

## **ECONOMIC CRISIS & INTER-KOREAN RELATIONS: POSITIVE AND NEGATIVE IMPACTS**

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A financial crisis has spread from the shores of the United States, impacting economies around the globe. South Korea has been no exception. In an instant, markets froze, unemployment skyrocketed, and economies continue to worsen. Despite being rated fundamentally sound, the South Korean economy cannot shake fears and uncertainty. Even with the government's display of confidence, the Won's exchange rate and the stock market are still shuddering. The economy's decline has led to witting investment and dull domestic demand for goods.

With the overall economic crisis, the South Korean government is turning its focus away from inter-Korean relations. During his election campaign, Lee Myung-bak projected himself as the 'economic President', promising economic growth and pragmatism. Following his win, as Lee's administration has to face serious financial crises, the government has prioritized economic recovery. As the South Korean economy continues to worsen due to the global financial instability, relations between Seoul and Pyongyang are being pushed to the back burner, so that ultimately, the main impact the global financial crisis has had on inter-Korean relations was to steal their limelight.

On top of this, with the focus now on economic concerns, if North Korea continues to ramp up its hard-line measures, it will serve only to make it more difficult for the South Korean government to shift its focus back to inter-Korean relations. The launch of the Lee government meant the first change of political power in ten years, as the South's conservative Grand National Party took the helm and reversed the direction of many policies.

This equated to the new government's failure to observe previous administrations' policies toward, and agreements with, North Korea, and this, combined with the last year of rhetoric and bickering from both sides of the DMZ has led to worsening, and now virtually frozen, inter-Korean relations. Now, there is a good chance the global financial crisis will serve to make it even more difficult to reopen dialog and improve ties between North and South Korea.

President Lee Myung-bak's approach to issues -- that the government must avoid hasty decisions -- appears to apply to today's situation, as well. With an economic crisis underway, the Lee administration appears to

prefer a deliberate, proper approach to North Korea, and is prepared to wait until it is comfortable with its plan. With North Korea policy already sidelined, mutual tensions and the North's growing hard-line response mean that it is increasingly difficult to see the Lee administration focus on advancing inter-Korean ties. As its domestic economic woes continue to grow, North Korea's hard-line approach to the South not only furthers disinterest in government circles for inter-Korean relations, but also serves to boost antipathy for improved relations among the general public.

The economic crisis is also likely to cause South Korean donor fatigue regarding aid to the North. With South Koreans facing increased economic burdens, it is difficult to maintain previous levels of enthusiasm and activity regarding humanitarian aid for North Koreans. The same is true for inter-Korean economic cooperation projects, as the massive investment necessary is difficult to raise in today's economy.

Previously, aid and economic cooperation served as the string that held together efforts to maintain inter-Korean trust and dialog. Therefore, as today's global financial woes serve to weaken the South Korean economy, these same woes serve to weaken inter-Korean relations, as the burden to the South Korean public ultimately undermines the basis for trust between Seoul and Pyongyang.

South Korea's economic crisis also has the potential to create difficulties for the inter-Korean Kaesong Industrial Complex (KIC). As the economy falters, exports and investment wither, as does South Korean domestic consumption. Companies invested in the complex, mostly small- and med-sized industries, have been unable to avoid the impact of the contracting economy.

Furthermore, as worsening inter-Korean relations led to restrictions on travel to and from the KIC and across the military demarcation line dividing the two Koreas, these measures will limit further development of the complex. Despite initial efforts by both governments to foster this complex as the representative inter-Korean cooperative project, these latest developments may well spell its demise.

On the other hand, however, the current economic crisis could also have a positive influence on long-term inter-Korean relations. With today's economic difficulties, there has been no option other than to let attention to inter-Korean relations, aid, and economic cooperation wither. That said, looking at the long-term picture, a strategic approach to overcoming economic instability could also play a positive role in helping to improve inter-Korean relations and creating economic opportunities. Abandoning inter-Korean relations is not a strategy for overcoming South Korea's economic difficulties and fostering future economic growth; it will take both Koreas working together.

A strategy of engaging the North economically could improve reconciliation and cooperation between the two Koreas, developing into an peninsular economic community through which the Koreas could finally move

past being the remaining 'island' of Cold War tensions and connect with the rest of the continent. This could allow the Korean Peninsula to serve as a 'bridge', giving a whole new role to inter-Korean relations as a springboard for the South Korean economy.

By linking the Trans-Korean and Trans-Siberian railways, the Korean Peninsula would serve as the link between Europe and Asia, and as such, a Korean peninsular economic bloc could take its place in the global economy. In addition, as inter-Korean economic cooperation grows, both the North's and South's production factors could efficiently combine, creating yet another breakthrough for the South's economy. If a new Korean peninsular economic community formed, combining North Korea's abundant underground resources and labor force, combined with South Korea's leading-edge technology and capital, it would provide fertile conditions for joint prosperity of both North and South Korea.

Incentive for such a large-scale economic cooperative project can be found not only in that it would further inter-Korean relations and the formation of a Korean peninsular economic community, but that it would serve to help overcome the current economic crisis as well. Joint shipping and joint use of the Han River estuary, as well as refurbishment of the North's railways and rail linkages between North and South can also provide profits for the South's industries.

In particular, if the current economic crisis requires government-led projects requiring an injection of large-scale public finances, it would be worth looking into infrastructure-development projects in the North as alternatives to projects in the South, such as the Grand Canal project, which faced considerable public opposition. Seoul may find the economic breakthrough it is looking for not in special interest group- or industry-driven projects, but North Korean infrastructure projects for which public support has already been shown.

Another issue hampering South Korean economic recovery is the so-called "Korea discount," brought on by inter-Korean tensions that increase security concerns on the peninsula. Seoul must avoid allowing the economic crisis and worsened inter-Korean relations to combine to further threaten overseas confidence in the South's economy. Therefore, in consideration for the South's economy, the Lee Myung-bak administration should work to salvage inter-Korean relations. The current economic situation is having a negative impact on inter-Korean ties, but on the other side of the coin, it is necessary to revive relations between Seoul and Pyongyang in order to overcome today's economic woes.

The global economic crisis has impacted China, as well, driving up the prices on raw materials, and there is a significant chance this could cause North Korea's trade deficit to skyrocket.<sup>1</sup> In the long-term, this could lead North Korea to become desperate for South Korean economic assistance and cooperation.

As the economy worsens, so, too, do inter-Korean relations, driving ties between China and North Korea to become relatively stronger. However, this is also leading to an increasing dependence on China, and as the North's trade deficit worsens, economic assistance through improved ties with South Korea becomes more strategically valuable to Pyongyang. In this way, another long-term implication of the current economic crisis is that it provides the North with incentive to improve inter-Korean relations, as well.

Ultimately, it appears that while the current economic crisis is initially having a negative impact on inter-Korean relations, in the long term, it could also provide the impetus for a breakthrough in ties between Seoul and Pyongyang. Just from an economic perspective, with North Korea's need to create an economically 'Strong and Prosperous Nation', its loss of South Korean aid and cooperation due to worsening ties with Seoul, and its growing economic dependence on China, Pyongyang needs to repair inter-Korean relations.

It would also serve South Korea's best interests to improve relations, reducing the sense of economic instability due to inter-Korean tensions and gaining the long-term economic benefits of economic cooperation. The problem is that the recent political bickering between the two Koreas is preventing movement on these economic goals. Both North and South need to set aside these political factors, and advance pragmatic inter-Korean economic relations.

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<sup>1</sup> In 2008, North Korea's overall trade with China grew 41.2% over the previous year, to 2.78 billion USD. Of this, exports to China accounted for a mere 750 million USD, while imports amounted to 2.03 billion USD, as North Korea's economic dependence on China continues to grow.