

Chapter 2

Inter-Korean Economic Cooperation: The Need for Reciprocity. Does Lopsided Cooperation Soothe the North's Bluffing Mentality?

They do not know how to do right, who hoard plunder and loot in their fortresses.

Amos 3:10.

I gave you empty stomach in every city and lack of bread in every town. Yet you have not returned to me, declares the Lord.

Amos 4:6.

2.1 The Definition: Economic Cooperation Versus Bilateral Trade

The term, economic cooperation, has very multifaceted implications. It may be generally meant to connote the “two-ways balanced transactions based on comparative advantages, cooperative economic projects, and mutual economic aids and supports,” and so forth. In the case of bilateral relations between North Korea and South Korea, economic cooperation has been used largely to encompass “human exchange” (meetings of separated families, mutual visits, and Mt. Keumkang tourism, and feasibility surveys for Gaesung special zone, and so forth), the South’s provision of various material supplies to meet the demands of the North, and both pecuniary and non-pecuniary aids and investments into North Korea. Most of the time, the main flow of such inter-Korean cooperation has so far run from the South to the North, not the other direction. It has been an utterly unbalanced transaction. Inter-Korean trade has also occurred in such a heavily biased direction that the purchases into the South have overwhelmed the imports into the North, because the trade has been conducted on the basis of political consideration rather than economic efficiency principle. According to the “Law Governing the North–South Exchange and Cooperation” (1990 August) of South Korea, the inter-Korean trade

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refers to the imports and exports between the North and South, which include movements of all goods between the two states via any third mediator country. The imports and exports statistics are, however, officially being compiled inclusively on the basis of all flows of goods, both commercial trade goods and free donation goods under “cooperative programs,” by the Custom Clearing Office in the South. Strictly speaking, the inter-Korean economic cooperation involves all public and civilian transactions and activities such as economic assistance in cash and materials, cultural performance swaps, tour visits, food and health and medical assistances, sports, and academic exchanges. Economic cooperation is broader than trade in its definition. But in reality, inter-Korean trade has so far been loosely used to involve not only commercial transactions but also non-economic flows of all sorts of materials and human services crossing the border between the North and the South. Such inclusive and open concepts would often be sources of definitional confusion and misunderstanding among people concerned about what is meant by the “inter-Korean economic cooperation” and the “inter-Korean trade,” respectively. Objectively speaking, trade is a subset of economic cooperation as mentioned above. But trade involves the interchange of the shipment of goods and services with the monetary payments for the purchase and sales of the goods and services. On the other hand, economic cooperation may not necessarily involve the counterflows or exchanges between goods and its corresponding monetary payments. Economic cooperation may be based either on reciprocity principle or on non-reciprocal principle. Aside from such definitional distinction, trade and cooperation are often being used interchangeably in the relations between the North and the South. That reflects the peculiarity of inter-Korean relations.

If we look at the inter-Korean economic cooperation, the North has always enjoyed assistance flown into the North. Even if the inflows of materials accompanied by the South’s investment into the North are hard to classify as “lopsided economic aid,” the North has been and is currently getting more than the South in the inter-Korean economic cooperation.

In this chapter, we will define the inter-economic cooperation as broadly including trade, investment, and economic assistance (aid) between the two Koreas. So far, inter-Korean trade as well as investment into the North has been promoted to assist North Korean economy. Therefore, we may use the term inter-Korean trade interchangeably with inter-Korean economic cooperation, even if the two terms strictly differ from one another, in that trade involves the exchange of goods and services involve monetary payments.

In terms of neo-classical economics theory, the investment – saving gap is equal to the external trade gap plus net capital outflow (or inflow) inclusive in the income transfer payments between two trade partners. Namely, $I - S = -(X - M) + F(r)$, where I is domestic investment, S is domestic saving, X is a country’s exports and M imports, and $F(r)$ is net outflows of capital, which is inversely related to the level of domestic interest rate (r) given international rate (r^*), which is also inclusive of net transfer payments such as aids and subsidies across the border. This trade gap equation explains that if a country’s (say, North Korea’s) investment (I) exceeds its

own domestic saving (S), it has trade deficits; that is, its exports (X) are less than its imports (M). The deficits need to be supplemented by net inflows of foreign capital and foreign aids (in this case “minus F ” meaning net inflows) in order to keep the balance of payments in equilibrium. In the bilateral trade between the North and South, the North’s exports into the South have always been greater than its imports from the South. But the total amount of money gained from trade has moved in the same direction as the flows of capital in the inter-Korean trade, which is contrary to the above theory. That is because the trade surplus of North Korea over South Korea has been possible only due to the South’s concession. If we include all beneficial returns obtained in the bilateral trade as well as investment and various aids and grants into the category of trade, the money flow into the North has always exceeded the flow into the South. This suggests that the South has a huge trade surplus in its transaction with the North. In reality, in terms of pecuniary flows involving the inter-Korean trade, the North has gotten the most out of the bilateral trade. The South has tried to import as much as possible from the North instead of attempting to export to the North in order to give more money to the North. Money runs opposite to the flow of physical import and export of goods. In the inter-Korean trade, for example, the sale of commodities from the North accompanies its counterflows of payment money from the South. The purchase of goods from the North is mostly due to political considerations by the South in that the imports are made to help the North’s economy. Meanwhile, in the accounting of the South’s exports to the North are included the tradable commodities as well as investment goods and transfer payment and aid goods which all pass and are recorded through the South’s custom clearing office. If all of these are considered together in accounting, the South appears to have a tremendous trade surplus because the South’s aggregate shipments (exports) sent to the North exceed its imports from the North. But in terms of aggregate monetary settlements, the North has, in fact, gained most of the pecuniary advantage in its transaction with the South.

Because the size of the inter-Korean economic cooperation is measured in terms of monetary flows, the term inter-Korean cooperation inclusive of the loosely defined- trade, investment and other transfers, and so forth, reduces “our confusion” as compared to the counterflows of payment involving the pure bilateral commercial trade, as explained above. In the peculiar inter-Korean trade, if more goods and services are shipped to the South, it means more payments are made to the North either on a pure commercial basis or complementary basis. But the trade surplus by the North is not necessarily grounded on the pure comparative advantage trading principle.

On the other hand, aggregate shipments into the North, including commercial goods and non-commercial assistance goods, are always larger than that from the North, which in turn shows as if the South is making the trade surplus. In reality, the assistance goods and investment goods do not carry immediate paybacks, though the latter may bring their returns in the long run. In the short run, the surplus from the inter-Korean cooperation has so far been in the pocket of North Korea, as the most money has been poured into it.

2.2 The Historical Outline of Inter-Korean Economic Cooperation

The inter-Korean economic cooperation was first proposed with “The Agreement on the Implementation of Trade and Economic Co-operation and the Establishment of the South-North Joint Economic Committee (23 articles)” signed by both the North and the South representatives on June 20, 1985, at Panmunjom. The joint proposal for inter-Korean economic cooperation had very important implications regarding various aspects including political, military, social, and cultural areas in the divided nation. But no actual implementation was made until South Korean President Roh Tae-Woo unilaterally announced his “Special Declaration on National Self-esteem, Unification and Prosperity” on July 7, 1988. After the 7.7 Declaration, small indirect trade (trade via a third country) was timidly attempted by the South businessmen. Since then, various trade promotion measures were promulgated in the South. Among them were the Inter-Korean Cooperation Custom Law and the Law of Inter-Korean Cooperation Fund (1990 August 1). The size of inter-Korean trade was a mere US 20 million dollars in 1989, which increased 90 times to US 1.8 billion dollars in 2007. In March 1993, North Korea declared its withdrawal from NPT (nuclear non-proliferation treaty), which threatened to interrupt the inter-trade relation. But as top level talks between the United States and DPRK agreed to end the nuclear issue on October 21, 1994, South Korea swiftly moved to expand the inter-trade relations. On November 9, the South Korean government announced “the Measures for Inter-Korean Economic Cooperation Promotion,” which opened the door, although under very restrictive control, to the mutual visits of businessmen, the limited investment into the North, and the establishment of the branch offices of the South Korean firms in the North. More active inter-cooperation began with the Kim Dae-Jung regime of the South. After his inauguration to the presidency in February 1998, Kim Dae-Jung (DJ in abbreviation) set up his policy objectives toward North Korea with the following three principles:

(1) Active promotion of the North–South economic cooperation based on the principle of the separation of the economy from politics, (2) cooperation on the basis of market function, and (3) promotion based on each participant’s own decision.

In October 1999, the DJ government issued “the Guidelines for the Uses of the Inter-Korean Economic Cooperation Funds” in order to subsidize investment into the North, establish imports and exports and commission-based processing trade (CPT), as well as finance the small and medium firms involved in the North projects.

Kim Dae-Jung’s *Sunshine policy* was mainly targeted to soften the political and military strains between the two Koreas and to induce the North to *glasnost and perestroika*.

Especially as a result of after the Kim–Kim¹ joint communiqué in Pyongyang in 2000, the Mt. Keumkang sightseeing project (first opened in November 1998),

¹ Kim Jong-Il and Kim Dae-Jung (DJ) met in Pyongyang and released a joint communiqué on June 15, 2000.

and the Gaesung industrial complex project (started in 1989), other intra-Korean trade ventures have greatly increased. In the name of mutual cooperation toward both common prosperity and peace, DJ's appeasement policy had mainly focused on helping the Great Dear Leader's regime in the North, particularly to maintain the political and military status quo in the peninsula. DJ's pro-North policy was succeeded by the leftist-leaning new administration led by the new President Roh Moo-Hyun in 2003.

Roh Moo-Hyun greatly promoted the exchanges of both people and materials across the border by working to provide the South's investors with various favorable legal systems, procedures, and office openings in the North. On December 24, 2003, two railroads were connected across the "heretofore no-return borders." On October 28, 2005, the North-South Joint Consultant Office for Economic Cooperation was opened in the Gaesung complex. Mr. Roh Moo-Hyun visited Pyongyang on October 2-4, 2007, to hold the summit talks with the Dear Leader Kim Jong-Il. Six weeks later, the North and the South Prime Ministers met (November 14-16), followed by Defense Ministers' meeting (November 27-29). It was also followed by Inter-Korean Economic Cooperation Committee meeting (December 4-6) and the West Sea Peaceful Cooperation Promotion Committee meeting (December 28-29).

The Roh Moo-Hyun government encouraged the South's Congress to pass the Law for the Promotion of the North-South Relation Development² in December 2005. Based on the law, the First Basic Plan for the North-South Relation Development³ was formulated to report to the House of Representatives on November 22, 2007. The Basic Plan contained three broad principles, six promotion directions, and seven strategic targets to implement from 2008 to the end of 2012, which all became uncertain under the new conservative government of President Lee Myung-Bak in February 2008.

2.3 The Status of the Inter-Korean Trade

It has been about 20 years since intra-trade began across the demarcation line on the Korean peninsula. In the first two years, annual intra-trade size remained at a mere level of less than US 20 million dollars. In 1991, when the inter-Korean Exchange and Cooperation Law was promulgated in the South, intra-trade increased 730% over the previous year. In spite of the DPRK's withdrawal from the IAEA (International Atomic Energy Agency) Non-Proliferation Treaty, the inter-Korean trade continued to grow pro-cyclically with the two Korean economic situations. Amid the newly closed-up nuclear issue between the IAEA (and the United States) and DPRK in 1988 and the financial crisis in South Korea, President Kim Dae-Jung announced his "Sunshine Policy," signaling his willingness to expand relations

²Law No. 7763, 2005.12.29.

³See the article 13 of Law No. 7763 cited above. The Basic Plan was made in accordance with the article 13: 3 item of the Law.

with North Korea. In 1988, the intra-trade amount was US \$221,943,000, which was about a 28% decline over the previous year (US \$308,339,000), but intra-trade regained strength to reaching \$1,797.9 million in 2007 and \$1,820.4 million in 2008. (See Table 2.1).

Table 2.1 Trend of annual intra-Korean trade (unit: 1000 US dollars)

Year	Import into South	Export from South	Total	Annual Growth (%)
1989	18,655	65	18,724	—
1990	12,278	1,188	13,466	−28.1
1991	105,719	5,547	111,266	726.3
1992	162,863	10,563	173,426	55.9
1993	178,167	8,425	186,592	7.6
1994	176,298	18,249	194,547	4.3
1995	222,855	64,436	287,291	47.5
1996	182,400	69,639	252,039	−12.3
1997	193,069	115,270	308,339	22.3
1998	92,264	129,679	221,943	−28.0
1999	121,604	211,832	333,437	50.2
2000	152,373	272,775	425,148	27.5
2001	176,170	226,787	402,957	−5.2
2002	271,575	370,155	641,730	59.3
2003	289,252	434,965	724,040	12.9
2004	258,039	439,001	697,040	−3.8
2005	340,281	715,472	1,055,754	51.5
2006	519,539	830,200	1,349,739	27.8
2007	765,346	1,032,550	1,797,896	33.2
2008	932,300	888,100	1,820,400	1.2

Note: Export from the South includes commercial (general) exports, materials for commission-based processing, investments, and humanitarian and other cooperation supports to the North while the import includes only purchases by the South

Source: The Ministry of Unification: *Trend of Inter-Korean Trade (annual)*, reorganized by author

The inter-Korean trade (or economic cooperation) is composed of the following: (1) commercial trade under which is general trade (GT); commission-based processing trade (CPT); economic cooperation (EC) inclusive of Gaesung Industrial Complex projects, the Mt. Keumgang sightseeing projects, and other public investment projects; and (2) non-commercial trade, which includes both the public and private social and cultural projects, aids and grants, grains and fertilizer supports, the light water reactor construction subsidies,⁴ and KEDO (Korean Peninsula Energy Development Organization) diesel oil supplies. As shown in Table 2.2, the commercial trade inclusive of economic cooperation projects (such as Mt. Keumgang projects, Gaesung industrial projects, and others) occupies a large proportion as

⁴Total budget for the light water energy project was set at 4.6 billion dollars of which South Korea was to assume 70% (3.22 billion dollars), but the project was suspended in December 2003. Actual spending for the project was 1.48 billion dollars up to the suspension. (South Korea: \$1.07 billion, Japan: \$0.39 billion, and EU: 0.02 billion).

Table 2.2 Inter-Korean trade by major categories (unit: million US dollars)

Commercial Trade								
	GT	CPT	Economic Cooperation				Non-comm.	Total
			(Mt. Keum.)	(Gaesung)	(others)	Sub-total		
1995	230.4	45.9	—	—	—		11.0	287.3
1998	73.0	71.0	37.7	0	1.2		39.4	221.9
1999	89.0	100.0	40.7	0	6.3	236.1	97.3	333.4
2000	110.5	129.2	16.2	0	17.4	273.3	151.8	425.1
2002	171.8	171.2	11.9	0	13.1	367.9	273.8	641.7
2004	171.8	176.0	41.8	41.7	5.8	436.5	260.5	697.0
2005	209.8	209.7	87.1	176.7	6.2	689.5	366.2	1,055.8
2006	304.1	253.0	56.7	298.8	15.5	928.1	421.7	1,349.7
2007	461.4	330.0	114.8	440.7	84.4	1,431.2	366.1	1,797.9

Source: The same as Table 2.1

compared to non-commercial trade. The narrowly defined (pure) economic cooperation (EC) projects which include the Mt. Keumgang tour-related project, Gaesung industrial complex projects and other economic cooperative assistance to the North, have greatly expanded since 2004. The share of this economic cooperation (EC) projects out of total commercial trade (GT+CPT+EC) was 6.8% in 2002, which jumped to 39.2% in 2005, 40.0% in 2006, and 44.7% in 2007. As of the end of 2007, the commercial trade consisted of the general trade (25.7%), commission-based processing trade (18.3%), Mt. Keumgang sightseeing (6.4), Gaesung industrial projects (24.5), and others (4.7), which altogether accounted for 79.6% with the remaining 20.4% being non-commercial trade (private and public assistance) in the total trade (imports + exports). In general, non-commercial trade is regarded as pure assistance being mostly moved from the South to the North. A considerable amount of commercial trade contains the characteristics of non-economical “aid measures,” although in the long run, some profits are expected to return back to those partners who are now extending “don’t-ask-investment” into the North either from a naive sense of fraternity or due to direct or indirect indications from those in political power. It is believed that a large composition of GT and CPT has also been propelled to support the North by the South Korean government.

As a result, both the economic and non-economic motives of many intra-Korean trade participants have been inconsequentially intermingled in their decision-making processes. But as time goes by, South Korean firms have learned their lessons and are more inclined to be profit motivated when they decide to trade with the North. Many companies are also experiencing the lack of basic infrastructures, including communication, transportation, and custom clearance across the borders, not to speak of such problems as “default products” which occurred in the commission-based processing works in the North. Above all, many unsolved political and military tensions remain as the “big uncertainty factors in the intra-Korean trade.”

Table 2.3 Annual exchange visits of people (unit: numbers)

	89-97	98	99	00	01	02	03	04	05	06	07	Total
S→N	2,405	3,317	5,599	7,280	8,551	12,825	15,280	26,213	87,028	100,838	158,170	427,506
N→S	575	-	62	706	191	1,052	1,023	321	1,313	870	1,044	7,157
Total	2,980	3,317	5,661	7,986	8,742	13,877	16,303	26,534	88,341	101,708	159,214	434,663

Table 2.4 Tour visits to Mt. Keumgang and Gaesung region

	98	99	00	01	02	03	04	05	06	07	Total
Mt. Keumgang	10,554	148,074	213,009	57,879	84,727	74,334	268,420	298,247	234,446	345,000	1,734,687
Gaesung								1,484		7,427	8,911
Total	10,554	148,074	213,009	57,879	84,727	74,334	268,420	299,731	234,446	352,433	1,743,607

Sources: The ministry of unification: exchanges of people between the South and the North (monthly statistics)

As for the exchanges of people between the South and North, visits to the North (excluding sightseeing visits to the Mt. Keumgang and Gaesung areas) dominate as shown in Table 2.3. Table 2.4 shows annual visits of South Korean residents to Mt. Keumgang and to the Gaesung area. The overall tilt to the North in the flows of both economic trade and human exchange are obviously the effect of the South's desire to have friendlier relations, the South's higher income, and South Koreans' general curiosity about the Hermit Kingdom as well as weakening political and military tensions between the two countries. It, of course, goes without saying that DJ *Sunshine Policy* has helped to make South Koreans more sympathetic, while their Northern brethren have not yet changed their true face. The South's provision of large economic assistance to the North during the last two decades has apparently helped the Dear Leader hold a bold bargaining position in the nuclear talks with the United States. Ironically, the South's assistance has so far contributed in some degree to the postponement of friendly diplomatic relations between the United States and the Democratic People's Republic of Korea. But in 2008 when Lee Myung-Bak, supported by anti-communist conservatives, took his presidency, the South–North relations as well as relations between the United States and North Korea appears to have entered into a new phase. North Korea has been seeking military and diplomatic talks with the United States while excluding South Korea in the issues.

Incidentally, the past two regimes led by Kim Dae-Jung and Roh Moo-Hyun were believed to have poured more than US 11.0 billion dollars into the cooperation projects for North Korea (Kim: 7.3 billion dollars in 1998–2002 and Roh: 3.7 billion dollars in 2003–2006, and the latter's 2007 budget amounted to 1.2 billion dollars.) In return for their contributions, Kim Jong-Il invited both Kim and Roh to visit him in Pyongyang in June 2000 and October 2007, respectively.

2.4 Comparison of the Inter-Korean Trade with the North Korea–China Trade

Since 2000, both South Korea and China have been two major trade partners of DPRK. During the period 2000–2005, the marginal increase of North Korean external trade amounting to US 1.6 billion dollars was exactly equal to the increases in both the South–North trade (0.6 billion) and China–North Korea trade (1.0 billion dollars).

A comparison of the inter-Korean economic cooperation with the bilateral economic cooperation between North Korea and China reveals some features on the characteristics of the inter-Korean relations. First, the annual growth rates of both China's and South Korea's economic cooperation with North Korea were about 30% before and after 2000, respectively. However, in terms of the contents, the South–North economic cooperation comprised a relatively lower share of pure commercial trade and a larger share in investment and aids versus the opposite in China–North Korea economic cooperation. North Korea has seldom provided either China

or South Korea with any subsidy aids and direct investment which could be included in its export statistics. Since the North exports (inclusive of its aids and investments in both China and South Korea) are very insignificant, we can only compare its imports (inclusive of aids and investments from China and South Korea) from the two countries for the sake of simplicity. In the case of the inter-Korean economic cooperation, the South's aids and investments were US 184 million dollars (which accounts for 67.5% of total South Korean exports to the North) in 2000, which rose to US 349 million dollars (79.5%) in 2004 and US 635 million dollars (88.8%) in 2005. In contrast, Chinese aids and investments into North Korea accounted for US 104 million (23.1%) in 2000, US 163 million dollars (20.4%) in 2004, and US 290 million dollars (26.8%). China has kept its economic cooperation with North Korea on a commercial basis rather than offering its "war brother country" "free gifts" (namely, aids and investments). In other words, China trades with North Korea on a much more reciprocity principle than the inter-Korean trade, which is based on lopsided fraternity favoritism, although the two Koreas are still technically in a state of war.

Second, South Korea and China are exporting intermediate inputs and materials to North Korea while importing mostly primary goods. But in terms of trade items and kind, South Korea's trade is rather simple and few as compared with that of the Chinese trade.⁵ Third, the portion of general trade in the inter-Korean economic cooperation has been less than the half while China's trade depends heavily on general trade with only a 5% share of the commission-based processing trade. South Korea has been "red" in its general trade with the North, while China has kept "blue." South Korea's pure commercial exports were merely about 1/50 of Chinese exports to North Korea as of 2005. This explains that the South's influence on the North's markets has far less impact than that of the Chinese. According to the Chinese People's Newspaper (2006.8.11 Internet edition), Chinese products account for 70%, South Korean products 20%, and Russia and Japan 10% combined among all commodities being imported into North Korea's markets.

Fourth, there are distinctively different patterns of direct investment into North Korea from South Korea and China.⁶ South Korea has mostly invested in the North's special economic zones (i.e., Gaesung industrial complex) with the goal of utilizing low wage laborers of the North in CPT and other manufacturing. On the other hand, China has concentrated in areas such as mining to obtain natural resources. Recently, China has begun to diversify its investment in infrastructure expansion to include manufacturing, circulation, and marketing areas. In short, South Korea looks forward with a short-sighted view while China looks to the long term. The Chinese road appears more promising in the long run, although the eventual outcome will depend upon God, not on who takes what road today.

⁵See Lee Young-Hoon (2006).

⁶North Korea announced its measures (named as 7.1 action plans) on July 1, 2002, in order to designate the Shineuijoo Special Administration Area (September 2002) and both the Gaesung Industrial Complex and the Mt. Keumgang Tourism Areas (November, 2002) with its eye on foreign capital inflows.

2.5 The Determinants of Inter-Korean Economic Cooperation

2.5.1 The Brief Outline

The major determinants of inter-Korean relations involve both “actors (participants)” and “environments” on both sides. Actors include the South’s government, the South’s enterprises, public and private organizations, and the North Korean government, which in broad context is the sole decision maker as well as the action planner in the peculiar North. The internal and external environments involve various factors affecting the two parties; that is, the South’s and the North’s respective relations with neighboring nations, particularly with the United States, as well as the two parties’ economic, political, and military problems. Once we confine our discussion within the contexts of the motives of the inter-Korean economic cooperation, it would be easier to traffic the respective interests of participating actors. Needless to say, South Korea’s private companies are mainly concerned with making money while other social NGO groups approach from a humanitarian point of view to help the people in the North. The South’s government inclusive of public organizations has approached North Korea to help relieve the latter’s economic hardships with the hope that the cooperation could contribute to easing the longstanding strains across the border. On the other hand, the North is apparently learning that its relationship with the United States will very much depend on its renewed relationship with the South.

North Korean leaders have apparently learned that its country’s system risks, its economic recovery, and a favorable international environment inducing foreign capital and even inter-Korean economic cooperation all depend on what kind of relationship it has with the United States.

2.5.2 Trade, Investment, and Economic Assistance

From the perspectives of South Korean business people, the motives for inter-Korean trade and investment into North Korea are manifold. These motives include current and future profitability, availability of low wage laborers, tariff-preferences, the establishment of a bridgehead, contribution to government policy, and last but not least “helping their own or their parent’s native home.” But the main incentive lies in profit-seeking. From the North Koreans’ viewpoint, however, inter-Korean economic cooperation must be no more or no less than “mutual sharing of income” based on “our own national fraternity.” The North side does not generally take into consideration the South business’s profit creation from the intra-Korean trade. Nevertheless, North Korea has enjoyed a considerable benefit in its exports of marine products and raw minerals (including coal) to the South due to the relatively short transportation distance and various favors (i.e., tariff exemption) extended by the South. The impediment to the North’s indigenous tradable items is the decreasing demand for such goods in the South.

The South's investments into North Korea are largely in the form of joint investment or joint operation companies,⁷ except for the Mt. Keumgang project, which is solely invested and operated by the South's Hyundai. Most South Korean investors build factories jointly with North Korean puppet companies. They import raw and intermediate goods from the South to process finished goods using low wage workers in the North and then re-export them to South Korea and third countries via South Korea. This intra-trade can continue as long as the overall cost (including plants) of production for a particular product in the South exceeds the overall cost of production of the product in the North. The choice of production locations as well as kinds of products depends on comparative costs of plants (including land and other facility), wage and productivity differentials, and all transportation costs involved between the two locations. Considering that the North's average monthly wage (\$36) is currently about 1.5% of the South's average monthly income (\$2,360) in 2008, there is good incentive for the South's labor-intensive goods' producers to look for investment opportunity in the North. In particular, the investments in Gaesung complex are being subsidized by the South Korean government in terms of provisions of basic infrastructure layouts and electricity supplies in addition to the availability of a new road across the border. However, the short- and long-run success of any investments not only in the Gaesung complex but elsewhere is likely to depend upon the changing dynamism of comparative advantage structures among alternative investment locations and projects across the world. Everything is changing so very quickly in this global and dynamic age.

Finally, the one-way assistance to the North has so far been influenced by non-economic and political considerations. The distinction is very difficult, but the private sectors provide the North with somewhat humanitarian aids, while the South government extends more or less politically implicative assistance. To date, the South Korean government has attempted to induce both a change in the North's behavior and a sense of peace in the peninsula. To meet those objectives, the South government has been willing to bribe as much as possible its unpredictable brothers in the North. Such a political position is related to the so-called "commercial liberalism," which believes that the inter-economic improvement will contribute to enhancing "the peace" among the concerned parties. Beginning with Roh Tae-Woo government in 1987, South Korea adopted *its policy of functionalism* to deepen the intra-Korean dependency and the inter-Korean economic cooperation with a goal of reducing the military tensions. The Kim Dae-Jung and Roh Moo-Hyun administrations aggressively advanced their policies on the basis of both *functionalism and liberalism*. The *functionalists* basically move from humanitarian projects to economic projects to military and political appeasement stage. The *neo-liberalism*, a hybrid of *functionalism and liberalism*, seeks to parallel the government policies in economic and political areas as well using a variety of mutual contacts without

⁷A joint investment company is one where two parties invest 50:50 each, but only one party is solely responsible for managing the company. Joint operation (management) company is one where two parties share equally their investment as well as the management of the company.

regard to ideological differences. Despite the South's aggressively friendly gestures toward North Korea in every respect, the North has maintained a very negative position with the South when it comes to talks about easing military confrontation, even after the 6.15 joint declarations.⁸ Therefore, many conservative Koreans suspect that there has been no real inter-Korean improvement for peace despite the enormous amount of money poured into North Korea under the past two progressive regimes. The return from the North has been too small compared with the South's big aid-dumping into the North. When the Dear Leader launched missiles in July 2006 and when he stubbornly tested a nuclear bomb in October 2006, many people began to see the need for reciprocity in inter-Korean economic cooperation. This awareness by the majority of the South's people led to the regime change in favor of the seemingly conservative Hannara (Grand National) Party candidate Lee Myung-Bak in the presidential election held in December 2007, which ended the past ten years' control by the leftist' liberal party (which was renamed as the United Democratic Party) in South Korea. However, the liberal (left-wing) factions had already proliferated greatly in every corner of South Korean society during the last ten lost years from the perspective of conservatives. Less than 3 months after President Lee Myung-Bak took office, they were staging street demonstrations (under the slogan of "candlelit vigil cultural activities" they avoided obtaining the legal permission for staging such demonstrations) of which their core target was to oust the right-wing regime under the pretense of protesting against the US beef imports. The leftist-prone civic coalition members and their supporters are using their internet news-medias and blogs to spread groundless rumors to paralyze the embattled Lee government. The wild wind may or may not be linked with the North's denotative move, but it is likely to get cyclically stronger across the landscape during the rest of Lee's term in the Blue House. If inter-Korean relations are waning for any reason, it is because the anti-government movements can be seen and felt in a series of events occurring here and there in the South whenever the incumbent government exposes any weakness, even tiny, in its governance and overall policy. The ideological splits and old hatreds will not end in the South unless the communist system of North Korea is dismantled.⁹

2.6 The Effects of the Inter-Korean Economic Cooperation

2.6.1 *The Impacts on the South Korean Economy*

It may be possible to evaluate that the policy of the inter-Korean economic cooperation has somewhat contributed to reduced military and political strains and tensions toward North Korea, at least in the South. In particular, the DJ's *Sunshine Policy* has largely contributed to mentally disarming South Koreans against any remaining

⁸Kim Jong-Il and Kim Dae-Jung made a joint declaration on June 15, 2000 at their summit in Pyongyang.

⁹See Hwang (2008).

dangers from Kim Jong-Il and his communist regime. Furthermore, the post-war generation no longer regards the North communists as an enemy. Instead, many of them believe that the United States is their main enemy. They have been brain-washed by many liberal-minded teachers in elementary and junior high schools, not to mention the influences from Korean history books and periodicals written by numerous leftist writers¹⁰ and circulated widely among youngsters without any effective caution. Such a drift has been reinforced by the DJ's radical policy shifts on domestic issues as well as on North Korea. It is not yet clear if the *Sunshine Policy* has ever worked in accordance with its proclaimed objective to undress the North's iron stance toward a free and flexible world.¹¹ Nevertheless, DJ's *Sunshine Policy* helped South Koreans, including business people and military soldiers to shake off their worries about the renewal of war on the peninsula, particularly encouraging many to visit North Korea either for sightseeing or for possible business opportunities. The aggregate inter-Korean trade occupies only 0.19% of the South's total external trade and 0.13% of its GDP, respectively, in 2005. Excluding the free supports to the North, the commercial trade (including pure trade and investment) accounted for a mere 0.13% of the South's total trade and 0.09% of the South's GDP, which is indeed not significant from the perspective of South Korea's economy. South Korea has annual trade deficits of about US 200 million dollars with North Korea, which, of course, is not a big burden in terms of its current economic strengths. South Korean economy is capable of providing the North with more economic cooperation and is willing to do so, if the North responded in a more friendly and honest way for the benefits of both its economy and people. The major obstacle now is related to the emotional issues involving the South's suspicions that the North's leaders might be diverting the South's money to build its nuclear and missile projects while leaving millions of its people to starvation. What is needed today for the inter-Korean cooperation is the need for reciprocity. The reciprocity does not necessarily involve the trade of goods and services with other economic commodities, but it can involve the transaction of economic supplies with such equivalent payoffs as positive responses toward common interests in the political, military, and international arenas (Table 2.5).

The South Korean government subsidies are made from the South-North Cooperation fund, which is classified into three categories: subsidies, investment, and other expenses. The Fund had generated about US 2.98 billion dollars (equivalent to 2,987.9 billion Korean won) for the period 1991–2005, out of which about US 262.0 million dollars (2,620.0 billion Korean won); that is, annual average of

¹⁰Bruce Cumings and his Korean students are responsible for having misled Korean youngsters. Probably DJ may also be one of the followers of Bruce Cumings on the Origins of the Korean War.

¹¹Nam Sung-Wook shows that there is some positive correlation between the South's stock price index and the inter-Korean trade in his study made after the IMF crisis. But his research is based on a too simple model with limited number of variables and observations, which do not guarantee sound results. See his paper titled "The North-South Relations and Country Credibility – With Emphasis on Correlation between Stock Prices and Inter-Korean Relations," presented at the Korean Political Association, July 9, 2007 (in Korean).

Table 2.5 The share of the Inter-Korean trade to the South Korea's economy (2005)

	Economic Cooperation (\$ million)	Share in the South's Trade (%)	Share in the South's GDP (%)
N-S Cooperation	1,055	0.19	0.13
(Trade)	420	0.08	0.05
Trade Balance	-194	-0.04	-0.02
(Investment)	270	0.05	0.03
(Subsidies)	365	0.07	0.05

Note: In 2005, South Korean total trade amounted to US 545.7 billion dollars and its GDP was US 787.5 billion dollars

Sources: The ministry of unification and the bank of Korea

about US 174.7 million dollars (174.7 billion won per year) were used. This amount is equivalent to about 0.1% of the South's total budget of about US 2.1 trillion dollars (2,123.7 trillion won) and about 0.04% of GDP of about US 7.3 trillion dollars (7,264.8 trillion won) during the 5-year period. This figure does not include the money donated to KEDO projects. The expenditure in the Grain Management Special Account is also excluded, because that aims to principally support the South Korean domestic farm households through government purchase of rice at the domestic price. But the government sent the purchased rice to North Korea as part of its aid¹² whereby the value was recorded at the international price, about one third of domestic rice price. A precise accounting for all money used to assist the North has never been clear and the accounting methods remain very elusive not only because of dual prices like the rice case above, but also because of the lack of information regarding private humanitarian aids provided through indirect and roundabout delivery channels.

Out of the official Cooperation Fund (1991–2005), the South Korean government used US 1.68 billion dollars equivalent to 1.68 trillion Korean won (64%) to send North Korea foods and fertilizers and about US 820.0 million dollars (31%) equivalent to 820 billion Korean won for the construction of railroads and roads as well as for other aids, with the remaining US 490.0 million dollars (0.5%) for social and cultural projects during the periods 1991–2005.

The aid provided by the South's private sector was officially about US 600.8 million dollars (about US 54.6 million dollars per year), which was about one third of the South government aids during the same period. However, the actual amount handed over to northern relatives and various organizations (i.e., various forms of church, Buddhist temples, orphanages, etc.) by the South residents is estimated to exceed the official figures. Nevertheless, the government's share is much larger than the money coming from the private business sectors in the inter-Korean

¹²There is some argument that a total of about 8.4 trillion won (that is US 8.4 billion dollars) was given to North Korea for ten years starting from 1988 to August 2007. See *The Reference Data for Aids to North*, the Ministry of Unification, October 13, 2006, and *Records of the National Assembly*, October 2008.

cooperation. Many South Korean companies participating in the cooperation projects have not been making profits, except for a few recent business activities in Gaesung projects.¹³ Aside from that, it is not known if the South government has ever clearly demanded any corresponding payoffs from the North in return for its continued assistance. This point is the source of disagreements among the left-wing and right-wing South Koreans regarding the real nature and intention of the inter-Korean economic cooperation advanced greatly by DJ's *Sunshine Policy*. The right-wing supporters believe that the South's *reckless pouring of aid into the North* has helped Kim Jong-Il to develop missiles and nuclear weapons that will target the *enemy in the South*.

The total opportunity costs of both the public aid and private investments into the North must include the non-profit-making investment times the compound interest rates forgone plus the internalized social costs involving the portion of the money from the South that the North might have diverted to develop its war weapons; thus causing unrests on South Korean people, minus the positive contribution of the cooperation to reducing the mutual tensions *inter alia*. For the period 1989–2005, annual public aids were about US 175 million dollars while annual private investments into the North were about US 55 million dollars of which about two thirds (67%) was lost, as mentioned earlier. Based on these figures, for example, the quick rule of thumb estimate shows that the annual opportunity costs of monetary values given to the North amount to about US 245,325 million dollars in 2005.¹⁴ For the last ten years as a whole, the total opportunity costs of the inter-Korean cooperation is estimated to approximate US 2,453,250 million dollars from the perspective of South Korea. If we add the external costs of those ideological conflicts involving the intra-Korean issues that would result in frequent anti-government demonstrations in South Korea, the internalized costs would be astronomical, even though the nominal amount of intra-Korean trade is not so significant in view of the current size of the South Korean economy. In passing, it may be worth noting that the Gaesung industrial complex was approaching near the breakeven point in 2007, according to a report by the Gaesung Industrial Complex Supporting Team of the Ministry of Unification in Seoul. Beginning in 2004 until the end of August 2006, total cash and material inputs for the Gaesung projects were about US 28,056,000 dollars, which included 16,000,000 dollars for land compensation (for 1 million pyong = 3.3 million square meter of area), 7,218,000 dollars for wage and salary for workers, 3,105,000 dollars for construction materials, 1,289,000 dollars for communication bills, and 444,000 dollars for tax payments. The exact cost-benefit needs

¹³ According to Kim Young-Yoon's study, about two thirds of the companies who conduct business in North Korea are losing money in their business dealings. See Kim (2004) (in Korean).

¹⁴ It is estimated as follows: (public aids + private investment times 0.67 times $(1 + r)$) times 0.01 times one half of the total population in South Korea, where 0.67 is failure rate of the investment, r is annual interest rate forgone assumed to be 0.05, and the number 0.01 indicates that about 10% of total public and private investments are going to strengthen the military power in the North. It is also assumed that only 50% of South Koreans are being affected with one US cents per person by the potential threats from the North.

further analysis to estimate the overall effects of the investments on value added, employment, and net exports of those South Korean participating firms.

2.6.2 The Impact on the North Korean Economy

The inter-Korean economic cooperation has increased the North Korean economy's dependency on the South. Generally, the inter-Korean trade statistics can be reclassified so that general trade is regarded as commercial trade while classifying the aids as a transfer payment. Most of material-type investments are made for South Korean branch companies in the North. Such investment in the form of input materials for the South Korean branch firms in the North is problematic if we regard it as a part constituting the North Korean GDP. Commission-based processing trade is related to the "transaction of labor forces," from which the North Korean workers take their processing commission, which accounts for approximately 50% of the total cost of CPT.¹⁵ On the other hand, we consider that the in-kind grants are no more different from the free aids in view of the special relation between the two Koreas. So in this analysis, we will simply treat it as a part of transfer payments from the South to the North. Although the data sets are simplified approximations as such, the North Korea's balance of trade from the inter-Korean economic cooperation, for illustration purposes, using the data of 2005 as a standard year, could be roughly estimated as shown in the Table 2.6.

The North Korean income increase owing to the inter-Korean economic cooperation is equal to "trade (commodities) balance + processing commission (CP revenue)," which constitute the parts of the North Korean GDP plus "the current transfer payments from the South to the North." The latter one (that includes humanitarian aids and foods grants from the South) does not belong to the concepts of either North's gross domestic products (GDP) or North's gross national income (GNI).

But the aids and grants (which are also de facto aids) constitute those items contributing to the increase in the North's gross disposable income (GNDI).

The net increase in North Korea's income in 2005 due to the inter-Korean economic cooperation was approximated to amount to US 194 million dollars (commodity trade: balance 168.0 million dollars plus processing commission revenue: 26.4 million dollars) in terms of the concepts of both nominal GDP and GNI. But it totaled US 559.4 million dollars in terms of the concept of GNDI (gross national disposable income) for North Korean people as a whole. This net effect of the inter-Korean economic cooperation (which was based on our very conservative approximation) on North Korean GNI and total exports (the sum of imports and

¹⁵In the total costs of the processed goods being re-imported into the South side, the cost of raw materials provided by the parent companies in the South, transportation costs, and processing costs are included. The costs of commission-based processing goods would vary depending upon both the kinds of goods and the companies involved. We consider the average cost to be about 50% of the total trade balance related to the CPT goods, for simplicity's sake, in this analysis.

Table 2.6 North Korea's trade balance earned from the inter-Korean economic cooperation in 2005. (unit: millions of US dollars)

Type	Exports	Imports	BOP Composition	Credits	Liabilities	Balance
Trade	99.4	320.1				
General	20.9	188.9	Trade balance	20.9	188.9	168.0
CPT	78.5	131.2	Commission			26.4
Aids & Grants	365.0	0	Current transfer	0	365.0	365.0
Humanitarian	241.0				241.0	
Food	124.0				124.0	
Grants						
Investments	251.1	20.1		20.0	251.1	
Light	0.4	—			0.4	
Water						
Mt.	87.0	0			87.0	
Keumgang						
Gaesung	156.9	19.8		19.8	156.9	
Other	6.8	0.2		0.2	6.8	
projects						
Total						559.4

Sources: The ministry of unification. This table is based on Lee Young-Hoon's *The status and evaluation of the Inter-Korean economic cooperation*, a working paper, Bank of Korea, 2007. p. 31 (in Korean)

exports) accounted for about 2.3% and 18.7%, respectively, in 2005. If we added other omitted cooperation items such as fertilizer aids, infrastructure facilities, electricity supplies, medicines, and various fees and tax payments, and so forth, its share of North Korean total trade rose from 13% in 1999, 26% in 2005 and most recently to 61.2% in 2007.¹⁶

In sum, the inter-Korean cooperation has seemingly helped the North to considerably fill its external trade gaps with China and other countries. It is estimated that North Korea has annually earned about US 180 million dollars from the inter-Korean economic cooperation. If other revenues from the visitors and relative remittances from the South were added, the figure would exceed more than US 200 million dollars annually since 1998. Since 1998 South Korea has literally contributed to sustaining the regime in the North regardless of the latter's constant bluff to consume it with "fire."

¹⁶Refer to both reports cited above on the inter-Korean trade and cooperation and *The Estimation of North Korean Economic Growth (Annual)* by the Bank of Korea (<http://www.bok.or.kr>) (in Korean). Also see KOTRA, *The Trends of North Korea Trade*. (<http://www.kotra.or.kr>).

2.7 New Policy Paradigm Under Lee Myung-Bak's Leadership?

National unification is the main hope of 70 million Korean people. The relationship between the South and the North must develop toward better productive ways more than ever before. I will solve our national division problem not by the measuring rod of ideology, but by the rule of pragmatism. Our goal lies in both helping the South and the North residents live happily and providing the common grounds for reunification. (President Lee Myung-Bak's Inauguration Address on February 25, 2008)

With the new government in the Blue House being backed by South Korean conservatives, many people are demanding fundamental shifts in the policy paradigm toward North Korea. The new President Lee announced that his administrations will pursue the roads of both *common survival and mutual prosperity* on the basis of pragmatism and productivity. In his remarks, he made it clear that his government would not recklessly pour money into the North unless the latter correspondingly responds to the benefits extended by the South. This did sound as if he fully recognized the need of reciprocity in every transaction between the two Koreas. The reciprocity could balance trade between the two Koreas, not necessarily in pecuniary two-ways but in the form of formidable give-and-take alternatives.

The new government in the South announced *its 2008 action plan comprising three main objectives with twelve supplementary tasks* that are considered necessary for achieving both "common survival and mutual prosperity."¹⁷ The new action plan intends to carry forward the inter-Korean economic cooperation in line with the North's response to reducing its nuclear projects. The four new principles propose that Lee's government will cooperate with the North step by step if, and only if, such preconditions as the North's denuclearization progress, economic feasibility, financial capability, and people's consensus regarding the inter-Korean economic cooperation are met.

As usual, the North bluntly ignored Lee's stance and began its criticism against his conservative approaches. In an interview with reporters in late March, the talkative President Lee said that his government would always leave the door open to talks with the North, revealing his somewhat laid-back position. To make matters worse in the South, the candlelight protests, namely against US beef imports, appear to be surreptitiously targeting the conservative pro-American regime. Amid anti-US

¹⁷The 2008 Action Plan has three objectives and twelve implementation tasks. The first objective targets to facilitate the North's denuclearization, which in turn consists of (a) achieving the North's nuclear dismantlement through the inter-Korean relation, and (b) inducing the North's denuclearization as well as its glasnost. The second objective aims to enlarge inter-cooperation with eyes on common survival, thus contributing to economic progress in the peninsula. Toward to this objective, it proposes (c) to reduce any barriers to the enterprises engaging in the cooperation, promoting (d) forestry area cooperation, (e) fishery area cooperation, and (f) resource area cooperation in addition to (g) the Na-deul island project. The third one aims to promote mutual welfare of people in both the South and the North. Toward this, (h) reunion of separate families, (i) POW's and kidnapping issues, (j) dissidents' settlement, (k) transparency of the distribution process of humanitarian aids, and (l) human rights in the North must be solved. (Source: Ministry of Unification, *The Status and The Directions of Policy toward North Korea*, 2008. 6.)

beef and anti-conservative street demonstrations continuing in June 2008, the Lee government appeared to bend to the liberal protestors whose core members appear suspiciously linked directly or indirectly to the Dear Leader in the North. As long as the liberal groups continue to harass the government, it will be hard to maintain Lee's initial policy direction. Unless the government strongly adheres to its policy in accordance with the laws and the principles whatever the cost, all action plans will fail. Lee Myung-Bak government appears to be trapped both by internal protests and by the North Korean leader's constant plot to sabotage all talks of reciprocity.

2.8 Closing Remarks on Reciprocity Principle

Ever since he has occupied the Blue House in early 2008, Lee Myung-Bak has offered to help the North improve its economy, education, infrastructure, finance, and living conditions within five years if the North shows that it will reduce its inordinate nuclear programs. He also presented his inter-Korean policies that would assist the North in raising its per capita income to US 3,000 dollars within ten years if the North begins its denuclearization processes. Lee's policy toward the North reflects the reciprocity principle so vividly different from the lopsided cooperation of the past regimes. For ten years, the *de facto* policy of the administrations of both Kim Dae-Jung and Roh Moo-Hyun has been to help the North communist leaders to increasingly do less for their striving populace despite increasing more aid. In our opinion, *DJ's Sunshine Policy* was a serious mistake – the product of wishful and unrealistic thinking. Generous aid will not help beggars change their begging mentality unless the aid is accompanied by the condition that the beggars promise to stand on their feet. Furthermore, the *Sunshine Policy* has South Koreans exposing themselves, while the North leaders are not giving anything in return. As a result of this policy, the North could rebuild its military strength while leaving many of its residents suffering under the shadow of economic shortage. Free aid could demoralize the spirit of the beneficiary unless he or she learns the lesson that *heaven helps those who help themselves*. The rock bottom economy and the total reluctance of the North Korean leadership to implement the most elementary and necessary *perestroika* and *glasnost* methods has resulted in its leaders looking for the easiest way to obtain aid *by warping and bluffing* the South.

The North's possession of nuclear weapons has made the rogue regime behave more aggressively in getting more support from the South. That is one of many reasons why the South must demand adherence to the reciprocity principle by the North. Installing reciprocity in the inter-Korean economic relation will not be cheap, but it is necessary. The benefits will outweigh the costs in the long run for both South Korea and North Korea.

As for the Lee Myung-Bak government's new approach, the North continues to respond negatively as of June 2008 when the candle lights have kept burning every night in Seoul. The North even turned down 50,000 tons of corn offered in June 2008 by the Lee government, although North Korea faces severe food shortages.

A recently obtained North Korean government document released by Good Friends, which is working to help hungry North Koreans, calls for a redoubling of the North's campaign to increase this (2008) year's crop production.¹⁸ This reveals that the country is in a severe state of food shortage.

Anyhow, Lee's earlier tough stance had infuriated the North, which considered it an insult to the Dear Leader Kim who had negotiated and signed previous deals. Lee soon to sense some kind of crisis ignited in the South by the resumption of US beef imports in late spring 2008. The beef fiasco appears to have made him reconsider, right or wrong, that he could not overcome the crisis by further isolating North Korea. In a reversal of his hard line stance toward North Korea, President Lee Myung-Bak offered to resume dialogue with the North during his first parliamentary presidential speech on July 11, 2008. The president stressed that his government was willing to engage in serious discussions with North Korea on how to implement the inter-Korean agreements made so far, including the 1991 Joint Declaration on the Denuclearization of the Korean Peninsula, the South–North Joint Declaration of June 15, 2000, and the October 4, 2007 summit declaration between the leaders of the two Koreas.¹⁹ Lee expressed his wish to engage in inter-Korean humanitarian cooperation. "From a humanitarian and fraternal standpoint, the South Korean government is ready to cooperate in efforts to help relieve the food shortage in the North as well as alleviate the pain felt by the North Korean people. Issues involving South Korean POWs, separated families and South Korean abductees should be resolved as well." "Inter-Korean relations should transcend changes in administrations and be pursued from a future-oriented perspective for all the Korean people," Lee told lawmakers.²⁰ There was no immediate reaction to Lee's speech by North Korea, which was considered a softening of his hard-line posture.²¹ Since his election, he had said he would "review" the inter-Korean agreements, which promised projects worth billions of dollars. He had during his election campaign ruled out expanding joint economic projects already under way, including the Gaesung industrial complex north of Seoul (another symbol of reconciliation pursued by his liberal predecessors). Lee's overture came amid a deepening chill in relations with the North Korea, even as he recognized the need for reciprocity in the inter-Korean relations.

The need for reciprocity in the inter-Korean relations cannot be over emphasized. The "reciprocity," that is, in other words, "cooperate if," is beneficial for

¹⁸The Korea Herald, p. 2, June 19, 2008.

¹⁹Lee Myung-Bak's liberal predecessor, Roh Moo-Hyun and North Korean leader Kim Jong-Il held the second inter-Korean summit in Pyongyang on October 2007 and signed a ten-point joint declaration calling for establishing permanent peace on the peninsula and significantly expanding the inter-Korean cooperation in politics, the economy, denuclearization and other issues.

²⁰Quoted from *Jong Ang* daily, July 12, 2008 (No. 2,372) p. 1. <http://joongangdaily.joins.com>.

²¹Earlier on July 7, 2008, Lee Myung-Bak said to reporters that he was willing to meet the North Korean leader any time in order to speed up the North's dismantling of its nuclear programs. North Korea rejected any possibility of summit talks with Lee, saying that "it is preposterous for Lee to suggest such a meeting." The North accused Lee of suggesting a summit with the North Korean leader in an attempt to "evade the responsibility for having bedeviled the inter-Korean relations."

both parties. Above all, “the cooperation if” principle will help improve each economic policy efficiently, providing both parties with “better understanding” about “economic functioning” of the other system. Learning about the policy efficiency of the other-side party is one of the important gains that could be earned through reciprocity deals. Likewise, “paying the price” is far more worthy in the long run than “free lunch” for the parties involved as they learn how to build their economy. The reciprocity deals will also allow both parties to complement one another on the basis of the comparative advantage of endowments in both software and hardware aspects. The reciprocity deals can also promote peaceful coexistence and strengthen the inter-Korean cooperation in both directions. Reciprocity is the starting point of a long-term joint effort toward inter-Korean cooperation as well as the building of mutual trust and common prosperity under a peaceful environment. Of course, an extremely isolated country like the DPRK must understand the long-term benefits from the reciprocal fair trade instead of beneficiary trade. Getting used to a new mode of mutual cooperation is something that requires a paradigm shift in the way that the leaders accept reality.

The reciprocity can function well not only when the two parties agree to follow “the give and take game” but also if each party can secure its internal consensus. Can any leader maintain his or her strong political stance if he or she lacks full supports from citizens?

The current ideological split among South Koreans is a staggering flaw that is dragging down the realistic reciprocity approach being pursued by Lee’s government. The South’s coalition groups bearing candle lights are demonstrating “against food,” namely, the beef imports from the United States²² The candlelight turmoil in the summer 2008 is apparently causing the Seoul government to back away from its initial “cooperate if” policy toward North Korea. With the current Lee Myung-Bak administration apparently bogging down and unready to face the opposing forces sternly, further conflict could arise inside the state. This would in turn cause the administration to be incapable of pursuing straightforward reciprocal deals with the North.

On the other side of the border, many hungry people are striving “for food.” A country with chronic food shortages is also not in a position to take a reciprocity stance at all. Pyongyang’s stubborn refusal to embrace Lee’s offer also seems to be driven by its distrust of the conservatives in the South.

²²On April 18, 2008, South Korean and US negotiators reached an agreement on the sanitary rules that Korea would apply to all beef (irrespective of age) imports from the United States. The rules were expected to take effect in mid-May when Korea published implementing regulations. However, continued strong Korean public opposition ignited via TV coverage of the issue and internet-spread rumors on US beef infected with mad cow disease, or BSE (bovine spongiform encephalopathy), has resulted in escalating protests. Behind the protests is the suspected influence from the North Korean leader or his followers in the South strongly suspected of plotting to undermine the standing of the South Korean President Lee and his conservative political party, which holds a slim majority in the South’s parliament.

The North's monolithic group of elites who share the same views, values, and visions must move away from their closed mindsets and try to understand the outside world if they want to go forward and overcome the vicious circle of economic and political stagnation.

The comparative situations illustrated above reflect the unsolved reality stifling the two Koreas as of mid-2008. While the Six Party (South Korea, North Korea, United States, China, Russia, and Japan) talks could barely persuade North Korea to abandon its nuclear arsenal, the United States announced that it would remove North Korea from its list of states that sponsor terrorism. Concurrently, President Lee Myung-Bak said that "full dialogue between the two Koreas must resume" in his speech at the newly convened National Assembly on July 11, 2008. But on his way to the National Assembly, the president was informed that a South Korean tourist was shot to death near the beach hotel of Mt. Keumgang by a North Korean soldier in the early morning of that very day. Seoul announced it would temporarily halt its tourism program as of July 12, 2008. The shot woman was one of some 1,500 tourists visiting the Mt. Keumgang area in the week of the accident. More than 1 million South Koreans have visited the mountainous area since 1989 until this accident. This shooting, whether intentional or not, would be a cloud over inter-Korean relations, at least temporarily.

On the other hand, so many liberals who were recently out protesting in the streets with candle lights and loud voices against Lee's policy of resuming US beef imports remained "strangely quiet" about the shooting of an innocent tourist by a North Korean soldier, not to mention their continuing silence about human rights suppression in the North.

The future win-win outcome in inter-Korean relations will not only depend on the removal of military, political, economic, and ideological barriers on the basis of a reciprocal framework between the two Koreas, but also on overcoming the crashes and divergences between conservatives and liberals in South Korea.

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