

Policy Research and Dialogue
Student Loans Schemes in Asia

Student loan schemes in the Republic of Korea: review and recommendations

Anna Kim and **Young Lee**



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The adjective 'Korean' is used in this booklet to refer to the Republic of Korea.

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List of abbreviations

CPI	Consumer Price Index
GEPC	Government Employees Pension Corporation
GNP	Gross National Product
GPA	Grade Point Average
HE	Higher Education
HRD	Human Resources Development
IIEP	International Institute for Educational Planning
KEDI	Korean Educational Development Institution
KLWC	Korea Labour Welfare Corporation
KRF	Korea Research Foundation
KSF	Korea Scholarship Foundation
KTP	Korea Teachers' Pension
MOE&HRD	Ministry of Education and Human Resources Development
MOL	Ministry of Labour
OECD	Organisation for Economic Cooperation and Development
PROAP	Principal Regional Office for Asia and the Pacific
PSA	Planning and Sector Analysis Unit
SLS	Student Loans Schemes

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Foreword

UNESCO's mandate – both globally and in Asia and the Pacific – is the important mandate to serve as a standard setter, a clearing house, a capacity builder, a catalyst for international co-operation and a provider of impartial policy advisory services to governments and other partners in the region.

In the furtherance of this mandate, the UNESCO Asia and Pacific Regional Bureau for Education in Bangkok (UNESCO Bangkok) is developing an active portfolio of research and policy analysis studies which will serve as input into ongoing policy debates on education development and reform. Such studies will explore a wide range of issues found both within all levels and forms of education and in the linkages between education and other development sectors. Major policy challenges and priorities in the Asia and Pacific region will guide the selection of operational research topics. The ambition is to support and publish action-oriented, state-of-the-art research grounded in longstanding practical experience of countries in the region and of UNESCO. The series aims at providing education practitioners and advisors working in government institutions and the private sector with a comparative information and knowledge base to support policy dialogue and decision-making in education sector management and reform.

Most of the research to be published under the series will be part of ongoing UNESCO work in the areas of education sector policy and management of countries in the region. Relevant research prepared by partner institutions and individuals will also be considered for publication.

Sheldon Shaeffer
Director
UNESCO Bangkok

Preface to the series

This book is part of a series of in-depth studies on the functioning of government-sponsored student loans schemes in Asia. It was written in the framework of a regional comparative policy review on student loans schemes undertaken by the Bangkok-based UNESCO Asia and Pacific Regional Bureau for Education (UNESCO Bangkok) in association with the International Institute for Educational Planning (IIEP). This regional project covered five countries and territories including P.R. China, Hong Kong S.A.R. China, the Republic of Korea, the Philippines and Thailand. Additional studies are being commissioned by IIEP, and a regional comparative assessment prepared by UNESCO Bangkok is forthcoming.

Most countries in Asia are experiencing a dramatic increase in demand for higher levels of education at a time of both severe public budget constraints and profound overhaul of education systems aimed at significantly increasing their impact and relevance. In an attempt to ease the burden on public budgets, a number of countries have introduced student loans schemes, hoping to recover costs and increase the revenue base for the expansion of education, while at the same time providing opportunities for poorer segments of the population to access higher levels of education.

In an attempt to increase the knowledge base available to governments and provide practical insights which might be useful for national education policy, the UNESCO Asia and Pacific Regional Bureau for Education initiated in 2001 a regional comparative study to examine the performance of student loans schemes in a number of countries in Asia. The study is intended to be instrumental in improving the efficacy and financial efficiency of existing schemes and in providing a comparative information base for countries intending to introduce a student loans scheme.

A joint endeavor by UNESCO Bangkok and IIEP, this regional policy study was initiated and its implementation co-ordinated by the Planning and Sector Analysis Unit (PSA) at UNESCO Bangkok. It benefited from technical support by IIEP and was able to draw on a wide range of regional and international expertise available at research institutes, universities and ministries in the participating countries. Five research teams led by academics and senior-level practitioners were involved in producing the monographs. UNESCO Bangkok and the Korean Educational Development Institute (KEDI) hosted several research seminars bringing together research teams and practitioners from the countries participating in the project.

Partner institutions involved in the study included the Korean Educational Development Institute (KEDI); Huazhong University of Science and Technology (Graduate School of Education), Wuhan; Peking University (Graduate School of Education); the Chinese University of Hong Kong (Department of Educational Policy and Administration); the Commission for Higher Education (CHED) in the Philippines (Office of Student Services, Office of Policy Planning, Research and Information) and the Asian Development Bank collaborating in the framework of an ongoing Education Sector Development Program in the Philippines. Researchers and officials from several universities, education and finance ministries and national agencies such as student loans offices in the participating countries collaborated in the preparation of the case studies. UNESCO Bangkok and IIEP would like to thank all those individuals who provided their expertise and professional experience to this research and therefore helped to assemble a considerable cross-sectoral information base required for comparative loans policy analysis. The important contributions by individual researchers and authors are acknowledged in this book.

The policy study benefited from the technical expertise of Adrian Ziderman, Professor of Economics at Bar-Ilan University, Israel, acting as UNESCO international lead consultant. He provided methodological guidance to research teams along the lines of his earlier study on loans in Thailand, prepared under a joint UNESCO Bangkok – Asian Development Bank project, ‘Education management and financing study’, in 1999. Igor Kitaev, Programme Specialist (education financing), served as resource

person from the IIEP in addition to authoring one of the studies. Dominique Altner, Chief, Planning and Sector Analysis Unit, UNESCO Bangkok, with support from Toshiyuki Matsumoto, Assistant Programme Specialist, PSA, initiated and ensured the professional co-ordination for this study.

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Chapter 1

The Korean¹ education system

1. Social and economic background

The population of the Republic of Korea was approximately 47 million as of 2001, with nearly a quarter living in Seoul, the capital city. As a result of lengthened life expectancy (70.6 years for men and 78.1 for women as of 2000) and sustained birth control, the elderly population above age 65 grew at a rate of 7 per cent, signalling the beginning of an ageing society.

Since the Republic of Korea launched an economic development programme early in the 1960s, industrialization and urbanization have accelerated over the past three decades. With the poor natural resources available, the Government of the Republic of Korea has pressed for the development of heavy and chemical industries, high technology and the expansion of exports. The Republic of Korea has made steady progress in industrialization, and was able to join the leading group among developing countries. As of 2000, per capita GNP stood at \$9,628, and the volume of trade amounted to \$222.6 billion, making the Republic of Korea the thirteenth largest trading country in the world.

In the absence of other kinds of resources, the quality of human resources produced through education stands out as the crucial factor behind the Republic of Korea's political, economic, social and cultural development. However, rapid economic growth and the recent restructuring process after the foreign currency crisis in late 1997 has brought about and deepened various social problems. It is necessary to overcome the unequal distribution of wealth and the inefficient distribution of resources, on the one hand, and to simultaneously press for growth, on the other.

1. The adjective 'Korean' is used in this booklet to refer to the Republic of Korea.

The education system overall

■ Administrative structure

The structure of educational administration includes the Ministry of Education and Human Resources Development (MOE&HRD), at the national level, and Regional Offices of Education at the metropolitan or provincial level.

The MOE&HRD is the government body responsible for the formulation and implementation of policies related to academic activities, sciences and public education. The Ministry is divided into two offices, four bureaux, four Councils and thirty-two divisions. The Ministry plans and co-ordinates educational policies for elementary, secondary and higher education, publishes and approves textbooks, provides administrative and financial support for all levels of schools, supports local educational agencies and national universities, operates the teacher-training system and is responsible for lifelong education and developing human resource policy.

Local offices of education, in response to the growing concern for the diverse needs of local education, have been established in seven major cities and nine provinces, as well as subordinate offices of education in country and equivalent administrative areas. These offices make decisions regarding education, art and science pertaining to their own local areas. Elementary, middle and high schools are under the control of regional entities, the metropolitan and provincial offices of education.

For primary and secondary education, a heavily centralized system was established in the Republic of Korea, with the aim of achieving equity and generalizing access. Local units of the education system were established under the MOE&HRD, not closely linked to local governments. Schools are virtually sub-units of the MOE&HRD, responsible for delivering a standard, general education, and are not independent institutes with responsibility and autonomy.

- School ladder system

The formal education system follows a single track of six years in elementary school, three years in middle school, three years in high school and four years in college or university.

Elementary education is free and compulsory. Upon reaching the age of six, children receive a notification of admission to a school located in their residential area. Upon entrance to elementary school, children automatically advance to the next grade each year. Free compulsory middle-school education began in 1985 in farming and fishing areas and has been expanded nationwide step by step.

Student selection and screening is reserved until the final stage of public schooling, when candidates are selected for university. Everyone is encouraged to participate in the competition for educational mobility. This system of delayed selection and ‘contest mobility’, as conceptualized by Ralph Turner (1960), resulted in a continual increase in the demand for educational opportunities and thus pushed the government to extend the provision of such opportunities.

Almost all adults are literate, and the average grade attainment of the current school-age population is well above the average for Asia. The difference between male and female students at all levels of schooling has continuously decreased and as of 1990 there was almost no difference, except for higher education. The student population is now about one-fourth of the total population.

Educational expansion

- Primary and secondary level

Primary-level enrolment ‘reached the ceiling’ in the late sixties, and the fluctuations in growth reflect demographic shifts in the school-age population. At the middle-school level, universal enrolment was achieved in the mid-eighties. For high schools, the enrolment rate was 95.6 per cent as of 1998.

The following *Table 1.1* shows the rapid growth in primary and secondary education.

Table 1.1 Expansion of primary and secondary education
in the Republic of Korea, 1970-2000

	Elementary school		Middle school		High school	
	Number of students	Entrance rate	Number of students	Entrance rate	Number of students	Entrance rate
1970	5,749,301	66.1	1,318,808	70.1	590,382	40.2
1975	5,599,074	77.2	2,026,823	74.7	1,123,017	41.5
1980	5,658,002	95.8	2,471,997	84.5	1,696,792	39.2
1985	4,856,752	99.2	2,782,173	90.7	2,152,802	53.8
1990	4,868,520	99.8	2,275,751	95.7	2,283,806	47.2
1995	3,905,163	99.9	2,481,848	98.5	2,157,880	72.8
2000	4,019,991	99.9	1,860,539	99.5	2,071,468	83.9

Source: Statistical yearbook of education, 2000.

These observations imply that the Korean education system has been successful at the primary and secondary levels in providing equal educational access to students, irrespective of their gender, geographic location and socio-economic background. The rate of retention is nearly 100 per cent in the lower cycles of education. Thus selection in the system takes place in the transition between cycles.

The school-age population is forecast to grow at a slow pace and, as a result, the dependency ratio will decline further in future decades, thus easing the tax burden of financing education. This outlook suggests a strong likelihood that public resources will be available for expanding or upgrading the provision of educational services.

■ Higher-education level

The rate of educational expansion is more remarkable at the tertiary level. As of 2000, the transition ratio of general high-school students is 83.9 per cent. The expansion of higher education is due to the government's liberal policy. In general, higher-education expansion policies, adopted by the government, have been effective in terms of supplying quality white-collar workers and research and development (R&D) personnel according to each stage of economic development.

The following *Table 1.2* indicates the rapid growth in higher education of the Republic of Korea.

Table 1.2 Expansion of higher education

Year	Schools	Enrolments	Teachers and assistants
1970	232	201,436	10,435
1975	286	238,719	13,981
1980	357	601,494	20,900
1985	456	1,277,825	33,895
1990	556	1,490,809	41,920
1995	754	2,343,984	58,977
2000	1,184	3,363,549	79,136

Note: The number of schools indicates the numerical sum of 'junior college', 'university of education', 'college and university', 'air and correspondence university', 'industrial university', 'technical college', 'miscellaneous school' and 'graduate school'.

Source: *Statistical yearbook of education*, 2000.

The following *Table 1.3* shows the types of higher-education institutions and student numbers in each institution as of 2000.

Table 1.3 Institutions of higher education

Classification	Number of schools							Number of enrolled students	
	By Day and Evening				By gender			Total	
	Total	Daytime	Evening	Day and Evening	Men's	Women's	Co-education	Total	Female
Grand total	372 (18)	109	2	261	1	16	355	3,363,549	1,286,762
National/Public	62(1)	34	-	28	-	-	62	943,051	408,553
Private	310 (17)	75	2	233	1	16	293	2,420,498	878,209
Types of institutions									
Junior College	158	29	-	129	-	9	149	913,273	339,233
University of Education	11	8	-	3	-	-	11	20,907	15,032
College and University	161 (18)	58	-	103	1	7	153	1,665,398	596,389
Air and Correspondence university	1	1	-	-	-	-	1	360,051	216,741
Industrial university	19	-	-	19	-	-	19	170,622	38,232
Technical college	1	-	1	-	-	-	1	100	7
Miscellaneous school	4	1	-	3	-	-	4	3,761	1,056
Graduate school	<829> {17}	<238> {12}	<560> {1}	<31> {4}	<3>	<18>	<808> {17}	229,437	80,072

Notes:

1. The figures in () indicate the number of local campuses, and are not included in the total number of schools.
2. < > are not included in the total number of schools.
3. The total number of graduate schools indicates the numerical sum of graduate schools within university and independent graduate schools, and { } indicates the number of independent graduate schools.
4. The total number of schools includes 17 independent graduate schools.

Source: *Statistical yearbook of education, 2000.*

In a meritocratic modern society, the belief that education mitigates the impact of an individual's original family background on his/her market outcome has been widely supported. However, in spite of the educational expansion in the latter half of the last century, it is observed that socio-economic inequality between classes has not been improved. Thurow (1972) explains this phenomenon with the concept of 'defensive expenditure'. According to him, the dominant class uses more resources for qualitative differentiation in education to defend its predominant position when the general educational level is raised. Hierarchy in higher-education institutions and the competition for top-class universities in the Republic of Korea reflects this defensive mechanism.

In Korean society, higher education has seen rapid expansion unparalleled anywhere in the world. And this has been a vital factor of the country's successful socio-economic development. However, in a credential-based society like the Republic of Korea, we still have many barriers for the disadvantaged in educational competition. Higher education, the key mechanism of upward social mobility, is disproportionately distributed between social classes in terms of educational outcome as well as access. This is connected to the fact that income disparity increases in spite of the economic growth. We find difficulties for the poor to continue their education in the educational financing system.

Educational finance

The size of the central government's education budget is 20.2 trillion won, which was 20.0 per cent of the central government's total budget in 2001. Of the 20 trillion-won annual educational expenditures of the central government, 83.1 per cent was transferred to the metropolitan and provincial offices of education for funding elementary and secondary education, the remaining 16.9 per cent was directly managed as national funds by the central MOE&HRD. *Table 1.4* shows the trend and structure of educational finance of the Republic of Korea.

■ Financial structure

The wide coverage of the education system and the strong academic achievement of students are remarkable. The Korean education system has a balanced structure, and the financing arrangements promote efficient options in schools and achieve a relatively high level of equity in the distribution of public spending on education (Tan and Mingat, 1992).

In the structure, the pattern of costs reveals a clear emphasis on primary education. Private education plays an important role at the post-primary levels. The private share is over 40 per cent at the secondary level, and it is over 70 per cent at the tertiary level. Therefore, a substantial amount of funding comes from the private sector, such as households and private foundations for secondary and higher education. Due to budget constraints, the government has encouraged private foundations to establish secondary schools and higher-education institutions. Private financing accounts for about two-thirds of the total direct costs on education.

The central government distributes the local education grant based on the estimated difference between standard fiscal demand and standard fiscal revenue of each local government. The main purpose of the local education grant is to guarantee equal educational expenditure for all students in each province. Local governments distribute the funds to country offices of education and high schools. Offices of education are then responsible for distributing funds for elementary and middle schools. In principle, each municipal and provincial office of education has its own distribution mechanism, such as, unit cost per school, per class, and per student.

The ratio of educational expenditure to GDP of the Republic of Korea in 1998 was 7 per cent, which is 1.3 per cent higher than the OECD average.¹ Large private expenditure financing the rapid expansion of tertiary education has been the main factor that makes the Republic of Korea a country spending a large sum on education.

1. Since the definition of education in *Education at a glance* (2001) is more broad, the ratio in *Education at a glance* (2001) is higher than in the *Korean Statistical yearbook of education* (1998).

Table 1.4 Trend and structure of educational finance in the Republic of Korea

Type of education	Level of education	Finance method	Republic of Korea						OECD average
			1977	1985	1990	1994	1998	1998	1998
Public	All levels		4.60	5.73	4.86	5.14	6.84	7.03	5.66
		Public	2.44	3.13	2.97	3.29	4.32	4.07	5.00
		Private	2.16	2.60	1.89	1.85	2.52	2.96	0.66
	Pre-primary		0.00	0.07	0.09	0.12	0.15	0.10	0.40
		Public	0.00	0.02	0.02	0.03	0.05		
		Private	0.00	0.05	0.07	0.09	0.10		
	Primary and secondary		3.82	3.98	3.44	3.47	4.21	3.95	3.71
		Public	2.22	2.59	2.47	2.73	3.37	3.15	3.47
		Private	1.60	1.39	0.97	0.74	0.84	0.80	0.35
	Tertiary		0.78	1.68	1.33	1.55	2.48	2.51	1.33
		Public	0.22	0.52	0.48	0.53	0.90	0.44	1.06
		Private	0.56	1.16	0.85	1.02	1.58	2.07	0.29
Private		0.70	0.90	1.20	1.80	2.90			

Source: Authors' calculation using *Statistical yearbook of education* (1977-1998), *Education at a glance* (2001).

There are four kinds of sources of financing in higher education: central government, local government, parents and students, and private foundations. But, grants from the central government and tuition and fees from students are the major sources of financing for higher education in the Republic of Korea. Contributions from local governments are relatively marginal. Moreover, additional resources generated from income-earning activities, endowments and other donations from philanthropists, local communities, parents' associations and so on, yield relatively little income for public education in aggregate and are not as amenable to policy intervention as direct charges to students.

In particular, as shown in the following *Table 1.5*, support from the national treasury for private universities is very limited, compared with that for national universities. Private universities' finance largely depends on students' fees. Most private institutions in the Republic of Korea suffer from financial weakness under the government's restrictions on tuition-fee policies and admission policies and, therefore, it is very difficult to generate divergent revenue sources for private institutions.

Table 1.5 Structure of financial resources of national and private universities (in 100 million won)

By financial resources	National university (1999)		By financial resources	Private university (1998)	
	Amount	Component ratio (%)		Amount	Component ratio (%)
Total amount	33,251	100	Total amount	67,875	100
National Treasury	19,100	57.5	Operating incomes	60,838	89.6
			Tuition fee	41,921	61.8
			Transfer income	5,433	8.0
Student's burden	14,151	42.5	Endowment	5,207	7.7
			National Treasury	2,377	3.5
			Educational subsidiary	1,412	2.1
Tuition fees	1,472	4.4	Non-education incomes	4,489	6.6
Other fees	12,679	38.1	Capital and debt incomes	3,041	4.5
			Balance from previous incomes	3,996	5.9

Source: Statistical yearbook of education, 1999; Ministry of Education, 2000.

The financial difficulties in the higher education of the Republic of Korea, as with many other countries, lie in the combination of a dramatic and continuing growth in student numbers unmatched by public expenditures on higher education. Moreover, the erosion in real resources available to universities stems from policy environments that have not been conducive to the promotion of greater internal efficiency within the universities, nor have they facilitated the development of alternative, non-governmental, sources of funding. High reliance on the private institutions increases the difficulty in financing in this case. The private sector is largely self-financing, depending on non-governmental funding, usually student fees, for the bulk of operating incomes. In the Republic of Korea, more than half of the finance for public colleges/universities is accounted for by government support, while less than 5 per cent of finance for private schools is accounted for by government support.

The share of costs recovered through fees shows a definite and consistent rise with the level of education. It has been argued that there is a positive link between the level of private financing and the economic power of a nation. The demand for education is stronger because job prospects are better in wealthy countries, thus people are more willing and able to pay for their education. In addition, the institutional infrastructure in wealthy countries is better developed to support cost-recovery policies.

However, this explanation does not fit in with the Korean case. Households in the Republic of Korea cover much more of the costs (62 per cent) than do its counterparts in most European countries. The net household share of expenditure averages about 12.9 per cent for the 16 OECD countries included in the study (OECD, 1998). This implies that private financing is responsible for low unit costs; with highly limited support, such as scholarship and loans, students have to pay for the cost of attendance including direct costs of education and allowances. This situation is causing serious hardship especially for poor students.

■ Financial support for students

According to a recent survey on household expenses (Joong-Ang Daily, 2001), in the Republic of Korea, people spend 36.4 per cent of their financial budget on house maintenance and rent, 28.7 per cent on tax, 27.7 per cent on private tutoring, 17.7 per cent on public education, 17.5 per cent on loan repayment, 10.9 per cent on food and 9.3 per cent on medical expenses. Educational expenditure for private tutoring and public education is 45.4 per cent in total, and the largest share of the household expenses.

Much research show that family income and educational expenses have a low correlation, and there is almost no relation between living standards estimated by Engel's coefficient and educational expenses (Lee, 2001). This implies that the burden of educational expenses for the lower-income class is very heavy. Educational expenses of the high-income group are three times that of the low-income group, and the ratio of educational expenses to the cost of living is higher at the low-income class level.

Up to recently, the government has regulated university fee and tuition policy. Elasticity of the educational price for university was very low because demand for higher education has always exceeded the supply. Therefore, the rationalization of the price has been neglected. The fixing of the price was not based on the estimated value of educational services, but was based on policy concerns (the expansion of educational opportunity and a price-stabilization policy).

In the context that educational costs are based on a user-fees principle, higher-education financing depends primarily on tuition fees, and tuition policy is controlled by the central government, then financial support

for the poor students must be limited within the higher-education institutions without specific policy provisions for them.

The traditional, and most effective, method of enhancing the educational access of the poor is by the provision of scholarships to cover tuition fees and living expenses. The following *Table 1.6* indicates the scholarship provision for higher education in 2001. Of the public-university students in undergraduate and graduate programmes, 42.2 per cent receive scholarships from various sources, and 35.3 per cent in private institutions receive scholarships. But the total amount of scholarships relative to the amount of tuition and fees is much smaller: 19.1 per cent for the public-university students and 14.1 per cent for the private-university students.

Table 1.6 Scholarships for higher education in 2001

Type of institution	Type of programme	Number of registered students (A)	Amount of tuition and fees (B)	Number of scholarship recipients (C)	Amount of scholarship (D)	C/A %	D/B %
Public	Undergraduate	642,327	717,078,979	264,211	132,552,064	41.1	18.5
	Master's degree	95,600	119,244,543	47,881	27,174,927	50.1	22.8
	Doctoral degree	19,875	31,337,526	7,522	6,406,703	37.8	20.4
	Total	757,802	867,661,048	319,614	166,133,694	42.2	19.1
Private	Undergraduate	1,803,419	4,375,465,747	536,312	492,277,149	29.7	11.3
	Master's degree	221,428	617,699,028	123,646	154,267,713	55.8	25.0
	Doctoral degree	40,730	119,128,947	15,988	32,137,841	39.3	27.0
	Total	2,065,577	5,112,293,722	675,946	678,682,703	32.7	13.3
Total		2,823,379	5,979,954,770	995,560	844,816,397	35.3	14.1

Source: MOE&HRD, 2001.

With the limited scholarships available, the poor students cannot easily find financial-support programmes in the Korean higher-education sector. The scholarship system does not usually focus on a student's financial status, but on academic ability. According to research on the criteria of scholarship provision in 1990, scholarships for the students in financial need accounted for only 17.8 per cent of the whole scholarship fund, and merit-based scholarship took up 53.9 per cent. Moreover, among the lowest income class registered in higher-education institutions, only 27 per cent

of students share the benefits of financial aid (Yoon et al., 1990). *Table 1.7* gives recipient ratio of scholarship by family-income level.

Table 7. Recipient ratio of scholarship by family-income level

Average family income (unit: 10 thousand won)	Composition rate (%)	Recipient ratio (%)
Average 70	100	41.2
0-29	5.7	27.3
30-39	10.6	48.8
40-49	12.7	49.0
50-59	19.7	46.1
60-69	12.4	43.8
70-79	8.5	36.4
80-99	7.5	51.7
100-119	14.5	26.8
120-	8.3	34.4

Source: Yoon et al., 1990: 70-71.

Other financial-aid programmes for students commonly emphasize educational achievement. Although the criterion of the programmes is clearly stated as targeting the poor, the scholarships are usually distributed to the competent students in reality. But considering the educational achievement itself reflects the influence of the family background, that is, there is a positive relation between educational achievement and socio-economic status, emphasis on merit-based scholarship reinforces the gap between the classes.

The following *Table 1.8* summarizes the characteristics of the current scholarship system, together with the direction of desirable reforms. The system aims at incentive provision for academically competent students and also expansion of educational opportunity for poor students. The forms of financial aid are diversified as free grants, loans, and work-study programmes. But in its performance, the system lays disproportionate

emphasis on students' academic achievement and competency-based grants.

Table 1.8 Characteristics of the Korean scholarship system

	Objective	Present system	Direction for reform
Objective	Incentive provision, equity of opportunity	Incentive system	Balancing incentive provision and promotion of equity
Type	Grant, loan, work-study	Grant-centred	Expanding loans
Criteria	Grade, financial need	Placing emphasis on grade	Moving the emphasis to financial need

Source: Ministry of Education, 1998: 46.

Chapter 2

Main lines of development of the Korean student loans scheme

The government-supported student loans scheme in the Republic of Korea is of long standing, but there have been few in-depth analyses regarding its performance until recently. One of the main reasons for this can be traced to the fact that the scheme covers relatively few students in the higher-education sector. More profoundly, this is related to the structure of educational finance in the Republic of Korea. Public educational expenditure has placed more weight on primary and secondary sectors, and educational financing in higher education depends on the private expenditure. Therefore, the government loans scheme has been given low policy priority in higher-education finance.

However, as the quality of higher education has come to be a critical issue recently, it has often been suggested that university tuition should be increased to a realistic level to help to overcome the financial difficulty of higher-education institutions. In this context, the student loans scheme has increasingly been targeted as a solution to a range of pressing policy problems facing governments. Since it is considered as an option to relieve pressures on national budgets by expanding the access of the poor to university education, as well as by increasing the cost recovery of higher education, the need for thorough examination of the scheme is evident.

In this chapter, we deal with the main features of the student loans schemes in the Republic of Korea. We review the historical background, the objectives and expectations, overall administrative structure and current status of the student loans schemes. Here, statistics on numbers of students receiving loans, growth over time, loan recipients by type of institution, and total loan distribution by type of institution and average size loan will be examined.

1. History of the student loans schemes

The first legal provision for student loans was set up in the Education Act early in the 1960s. The scholarship system provided for in the Act became concrete by the laws pertaining to student loans in 1961, and by its enforcement regulations in 1962. The law clarified to draw up the national budget for the student loan and specified the loan process. The stated purpose of the student loan is to financially support the poor students enrolled in tertiary schools, including graduate schools, technical colleges and secondary-vocational schools.

The Ministry of Education started its loans programme in 1975. The loans programme has been activated since 1985, and enlarged its target population after the foreign currency crisis late in 1997. It disburses interest-subsidized student loans for the poor in the entire higher-education sector and is the largest in scale among the six loans schemes run with the government's financial support. Before the MOE&HRD scheme, the Korea Teachers' Pension (KTP) started its student loans programme in 1967. The loans programme aims at promoting teachers' welfare by financial support for the education of the teachers themselves and for their children.

With a similar purpose to the KTP, the Government Employees Pension Corporation has provided student loans since 1976. The loans scheme targets public officials. It was supported from the officer annuity fund until 1999, but was then discontinued temporarily because of the financial condition of the fund, but continued to obtain support from the financial budget of the central government and local governments.

More recently, the Korea Labour Welfare Corporation has offered scholarships and loans for employees certified as industrial accident victims from 1987. In addition, the Ministry of Labour has provided student loans for employees, since 1995. The target of this loans programme is insured people, hired in companies that have more than one regular employee. Also, the Korea Research Foundation has been providing subsidized loans since it was merged with the Korea Scholarship Foundation in 1999. Before 1999, the Korea Scholarship Foundation was in charge of the loans programmes.

2. Objectives of the student loans schemes

To the extent that loans schemes are improved and new ones established on a solid basis, the project will make a contribution to the achievement of various national objectives of high priority. These include achieving a more socially efficient allocation of education budgets; improving social equity through the greater access to tertiary education of disadvantaged groups; achieving greater university cost recovery and cost sharing to reduce the overall pressures on the government budget; and securing manpower needs for national development (Ziderman, 2002).

Economic logic underlying student loans based on the assumption that higher educational qualifications lead to enhanced labour-market earnings, a form of human capital investment, is well established. Student loans schemes ease the payment burden of education falling on students by enabling them to delay payment until they make higher earnings that the additional education has made possible. However, specific objectives of each loans scheme are different depending on its objectives; and this provides the reason why the governments have set up subsidized student loans schemes.

The main objective of the student loans schemes in the Republic of Korea is social, in general, although the target groups of six student loans schemes are different, and each scheme pursues several objectives at the same time.

The MOE&HRD is more strict in its purpose of targeting the poor students, and aims to increase the access of the poor to higher education. To encourage the poor students to study continuously, the MOE&HRD loans the attendance cost to the undergraduate as well as the graduate students, at low interest rates through private lenders, that is commercial banks, and seeks repayment of the loan after graduation.

The loans programme from the KRF also targets the poor student, but it is a merit-based loan at the same time. Therefore, the KRF loan goes to poor but academically competent students. Also, the KRF provides loans having a special focus on students from farming and fishing villages.

On the other hand, the other four schemes are not targeting the poor directly. In the case of the MOL scheme, the loans are targeting industrial workers. In this sense, the scheme aims at manpower development. But

there is much room for interpreting that it also aims at increasing access of the poor as well as easing the financial burden for higher education. The rationale of this reasoning is that young workers in industrial sectors usually come from a poor family background, considering the high ratio of college entrance among the cohort population in the Republic of Korea. In other words, even though the MOL scheme is targeting industrial workers, it eventually helps the poor to continue their higher education. The fact that this scheme is highly subsidized is also consistent with the social objectives of the student loans scheme.

As for loans from the GECP, the target group is the government employees and their children. The KTP is targeting teachers and their children in the same context. These schemes are provided for the social welfare of each target group. And the KLWC scheme is targeting students from amongst industrial accident victims.

At present, increasing private costs keep qualified students from poor families out of school unless they have access to loans or grants for their higher education in the Republic of Korea. Because students lack collateral, many individuals cannot borrow to finance their own or their children's education, although the returns on such investments are high. Because tuition is increasing gradually, the elimination of allowances in higher education should be supplemented by student loans schemes to improve individuals' access to financial credit.

In general, student loans in the Republic of Korea are highly subsidized, and student loans programmes have not been used to support cost recovery for higher education. Borrowers pay little or no interest. Such subsidies may be necessary initially to make student loans acceptable and to relieve hardship for families, unemployed graduates, or other disadvantaged groups.

3. Administrative structure

The student loans schemes run from the government budget are classified into six schemes according to administrative organizations. These are: the Ministry of Education and Human Resources Development, the Ministry of Labour, the Korea Research Foundation, the Government Employees Pension Corporation, the Korea Teachers Pension Corporation, and the Korea Labour Welfare Corporation. Of course, non-governmental

student loans programmes are also common in the Republic of Korea. For example, most large firms and state-owned enterprises provide student loans for their employees. Unfortunately the data for these programmes are not available at this stage.

The Ministry of Education and Human Resources Development

The major purpose of the loans scheme is to enable students to share the financial burdens for tuition and maintenance expenses with the government through payments from their future earned incomes. Priority is given to children of the unemployed and who have difficulty in family finance. In fact, commercial credit markets work relatively well in the Republic of Korea, but the poor still face difficulties in borrowing to finance education. This is because extensive financial regulation limits the total supply of available funds for lending in the economy, and private banks are unwilling to lend to students, especially poor students.

Since it was first introduced to assist university and college students in financial need, the loans scheme escalated during the 1980s. At that time, the loans scheme was expanded as a complementary measure to prohibit undergraduate students' tutoring. In fact, the number of students in higher education rapidly expanded, due to the establishment of the 'Graduation Quota System', during the 1980s, and therefore, the opportunity for gaining access to higher education for the underprivileged also expanded. This increased the necessity of public financial support for them. But from 1986, the government budget for student loans was reduced because of the allowance of undergraduate students' tutoring and economic growth. This trend continued until the late 1990s, but in 1998, the loans scheme expanded again as demand was increased due to changes in national economic conditions, owing to the foreign currency crisis.

The total number of students in higher education was counted as 3,363,549 including two-year college (914,347), four-year college and university (2,219,765), and graduate school (229,437) as of 2000. The scale of the MOE&HRD student loan has been increased every year, and reached 454,700 million won in 2000. The recipients of the MOE&HRD loan total 215,000, which is about 6.4 per cent of all students in higher education.

The rate of increase in 1996 was 40.5 per cent relative to the previous year. It was 33.3 per cent in 1997, 23.1 per cent in 1998, 152 per cent in

1999, and 175.4 per cent in 2000. In terms of the number of recipients, it increased by 20 per cent in 1996, 23.3 per cent in 1997, 21.6 per cent in 1998, 124.4 per cent in 1999, and 112.9 per cent in 2000.

The Ministry of Labour

The student loans scheme by the MOL is based on the Workers' Vocational Training Promotion Act. The source of loan budget is the insurance fund for vocational skill development according to the Employment Insurance Act.

Employees who newly enter or are enrolled in technical college, two-year or four-year college can apply for the MOL loan. But graduate students in doctoral courses are excluded. Priority is given to employees of the manufacturing industry, of medium and small enterprises, and those in natural science and engineering departments of colleges, in that order. Applicants can apply for the loan every semester within the total numbers of semester, and the loaned amount covers registration fees, entrance fee, tuition fees and dues for school supporting organization.

The interest rate of the scheme is very low (annual interest rate is 1 per cent), and the government guarantees any loss to banks, owing to default, which take charge of administrative work for the loans. In order to encourage recipients to borrow money for education, the government abolished the joint guarantor system in 2002. The graduates from two-year college and graduate school are entitled to a two-year grace period and should repay in two years by a standard repayment method, while those from four-year college must repay in four years, with the same grace period.

The amount of the student loan has been increased each year, and reached around 346 hundred million won in 2000, and 1,374 hundred million won overall. The number of recipients was 18,590 as of 2000, about 0.6 per cent of the whole of students in higher education. The rate of increase in 1997 was about 205.8 per cent relative to the previous year. It was about 16.4 per cent in 1998, 38.6 per cent in 1999, 47.4 per cent in 2000, and 24.3 per cent in 2001. In terms of the number of recipients, it increased 183.2 per cent in 1997, 18.1 per cent in 1998, 37.2 per cent in 1999, 37.2 per cent in 2000, and 16.5 per cent in 2001. The average amount of loan per person was about 1,612,000 won in 1996, 1,741,000 won

in 1997, 1,716,000 won in 1998, 1,733,000 won in 1999, 1,863,000 won in 2000, and 1,987,000 won in 2001.

The Korea Research Foundation

The Korea Research Foundation is a government-funded institution established to enhance the overall academic research foothold of the Republic of Korea. The foundation has been supportive to the national academic policies including granting academic research funds, providing opportunities to the newly entering scholars, and aiding various academic activities. There is not any original enforcement ordinance or provision related to student loans because it was combined with the Korea Scholarship Foundation established in 1989. According to Article 12 of the Scholarship Promotion Act, loans are classified into unsubsidized and subsidized, but the KRF runs interest-free loans only for university and college students, as well as loans for students from farm and sea villages.

In the case of the KRF loans scheme, the allotment to each school is trifling because the total budget for financial loans is not large, and the loan and repayment terms are more generous. Therefore, repayment default occurs more often. The allowance per capita is limited to the student's real share in tuition after other grants are deducted, regardless of his or her financial need. It is expressly specified that the coverage of cost of attendance is "regular school payment (entrance fee, tuition fee, dues for school supporting organization), boarding expenses (living expenses), and a book budget". But, in actual practice, there is no support for boarding expenses and a book budget, but only help for the student's real share in tuition.

'Eclectic' criteria are applied to the selection of loan recipients. That is, recipients of loans should satisfy two conditions at the same time. First, among students of university or college, teachers college, junior college, air and correspondence university, and so on, it should be acknowledged that the individual cannot afford the attendance cost by the president of a school. Second, a new student should obtain a grade within the upper 50 per cent of the full quota of entrants and an enrolled student should obtain a grade within the upper 50 per cent of the whole of the enrolled students. In addition, priority is given to the student who cannot obtain a grant or subsidized loan from other agencies. It is more similar to the student loans programme in Japan, that requires both financial and grade

preconditions, than that of the USA, which requires only the financial precondition.

The KRF gives the allocated money directly to the relevant school or to the commercial bank designated by the school. The KRF can suspend lending in the following cases: first, the student's grade is below standard; second, the student is sentenced to disciplinary punishment beyond a suspension from school; third, temporary absence from school; and fourth, recipient uses the supplied or loaned money for another purpose.

The period of repayment starts from the year following graduation. Borrowers can repay by a monthly standard repayment method, or alternatives of every three months, every six months, every year or in a lump sum. It is also possible to delay repayment by presenting an application, together with the documentary evidence according to the corresponding reason. The reason for deferment could be a draft or a call-up for military service, entrance into a school of higher grade, study abroad, a disease, disaster, imprisonment, problem of family finance, etc. Once the deferment period is given, the repayment terms are automatically deferred to the expiration of the delay terms.

The average amount of loan per person was 2,115,000 won in 2000. The scale of the student loan has steadily increased since 1990, reaching about 92 hundred million won in 2000 and 398 hundred million won overall for the past 10 years. The number of recipients was 5,132 as of 2000, about 0.15 per cent of all students in higher education. The rate of increase in 1996 was about 14.7 per cent relative to the previous year. It was about 10.7 per cent in 1997, 29.4 per cent in 1998, 37.5 per cent in 1999, and 19.8 per cent in 2000. In terms of the number of recipients, it increased 4.3 per cent in 1996, 7.8 per cent in 1997, 22 per cent in 1998, 44 per cent in 1999 and 10.3 per cent in 2000.

The Government Employees Pension Corporation

The Government Employees Pension Corporation has provided student loans since 1976. The loans for public officials that had been supported from the officer annuity fund since 1976 were discontinued in 1999 because of the financial condition of the fund, but the loan for public officials' children continues to be supported by central government resources and local governments. In 2001, by an amended law, the loans

for public officials were resumed under the same conditions as the loans for officials' children. The government-supported grant by the GEPC comes under the jurisdiction of the Ministry of Government Administration and Home Affairs.

The amount of the student loan has been increased every year, and reached around 391,500 million won in 2000, and 2,872,859 million won overall since 1981. Recipients of the GEPC loan numbered 201,151 as of 2000, about 6 per cent of all students in higher education. The rate of increase in 1999 was about -4 per cent relative to the previous year. It was about 4 per cent in 2000. In terms of the number of recipients, it decreased 4.2 per cent in 1999 and 4.1 per cent in 2000. The average amount of loan per person was about 1,793,000 won in 1998, 1,796,000 won in 1999, and 1,947,000 won in 2000.

The Korea Teachers Pension Corporation

Government-subsidized loans by the KTP come under the jurisdiction of the MOE&HRD. This scheme targets the faculty and their children who newly enter or are enrolled in domestic colleges, except for graduate schools.

The loan covers registration fees including entrance fee, tuition fees, dues for school supporting organization, but in case of partial exemption of the registration fees or the taking of a scholarship, the balance is paid. One can receive the loan within eight semesters except for the college, which entails in excess of four years of study, such as medical school.

Annual interest is zero and terms for repayment of the loan is three years after graduation in the case of four-year college graduates and two years in the case of two-year college graduates. Borrowers should repay the principal by monthly instalments.

The amount of the total student loan was 55,700 million won in 2000, and the number of recipients was 27,521, which was about 0.82 per cent of all students in higher education. The average amount of loan per person is increasing gradually upon the increase of tuition fees. It was about 1,697,000 won in 1996, 1,811,000 won in 1997, 1,850,000 won in 1998, 1,864,000 won in 1999, and 2,023,000 won in 2000. The rate of increase in 1996 was about 29.6 per cent relative to the previous year. It was about

11.2 per cent in 1997, 14.2 per cent in 1998, 3.8 per cent in 1999, and 13 per cent in 2000. In terms of the number of recipients, it increased 5.5 per cent in 1996, 4.1 per cent in 1997, 12 per cent in 1998, 3 per cent in 1999, and 4.1 per cent in 2000.

The Korea Labour Welfare Corporation

The Korea Labour Welfare Corporation has offered scholarships and loans for employees certified as industrial accident victims with an industrial accident compensation insurance fund since 1987. According to the Industrial Accident Compensation Insurance Act, one who enters or is enrolled in college and is among the children of families of industrial accident victims, recipients of annual pensions, and the handicapped of 1-9 degree, can apply for the loans. Loans to cover school expenses are provided, with a low interest rate and long-term repayment period, to expand educational opportunities and to support stable living conditions of the families of industrial accident victims.

The limit of the loan amount is 2 million won per person each term, and annual interest is 1 per cent until February in the year of graduation and 5 per cent from the year after graduation. Borrowers should repay the principal by standard repayment every month for four years. Borrowers need to have a joint guarantor when the recipient's loan is over half of his retirement allowance. A double loan in the same semester is impossible and receivers of another scholarship, school drop-outs, interest delinquents and persons restricted in their financial transactions are excluded from the applicants.

The amount of the student loan reached 1,486 million won in 2000 and 4,979 million won overall. Recipients of the KLWC loan numbered 855 as of 2000, about 0.1 per cent of all students in higher education. The average amount of loan per person was about 1,940,000 won in 1997, 1,424,000 won in 1998, 1,413,000 won in 1999, 1,738,000 won in 2000, and 1,821,000 won in 2001. The rate of increase in 1998 was about 162.2 per cent relative to the previous year. It was about 24.2 per cent in 1999, 56.8 per cent in 2000, and 0.3 per cent in 2001. In terms of the number of recipients, it increased 257.3 per cent in 1998, 25.2 per cent in 1999, 27.4 per cent in 2000, and -4.2 per cent in 2001.

4. General comparisons of six loans schemes

The six student loans programmes are administered through public institutions. Even where the private sector is responsible for lending, the government acts as a guarantor on loans or subsidizes the loan. Public intervention stems from a failure on the part of private markets to supply credit for unsecured loans. Sometimes, public intervention has led to the creation of autonomous public lending bodies like the KRF. These institutions have often been labelled ‘revolving funds’ which are expected to finance themselves through repayments from earlier loans. But in this case, loans are generally heavily subsidized and result in losses. The advantage of this type of lending institution is that it allows stronger control over targeting policies.

The most common administrative arrangement is the use of commercial banks. Some manage programmes entirely, with or without government guarantees, while others act simply as collection agents. The administrative efficiency of these institutions tends to be better than the autonomous bodies.

There are three major motivations for relying on commercial banks. First, the government does not have to make initial capital outlays; second, the government may harness the efficiencies of the private sector and reduce the costs of a loans programme; third, the government does not have to set up a costly administrative apparatus to handle the programme. But, the government does not guarantee for the possible loss by a high default rate, though government intervention in these instances is usually in the form of a partial or full guarantee on loans. As the student repayments are relatively insignificant, total support in a given year is determined by government allocations.

In the Republic of Korea, most of the loans programmes offer students credit in the form of a ‘mortgage’ loan. In this traditional mortgage-type loan, repayment is made over a specific period, usually with fixed monthly payments; interest rates and the maximum length of repayment are used to calculate the fixed periodic payments.

Education is a particularly long-term investment, and risks are high because few students have acceptable collateral and graduates may be unable to repay loans if they are ill or unemployed. The risk is greatest for

students from poorer backgrounds; future job and earnings opportunities may be less favourable for the poor, and fixed future repayments commit the debtor to repay an open-ended proportion of his/her income. In addition, the poor tend to be more risk averse. And the administrative costs of collection tend to be high because graduates are mobile. Many commercial banks are simply too small to absorb these high risks and costs without charging prohibitive interest rates.

The Korean Government provides student loans at national level. This means that there are no restrictions on location or type of educational institutions that recipients belong to. The main target group of the MOE&HRD scheme and the KRF scheme is the poor, and the other schemes have their own specific target group. But the main objectives of all the schemes are social in the sense that they aim to increase the opportunity of higher education. All schemes except for the KRF programme use commercial banks in funding and administering the programme. Most schemes require a guarantor for loans. The loan coverage is different, and the MOE&HRD and GEPC provide about 86 per cent of the whole. Mostly, the loan covers tuition and registration fees except for living expenses. Interest rates are slightly different by scheme, and the highest is the MOE&HRD scheme.

The following *Table 2.1* summarizes the main characteristics of the six listed students loans schemes.

Table 2.1 Classification of the student loans schemes in the Republic of Korea

Items	MOE&HRD	KRF	MOL
Implemented year	1975	1999	1995
Scope	National	National	National
Central objective	Social	Social	Social
Public/private	Public	Public	Public
Education level	Higher education	HE/High school	Higher education
Loan distribution	Commercial bank	KRF	Commercial bank
Size of new loan in 2000 (billion won)	454.7	29.6	34.6
Number of recipients in 2000 (thousand won)	215.0	25.8	18.6
Coverage	Limited (6.4%)	Limited (0.15%)	Limited (0.6%)
Loan payment and collection	Commercial bank	KRF	Commercial bank
Interest rate	Student: 5.75% Government: 4.75%	Free interest	1%
Grace period	3+7 (long term)	1+1~8	2+2 (2-year college, graduate school)
Terms of repayment (Number of years)	0+2 (short term)		2+4 (4-year college)
Funding source	Bank	KRF	Employment insurance fund
Legal basis	Legislation	Legislation	Legislation
Coverage	Full registration fee	Tuition Other education cost (entrance fee)	Full registration fee
Guarantor	Joint surety (parents) Guarantee insurance	Individual credit	Joint surety
Sanction	Credit rating	Credit rating	Credit rating
Main target group	Poor	Poor and competent	Industrial employee

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Items	KTP	GEPC	KLWC
Implemented year	1976	1967	1987
Scope	National	National	National
Central objective	Social	Social	Social
Public/private	Public	Public	Public
Education level	Higher education	Higher education	Higher education
Loan distribution	Commercial bank	Commercial bank	Commercial bank
Size of new loan in 2000 (billion won)	55.7	391.5	1.5
Number of recipients in 2000 (thousand won)	27.5	201.2	0.8
Coverage	Limited (0.82%)	Limited (6%)	Limited (0.1%)
Loan payment and collection	Commercial bank	Commercial bank	Commercial bank
Interest rate	Free interest	Free interest	1% (grace period) 5% (after graduation)
Grace period Terms of repayment (number of years)	2+4 (4-year college, graduates) 2+3 (3-year college, graduates) 2+2~3 (dropouts)	2+4 (4-year college) 2+3 (2-year college)	1+4
Funding source	Government Annuity fund	Government (State and local)	Industrial accident compensation insurance fund
Legal basis	Legislation	Legislation	Legislation
Coverage	Full registration fee	Full registration fee	Up to 2 million won
Guarantor	Joint surety	Joint surety	Joint surety
Sanction	Credit rating	Credit rating	Credit rating
Main target group	Faculty and their children	Government employees and their children	Industrial accident victims

Source: Manuals of each loans programme.

Chapter 3

Comparisons of the two major loans schemes

Among the six loans schemes examined in the previous chapter, loans programmes from the Ministry of Education and Human Resources Development and the Government Employees Pension Corporation cover almost 86 per cent of the whole of student loans. In this chapter, we will analyze the characteristics of the two schemes in more detail. This includes which population groups are targeted by the scheme, and how the performance and practice reach this objective. Whether the university system is sufficiently open to the non-privileged, or how well the loans scheme is working as a social instrument for increasing access and participation of disadvantaged groups in tertiary education, is the main question to be answered. Also, the institutional and administrative structure of the loans schemes will be explored, including sources and allocation of loan fund budgets, the lending procedures and lending terms, etc. Institutions responsible for the selection of loans recipients, and evidence of malfunctioning and abuse, will be appraised.

1. The Ministry of Education and Human Resources Development Scheme

Targeting

The major purpose of the loans scheme is to encourage the poorer students to study continuously. For this purpose, the MOE&HRD loans attendance costs to the undergraduate and the graduate students at low interest rates through private lenders, commercial banks, and requires them to repay the loans after graduation. Therefore, in principle, priority is given to children of the unemployed and those who have difficulty in family finance.

However, only 12.8 per cent of students among the lowest family-income group can access the MOE&HRD loan, and 15.0 per cent from the second-lowest layer. On the other hand, 8.9 per cent of students from the highest-income families receive the loan (Kim et al., 2002). This means that the loans programme runs counter to its aims. We find the reason for this malfunctioning in the selection process of the recipients. In fact, every student can apply for the loan, regardless of the specified criteria, and the selection by each higher-education institution is usually made on a first-come-first-served basis. Therefore, the MOE&HRD loan is far from reaching its target group.

The following *Table 3.1* shows the composition ratio of each family-income group among the student population and the MOE&HRD loan recipient ratio by family income.

Table 3.1 Student loan recipient ratio by family-income level

Average family income (unit: 10 thousand won)	Composition rate (%)	Recipient ratio (%)
Less than 100	7.1	12.8
100-149	19.3	15.0
150-199	22.2	12.7
200-249	16.5	5.5
250-299	15.9	7.1
300-399	10.9	2.8
400-499	3.8	2.0
More than 500	4.3	8.9

Source: Kim et al., 2002.

Institutional structure and lending procedures

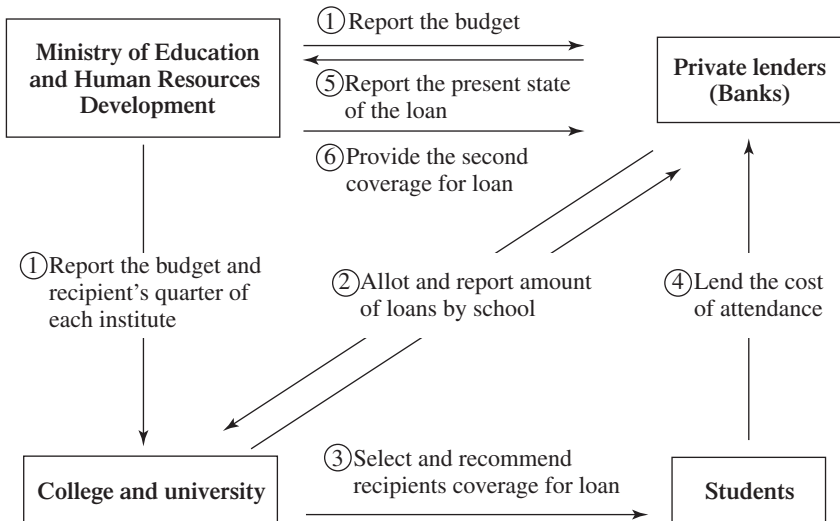
The budget source of the MOE&HRD loan is funds of 13 commercial banks. After discussion with banks, the MOE&HRD decides the interest rate on the student loan, below the market rate, and subsidizes the difference between the student-burdened interest and the total interest. As a kind of financing policy, the government decides the whole budget to

be allocated for the interest subsidy, and the amount of the loan is decided upon the estimated budget. Following the decision, the government notifies the amount of loan and the number of recipients to each higher-education institution. The quota of recipients from each university and college is evenly allocated based on the size of the school, regardless of its location or type of foundation.

Upon the report of the MOE&HRD, colleges and universities select and recommend students to the pertinent banks. Then the banks provide loans to undergraduate and graduate students who are recommended by universities and colleges during the enrolment period. Once the loan is advanced, the responsibility of post management, such as collection and monitoring, is placed on the bank.

The lending procedure of the government-sponsored student loans programmes run by the MOE&HRD is as in the following *Chart 3.1*.

Chart 3.1 Lending procedures of the MOE&HRD loans programme



Source: Ministry of Education and Human Resources Development.

Lending conditions and performance

The recipient criterion is undergraduate or graduate students who cannot afford tuition and registration fees. The loan covers school fees, such as entrance fee, tuition fee, and dues for school supporting organization and insurance fee. To secure withdrawing loans, the banks require a joint guarantor, and some of them use a guarantee insurance system.

The annual interest rate is fixed at 10.5 per cent, the government subsidizes 4.75 per cent and students are responsible for 5.75 per cent of the whole interest. The annual interest rate was 9.5 per cent until 1998, 11.5 per cent in 1999, and has been fixed at 10.5 per cent since 2000. Recently, the government has been considering whether to lower the rate, following the fall in market loan interest rates.

There are two types of student loan depending on the terms and methods of repayment (see *Table 3.2*). First, in the case of the long-term student loan, borrowers should repay the principal evenly every month for seven years after graduation. Second, the short-term borrowers should start to repay from the following month in two years, or repay in a lump sum at the expiry date. However, if borrowers join the army or cannot find jobs after graduation, they can defer the repayment for two to three years.

Table 3.2 Lending and repayment terms of the MOE&HRD loans scheme

Classification	Principal	Interest
Long-term lending	Standard repayment in 7 years following the grace period student attended school (3 years of grace period for military service and entrance into graduate school)	Alternative of monthly, every 3 months, or every 6 months payment
Short-term lending	Standard repayment within 2 years from the next month of lending	Alternative of monthly, 3 months, or every 6 months payment

Source: Ministry of Education and Human Resources Development, 2001.

The number of loan recipients and total amount of the MOE&HRD loan by year is shown in the following *Table 3.3*.

Table 3.3 Number of loan recipients and total amount of the MOE&HRD loans scheme (unit: person, million won)

	1993	1994	1995	1996	1997
Amount	38,700	29,600	28,400	39,900	53,200
Number	40,000	29,000	25,000	30,000	37,000
	1998	1999	2000	2001	Total
Amount	65,500	165,100	454,700	455,000	1,330,100
Number	45,000	101,000	215,000	210,000	732,000

Source: MOE&HRD, 2001.

2. The Government Employees Pension Corporation Scheme

Targeting

The student loans scheme run by the GEPC targets incumbent government employees subject to the government employee pension plan and their children. The financial source of the loan comes from the central and local governments' share in the pension. The Government Employees Pension System is a kind of social insurance that is different from direct public aid from national finance. The system aims at the well-being of government employees and their family. The legal basis of the insurance system was laid down in 1960, and the number of government employees who are subject to the insurance was 914, 409 as of 2001.

With the financial difficulty of the pension fund, the student loan was temporarily suspended in 1999, but resumed with the financial resources of government and local governments in 2001. According to the amended law, the loans for public officers were resumed under the same condition as the loans for their children. In order to relieve the financial burden substantially, many restrictions were eased: to abolish the restrictions on the number of children, to mitigate the limits to the number of recipients, to expand the repayment period, etc.

We do not have the exact ratio of the loan recipients to total government employees. It can be estimated roughly from the number of

loan recipients (217,015 in 2001) and the number of government employees (914, 409 in 2001).

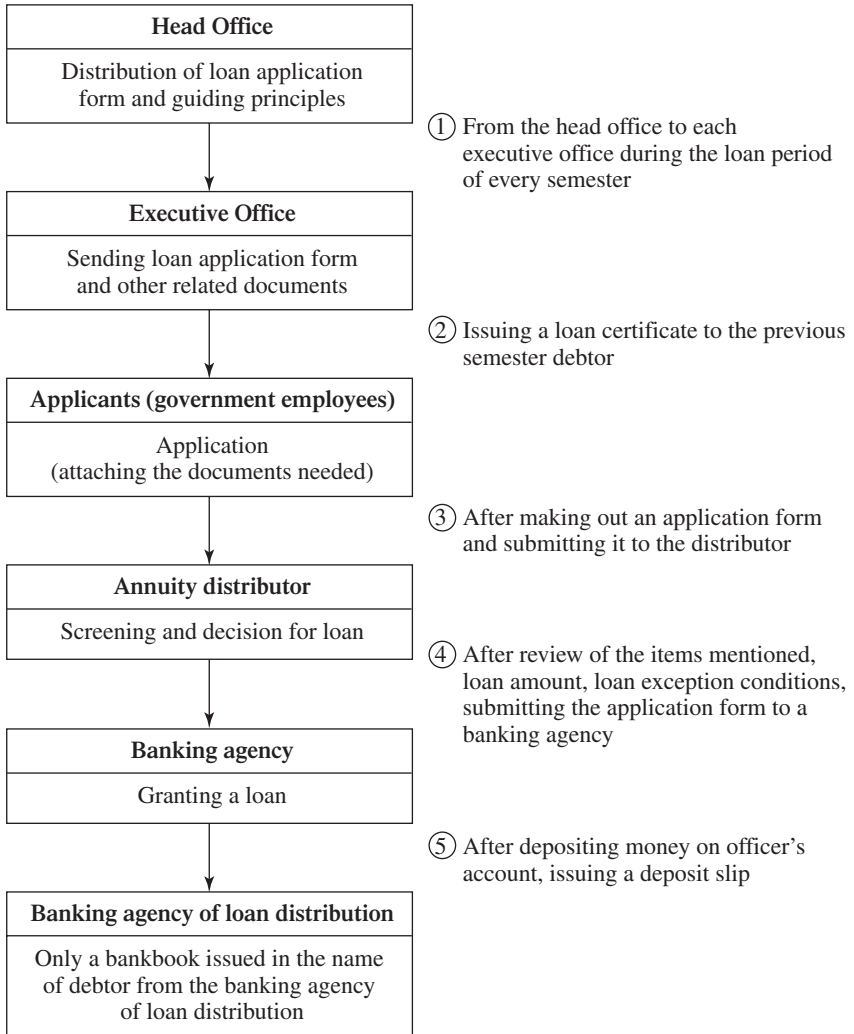
Institutional structure and lending procedures

The Ministry of Government Administration and Home Affairs takes the responsibility of administration and supervision of the pension insurance system. Under the umbrella of the Ministry, the Government Employees Pension Corporation executes the practical business regarding the management of the pension system, such as, provision of allowances, collection of expenses, and other duties such as work for the student loans programme.

The GEPC loan is available to students in both domestic and foreign colleges or universities. For domestic loans, the lending procedure is as follows. First, GEPC headquarters distributes application forms for every semester before the period of lending to each regional office that handles the loans administration. Second, each regional office produces related documents to the annuity-distributing organization. Third, after completing a loan application form, or a loan certificate, applicants apply to an annuity-distributing organization under the corporation, with a receipt of school fees or a notice of payment of school fees, as well as a copy of a medical insurance card and copy of resident registration. Fourth, annuity-distributing organizations screen the suitability of the applicants. Finally, a loan is deposited to the public official's individual account opened with one of the service-providing banks.

The following *Chart 3.2* shows the flow of the lending procedure of the GEPC loans for students enrolled in domestic higher-education institutions.

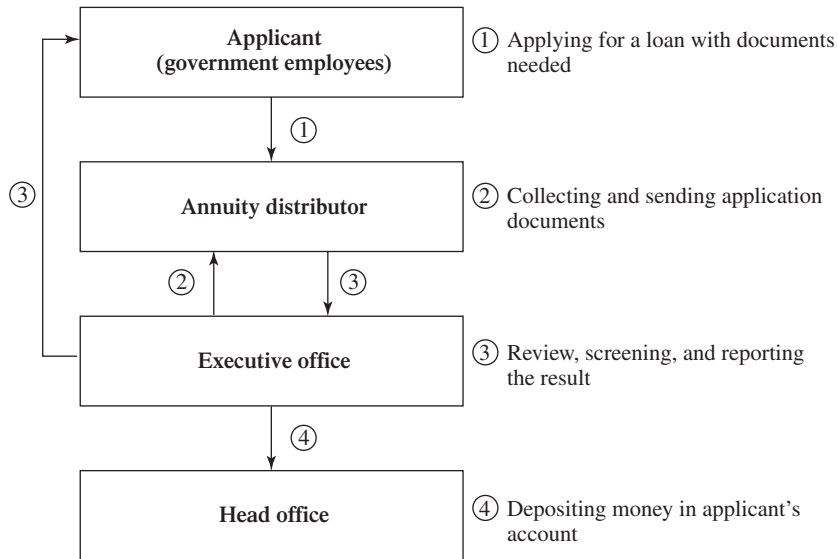
Chart 3.2 Lending procedures of the GECP loan for a domestic-college student



Source: The government Employees Pension Corporation, 2001.

On the other hand, government employees can apply for loans for themselves or for their child studying abroad (see *Chart 3.3*). First, government employees apply for a loan to the organizations for which they work, with application forms and other related documents. Second, the annuity-distributing organizations collect the applications and send them to the Pension Corporation. Third, personnel of the executive offices review the papers and screen for suitability, and then notify the amount of loan to the annuity-distributing organization. Finally, the loan is credited to the recipient's account, opened at the service-providing bank, by headquarters.

Chart 3.3 Lending procedures of the GECP loan for students studying abroad



Source: The Government Employees Pension Corporation, 2001.

Lending conditions and performance

The loan covers school fees including entrance fee, tuition fees, dues for school supporting organization, with no interest charge for the domestic-college or university students. Students who study abroad can borrow an amount of tuition and registration fees within a limit of 5,000 dollars for a year. This does not include housing expenses and other living costs.

There is no interest charge on the GECP loans. The recipients from four-year college or university should repay the principal for four years with a two-year grace period after graduation. And two-year college graduates should repay for three years with the same grace period.

The following do not qualify for a GEPC loan. First, officers' children enrolled in an unauthorized college, vocational institute, technical institution etc. Second, any officer and his children whose un-repaid money exceeds his retirement allowance. Third, any officer and his children whose un-repaid money exceeds half of his retirement allowance (in this case, to obtain a loan, someone who has served in government for more than five years should be a joint guarantor). Fourth, any student exempted from a registration fee, or scholarship recipient (lending the difference between any scholarship or grant and the maximum loan amount). Fifth, one who exceeds the number of times granted a loan (below 4-year college: eight times; 6-year college: 12 times). Sixth, children of a student sent abroad at state expense. Seventh, a double loan in the same semester. Eighth, a double loan for one child of an officer couple (includes the faculty of private school).

A total of 392.2 billion won was lent to 218,777 persons in 1998 and 376.6 billion won to 209,665 persons in 1999. The loan can be lent continuously, the financial condition of the annuity having no influence, because it is derived from governmental resources. The annuity-based loans scheme has distributed 236.3 billion won to 758,120 persons since 1967. It was discontinued in 1999 to secure a retirement allowance because it was forecast that the fund would rapidly decrease due to a mass dismissal followed by governmental lay-offs from 1998. But student loans for children of officers is continued as a minimum treatment policy. The number of loan recipients and total amount of the GEPC loans scheme, by year, is indicated in the following *Table 3.4*.

Table 3.4. Number of loan recipients and total amount by year of the GEPC loans scheme (unit: person, million won)

	1981-1997	1998	1999	2000	Total
Amount	1,712,449	392,211	376,641	391,558	2,872,859
Number	2,292,650	218,777	209,665	201,151	2,922,243

Source: The Government Employees Pension Corporation, 2001.

3. Comparisons of the MOE&HRD and the GEPC loans schemes

As the major student loans schemes, both the MOE&HRD scheme and the GEPC scheme play an important role in expanding higher-education opportunity through financial support for their recipients. They have some similarities as well as differences in many aspects.

First, the MOE&HRD scheme is targeting the poorer students in general. In this sense, the objective of the scheme is to promote the equity of higher-education opportunity. For this purpose, the scheme gives priority to students from the unemployed and low-income class. On the other hand, the GEPC scheme pursues the social welfare of the government employees. It is targeting the government employees themselves and their children. Therefore, its control is stronger over the targeting policy and is more subsidized than the MOE&HRD scheme.

Second, the MOE&HRD scheme uses commercial banks in many ways: as source of the loan fund, for loan administration, collection, etc. The Ministry only decides the amount of loan and loan policy, such as interest rates, selection criteria and quota for each institution, for each year, and makes up the interest difference. But, the GEPC scheme uses its own fund for the loan amount and credits the loan to the individual bank account of the recipient. In this case, banks only keep the individual's account when necessary. Therefore, in the case of the MOE&HRD scheme, the banks sometimes risk default of repayment, and it is necessary for the government to give some kind of incentive to banks. But, for the GEPC scheme, banks take no risk in handling the loan business.

Third, both schemes are similar in loan coverage. They usually cover tuition and registration fees except for living costs. In this case, the

MOE&HRD scheme has more limits to reaching its objective. In the light of its target and objective, this amount of loan cannot promote substantially the poor students' ability to finish their education. Moreover, in the case of the GECP scheme, government employees find it relatively easy to obtain other loans as well as the corporation loan, with their reliable status, but the poor cannot easily find a joint guarantor for loans from the MOE&HRD. This restrains the poor students from borrowing the money, although the opportunity exists. Moreover, the GECP loan is also open to students studying abroad, but the MOE&HRD loan is unavailable to them.

Fourth, as for the GECP loan, the screening process is relatively strict. The corporation has its own system that takes full charge of the executive process, screening and selection etc. In the case of the MOE&HRD scheme, higher-education institutions select and recommend loan applicants, but without any organization taking exclusive charge of the loan business, universities or colleges often do not observe the selection criteria with advantage in this process.

Fifth, the MOE&HRD scheme allows longer terms of repayment, including grace period, than the GECP scheme with its higher interest rate. In the case of the MOE&HRD scheme, the responsibility for repayment lies with the students themselves. They must repay the loan after graduation. But recipients of the GECP loan are government employees and, therefore, they should pay back the money for their children's education. Therefore, both schemes aim at financial support for higher education, but the GECP loan is different from the typical student loans that ease the payment burden falling on students themselves by enabling them to delay payment until they obtain higher earnings.

Both schemes have different purposes and develop their own management systems, but each scheme has compensated each other by way of expanding higher-education opportunity in general. Overall, the GECP scheme is more flexible and generous in terms of loan conditions: subsidiary rate, loan criteria, guarantor requirement, etc., than the MOE&HRD scheme. In order to make the MOE&HRD scheme more effective and properly to realize its objective, the scheme should include some of the merits of the GECP scheme: to include students studying abroad, to apply a more strict screening process in selection, to increase the amount of loan coverage and to improve the guarantor system are the options by which the loans could contribute to supporting the poor more substantially.

Chapter 4

Financial analysis of the loans schemes

In this chapter, the results of financial analysis of the Korean student loans scheme are presented. We will analyze formal loan conditions (lending and repayment terms in relation to the repayment period, interest rate charged, level of interest-rate subsidy, and grace periods), individual accounts (the average repayment ratio, hidden-grant level, and the size of the repayment burden), and net recovery ratio with administration costs and default.

In order to grasp the whole scale of governmental support for financing higher education through loans, we include all six schemes in this study. This will give us a more concrete idea about their exact sharing of the public-education expenditure. The methodology for computing the average repayment ratio for individual borrowers and the average net recovery ratio per loan, is set out in the Appendix to Ziderman and Albrecht (1995); applications of the methodology are provided in Ziderman (1999) for Thailand.

1. Formal loan conditions

Loan size

As explained earlier, various ministries/agencies of the Korean Government operate student loans programmes. In this analysis, all financial information is for the year 2000 because figures for some programmes in 2001 are not available. The total amount of loans provided amounts to 970 billion won (or US\$ 750 million).

The MOE&HRD student loans programme is the largest student loans programme of the Korean Government, accounting for slightly less than half (46 per cent) of total student loans. The student loans programme for children of public officials operated by the Government Employees Pension Corporation accounts for another 40 per cent of the total amount.

The number of recipients of six student loans programmes listed is 488,900 (see *Table 4.1*), equivalent to around 30 per cent of all university/college students in the Republic of Korea. This coverage of the student loans programme of the Korean Government is somewhat smaller than that in the USA, which is around 45 per cent (US Department of Education, 2000).

Table 4.1 Comparison of six loans schemes in loan size

Programme	MOE& HRD	KRF	GEPC	KTP	MOL	KLWC	Sum
Size of new loan (billion won)	454.7	29.6	391.5	55.7	34.6	1.5	967.6
Number of recipients (thousand persons)	215.0	25.8	201.2	27.5	18.6	0.8	488.9
Loan per recipient (thousand won)	2,115	1,147	1,946	2,025	1,863	1,821	2,002
Relative size to total loan (% of total loans)	46	4	40	7	4	0	100

Source: Authors' calculation using manuals and status reports for each loans programme.

The average loan amount per student is around 2,000,000 won for all programmes except for the KRF loans programme, which provides half of that. This amount can typically cover the tuition fee. The default rate can be calculated only for the first two programmes due to limited data availability. The rest of the four programmes are assumed to have a default rate equal to the rate of the MOE&HRD programme, 10 per cent. We conjecture that the assumed default rate is a conservative estimate and that the actual default rate would be lower. The way that we calculate the default rate is the ratio of arrears to the total amount of repayment due, which is simply equal to repayment plus arrears.

Repayment conditions

In the Republic of Korea, nominal interest rates of the six listed programmes vary from 0 per cent to 5.75 per cent. The highest interest rate is charged in the MOE&HRD loans programme, while no interest is charged in the Korea Research Foundation loans programme, the loans programme operated by the Government Employees Pension Corporation, or by the Korea Teachers Pension Corporation. The interest rate of the

loans programme operated by the Ministry of Labour is 1 per cent, and the student loans programme for children of disabled workers covered by Worker Accident Insurance, charges 1 per cent while the recipient is in school and 5 per cent after finishing study. The real interest rates are simply calculated as the nominal interest rates minus CPI (Consumer Price Index) in 2000, which was 2.3 per cent.

The typical repayment period is four years. Exceptions are the MOE&HRD loans programme and the KRF loans programme, each of which has a seven-year and eight-year repayment period, respectively. A longer repayment period implies a larger subsidy, since the interest rates are much below the market interest rate.

The following *Table 4.2* shows the interest rate and repayment period of the six loans schemes in the Republic of Korea.

Table 4.2 Comparison of six loans schemes in repayment conditions

Programme	MOE& HRD	KRF	GEPC	KTP	MOL	KLWC	Sum or weighted average
Nominal interest rate (%)	5.75	0.0	0.0	0.0	1.0	3.0	2.2
Real interest rate (%)	3.45	-2.3	-2.3	-2.3	-1.3	0.7	-0.1
Maximum repayment period (year)	7	8	4	4	4	4	5.5
Government interest subsidy (% of loan)	19	49	45	45	41	23	33

Source: Authors' calculation using manuals and status reports for each loans programme.

2. The individual loan account

For each of these six programmes, we calculate the share of burden to students and governments. Since interest rates for student loans are lower than the market rate and some students fail to repay, students bear only a part of total burden. In addition to the interest-rate subsidy and default cost, the government needs to bear the cost for administration of

the loans programme. In calculating the share of burden, we generally follow the methodology used in Albrecht and Ziderman (1991) in order to make our estimates comparable to those calculated for other countries using the same methodology.

The government interest-subsidy rate, which is equivalent to the hidden-grant rate to students according to this methodology, is calculated as the ratio of the present value of loan minus repayment to the present value of loan. The government interest-subsidy rate plus default cost (or government loss with default) is calculated as the ratio of the present value of hidden grants plus default loss to the present value of loan. Finally, the government interest subsidy plus default cost plus administration cost (government loss with default and administration) is calculated as the ratio of the present value of these three government costs to the present value of loan. These three measures for the share of government burden for the loans programme are defined in an increasing way, starting with interest-payment subsidy and adding default cost and administration cost sequentially.

The repayment ratio and hidden grants

Not surprisingly, the government interest subsidy rate is larger for programmes with lower interest rates for students and with longer repayment periods. The MOE&HRD loans programme with highest interest rate, has the lowest hidden-grant rate, 19 per cent², while the hidden-grant rate to the student is larger than 40 per cent in the KRF loan, the GEPC loan, the KTP loan, and the MOL loan. The weighted average of the hidden-grant rate, weighting by loan size, is 33 per cent, which is similar to the rates of UK, USA, Norway, and Quebec, reported in Albrecht and Ziderman (1991). This international comparison suggests that the interest-subsidy rate of the Republic of Korea is overall similar to those in developed countries. The interest-subsidy rate for each programme varies greatly, some programmes having a lower rate than the typical rate in developed countries, while other programmes have a higher rate.

2. For the MOE&HRD loans programme, the interest rate for students will be lowered to 5.25 per cent and the government subsidy rate will also be lowered, to 4.25 per cent in 2002. Under these new rates, the hidden grant, government loss with default, and government loss with default and administration costs will decrease slightly to 17 per cent, 26 per cent, and 34 per cent, respectively.

The repayment burden

Now we check whether the burden to students is bearable. For this purpose, we will basically compare the repayment amount and the typical initial salary of the university/college graduate. The amount of repayment varies from a mere 500,000 won in the KRF loans programme, to 2,100,000-2,400,000 won in the KLWC loan. The KRF loans programme has a low repayment because the loan amount is only 1,000,000 won, half of the typical loan amount of other programmes, and the repayment period is eight years. Required repayment for the MOE&HRD loans programme is 1,200,000-1,600,000 won, and that for loans programmes from the GEPC, KTP, and MOL is 2,000,000 won. The typical initial salary of the university/college graduate is 14,000,000 won, implying that the repayment amounts to around 14 per cent of typical salary. We judge that the burden for the student is bearable. The question, however, is not whether repayment is within their reach, but whether the loan amount is adequate for study.

3. Loan recovery with default and administrative costs

The financial efficacy of any loans scheme will depend essentially on the loan recovery ratio, the extent to which the loan is repaid in full. One can consider the relationship between what governments lend out to students and what is returned in repayments as an indicator of the loan's efficiency.

According to Ziderman and Albrecht (1995), loan recovery will depend on three major issues: the amount of hidden interest subsidies on loans; repayment losses due to default; and administration costs. Student loans are subsidized if they charge an interest rate that is less than normal market rates for borrowing; this subsidy can be considered a 'hidden grant' to students. The factors that influence the size of the subsidy are the real interest rate charged and the length of repayment. The goal of minimizing subsidies to keep a programme sustainable, needs to be carefully weighed against the equity impacts of doing so and the likely impact on more risk-averse groups. While loans can be an important tool to assist people to meet their educational costs, poorer individuals are less likely to borrow than middle-class students. The problem of 'risk aversion' has been confirmed by empirical studies. For example, Sweden's former mortgage-type loan was not found to promote access among lower-income groups.

To some extent, the variation in default rates reflects differences in definition: a distinction is not always drawn between those who missed one or two payments early on and those who cannot or will not repay. This measurement problem aside, high default rates sometimes reflect poor record keeping by the loan agency or a failure to establish appropriate eligibility criteria for loans. If education credit schemes are to succeed, eligibility must be closely evaluated so that loans are provided only to students who are likely to succeed in their study. Also to be considered are country-specific conditions that influence the public cost of higher education per student, the profile of graduates' earnings and variations in repayment terms.

To minimize the risk to low-income students, most governments subsidize loans. The student loans programme operated by governments of various countries almost always contain the aspect of subsidy because externality of higher education rationalizes subsidy. Albrecht and Ziderman (1991) report that this type of subsidy exists in 20 countries where they studied and that the subsidy rates vary from 13 per cent to 91 per cent, averaged at around 50 per cent.

But large subsidies undermine the purpose of having the loan in the first place. Government can minimize more effectively the problem of risk aversion by limiting the repayment burden in any given year through linking payments to income, imposing payment ceilings, or providing exemptions if income falls. Such measures can minimize the risk to low-income students, and encourage them to borrow to finance their studies.

The loan subsidy measures the percentage loss to the government from each loan that is repaid according to the established loan conditions; however, it fails to reveal the overall loss to the government from the loans programme. Lending agencies receive back less than is indicated by the hidden student subsidy because not all students meet their repayment obligations and the administration of the programme costs. The experience of default has been mixed.

In the case of the Republic of Korea, default and evasion does not seem to be a severe problem because the total amount of the student loan is relatively small, and so recipients are easy to track. In addition, since the government lends through commercial banks, overall administrative costs and management costs seem to be minimized, although no detailed

empirical study of administrative costs of loans programmes has yet been conducted.

Table 4.3 gives a comparison of six loans schemes in recovery ratio.

4. Loans scheme viability

How fully costs can be recovered under a loans scheme depends crucially on the repayment terms. It is in the government's interest to keep the repayment period short so that the loans scheme becomes self-financing rapidly. The student, however, wants a long repayment period so that the debt burden does not become insupportable, especially during temporary unemployment or the extended job search that often follows graduation. Critics of loans schemes argue that they are difficult and expensive to administer. The two main problems are high default rates and the high costs of collecting small loans over a long period from highly mobile graduates. But the Korean experience shows that these problems are sometimes exaggerated.

For each of these six programmes, we calculate the share of burden to students and governments. Since interest rates for student loans are lower than the market rate and some students fail to repay, students bear only a part of total burden. In addition to the interest-rate subsidy and default cost, the government needs to bear the cost for administration of the loans programme. In calculating the share of burden, we generally follow the methodology used in Albrecht and Ziderman (1991).

When the cost associated with arrears is added to interest-subsidy cost, the cost borne by the government increases to 40 per cent of the loan amount. Put differently, the government pays for 40 per cent of the loan borrowed by students when both interest subsidy and default cost are considered. Data necessary to analyze the administration cost for managing student loans programmes are very scanty, and we are forced to assume that the administration cost is simply equal to 2 per cent of the loan amount each year, as assumed in Albrecht and Ziderman (1991).

Table 4.3 Comparison of six loans schemes in recovery ratio

Programme	MOE& HRD	KRF	GEPC	KTP	MOL	KLWC	Sum or weighted average
Size of new loan (billion won)	454.7	29.6	391.5	55.7	34.6	1.5	967.6
Number of recipients (thousand persons)	215.0	25.8	201.2	27.5	18.6	0.8	488.9
Default rate (% of standing loan)	10	14	10	10	10	10	10
Nominal interest rate (%)	5.75	0.0	0.0	0.0	1.0	1.0 -5.0	2.7
Real interest rate (%)	3.45	-2.3	-2.3	-2.3	-1.3	0.7	0.4
Maximum repayment period (year)	7	8	4	4	4	4	5.5
Government interest subsidy (% of loan)	19	49	45	45	41	23	32.7
Government interest subsidy + default (% of loan)	27	56	51	51	47	30	39.7
Government interest subsidy +default+adm. (% of loan)	36	67	60	60	56	37	48.8

Source: Authors' calculation using manuals and status reports for each loans programme.

The total cost for the government is calculated around half of the loan amount, implying that the government recovers half of the loan amount. The level of cost recovery of student loans programmes in the Republic of Korea is comparable to that of developed countries and much lower than that of most developing countries. Due to very low real interest rates and a very high default rate, recovery rates of many developing countries are only 15-30 per cent. The burden of student loans programmes

to the government in the Republic of Korea seems reasonable and comparable to that in developed countries.

Even when the government share of the burden of student loans programmes is comparable to that of developed countries, the resulting budgetary pressure could be burdensome if the size of student loans programmes is too large relative to the size of the government. In order to check whether the burden of various student loans programmes is bearable to the government, we estimate current expenditure necessary to maintain the student loans programmes.

The following *Table 4.4* reports that the government is estimated to pay 170 billion won in interest subsidy for the listed six student loans programmes, 220 billion won when both interest subsidy and default are considered, and 245 billion won when all three costs are included. Since cost associated with default is a rough estimate and might be borne by a third party, such as banks, we focus on the size of the interest-subsidy cost to check financial feasibility for the government. In 2000, the GDP of the Republic of Korea was 517,100 billion won and the government budget, defined as the sum of the general account and special accounts excluding the public fund, was 127,442 billion won, implying that the interest subsidy associated with student loans programmes is 0.033 per cent of GDP and 0.13 per cent of the government budget. It is hard to come by comparable figures from other countries. Using various sources, the comparable figures for the USA are estimated to be 0.21 per cent and 1.11 per cent, respectively.

This implies that the Republic of Korea spends only one-seventh – one-ninth of its GDP and government budget on student loans programmes relative to the USA. We believe that it is feasible to increase the government budget for student loans programmes, especially considering the desirability of student loans programmes. The increased budget can be used to expand the coverage of the programme, targeting the poor. Among six programmes, the budgetary burden is larger for student loans for public officials and the MOE&HRD loans programme.

Table 4.4 Burden of student loans schemes to the government, 2000
(unit: billion won)

Programme	MOE& HRD	KRF	GEPC	KTP	MOL	KLWC	Sum or weighted average
Government average current interest-subsidy cost (share to total burden)	44.9 (27%)	9.0 (5%)	92.2 (55%)	15.0 (9%)	7.7 (5%)	0.2 (0.1%)	169.0 (100%)
Government average current interest subsidy + default cost	67.6	11.2	113.3	18.4	9.7	0.3	220.4
Government average current interest subsidy + default + administration cost	78.3	12.1	123.5	20.1	10.6	0.3	244.9

Source: Authors' calculation using manuals and status reports for each loans programme.

Chapter 5

Equity issues in performance

The Republic of Korea was able to address one of the equity issues, basic education for all, by leaving higher levels of education to the private sector and targeting public resources for primary education. Timely supply of manpower and offsetting of diminishing returns to physical capital through increasing human capital indicate that Korean education policies have been successful from the economic point of view. The Republic of Korea first expanded and universalized primary education followed by secondary education, and only then did it shift emphasis to the expansion of higher education. These government policies for educational expansion have fitted in well to the national economic development plans. This was possible due to the high degree of cost recovery from students and parents in secondary and especially higher education, given the government's budget constraints. Contributions from the private sector and households led to successful implementation of national education development policies.

1. Funding sources

These patterns of educational expansion by stages and the means of financing are consistent with what the World Bank recommends for public investment in education of developing countries. To implement their educational and economic development plan, more funding sources, other than governmental, need to be mobilized from individuals, communities, private organizations, and foundations in developing countries. In this context, first, it is recommended to increase school fees, and to eliminate or at least reduce substantially government spending on students' boarding and transport by emphasizing parental responsibility, with financial assistance given to a small number of students on the basis of need. For tertiary education, it is desirable to reduce direct support to students and to introduce a student loans scheme. Secondly, it is recommended to expand the role of private schools in providing education. It is an effective way of financing educational expansion to induce private schools into providing education.

However, the heavy reliance on private funding in secondary and higher education gradually raises important policy arguments for the utilization of government resources as higher education is universalized in the Republic of Korea. The main argument is that a private-sector strategy may lead to unequal access to higher education, especially for the underprivileged. It is not just a matter of an expansion of financial revenues, but an entire restructuring of the system of higher education including its finance, delivery, participation, and accountability.

2. The class gap

Many researches on students' transition to higher-education institutions reveal that there is a positive relation between attendance in higher-education institutions and parents' level of education, occupational status, family income, and family social capital. These factors also impact on the choice of high-school track. When parents' socio-economic status is high, students tend to go to general high school rather than vocational high schools. Under the dual high-school system, students are primarily selected by social status, and go through the discriminating socialization process. That is, the middle-class students primarily enter general high schools while lower-class students go to vocational high schools. In the case of vocational-high-school graduates, the impact of parents' income level on university entrance is clear, while economic capital does not feature significantly in the case of general-high-school students (Lee, 2001).

In Korean society, where higher education has expanded rapidly with economic growth, the education system seems to support the mobilized competition for formality's sake. But because of the difference in available resources to be mobilized for educational achievement, competition is not fair between classes. Therefore, while educational expansion has raised the educational level in general, and has been expected to decrease the class gap, it could not mitigate the difference of educational and socio-economic achievements between classes. Many researches on the influence of family background on educational achievement support this claim, in the Republic of Korea.

In a typical credential-based society like the Republic of Korea (Collins, 1979), educational inequality appears both in qualitative as well as in quantitative aspects. In Korean society, where the socio-economic opportunity structure is unequally distributed between classes, the high-

status group continues to invest in education, and raises the lower class's desire for social mobility. This desire reflects its competitive investment in education in spite of limited available resources. In this case, the dominant class invests more not for quantitative, but for qualitative differentiation at the higher-education level. This differentiation strategy leads to classification of higher-education institutions according to their excellence. The dominant class therefore devotes itself to sending its children to the most highly ranked university.

This situation should be improved through well-designed scholarships, student loans schemes and other policy measures. These financing strategies aim not only to mobilize needed resources from a wider range of public and private sources, but also to influence student behaviour in ways that make tertiary education more cost-effective. The aim also is to provide wide access to a range of study options, while encouraging students to move more rapidly to complete their study programmes.

3. Efficiency and equity

Efficiency and equity, the main principles in educational financing policy-making, are often on the horns of a dilemma. Efficiency in educational finance aims for maximum effect with minimum cost, within the limited financial resources, in order to accomplish the purpose of the specific national educational policy. Cost-effective analysis is a good example of the educational finance based on an efficiency principle. But, when efficiency is emphasized without the concerns for equity, it is clear that the poor get poorer, and the rich get richer. Especially in the Korean higher-education financing structure, the disadvantaged are still very vulnerable.

Equity in education implies not just open access to higher education, but also to equal treatment to realize one's full potential. Taking one more step forward, a more positive discrimination policy for the disadvantaged should be considered to compensate for the discriminating conditions based on one's family background. From the perspective of social justice, equal educational opportunity should be guaranteed to redistribute the social and economic wealth. This is based on the assumption that educational achievement has a positive impact on the increase of an individual's income, and leads to the opportunity for upward social mobility.

In the case of higher education, a strong government role in the provision of education may have a rationale as long as this remains effective, responsive and efficient. There may be factors present that militate against efficient public provision of higher education, such as bureaucratic practices and lack of discipline of market competition in the Republic of Korea. In this context, theoretically perfect equity can be realized when the following four principles are balanced in educational policy. First, the government should be responsible for secure educational resources to guarantee equal treatment for all at each level of education. Second, the government should set policy priority based on the aims of educational policy. Third, policy consideration for the low-income class should be justified from the social goal of justice. Fourth, the government should raise educational quality and distribute the benefit to all.

Two traditional economic arguments are often advanced to justify state subsidies: the presence of positive external benefits of higher education, and of market imperfections. It is true that neither of these is pervasive in the case of higher education. However, the argument for subsidy based on promoting equity should be considered at the same time. Educational investment, which becomes embodied in the recipients themselves, especially for the poor students, is not easily accepted as security by lending institutions. The appropriate government response is the establishment of mechanisms for student loans that the market cannot supply.

To set up realistic tuition fees and also to pursue social goals of equity simultaneously, a correct targeting policy for the poor needs to be established. However, financial aid for the poor that aims to give them easy educational access, to give them school choice at will, and to sustain the benefits of higher education, reveals many flaws. At present, there are merit-based scholarships, scholarships from university and government loan, and private companies' financial aid programmes in the Republic of Korea. However, the selection criteria are mainly academic capability and achievements, not financial need.

Based on the above discussion, we raise here the main equity issues in the Korean student loans scheme, calling on the results from the survey we conducted to grasp in detail the current conditions of the student loans scheme, in context.

First, the loan coverage is too limited to relieve substantially the poor students' financial burden for higher education.

We carried out surveys, using questionnaires of university staff in charge of student loans programmes, and also conducted interviews with student recipients and staff of the banks operating the loans programmes. For the university survey, we sent questionnaires to 150 universities that have run a student loans programme. A total of 77 schools participated in this survey. Interviews with students were conducted involving 63 students from 4 colleges, taking into consideration location and type of foundation. In addition to student recipients, we interviewed staff in charge of the student loans programme of the commercial banks. At present, there are 13 commercial banks operating the loans programme, including two branch offices in a local town. Among them, except for the two branch offices, we interviewed all staff.

The survey showed that most universities started to run student loans programmes quite recently. More than half of the schools had run the programme for 2-12 years. A total of 32 schools (52.5 per cent) had started a programme in the 1990s, 25 schools (41 per cent) in 2000, 3 schools had had a programme since the 1980s, 1 school (1.6 per cent) had had a programme since 1980. The numbers of student loan recipients per school were as follows: 24 schools (33.3 per cent) had between 100 to 500 students, 21 schools (29.2 per cent) had under 100 recipients, 20 schools (27.8 per cent) had between 500 to 1,000 recipients, and 7 schools (9.7 per cent) had over 1,000 recipients.

The percentage of students who receive the student loan compared to the number of students who actually applied for the programme shows that there is much higher demand for student loans than the supply. A total of 26 schools (26 per cent) had over 90 per cent acceptance rate, 15 schools (21.4 per cent) had between 70-80 per cent, 12 schools (17.1 per cent) had under 50 per cent, 10 schools (14.3 per cent) had 80-90 per cent, and 7 schools (10 per cent) had 50-60 per cent. The range of the number of borrowers of government-subsidized loans of 11 banks is wide: from 1,288 to 36,599. Nine staff members of the banks of which borrowers number between 1,000 to 3,000, reported that their administrative burden is not high, and that the loan is not significant compared with other business. But two other staff members from the bank which provides loans to more than 30,000 students pointed out that the burden of the student loans programme is heavier than in other government-supported loans programmes.

4. Possible expansion of the loans programme

Most of the respondents and interviewees expressed the opinion that the loans scheme should be expanded. The majority of officials felt that the student loans programme needs to be expanded. Students were interested in expansion of the loans programme to cover living expenses. They said that they would fully utilize the extra money. In addition, most students accepted the extension of the loans programme. They thought the student loans programme could assist those in poor financial circumstances, relieve parents' financial burden, and promote students' self-reliance and independence. The response showed that most parents were favourable to the student loans programme as well. The parents favoured the programme because of the decrease in their financial burden, and relatively low interest rate.

On the other hand, the majority of the students responded that they did not think that they would have time to repay the loan because the loan requires long-term payment, which is congruent with result findings from financial analysis in the previous chapter. It was the consensus of opinion that they must pay back the student loan fully. Nevertheless, some graduate students were pressured by the loan more than others; this is because only a short-term loan is available for a graduate student, and it was suggested that the repayment period be calculated from the start of employment instead of at graduation. Some wanted to see a lower interest rate and longer repayment period.

Most of the school officials agreed (34.2 per cent) or strongly agreed (53.9 per cent) that students would be forced to drop out of school if the loan became unavailable. It turned out that most of the loan recipients were heavily dependent on the student loan for their financial support. When we asked the students how they supported themselves before receiving the student loan, the most common answer was through parental assistance, and other answers were through scholarship, or fellowship. Most students said that they could not continue schooling without a student loan, and should their loan be discontinued, they would find another commercial loan or income. As alternative ways to support their school expenses, most students responded that they would find a part-time job, while some said that they would ask for assistance from their parents. The other interesting answer was that they would skip a few semesters to raise enough money for school.

On the other hand, bank staff reported that the demand for government-subsidized loans has increased since the economic situation of the Republic of Korea worsened due to the foreign exchange crisis in 1997. Also, the demand for other loans for study has increased in cases where the student cannot obtain the government-subsidized loan. One staff member mentioned that there are calls to lower the interest rate, following the fall in interest rates of other loans for individuals. All of the bank staff said that the student loan should be expanded because the scale of the student loan is very small, and many students who want to borrow money for study do not have the opportunity. But one of them suggested that the government should guarantee the repayments.

5. Selection criteria

Another issue is that eclectic eligibility criteria and the screening process limit the poor students' chances of obtaining loans and distort targeting policy.

Most schools used the financial status of the students as the main selection criteria for the student loan and 35 schools (46.1 per cent) used financial status alone. A combination of financial status and academic achievement was used in 26 schools (34.2 per cent), and 15 schools (19.7 per cent) had their own selection criteria.

According to the interviews with recipients, most of the students who use the loans programme are in need of financial support for funding their education. However, regarding the selection criteria, there was found to be a serious problem. Most staff in charge of student loans programmes at universities pointed out that the letter of recommendation for obtaining the loan is issued on a first-come-first-served basis, so students who urgently need a loan cannot benefit. Moreover, the scheme is targeting the poor, but academic achievement plays an important part in selection. This is confirmed by the respondents from the universities' staff, and also by the distribution of the recipients' grades. In order to find out students' academic achievement, we asked about their GPA (Grade Point Average). The majority of the students had their GPA between 3.5 and 4.0 – 30 students were in this range. There were 21 students who had between 3.0 and 4.0; 3 students had above 4.0; 6 students had below 3.0; and no response was given from 3 students.

One official pointed out that the loan applications converge on large banks and banks issue a letter of recommendation to each university, by the number of students. And another official suggested that it was better to distribute the loan after ascertaining the loan demand, than to distribute upon the scale of student numbers. It turned out that universities do not have accurate information about the number of real recipients of the loan, because they do not follow up students after issuing recommendation letters. This fact raises the need for information exchange between bank and school. Many staff in universities said, “We only give out a letter of recommendation to students, so we do not know about the present condition of loans, for example, how many students received a loan and how much they got, etc.” They suggested that banks report the list of recipients and amount of loan to schools to promote the efficiency of the loan operation.

The student loans scheme of the Republic of Korea is still very limited in terms of its coverage. Within the limit of their coverage, the student loans schemes have served as support mechanisms for the maintenance of students, at somewhat lower costs than outright grants. However, the loans scheme should ensure that for poor students who anticipate benefits but lack current means, living expenses should not be excluded along with the tuition fees. Such a scheme gives poor families or students access to finance when needed and enables them to repay the debt when they can afford it. Also, since the subsidies are hidden, they are likely to reach groups other than the intended recipients, unless eligibility for such loans is carefully defined.

Special features to promote equity

For the loans scheme to be more equitable than with the unselective subsidies, the Korean loans schemes should incorporate special features that further promote equity. For example, the interest charged on loans can vary with a graduate’s income, an arrangement that alleviates the hardship faced by those who are temporarily unemployed or who fail to obtain high-paying jobs. The government should take a more active responsibility in alleviating students’ difficulties in obtaining educational credit by guaranteeing the repayment. Whether it makes the loans or insures commercially loaned funds, the government is big enough to absorb risks that private lenders cannot or will not bear. In addition, collection of repayment may be less problematic since most graduates can be traced through the government bureaucracy or through the income-tax system. If loans are under governmental authority, employers may also be willing to make deductions from former students’ salaries for loan repayment.

Chapter 6

Conclusions and policy implications

1. Conclusions

In the previous chapters, we examined the main features of the student loans scheme in the Republic of Korea. Included are its historical development, current conditions, objectives, organizational and administrative structures, financial sustainability, etc. Regarding each aspect, we dealt with the relevant issues following the framework set up for the comparative purpose. In addition to this, we discussed issues about equity in the performance of the loans schemes, presenting the survey results from the student recipients and university and bank staff in charge of the loans programmes.

The following *Table 6.1* shows the main structure of the current student loans schemes in the Republic of Korea.

Table 6.1 Structure and options of the student loans schemes in the Republic of Korea

Structure	Options	Description
Lending institution	a. Government ministries and autonomous public body b. Private commercial banks c. Educational institution (selection only)	a. Government ministries allocate quota and subsidize interest within the limit of government budget; publicly administered and financed loan organizations distribute and collect loans b. With developed banking systems, private banks allocate and collect loans c. Educational institutions select loan recipients
Repayment mechanism	a. Mortgage-type loan	a. The capitalized loan is broken into monthly payments (standardized repayment)
Interest rates and subsidies	a. Fixed interest rate	a. Interest rate which recipients have to pay is fixed from zero to 4.75%. b. The length of the repayment period is varied to achieve a balance between debt burden and financial stability

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Default minimization	<ul style="list-style-type: none"> a. Grace period b. Incentives for financial agent c. Require guarantor d. Moral pressure e. Bar further credit 	<ul style="list-style-type: none"> a. Allow students a specified time after graduation before repayment begins b. The government guarantees the loans (MOL loans scheme); banks entice prospective customers c. Requiring an income-earning co-signer on a loan who agrees to pay in the event that the graduate does not pay d. Publish lists of defaulters e. Bar access to further credit if in default
Targeting	<ul style="list-style-type: none"> a. Means testing b. Ability criteria c. Social welfare service 	<ul style="list-style-type: none"> a. Selection of credit recipients on the basis of family or individual income or more complex socio-economic status indicators b. Selection of students on the basis of academic performance c. Provision of loans for public-service workers, teachers, industrial workers and the handicapped

Note: The format of this table is based on Ziderman and Albrecht (1995).

In many countries, the motivation to achieve greater cost recovery has shifted the burden of higher-education costs away from government (or the taxpayer) to the main beneficiaries of education – the students. The combination of rapid university expansion, macroeconomic difficulties and increasing calls, by other sectors, on the public purse has led to the search for greater cost recovery in higher education. The main thrust of these policies to tap additional sources of funding has been in the introduction, or raising, of student fees for services rendered, whether for tuition or board and lodgings.

However, many students, particularly the less well-off, may be forced to drop out from higher-education studies because of the additional financial burden of studying. Resort to commercial borrowing to relieve these financial pressures is largely ruled out because of the banking system's traditional reluctance to lend for education courses, a clear case of market failure. Hence the government-backed loans scheme should fill this gap. Loans enable students to meet increased tuition and living costs; repayment is eased by augmented income in the future.

Based on the review of the student loans scheme, we can reach the conclusion that the Korean student loans scheme has been financially sound with low administrative costs and default rate and with a well-developed banking system. Moreover, the burden of repayment for students is tolerable.

However, we also found some profound problems in the reach of the target group as well as in administrative arrangements for the loans scheme. Also, we suggest the coverage of the loans scheme should be expanded considering the social demand from the poor. Although the loan coverage of the six loans schemes reviewed in this study is about 30 per cent, the coverage of the MOE&HRD scheme, targeting the poor, is less than 7 per cent. Furthermore, loans for the poor do not sometimes reach the target group because of the distorted selection process.

Therefore, we suggest several policy issues which should be examined further based on the findings of the research.

2. Policy implications

Targeting of the student loans scheme

The listed six Korean student loans schemes specify their target group and provide loans for students in financial need. While other schemes are focusing on their targeting group, the loans programme of the MOE&HRD, the largest student loans scheme, is not successful in focusing on its target group. The programme clarifies its objective as being to support the poor in their access to higher education, but it is open to all students in practice, regardless of their financial situation. Because universities and colleges allocate the loan on a first-come-first-served basis, the poorest students happen to be excluded. Some colleges and universities also applied merit-based and need-based criteria together, although financial status is the only criterion for the loan.

Open access to student loans is expensive for governments, particularly if support is subsidized. A successful support programme needs to be targeted effectively at those who are deemed most deserving of support. Without effective targeting, growing student numbers in the future, as well as less than full loan recovery, will result in increasing, and unsustainable, pressures on limited loan funds. Given that loan funds are subsidized and most likely will continue to be so, targeting will facilitate the task of limiting the extent of loan subsidization. Therefore, there should be a more strict selection process to target the students most in need.

3. Minimum restrictions on ability criteria

Ability restrictions give students a strong performance incentive, while also rewarding those who are most likely to benefit from higher education. Restricting eligibility in this way can help to avoid providing subsidies to students that are most likely to repeat or drop out. The failure to limit funds to qualified students can lead to higher default, as experienced in the USA. Relatively high default rates on student loans stem from the lack of ability criteria in allocating support. The lack of quality standards has led to an increasingly costly programme.

However, it should not be as high as merit-based grants, and the reform of the programme requires the government to reconcile increasing quality standards with the need to preserve access for the students most in need. For example, the loans programme run by the Korean Research Foundation limits its qualification to students who are placed above 50 per cent in their school record; but, considering that its main objective is to expand opportunity for higher education, the quality standard should be minimized.

Expansion of loan coverage

The student loans schemes in the Republic of Korea only cover tuition fees. Even the KRF loan, which indicates clearly that it covers cost of attendance, in practice covers only tuition. But, in order to substantially aid the promotion of poorer people's higher-education opportunity, the loan coverage should be expanded to encompass the full cost of attendance for higher education including cost of living, a book budget, and boarding expenses, not to mention tuition fees. In addition, most loans schemes open to undergraduate students should be expanded to include graduate students.

One way to expand the loan coverage is to tailor it to fit different cases, depending on the assessment of the personal need; that is, the limit of loan coverage may be decided by students' financial need, or social status; dependence or independence, married or unmarried status and so on. To expand the limits of the loan, additional financial resources are required. For this, the current government's interest-subsidization rate and terms of repayment, such as duration of repayment and interest rate, should be rearranged, and therefore further research to assess the appropriate interest rate and other terms should be carried out.

Interest assessment

At present, there is no interest-assessment formula, and the MOE&HRD and banks decide upon joint deliberation instead. The interest rate on the student loan is fixed from zero per cent to 10.5 per cent. The interest rate of the student loan was 10.5 per cent, while market interest rate was 14.45 per cent in 1999, and 12.25 per cent in 2000. On the other hand, the interest rate on the student loan is the same, although the market interest went down in 2001.

It is necessary, therefore, to make a proper interest-assessment formula, which moves together with the fluctuation of the market interest rates. Advantages of interest assessment are as follows: first, most return on the educational investment is brought to the investor himself; to that extent, the investor should bear an investment cost (benefit principle). Second, targeting loan support as much as possible, to maximize coverage with limited public funds, it is appropriate to minimize a grant and to assess interest on the principal at a reasonable level. Third, assessing an interest rate at a level that reduces the recipient's substantial burden can lessen the recipient's hardship.

Reducing subsidies while limiting the debt burden with flexible loan terms and repayment plan

The manner in which interest charges are assessed is central to the balance between efficient cash flows and equitable debt burdens. The lower the interest rate, the larger the subsidy on loans. But higher interest rates increase debt burden and the likelihood of default. In designing repayment plans that limit the subsidy element in the loan, it is important to examine the likely range of incomes that graduates will earn. A successful loans programme will not simply raise interest rates, but will redesign the repayment format so that graduates will be in a position to repay.

Various options regarding a repayment schedule are possible: standard repayment; extended repayment plan; graduated repayment plan; adjusted gross income repayment plan etc. Instead of the equal nominal payments of the Korean loans schemes, graduated nominal payments may be an option to reduce debt burden. That is, borrowers pay equal real (rather than nominal) amounts, thus ensuring that the first payments are not excessively large in real terms. In addition, an income-contingent loan,

where loans are repaid as a proportion of a graduate's income each year, is another option. Income-contingent loans are expected to be more favourable to lower-income students (Ziderman and Albrecht, 1995). Tax exemption for loan interest during the repayment period can also be considered to reduce students' or parents' repayment burden.

Post-management system

Choosing an appropriate collection institution is central to effective recovery. While autonomous bodies and universities may possess comparative advantages in selecting students and targeting support, it is less clear that they have the capacity to collect repayments. The relatively high default rate of the KRF loan shows this difficulty in its collection process. Especially for the institutions run by public funds such as the KRF, clear incentives to collect need to be established to reduce deferral.

To raise the efficiency in post management, the KRF may utilize the third-party collection agencies. Or it may rely on a banking system; other schemes using a bank system for lending and collecting loans have a more efficient post-management system. There is always the possibility of diversion of a loan to other uses and not educational expenses. Because the student loan is lent at a low interest rate, students or their parents can use the money for other purposes, for example, household expenses, entertainment costs or expenses of investment in stock, and so on. It is necessary, therefore, to confirm that the applicants urgently need the loan, and that they spend the money on studies. Banks have the necessary infrastructure and operate efficiently at collecting money so long as the policy does not undermine their incentive to do so.

Unification of running organizations

The scale of the KRF loan is just one-tenth of the MOE&HRD scheme. Considering the small loan budget of the KRF, it may be more rational to unify the loan services of the MOE&HRD and the KRF to curtail the execution cost. In this case, the following alternative measures can be considered. First, to keep the present supply method and provide loans as both unsubsidized and subsidized according to a student's financial state. Second, if there is a technical problem followed by differentiating and that differentiation is not efficient in view of the present work scale, to unify the present supply methods into one. To unify the services, we

recommend the establishment of an organization to take full charge of the loans scheme under the MOE&HRD.

Other incentives to establish an organization exclusively charged with the management of the student loans scheme are as follows. First, it can manage the selection process of recipients. Second, it can follow up recipients' whereabouts and co-operatively work with colleges and universities. Third, it can manage the repayment schedules and control recipients' deferrals. Fourth, it can mobilize a legal force for repayment.

The designation of one or two banks to take charge of the student loans programme is another option to make loan management more efficient, considering the characteristics of student loans as policy financing. Regarding the designation of banks that exclusively take charge of the student loans programme, there are diverse opinions between university and bank, and among the banks. Those who agree with the idea argue that it may make the administrative procedures more simple and efficient. They argue that it is inconvenient that each bank has different loan criteria, time of issuing a letter of recommendation, document requests and so on. But those who oppose it argue that it may restrict the options of the recipients. This is also a matter to be explored in further research.

Simplification of administrative procedures

Administrative procedures for borrowing should be improved and simplified. Many people, recipients and university staffs, argue that administrative procedures are too complicated and inefficient. For example, the schedule of the present loans scheme is run in accordance with the regular registration period, but the new students of occasional admission and the freshmen of graduate school find difficulties in applying. To issue a letter of recommendation also seems unnecessary. Because the time of issuing a letter of recommendation is during the vacation period, students must visit school to obtain the recommendation of the president, in spite of the vacation. Many report that the request of the president's official seal is nothing but a formal act. Many university staffs suggested that all designated banks unify the form of recommendation and the distribution time of the recommendation letter.

With the simplification of administration procedures, it is also necessary to make loan conditions more easily understood. The students are

unfamiliar with the conditions (repayment term, amortization plan, interest rate) of their loan and more than half of them reported that they did not know the details or had only a rough idea about the plan. Some stated that it was difficult for them to understand, because the loan agreement used financial terminology.

*Provision of incentives to the commercial banks
through the government's guarantee of repayment*

To increase the student loan supply, it is indispensable to mobilize private lenders' participation. The loans programmes are not profitable enough to banks at the present time. Far from being supported by the government, some of the banks that provide the student loan services bear the burden of the loss of interest. In this current system, it is difficult to mobilize a voluntary participation of lenders. Therefore, to escalate participation, the government should guarantee the repayments, and monitor the borrower efficiently, in addition to adjusting the interest rate.

Widespread policy to ensure repayment of loans is requiring a wage-earning guarantor who agrees to pay the loan if the student does not or cannot. The result of such an effective guarantee should be that default would be negligible. Requiring a guarantor, however, can have negative consequences that defeat the purpose of a credit scheme: precisely those people who most need support may be the least able to provide guarantors. On the other hand, some banks use a loan insurance system. In this case, it has the effect of increasing the borrower's burden, like paying more interest. Therefore, the government needs to reduce banks' risk by guaranteeing the losses of the bank, and this will also have the effect of lowering the interest rate for borrowers.

4. Suggestions for further studies

Experience in both developed and developing countries has shown that student loans are feasible, despite the problems associated with high default rates. Apart from increased cost recovery, loans schemes have other positive effects. Competition for places in higher education would no longer be limited to applicants who can pay at the time of enrolment. Since a large number of highly motivated students would be able to compete for places, a better selection of students for higher education is likely to result. Studies show that by enabling qualified students from poor families

to enter higher education, a well-functioning loans scheme can generate substantial efficiency gains, though the size of such gains varies by country. Moreover, students with loans are more likely to complete their studies successfully, and in the minimum time, than are non-borrowers.

After experience of the working of the student loans scheme, we confirmed that students' financial burdens, militating against effective study, are eased by the availability of student loans. However, it has also been argued that highly subsidized university education may lead to negative outcomes in the form of a lack of student commitment and a free-and-easy approach to study. In addition to this, most students in the Republic of Korea who have reached adulthood, nevertheless rely on parental financial support. Therefore, we need to figure out whether the availability of student loans is leading to a more effective selection of courses of study, more serious study habits and higher course completion rates or vice versa. Whether loans have an effect on enabling students to achieve financial independence is another issue to be explored.

Appendix 1

Loan interviews and questionnaire survey

Purpose

In the last semester of 2001, field surveys were carried out to provide background information for the loans scheme policy review. The central purpose of the surveys is to collect information from loans scheme recipients and loan staff of universities and banks on the efficacy of the scheme in meeting its central objectives.

Key questions of the surveys for the university staff:

- How much is the demand for the student loan?
- What are the main selection criteria?
- Why did many eligible students not take up a loan?
- What would be devices for improvement of the student loans programme?

Key questions of the survey for the recipients:

- How would loan recipients manage to finance education in the absence of the loans scheme?
- How important is the loans scheme in discouraging drop-out?
- Should the student loans programme be expanded to cover the living cost?
- What is the expectation of the repayment burden after graduation?

Key questions of the survey for the bank staff:

- What are the difficulties in the student loans business?
- What would be the devices for improvement of the student loans programme?
- Which guarantor system do you have for the student loans scheme?
- How do you monitor for collecting loans?

Sample design

The recipient samples were identified via student listing at each university. The university and bank staff taking charge of the loans programme were from the MOE&HRD. For the university survey, we sent questionnaires to 150 universities that have run a student loans programme. A total of 77 schools participated in this survey (15 public and 62 private). Interviews were conducted with 63 students from 4 colleges, taking account of location and types of foundation. The participants' gender was evenly distributed in this survey. We interviewed all staff (except for the two branch offices) in charge of the student loans programme from 13 commercial banks operating the loans programme, including two branch offices in the local town.

Fieldwork

Questionnaire survey data were collected by mail and interviews were conducted through field visits by authors.

Major findings

While detailed survey results have not been published separately, selected findings are provided in this monograph. Some of the central results from the surveys are presented in *Chapters 5 and 6*.

Appendix 2

Statistics on loan performance

Table A1. Comparison of the annual amount and number of recipients of six loans schemes (units: won, persons)

		MOE&HRD	KRF	GEPC
1989	Amount			
	Number			
1990	Amount		334,058,970	
	Number		495	
1991	Amount		705,010,680	
	Number		988	
1992	Amount		808,084,630	
	Number		935	
1993	Amount	38,700,000,000	1,496,760,530	
	Number	40,000	1,482	
1994	Amount	29,600,000,000	4,191,189,200	
	Number	29,000	3,789	
1995	Amount	28,400,000,000	22,482,562,580	
	Number	25,000	21,532	
1996	Amount	39,900,000,000	22,144,046,330	
	Number	30,000	21,757	
1997	Amount	53,200,000,000	24,159,769,860	*1,712,449,000,000
	Number	37,000	22,583	*2,292,650
1998	Amount	65,500,000,000	24,973,561,625	392,211,000,000
	Number	45,000	22,793	218,777
1999	Amount	165,100,000,000	27,730,981,970	376,641,000,000
	Number	101,000	24,774	209,665
2000	Amount	454,700,000,000	29,606,495,200	391,558,000,000
	Number	215,000	25,782	201,151
2001	Amount	455,000,000,000		
	Number	210,000		

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		KTP	MOL	KLWC	Total
1981	Amount	1,934,700,000		1,934,700,000	
	Number	9,149		9,149	
1982	Amount	3,603,380,000		3,603,380,000	
	Number	12,882		12,882	
1983	Amount	3,579,550,000		3,579,550,000	
	Number	13,036		13,036	
1984	Amount	3,185,680,000		3,185,680,000	
	Number	11,672		11,672	
1985	Amount	3,334,100,000		3,334,100,000	
	Number	12,227		12,227	
1986	Amount	3,269,080,000		3,269,080,000	
	Number	12,006		12,006	
1987	Amount	3,946,520,000		3,946,520,000	
	Number	11,456		11,456	
1988	Amount	5,391,430,000		5,391,430,000	
	Number	12,071		12,071	
1989	Amount	6,485,340,000		6,485,340,000	
	Number	12,951		12,951	
1990	Amount	8,496,680,000		8,830,738,970	
	Number	13,450		13,945	
1991	Amount	10,655,020,000		11,360,030,680	
	Number	15,141		16,129	
1992	Amount	13,253,860,000		14,061,944,630	
	Number	16,433		17,368	
1993	Amount	14,592,520,000		54,789,280,530	
	Number	18,185		59,667	
1994	Amount	19,114,470,000		52,905,659,200	
	Number	19,918		52,707	
1995	Amount	28,838,520,000		79,721,082,580	
	Number	20,867		67,399	
1996	Amount	37,360,710,000	4,761,000,000	104,165,756,330	
	Number	22,015	2,954	78,726	
1997	Amount	41,552,840,000	14,560,000,000	291,000,000	1,846,182,609,860
	Number	22,924	8,365	150	2,383,672
1998	Amount	47,456,360,000	16,949,000,000	763,000,000	549,661,021,625
	Number	25,652	9,878	536	322,636

1999	Amount	49,264,460,000	23,484,000,000	948,000,000	643,168,441,970
	Number	26,432	13,552	671	376,094
2000	Amount	55,682,930,000	34,626,000,000	1,486,000,000	967,659,425,200
	Number	27,521	18,590	855	488,899
2001	Amount		43,036,000,000	1,491,000,000	499,527,000,000
	Number		21,658	819	232,477

Note: * The total amount and number of recipients in 1997 is not the net total of 1997 but the aggregate from 1981 to 1997.

Source: Authors' calculation using manuals and status reports for each loans programme.

Table A2. Default rate of the MOE&HRD loans scheme, 1996-2000
(unit: million won, person)

Name of bank	Total loan amount	Repayment	Remainder (A)	Arrears (B)	Number of delinquents	Default ratio (B/A)
Kookmin	295,569	71,680	223,885	28,608	19,391	12.8%
Nonghuyp	381,983	164,840	217,143	1,269	2,072	0.6%
Koram	4,821	2,820	2,001	75	183	3.7%
Seoul	12,392	1,429	10,963	354	449	3.2%
H & CB	132,765	17,268	115,497	822	6,950	0.7%
Hana	21,026	9,933	11,093	618	1,077	5.6%
Pusan	6,794	1,848	4,946	283	202	5.7%
Kyungnam	5,025	2,005	3,020	237	304	7.8%
Chunbuk	11,313	3,373	7,940	8	5	0.1%
Kwangju	16,364	4,385	11,979	475	1,636	4.0%
Daegu	16,303	3,929	12,374	29	278	0.2%
Cheju	2,215	305	1,910	375	248	19.6%
CHB (Chungbuk)	649	523	126	8	5	6.3%
CHB (Kangwon)	302	165	137	5	7	3.6%
Total	907,517	284,503	623,014	33,166	32,807	5.3%

Source: The Ministry of Education and Human Resources Development, 2001.

Table A3. Loan repayment condition of the KRF loans scheme by year (in person/million won)

Classification	Coverage		Repayment		Recovery rate (%)
	Amount	Number of persons	Amount	Number of Persons	
1995	-	-	5	7	
1996	370	410	295	392	79.83
1997	4,373	4,988	3,487	4,312	79.74
1998	8,543	11,694	7,540	9,650	88.26
1999	12,272	16,702	10,920	13,820	88.98
2000	14,694	20,601	14,013	17,690	95.36
Total	40,252	-	36,260	-	86.43

Source: Korea Research Foundation, 2001.

Table A4. Number of recipients by grade and sex of the KRF loans scheme (unit: person)

	Freshman	Sophomore	Junior	Senior	Total	Male	Female	Total
1990	482	1,468	605	129	2,684	1,635	1,049	2,684
1991	592	2,078	2,148	925	5,743	3,283	2,460	5,743
1992	92	1,699	1,527	2,035	5,353	2,826	2,527	5,353
1993	159	2,486	1,622	1,468	5,735	3,131	2,604	5,735
1994	123	2,165	1,926	1,682	5,896	3,251	2,645	5,896
1995	279	2,699	1,762	1,603	6,343	3,285	3,058	6,343
1996	231	2,813	1,823	1,651	6,518	3,282	3,236	6,518
1997	288	2,901	1,843	1,618	6,650	3,215	3,435	6,650
1998	453	3,024	1,882	1,903	7,262	3,417	3,845	7,262

Source: Korea Research Foundation, 2001.

Table A5. Number of recipients by six major fields of the KRF loans scheme (unit: person)

	Cultural science	Social science	Education	Natural science	Medical science	Art and Physical science	Total
1990	374	679	221	1,227	124	59	2,684
1991	603	1,535	444	2,639	371	151	5,743
1992	806	1,017	331	1,738	1,186	275	5,353
1993	752	1,088	252	2,906	392	345	5,735
1994	681	1,217	286	2,977	350	385	5,896
1995	790	1,255	252	3,113	445	488	6,343
1996	784	1,448	224	3,123	478	497	6,518
1997	843	1,456	193	3,134	466	558	6,650
1998	749	1,559	201	3,422	595	736	7,262

Source: Korea Research Foundation, 2001.

Table A6. Number of recipients and total amount of the KTP loans scheme by school type

Year	Classification	Government-subsidized loan				
		Total	College college	2-year education	College of university	Open
1981	Case	9,149	7,946	1,127	76	-
	Amount	1,934,700	1,695,940	231,470	7,290	-
1982	Case	12,882	11,614	1,167	101	-
	Amount	3,603,380	3,295,120	297,480	10,780	-
1983	Case	13,036	11,932	975	129	-
	Amount	3,579,550	3,318,630	247,560	13,360	-
1984	Case	11,672	10,709	820	115	28
	Amount	3,185,680	2,958,100	209,400	11,660	6,520
1985	Case	12,227	11,246	810	118	53
	Amount	3,334,100	3,103,900	205,920	12,020	12,260
1986	Case	12,006	11,100	753	94	59
	Amount	3,269,080	2,055,180	190,620	9,600	13,680

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1987	Case	11,456	10,613	713	79	51
	Amount	3,946,520	3,744,550	181,140	8,080	12,750
1988	Case	12,071	11,199	703	73	96
	Amount	5,391,430	5,134,700	216,440	9,610	30,680
1989	Case	12,951	11,932	904	57	58
	Amount	6,485,340	6,136,936	326,250	8,580	13,574
1990	Case	13,450	12,250	945	55	200
	Amount	8,496,680	7,990,380	412,120	10,120	84,060
1991	Case	15,141	13,617	1,177	87	260
	Amount	10,655,020	9,858,760	632,630	36,220	127,410
1992	Case	16,433	14,551	1,443	133	306
	Amount	13,253,860	12,173,910	830,080	72,790	177,080
1993	Case	18,185	15,804	1,819	169	393
	Amount	14,592,520	13,218,810	1,051,760	94,710	227,240
1994	Case	19,918	17,147	2,105	203	463
	Amount	19,114,470	16,939,620	1,745,980	117,740	311,180
1995	Case	20,867	18,228	2,082	-	557
	Amount	28,838,520	25,804,320	2,511,710	-	522,490
1996	Case	22,015	18,910	2,477	-	628
	Amount	37,360,710	32,712,070	3,872,660	-	775,980
1997	Case	22,924	19,657	2,618	-	649
	Amount	41,552,840	36,249,980	4,357,110	-	945,750
1998	Case	25,652	21,937	2,904	-	791
	Amount	47,456,360	41,415,480	4,811,980	-	1,158,900
1999	Case	26,432	22,853	2,879	-	700
	Amount	49,264,460	43,382,520	4,848,980	-	1,032,960
2000	Case	27,521	23,974	2,983	-	564
	Amount	55,682,930	49,362,470	5,381,330	-	939,130

Source: Korea Teacher's Pension, 2001.

Table A7. Default rate of the KTP loans scheme
(unit: thousand won)

Year	Resource				Loan amount of this year	Repayment of this year	Balance
	Total	Trust money (business expenses)	Redemption money	Debt of pension fund			
1981	3,218,096	3,150,000	68,096	-	1,934,700	23,230	1,911,470
1982	3,367,178	3,012,422	354,756	-	3,603,380	178,130	5,336,720
1983	4,324,952	3,850,000	474,952	-	3,579,550	357,533	8,558,737
1984	4,471,750	3,823,881	647,869	-	3,185,680	516,863	11,227,554
1985	1,093,198	-	1,039,198	-	3,334,100	952,898	13,608,756
1986	3,043,606	-	1,558,717	1,484,889	3,269,080	1,528,369	15,349,467
1987	4,170,743	50,000	2,083,464	2,037,279	3,946,520	2,053,314	17,242,673
1988	5,349,840	50,000	2,596,143	2,703,697	5,391,430	2,568,335	20,065,768
1989	6,562,454	50,000	2,982,366	3,530,088	6,485,340	2,950,525	23,600,583
1990	8,557,102	50,000	3,299,969	5,207,133	8,496,680	3,282,704	28,814,558
1991	10,767,233	50,000	3,453,687	5,236,546	10,655,020	3,449,308	36,020,270
1992	13,531,141	50,000	4,014,224	9,466,917	13,253,860	4,008,391	45,265,739
1993	14,797,880	50,000	5,025,303	9,722,577	14,529,520	4,986,117	54,872,142
1994	19,469,411	50,000	6,676,517	12,742,924	19,114,470	6,648,161	67,338,451
1995	29,391,824	372,643	8,137,751	20,881,430	28,838,520	8,096,149	88,080,822
1996	37,283,325	8,491,214	9,923,229	18,868,882	37,360,710	9,788,452	115,653,080
1997	41,906,650	27,360,095	12,567,541	1,979,014	41,552,840	12,188,615	145,017,306
1998	39,399,875	14,981,414	19,568,465	4,849,996	47,456,360	18,740,408	173,783,257
1999	53,967,526	22,262,231	31,705,295	-	49,264,460	31,503,134	191,494,583
2000	53,885,377	22,763,511	28,973,083	2,148,783	55,682,930	28,797,360	218,380,153

Source: Korea Teachers' Pension, 2001.

**Table A8. Ratio of abandonment of the MOL loans scheme
(unit: person, million won, %)**

Year	Budget	Loan result		Ratio of abandonment
		Person	Amount	
Total	164,168	74,997	137,371	16.3
1996	5,789	2,954	4,761	18.5
1997	17,022	8,365	14,560	14.5
1998	18,790	9,878	16,949	9.8
1999	30,647	13,552	23,484	23.4
2000	45,376	18,590	34,626	23.7
2001	46,544	21,658	43,036	7.5

Source: Ministry of Labour, 2001.

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