s. These terms probably refer to the location of Seoul's poor settlements, many of which were built on the steep hill-slopes and undevelopable hilltops throughout the city, where the moon was indeed a bit closer.

¹⁷ KRIHS (Korea Research Institute for Human Settlements), 2000

government budget for construction-related projects¹⁸. The government is first expected to spend much of its fiscal budget in the first half of this year in order to support the hard-hit construction sector through a number of public housing and nursing home projects across the country. From 2006, the government intends to spend billions of dollars more from state funds and private capital to build new satellite cities in and around the Seoul Metropolitan Area, including Pangyo and Paju. Its ambitious construction project for free economic zones will also kick off in Incheon, Pusan/Chinhae, and Kwangyang in a bid to transform Korea into a Northeast Asian economic hub. Furthermore, many local construction firms are expected to benefit from participating in building company towns and leisure and recreation complexes across the country from 2006. The government strongly believes that this package of fiscal expansionary policy measures, centered on large-scale construction projects, would certainly invigorate the sagging local economy and thus boost private consumption and investments by the end of this year.

Coupled with this “New Deal” policy, the government has established a comprehensive housing policy plan in 2003¹⁹, which will guide housing policy for Korea for the next 10 years. This plan aims to improve housing welfare and to curb social and regional inequality in terms of housing allocation and access, which have been discussed in the previous chapter. The policy direction to promote these goals is formulated as follows:

- Sustainable housing supply to cope with housing demand
- Housing policy focused on supporting low-income households with the expansion of public housing supply
- Maintenance of a stable housing market and fair market values
- Efficient utilization of housing resources with coordination of housing construction supply and housing renovation

Housing Construction Supply

The comprehensive housing policy plan (2003 ~ 2012) to ease housing shortage aims to raise the housing supply rate to 116.7% by the year 2012, which would place Korea at the same level as that of developed countries. It also plans to increase the number of housing units per 1,000 persons to 320. The housing rate in the Capital Region is expected to increase to 112.4%, thereby reducing the disparity of housing demand and

¹⁸ “New Deal Entails New Hope, New Debt,” Korean Times, November 2004

¹⁹ Korea’s Territory and Transportation, Ministry of Construction and Transportation, 2003

supply. For housing construction, 23.3 square km of housing sites in the Capital Region and 19.6 square km in other regions are planned for acquisition by the public sector, and housing demand in the central district of the Capital Region is to be distributed to the southern and northern districts for the purpose of reducing the housing shortage and encouraging balanced housing development. It is necessary to promote environmentally friendly, low-density development of housing sites, develop more large-scale housing sites and establish an individual development plan, so as to enhance resident self-sufficiency. In addition, based on the Comprehensive Housing Policy Plan it is required to establish local housing policy plans and to put forth efforts to increase the effects of housing policy by supporting the strengthened role of local authorities well acquainted with regional conditions.

Housing Assistance for Low-Income Households

One of the core issues in the Plan is to promote housing welfare for low-income households. In this regard, housing assistance is to be concentrated on households with substandard housing conditions, which will be supported by public housing policy. It is necessary to divide these households into direct and indirect assistance classes in order to provide efficient housing assistance, and to establish various housing assistance plans that take into account the reasons behind households living in substandard housing conditions, housing type, income, and so on; housing assistance, public housing construction supply, assistance for housing expense or housing renovation, and other measures may be suggested. To improve public housing supply, firstly, one million public rental housing units are planned for construction in the coming ten years, and these will be distributed based on regional housing demand. Also, a program to make available various types of public housing units to low-income households according to housing type and locational preference will be instituted. Expansion of the scope of housing assistance in the National Basic Living Security Act is expected, as well as promotion of a plan to provide housing expense assistance by way of housing vouchers if housing expenses for minimum standard housing exceed 30% of income. It is also planned to provide financial aid and tax benefits to low-income households in possession of dilapidated housing requiring replacement, and to actively promote housing renovation through housing partnerships between the public and private sectors.

Stabilization of the Housing Market

It is critical for national housing welfare to maintain housing market stability. The government plans to continue housing construction, so as to ease the imbalance of

housing demand and supply in the Capital Region, and to establish stable housing market settlements by securing public rental housing stock. By doing so, we can achieve stable housing prices through stabilization of the level of *Jeonse*. In addition to strategies to deal with housing supply, it is also necessary to establish a plan to control housing demand. The government plans to promote the development of housing sites with self-sufficiency, and improvement of the traffic network and living conditions in existing districts, as well as establish a living environment system in each neighborhood unit so as to distribute excessive housing demand in Seoul Metropolitan Area. Aside from the strategies mentioned above, it is necessary to restrict speculative and excessive competition for housing purchases and tighten management and control of the housing market. The planned introduction of a housing warranty system, housing performance indicators, and other measures should lead to stronger consumer protection. In order to minimize housing market instability caused by external factors such as the financial market, the government plans to stimulate indirect investment and promote funding of housing construction by absorbing market liquidity. Along with this, the government plans to support the secondary mortgage market and convert housing fund loans with shortterm floating rates into long-term loans, thereby reducing the impact of an unstable housing market on the general economy.

V. CONCLUDING REMARKS

Korean society has been undergoing some drastic changes since Korean War, and so has the housing sector. The housing supply ratio, which refers to the ratio of housing units relative to the number of households, reached 100.6% as of 2002 in Korea. This can be interpreted as that the housing shortage problem has been much alleviated in an absolute sense. In recent years, the government has introduced new housing programs which revealed the government's efforts to shift the housing policy goal from 'mass production of housing units' to 'housing welfare'. With its ambitious Korean Version of "New Deal" policy, now the government wants to see one million new rental dwellings!

Taking all those previous policies and current issues into account, the following suggestions are made for the future housing policy directions. They are basically of the four types; deregulation consistent with market oriented economic and financial policy, promotion of housing industry, improvement of policy instruments; housing finance and housing related taxation in particular, and equitable distribution of housing welfare.

As emphasized, various government controls have been partially, if not totally, responsible for market distortion as partly evidenced by extremely low estimates of demand, supply, and production parameters. They are detrimental to the expansion of housing production as much as to the provision of a variety of housing. Housing industry has been slow to adjust to changes in input markets as well as in demand. The industry is still overly regulated by way of special laws; e.g., the Housing Construction Promotion Law, the City Planning Law, the Land Use Law, the Housing Supply Regulations, the National Land Use and Management Law, etc. Even the Housing Construction Promotion Law seems to serve the industry very poorly, because it emphasizes on "regulating" rather than promoting the industry. These laws and regulations must be completely overhauled; relevant ones must be streamlined and strengthened whereas irrelevant ones must be eliminated and if applicable, their statutory power must be terminated.

At the same time the housing industry must be actively promoted. Most important is to strengthen the housing finance system in order to help the small and medium sized builders actively participate in housing development. The key strategy is to have as many capable firms compete in quality housing production. Infrastructure financing is another subject that must be strongly addressed to when promoting residential development. Some of the financing techniques being widely utilized in advanced countries should be thoroughly examined for their possible application to Korean

situation. It is evident that the urban infrastructure development can't be successful unless it is tied into capital market.

Tax incentives are more effective in promoting the industry. They can be used to discourage production of luxury units and to promote the low- and moderate-income housing construction. Both local and national taxes can be combined to maximize the effects of tax incentives and disincentives. Studies may be required to determine the degree to which different types of tax will affect the housing market, with particular emphasis on production, price, and supply.

Both financial and taxation tools can be employed to indirectly manipulate housing demand also. For example, when excess demand occurs, one can adjust lending terms to reduce it. Similarly, when one either over-consumes or under-consumes housing, tax measures can be used to “normalize” the housing consumption behavior. Up to now, however, these tools are not adequately developed. One must realize that improvement in housing finance, both in volume and in allocative efficiency, is the key to effective housing policy.

The other important agenda is the way in which these policies are reconciled with those dealing with the national economy. The macro-economic policy, as briefly reviewed, is very likely to discourage the housing investment deliberately. However, any arbitrary measures to substantially reduce the housing investment may pose serious problems when the society demands more and better housing. If such a demand is tightly controlled, housing situation will get worse as Korea previously experienced throughout the 1980's. Housing investment basically represents the average propensity to consume for housing, and thus, it should be considered as an anticipated aggregate consumption for housing.

Housing consumption accelerates with rise in income. One must realize that the housing investment is, therefore, affected by the underlying pattern of household demand for housing. What the government must do is to moderate the housing investment in a manner that is consistent with the national economic policy direction, e.g., policies such as economic stabilization and full employment.

The government is also responsible for equitable distribution of housing welfare. In so doing it must put an end to housing speculation once and for all. Eventually the income

tax system needs to be drastically revised to deal with speculation problem. People should recognize that “when there is income, there is tax.” Nobody should not be evaded from tax payment. Fair taxation requires the real estate transactions to be transparent and honest. Global standards must be applicable in real estate industry as well. All these actions, if taken properly and timely, will help make the housing industry more competitive.

Finally it should be re-emphasized that the role of the government is basically twofold; one, institutionally modernizing and advancing the housing and related industries at the initial stage of development, and two, indirectly moderating and facilitating the market once the country becomes economically matured. Housing is viewed both as an asset and as a consumption good. Both aspects may have to be equally considered from the policy standpoint, but the latter aspect is much more important than the former when a country moves toward a welfare society. Government may have to intervene in the market if the latter can’t allocate housing resources in favor of the poor and the disadvantaged. Problem with the Korean government was that it did for a wrong cause, i.e., simply to stimulate the market without due considerations of such a stimulative policy on income and asset distributions.

REFERENCES

- Burns L.S and Crebler, *The Housing of Nations*, L. John Wiley and Sons: New York, 1977.
- Castells, M. Goh, L. and Kwok, R., *The Shek Kip Mei Syndrome: Economic Development and Public Housing in Hong Kong and Singapore*, Pion: London, 1990.
- Charles, S., *Housing Economics*, Palgrave Macmillan: London, 1977.
- Chung, H. S. and Lee, D. S., Low-Density Suburban Housing Development in Seoul Area, Korea, in Chung, H. S. and Lee, D. S. (eds), *Suburbanization and Housing Development*, Nanam Publishing House: Seoul, 1998.
- Donnison, D. and Ungerson, C., *Housing Policy*, Penguin Books: Harmondsworth, 1982.
- Follain, Lim, and Renaud, "The Demand for Housing in Developing Countries: the Case of Korea," *Journal of Urban Economics*, 7, 315-326, 1980.
- Grigsby W. and Kim J.H., "An Exploratory Review of the Potential Demand for New Dwellings," *Working Paper #2*, the Korea Research Institute for Human Settlements (KRIHS): Seoul, 1981.
- Ha, S. K., *State Developed Housing in Korea: a Case Study of Seoul*, unpublished PhD thesis, The University of London: 1984.
- Ha, S. K., *The Role of Central-Local Government in Housing Policy, Housing 21 – the Quality of Life*, proceedings of the 2nd International Symposium on Housing, Korea National Housing Corporation: Seoul, 1995.
- Hatada, T., *A History of Korea*, Clio Press: New York, 1969.
- Henderson, G., Korea, in Henderson, G, Ved Lebow, R. and Stoessinger, J. G. (eds) *Divided Nations in a Divided World*, David McKay: New York, 1974.
- Huh, J. W., Appraisal Report of New Town Development in Seoul Metropolitan Area, *Housing Studies Review*, 3(1) 55-72: 1995.
- Hwang, M. C., *Self Help Site Development in Korea: An Overall Evaluation*, Habitat Forum, United Nations Conference on Human Settlements: Vancouver, 1976.
- Kim, J. H., Problems of and Suggestions for House Price Control, *Kook To Jong Bo*, KRIHS: Seoul, 1991.
- Kim, K. D., *Sociology of Development*, Moon Hwa Chang Jak Sa: Seoul, 1979.
- Kim, K. H., *Management Policy of Housing Market*, Hyundai Economic and Social Research Institute: Seoul, 1991.
- Kim, Y. H., *Theory and Practice of Housing Redevelopment*, The Center for Judicial and Administrative Culture: Seoul, 1995.
- Kim, W. J., *Economic Growth, Low Income and Housing*, Palgrave Macmillan: London, 1997.

- Korea Home Builders Association, *Ten-Year History of KHBA*, KHBA: Seoul, 1996.
- Korea Housing Institute, *A Study on the Pricing System of Apartments: Focused on Housing Characteristics*, KHI: Seoul, 1998.
- Korea Housing Institute, *A Study on the Characteristics of Housing Demand of the Middle Income Households*, KHI: Seoul, 1999.
- Korea Housing Institute, *Problems of and Policy Suggestions for Housing Tax System in Korea: Focused on the Capital Gains Tax*, KHI: Seoul, 1999.
- Korea National Housing Corporation, *Housing Statistics Yearbook*: Seoul, 2001.
- Korea Research Institute for Human Settlement, *Reports of the Policy Debate on the Outcome of the Two Million Houses Construction Plan*, KRIHS: Seoul, 1992.
- Lee, D. S., *Public Housing Policies for the Low Income Dwellers in Korea*, Hyundai Research Institute: Seoul, 1990.
- Lee, D. S., *The Relationship Between the Stages of the Family Life Cycle and Housing Consumption and Residential Mobility: A Study of Urban Areas in Korea*, unpublished PhD Thesis, The University of Birmingham, 1995.
- Lee, D. S., Globalization, Urbanization and Housing Policy in Korea, in Chung, H. S and Lee, D. S. (eds) *Korea, Globalization and Housing Industry*, Nanam Publishing House: Seoul, 1996 a.
- Lee, D. S., *Policy Directions for Housing Industry*, Kook To Jong Bo, KRIHS: Seoul, 1996 b.
- Lee, J. H., "Mortgage Securitization in Korea," *Housing Finance International* 18(3), 24-30: Seoul, 2003.
- Lee, K. B. and Yang, B. M., *Suggestions for Korea Housing Policy*, Korea Institute for Labor Economy: Seoul, 1992.
- Lee, S. Y. and Yang, B. M., "Prospects on Apartment Housing Market in 2002," *Proceedings of the Seminar on Construction and Real Estate Market Trends in 2002*, Construction and Economic Research Institute of Korea.: Seoul, 2001.
- Lim, G. J., Follain, J. and Renaud, B., *Determinants of Home-Ownership in a Developing Economy: the Case of Korea*, *Urban Studies*, 17(1) 13-23: 1980.
- Lowe, S., The Social and Economic Consequences of the Growth of Home Ownership, in Birchall, J. (ed.) *Housing Policy in the 1990s*, Routledge: London, 1992.
- Ministry of Construction & Transportation, *Twenty Years of National Physical Development*: Seoul, 1987.
- Ministry of Construction & Transportation, *Statistical Yearbook, MOC*: Seoul, 2000.
- Murphy, M, J., Housing the People: From Shortage to Surplus?, in Joshi, H. (ed.) *The Changing Population of Britain*, Blackwell: Oxford, 1990.

National Statistical Office, *General Report of Population and Housing Survey*, NSO:
Korea, 1945.

National Statistical Office, *Population and Housing Census Report, 1960-1995*, NSO:
Seoul, 1995.

Ryu, S. Y., *Background and Outline of the Two Million Houses Construction Plan*,
Paper presented at the Policy Debate held on 2 May, KRIHS: Seoul, 1992.

Van Vliet, W. V. and Hirayama, Y., *Housing Conditions and Affordability in Japan*,
Housing Studies, 9 (3) 351-67: 1994.

Yoo, J. H., *The Deregulation of the Apartment Sale Price*, Paper presented at the
Seminar held on 10 October, Korea Housing Institute: Seoul, 1995.