

FUTURE OF INTER-KOREAN ECONOMIC COOPERATION

Soon-jik Hong & K. Audrey Lee

(sjhong@hri.co.kr, audreykl@hri.co.kr)

Inter-Korean Relationship in 1999

Although not much clear progress was marked in the field of political cooperation between the two Koreas, economic cooperation at the private level reaped significant results in 1999. In a nutshell, a new era began for economic cooperation between South and North Korea. Trade and investment activities regained the pre-crisis level, showing the best performance ever. In line with the reviving

South Korean economy, the Mt. Kumgang tour business expanded both quantitatively and qualitatively.

As of the end of October 1999, non-transaction economic activities have increased by 60.7% year-over-year, enabled by the Mt. Kumgang tour business, import of crude oil into North Korea by the KEDO and advancement of the light-water reactor project. Trade of production on commission, such as textile, machinery and transportation equipment, rose by 38.3%, and is expected to rise beyond \$100 million.

Table 1. Obstacles of Inter-Korean Economic Cooperation

Obstacles	Specific obstacles
High logistics cost (31.5%)	- Transportation cost (68.3%) - Shipping & loading cost (10.0%) - Demurrage (14.6%) - Wharfage (3.6%)
Non-economic uncertainties (24.3%)	- Insufficient official channel between South and North (53.3%) - Uncertainty of engagement policy (21.0%) - Economic instability of North Korea (17.1%)
Insufficient information on North Korea (21.6%)	- Lack of information center (44.4%) - Insufficient interaction between government and businesses (25.0%) - Insufficient government information (21.3%)
Shortage of SOC in North Korea (10.8%)	- Poor communication network infrastructure (49.1%) - Outmoded transportation system (20.8%) - Obsolete harbor facilities (15.1%) - Power supply shortage (12.3%)
Poor legal & institutional mechanism (9.0%)	- Absence of dispute settlement measures (32.1%) - Difficulties in permanent residence of technicians (25.7%) - Weak protection of investment losses (20.2%) - Licensing and authorization (14.7%) - Insufficient support for Fund (6.4%)

Prospects of the Year 2000

All in all, North Korea is expected to show a more cooperative, although still limited, attitude toward South Korea from this year. It is understood that the North Korean economy has bottomed out,

It is desirable that the government honors the independent efforts of the private sector and supports the latter's efforts, in addition consistently maintaining the principle of separating economic issues from political problems.

owing to outside aids and increase in provisions. From the year 2000, North Korea is likely to be more compromising than it has been until now, bearing in mind the economic profit out of business with the South, most

markedly the Mt. Kumgang tour business.

Provided that South Korea's principle of separating political issues with the economic ones goes hand in hand with North Korea's pragmatic attitude which is conducive to economic cooperation, inter-Korean economic cooperation is expected to further expand. In particular, the removal of US economic sanctions on North Korea and the more diversified Mt. Kumgang tour business are projected to create a rapid growth momentum for economic activities between the two Koreas. Also, foreign companies are expected to make indirect investment through businesses owned by South Koreans or overseas Koreans to disperse risk.

Production on commission is going to speed up increasingly with transfer of production facilities by both large and small businesses to the North. If construction of industrial complexes along the west coast and in Tongchun area takes off, it would boost inter-Korean trade tremendously. Trade centering on production on commission is expected to become more active, spurred on by increased government support for the South-North Cooperation Fund and possible market access of North Korean products to the US market with the removal of economic sanctions.

In addition to the comprehensive Mt. Kumgang development project and the light-water reactor construction, formation of joint businesses with foreign firms, especially those owned by overseas Koreans, is going to accelerate. Overseas Korean entrepreneurs and employees from Korean companies stationed abroad are being contacted to participate in investor relations meetings hosted by North Korea.

Many stumbling blocks remain in the road to economic cooperation. The biggest hurdle is high logistics cost. Non-economic factors of instability surrounding the business environment, insufficient information on business in North Korea and North Korea's poor SOC (Social overhead capital) among others are reported to be imminent obstacles.

Suggestions to improve efficiency of active economic cooperation include job-sharing between public and private sectors. It is desirable that the government honors the independent efforts of the private sector and supports the latter's efforts, in addition consistently maintaining the principle of separating economic issues from political problems.

What the government can do is create a legal and institutional mechanism for economic cooperation and eliminate obstacles to economic cooperation. It should run the South-North Cooperation Fund shrewdly and flexibly, especially to raise the level of industry infrastructure of North Korea. To avoid massive problems in the future, effective measures to protect investors and settle disputes between the two sides should be sought at the government level in the long run.

Finally, the private sector should make rational business decisions which aim not at short-term "quick returns" but at long-term profit. By building mutual confidence and forming economic partnership, North Korea may have higher purchasing power. Also, instead of excessive competition, Korean companies may enjoy lucrative results by making joint decisions and industry-specific business plans collectively. They would be better able to avoid business failures by making detailed preparations and verifying business feasibility. **VIP**