

# Press Release

*The National Economic Advisory Council, the Korea Institute for International Economic Policy and the US-Korea Institute at SAIS(at Johns Hopkins) present:*

## ***Inter-Korean Economic Cooperation to Prepare for an Era of Unification***

The National Economic Advisory Council (NEAC), jointly with the Johns Hopkins SAIS<sup>1</sup>, the Korea Institute for International Economic Policy (KIEP) and the Korea Development Institute, will hold a seminar on 「Inter-Korean Economic Cooperation to Prepare for an Era of Unification」 on Thursday, May 8th, at SAIS located in Washington D.C.

This seminar invited experts from Korea and the United States to discuss the realization plans on the ‘Dresden Declaration’ announced last March as the direction of the ‘Preparation for an Era of Unification,’ the core task of the 「Three-year Plan for Economic Innovation」.

This seminar changes the focus on the unification and the inter-Korean economic cooperation from ‘costs and burdens’ to ‘advantages and benefits’ by highlighting the expected effects of economic cooperation, development strategy, and costs and benefits of the unification.

Beyond financing and cooperation issues between South and North Korea, the importance of active involvement and participation methods of the international society will also be discussed in depth.

Furthermore, the precedence of market economy transition and implications from the unification of Germany will be comprehensively examined to gather various opinions on future directions of the inter-Korean economic cooperation and priority settings.

With variety of topics covered from different angles, this seminar is expected to facilitate further vibrant discussion to give shape and content to the new perspectives on the inter-Korean economic cooperation and the unification given by the Dresden Declaration.

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<sup>1</sup> Established in 1943 as a division of the Johns Hopkins University, SAIS (Paul H. Nitze School of Advanced International Studies) SAIS(Paul H. Nitze School of Advanced International Studies) had been established in 1943 as a division of the Johns Hopkins University, SAIS is a global institution that offers international perspectives in issues such as international economics, international law, and area studies.

## **1. North Korea's RCA and its Implications for Inter-Korean Economic Cooperation**

- Deok Ryong Yoon (KIEP)

Based on RCA<sup>2</sup>, which measures a particular export's comparative advantage in the total export market, North Korea's trade competitiveness reflects changes in the industrial structure. Currently, North Korea's foreign trade is highly dependent on specific items such as export of processed mineral resources to China, and the tendency is strengthening.

In 2010, North Korea's foreign trade scale recovered the level prior to its collapse in 1990 and is continuing to increase, thereby showing the "J-curve" that is witnessed in countries going through system transformation. Even with the increase in foreign trade, North Korea failed to show economic recovery or stable growth because of its trade structure where revenue from export of natural resources is used to import daily necessities. Increase in trade with China is mostly from export of resources, which in turn delays industrial restructuring and limits sustainability of North Korea. North Korea's import of light industry goods from China is increasing because China has comparative advantage in the field, and such tendency has negative effect on development of manufacturing sectors in North Korea.

The most practical way for North Korea to maintain sustainable growth is through vitalization and expansion of the inter-Korean economic cooperation that can strengthen North Korea's economic fundamentals. RCA in the inter-Korean trade shows South Korea is already influencing industrial restructuring in North Korea, even if the effect is limited to areas such as Gaeseong Industrial Complex. Therefore, the economic cooperation needs to be expanded along with improvements in political relations.

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<sup>2</sup> Revealed Comparative Advantage (RCA): Calculated by dividing the proportion that a particular export makes up the entire exports within a country by such ratio of the world's export market, where RCA over 1 indicates comparative advantage.

## **2. Current State of North Korea's Economy: Implication for Inter-Korean Cooperation**

- Jong Kyu Lee (KDI)

Economic cooperation with South Korea is necessary for North Korea to complement its channel of securing hard currency that is vulnerable to external shock. Despite the effort from the authorities, North Korea's trade dependency on China and the weight of export on coal and iron have increased, so economic impact is expected in case of external shock (e.g., decrease in demand for North Korean products, or 4<sup>th</sup> nuclear test). Recently, labor dispatch to China has rapidly increased, so there is increased political pressure in regard to the growth of demand for reform and market opening. As North Korean authorities effectively absorbed dollars held by North Korean people, downsizing of planned section is also becoming a political burden. In addition, promotion of 13 economic development zones and 1 special economic zone increased the uncertainty of the authorities' own accord that led to repeated failures.

Strategic economic cooperation to resolve income, labor, and capital differences between South and North Korea is required for sustainable cooperation independent from political conditions. Enhancement of quantity and quality of labour through diverse measures such as regular census of population through international society and reeducation of labour through Gaeseong Industrial Complex is necessary. South Korea should support infrastructure development in the special economic zone. Furthermore, South Korea should promote China to strengthen its cooperation with North Korea to expand trade market, and provide support through the Inter-Korean Cooperation Fund and Korean ODA to internationalize North Korean market.

Lastly, it is necessary to recognize and narrow the difference in the interests of South Korea (labor) and North Korea (capital) on the economic cooperation. Cooperation should be initiated in practicable area (labor) based on the current condition of North Korea and the restrictions in South-North relations. In addition, enhancing the quality of labor should generate consensus within South Korea as a policy on humanitarian assistance, and it should be perceived to the North Korean authorities as a cornerstone for economic development.

### 3. Preparation for the Unification Bonanza

- Chong-Bum An (National Assembly)

Since the unification not only requires costs but also accompanies tangible and intangible benefits, the unification bonanza is practicable by minimizing the costs and maximizing the benefits. Previous studies focused on the cost-side of the issue and thereby gave impression to people that the unification will be a burden on them. Macroscopic cost estimation methods yield different results depending on assumptions, making it impossible to draw policy implications necessary to prepare for the unification.

Detailed schemes for minimizing the costs and procuring various resources need to be drawn by estimating the unification costs separately item by item in order to gain policy implications for each system (microscopic estimation). Sustainable system should be established given consideration to the tax burden reflecting the unification and the aging phenomenon. Social safety networks should be changed from cash-based benefits to service-based benefits to reduce financial burden and maximize social adjustment effects of the recipients. To secure financial resources, participation of private fund should be promoted by guaranteeing profitability on projects such as construction of infrastructure<sup>3</sup> that are expected to produce social benefits. In addition, for efficient procurement of the financial resources, developing and utilizing the unification finance resources procurability index is suggested.

Unification Preparation Committee should serve as the control tower, and to do so, contingency plans must be established for each government department. Research activities in diverse fields should be supported and databases on the unification and North Korea should be constructed.

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<sup>3</sup> Establishment and utilization of Project Finance (PF) and Korean Investment Bank (KIB; a tentative name) can be considered as a mean to attract private financial resources

#### **4. Korea Reunification: Implications of the Unified Germany on the Reunification of Korea**

- Sukgeun Lee (Roland Berger)

Roland Berger was actively involved in THA (Treuhandanstalt), which privatized and restructured the majority of East Germany's corporations for 4 years after the unification in 1990.

Based on the experience, complying with the precedence of the unified Germany, this study explains a thorough analysis on systems and managing protocols of THA that categorized and restructured corporations to create synergy effects.

This study refers to the following 5-point plans that invigorated Germany's economy to draw implications for the unified Korea: expansion of free economy, boost of innovation clusters, future-oriented economic structure, flexible labor market, and continuous investment in infrastructure.

Based on the unification scenarios, this study forecasts the potential synergy effects from the integrated infrastructure in industry, corporations, natural resources, population, and logistics, and the enhanced sovereign credit rating resulted from decreased country risk.

In addition, this study emphasizes the need to initiate preparation for the unification at the federal, local, industry, and corporation levels, as well as the importance of establishing cross-national systems through planning and revising the preparation measures

## **5. What Can North Korea Learn from Transition Economies' Reform Process**

- Hyung-Gon Jeong (KIEP)

This study analyzes the determinants of economic growth in countries that adopted market economy in 1990s and draws implications for North Korea.

A radical reform is not expected in North Korea due to ingrained socialistic economic initial conditions, which influence economic growth during the system transformation process. Non-economical initial conditions such as single-power system, economic sanction from international society regarding nuclear issue, and conflict with neighboring states also hinder radical economic reform in North Korea. Without a major political shift, gradual reform is likely for North Korea considering the current political situation and economic initial condition.

However, the situation can be shifted if North Korea renounces nuclear development and promotes the reform and open market. While Eastern European nations experienced economic shock during the transformation process due to the high degree of interdependence among the socialist states prior to the transformation, such risk is not applicable to North Korea. In addition, active support and investment from neighboring states including South Korea and the international society, as well as the world's largest market surrounding North Korea, are favorable conditions for North Korea to achieve rapid economic growth.

Currently, it is necessary for North Korea to build advantageous initial condition for the reform and market opening, and it is especially significant to increase external openness of economy. While applying complete opening of market to recently appointed economic development zones and strategic economic zones, such as Gaeseong, Naseon, and Sinuiju, promoting gradual reform by developing industry related to the special zones is desirable for other areas.