

Preparing for Korea's Reunification

LIM, WON-HYUK

Korea Military Academy

I. Introduction

Although the democratic revolution of 1989 in Eastern Europe was closely watched all around the world, it left a particularly strong impression on the people of the Republic of Korea (ROK, or South Korea). After watching Germans hammer away at the Berlin Wall on November 9, 1989, South Koreans came to believe that Korea's own reunification *had to be* just around the corner-- given the collapse of communism worldwide and increasing economic troubles under the oppressive regime of the Democratic People's Republic of Korea (DPRK, or North Korea). When Rumania's Nicolae Ceaucescu, who had sometimes been compared to North Korea's Kim Il Sung, was put to death by angry demonstrators, South Koreans became even more confident that unification would come in the near future-- be it through transformation or collapse of the communist system in North Korea.

For the next three years, the unification policy of the South Korean government reflected this general confidence. Establishing diplomatic relations with North Korea's traditional allies, Seoul applied pressure on Pyongyang to engage actively in inter-Korean talks. Worried about the viability of the regime in the aftermath of the collapse of the Communist Bloc, Pyongyang complied. A series of high-level inter-Korean talks then led to the signing of the Basic Agreement and Joint Declaration on the Denuclearization of the Korean Peninsula in December 1991. These dramatic developments encouraged hopeful talk that the South and the North might even be able to form a commonwealth by 1995, fiftieth anniversary of Korea's liberation from Japanese colonial occupation.

It would not be unfair to say, however, that these high hopes vanished almost without a trace in less than three years. The politically motivated posturing prior to the presidential election of 1992 in South Korea, the death of Kim Il Sung and ensuing

controversy over the sending of condolence missions, and the nuclear brinkmanship of North Korea all contributed to the souring of inter-Korean relations. Moreover, Germany's economic troubles after unification led some South Koreans to question not only the feasibility, but also the very desirability of unification. Some of them even ask why the South should make sacrifices for the North just to have a unified nation.

Now that the "unification fever" of 1989 has all but evaporated and disillusionment has begun to set in, what seems to be needed to restart the unification process is a forward-looking yet realistic framework for Korean reunification. Certainly, Seoul and Pyongyang each has its own unification plan, but these multi-stage schemes tend to focus on procedural matters, and, on the whole, fail to provide the Korean people with a rationale for unification and a vision for the future. Most unification plans put forward by non-government bodies and individuals are also equally unclear on the shape of the unified political and economic system that they intend to create.

The purpose of this paper is to provide a convincing historical rationale for unification and a hopeful vision for the future of Unified Korea, and to outline the process through which unification may be achieved in accordance with this vision. As conventional discussions on Korean reunification have tended to focus on political and military issues and overlook the economic dimensions of the problem, this paper will attempt to highlight economic agenda for unification.

This paper is organized as follows. After a brief introduction, Chapter 2 critically examines the optimistic and pessimistic extremes of conventional views on unification and proposes an alternative based on the twin principles of self-determination and decentralization. From a historical perspective, this chapter briefly reviews the trials and tribulations that the Korean people have had to suffer through over the past century, and argues that the building of an independent democratic nation-state is the historical mission of the current generation. Pointing out that the threat of another fratricidal war and violation of human rights will never completely disappear without unification, this chapter concludes that the historical significance of Korean reunification must be sought in the securing of national independence and genuine democracy.

Chapter 3 examines economic agenda for unification within this basic framework founded on the principle of self-determination and decentralization. Reviewing the experience of the former Communist Bloc countries and other developing countries, this chapter argues that a social market economy-- "capitalism with a human face"-- is best suited to provide the material basis for a strong independent nation and vibrant democracy. In order to establish such an economy, it is argued that South and North Korea must solve the much-intertwined problems of (1) system transformation (in particular, price liberalization and assignment of property rights), (2) economic integration (creation of a single currency and labor market), and (3) economic

development (provision of public goods, both of material and institutional nature).

Chapter 4 suggests that only through unification can Korea complete its transformation from a target for colonial powers to a strong, independent democratic nation in the Northeast Asian region. Pointing out that the true significance of unification must be sought in the qualitative improvement in the people's lives rather than in the creation of a bigger nation, this paper concludes by once again emphasizing that self-determination and decentralization should be the guiding principle for Korean reunification.

II. A New Framework for Korean Reunification

1 Contrasting Views on Unification

Based on the vision offered of Unified Korea, conventional views on unification range from unbound optimism to bottomless pessimism, from those promoting unification for the sake of unification to those inciting fear of unification. A critical examination of these two extremes would go a long way toward clarifying some of the most commonly held misconceptions about Korean reunification.

The most optimistic, and perhaps nationalistic, of conventional views on unification is "unification first-ism," or what may be termed the doctrine of "unification for unification's sake." Starting from the premise that nation takes precedence over political system and ideology, this doctrine stresses the self-evident nature of Korean reunification and places an overriding emphasis on national unity: the Korean people in the South and the North share a common ethnic and cultural heritage, and it is only natural that they form a single nation-state. Overlooking ideological differences that clearly do exist between the two sides, this doctrine claims that many of the problems in South and North Korea will be resolved through unification.

There is little doubt that improvement in the South-North relations will require both governments to adopt a fundamentally nationalistic outlook, concerned more with the future of the Korean people as a whole than with short-term political gains. The intensely nationalistic doctrine of "unification first-ism," however, fails to define the political and economic system of Unified Korea and to outline a concrete process through which unification may be achieved. Its blind faith in the bright future of Unified Korea is, therefore, without adequate justification.

In fact, the recent experience of Yemen suggests that without a solid consensus on the shape of the unified system, the principle of national unity alone cannot provide a stable basis for unification. Although the government leaders of South and North Yemen were able to agree to national unification in May 1990, they failed to secure

international support for unification and provide the people with a vision for the future. In particular, the leaders of Unified Yemen were unable to control reactionary forces represented by northern tribal groups, and establish an economic foundation for independence from neighboring Saudi Arabia, who feared the influx of republican ideas from Yemen. After staggering along without a national consensus on the unified system and without economic support from its neighbors, Yemen fell apart at the seams again in less than four years. [Kukshin Kim(1993); Yu(1994)]

In contrast to Yemen's case, Germany was able to secure a solid foundation for unification by pursuing a well-defined unification principle and removing those elements that were potentially opposed to this principle. In the case of the military, where the potential for confrontation and internal conflict was the highest, Germany removed all anti-democratic elements associated with the former East German People's Army, dismissing all political officers and senior officers from colonel up. Only 10,000 professionals from the once 170,000- strong People's Army were retained, and they were in effect forced to be reborn as citizens-in-uniform according to the West German doctrine of *innere Führung* (inner leadership). Giving priority to internalized democratic values over external orders from superiors, inner leadership encourages members of the armed forces to refuse orders that might infringe the law or basic human rights. It thus demands from soldiers individual responsibility for their actions, and helps to prevent them from committing and later justifying atrocities on the ground that they were "just following orders." In short, Germany was able to complete its military integration by thoroughly blowing away the anti-democratic and militaristic elements of the People's Army and crafting a new Army of Unity according to the unifying principle of inner leadership. [Schonbohm(1994)]

What would have happened if Germany had used "national unity" as the sole guiding principle for military integration and completely overlooked ideological dimensions? In the Yosu-Sunchon Rebellion of 1948, the modern history of Korea offers all too vivid an example of such naively conceived integration and its catastrophic consequences. Although the leftist rebel leader Ji Chang Su only had the rank of master sergeant, he was able to assemble more than a thousand troops outside the chain of command, and pose a direct threat to the South Korean government at the time. The co-existence of ideologically incompatible groups within the Army under the principle of freedom of political expression had led to this armed rebellion. Similarly, if both South and North Korea fail to co-evolve toward a single unified system, the principle of national unity alone will not hold the nation together. The well-meaning yet naive nationalistic sentiment that runs through "unification first-ism" will not provide a stable basis for Korean reunification.

While "unification first-ism" is usually associated with peaceful, and somewhat naive,

proposals advanced by progressive nationalists, its characteristic emphasis on national unity can also be found in the so-called "unification-by-absorption" scheme-- albeit in a severely distorted form. Almost as anxious as progressive nationalists for Korean reunification, aggressive proponents of this scheme suggest that economic and military sanctions be imposed on North Korea to accelerate the collapse of its system and hence achieve national unification by absorption *a la* Germany. Although this scheme may at first sound realistic given the difficulty of achieving unification by agreement, it is really an irresponsible and dangerous plan based on a misreading of the Korean situation.

Traditionally, the North Korean regime has persuaded its populace to blame their economic troubles on external threats from the United States and South Korea. Under this circumstance, the most effective strategy that the South can take, then, is to stop acting like a potential adversary and start undermining the logic of the North's blame game, leaving Pyongyang with little choice but to pursue serious reform to address its economic ills. A hardline stance against the North, in contrast, will not only aggravate the siege mentality of North Koreans and strengthen their internal cohesiveness, but will also increase the risk of a second Korean War. Although it is certainly desirable to make preparations in case that the North Korean regime is toppled by an internal rebellion, the policy of risking a full-scale war to pursue national unification may amount to little more than an invitation to mutual destruction.

Moreover, even if war can be avoided, there is no guarantee that the *collapse* of North Korea's system will lead to the *absorption* of the North by the South. In this regard, South Korea's own experience in the early 1960s provides valuable lessons. The toppling of Syngman Rhee's dictatorial regime in 1960 by students only led to the establishment of a new, democratic system, not unification by absorption. Although the South's per-capita GNP was estimated to be only around half the North's level at that time, South Koreans did not choose to be absorbed by the North. And, when some progressive political groups began proposing radical unification schemes amidst the turmoil of the new democratic republic, the South Korean Army stepped in, and made anti-communism the guiding principle of the new military regime.

Applied to the North Korean situation, this experience implies that at least the following two conditions must be satisfied if unification-by-absorption is to succeed: (1) the North Korean people must so much envy, and expect generosity from, their Southern counterparts that they want to be absorbed by the South instead of reforming their own system; (2) those who have the most to lose by absorption (e.g., military) must be contained. Neither the active policy of strangling the North nor the passive, wait-and-see variety of unification-by-absorption policy, however, satisfies these

conditions. Few North Koreans will come to expect generosity from the South when all that they have evidenced is active hostility or aloofness from their so-called brethren. Moreover, without frequent contacts with their Southern counterparts in the first place, the North Korean people simply have little of knowing about the superiority of the South's system. In short, as serious as they are about achieving national unification, proponents of collapse-and-absorption policy seem to take little account of the psyche of the North Korean people.

While proponents of "unification first-ism" and "unification-by-absorption" schemes emphasize the principle of national unity and share a largely unexamined optimism in the future of Unified Korea, those supporting the status quo put economic calculations before nationalistic sentiments and express doubt about the desirability of unification. Of course, the fear of unification expressed by some conservatives in the South cannot be compared to that of the North Korean leadership, but both kinds of "unification-phobia" share the characteristic that they represent the establishment's resistance to change.

"Unification-phobia" on both sides, however, suffer from serious logical fallacies. In the North Korean case, although political and economic reform will certainly mark the end of the current system, the collapse of this system does not have to mean the fall of the current leadership from power and ensuing unification-by-absorption. As in Rumania, Vietnam, and China, the reformist faction within the existing communist leadership could lead system transformation and re-invent the communist party.

In the South Korean case, although it may be desirable to make realistic cost estimates for unification, it is unreasonable to presume that the South would have to take up all these costs alone. If the South is willing to provide assistance for the North's economic reform, it will not be difficult for North Korea to secure funds in this era of global capital mobility. In this regard, it must be kept in mind that South Korea, one of the world's poorest countries with bleak economic prospects in the early 1960s, was able to secure foreign loans in the initial phase of its own economic development.

Perhaps more to the point, much of the large "unification costs" feared by unification-phobes represents a long-term investment in the future rather than one-time cost that cannot be recovered. If the South shuns economic contact with the North for fear of getting sucked into the North's economic quagmire, it may actually end up losing valuable investment opportunities to foreigners.

Finally, it must be added that unification-phobes do not seem to know what they intend to do should the North Korean regime actually collapse. Their position, in fact, seems to be based on a fundamentally false premise that the South can reduce unification costs by continuing to ignore the North's economic troubles; however, if the

South waits until the North collapses, the eventual unification bill will have become larger, not smaller. Indeed, the economic calculations of unification-phobes are questionable on economic grounds alone.

As an alternative to the extremes of "unification first-ism" and "unification-phobia," what may be termed "a comparative-advantage scheme of unification" has been advanced by some economists and businessmen in South Korea. Its proponents claim that the South's capital and the North's labor can be combined to the benefit of both, and add that this should be an essential element in the economic integration of Korea. While economically sound on the whole, this scheme, in a negative sense, is a stop-gap measure intended to arrest the decline of labor-intensive industries in the South. Instead of continuing to rely on low wages for competitive advantage, South Korean firms must directly confront the economic challenges and invest in R&D on a long-term basis. Moreover, the comparative-advantage scheme of unification lacks a deeper historical perspective which can guide the South and North toward unification; to define Korean reunification merely as a kind of mutually beneficial economic integration is to ignore the larger historical context of this watershed event.

2 Twin Principles of Self-Determination and Decentralization

In discussing the future of Unified Korea, conventional views have tended to take the South and the North as basic building blocks and have attempted to envision how the union of these two halves will affect Korea's stature in the international community. In other words, their basic unit of analysis has been the state rather than individual citizens that make up the state.

The true significance of Korean reunification, however, must be sought in the qualitative improvement in the lives of these individual citizens rather than in the expansion of the nation. As high economic growth rates and the statistically impressive gains in "national power" from the 1970s to the mid-1980s failed to remove the pervasive sense of gloom that South Koreans suffered under the oppressive regimes, unification without concomitant improvement in human rights and welfare may lead to disillusionment.

Over the past two centuries, the Korean people have suffered through many trials and tribulations and endeavored to build a strong, independent democratic nation. Although democratically-minded Pragmatic Studies (*Shilhak*) blossomed during the Korean renaissance of the 18th century, the ruling Yi Dynasty failed to accommodate the reformist proposals advanced by pragmatic scholars and began to lag behind other countries in the drive toward modernization. Wasting away the 19th century in bitter factional strife, the Yi Dynasty turned increasingly reactionary and went so far as to

invite foreign troops to put down a peasant revolution in 1894. By the time the Yi Dynasty lost national sovereignty and Korea became a colony of Japan in 1910, it had basically given up all its claims to legitimacy. Building a modern democratic nation based on a republican system of government thus became an essential element of Korea's independence movement. However, brutal repression by the Japanese colonialists, collaboration by traitors, and factionalism within the independence movement itself limited the effectiveness of Korea's struggle for independence, and before the united front for national liberation movement could put an end to the Japanese colonial occupation, Korea was liberated when Japan surrendered at the end of World War II.

After liberation, it was imperative that the Korean people carry out a land reform and punish traitors who had collaborated with the Japanese colonial regime. With justice thus served, Korea could secure a foundation for the building of an independent democratic nation. However, the intervention of foreign powers and confrontation between extremists who put class interests before national interests led to the tragic division of the Korean Peninsula. The Korean War, which was started by the North and ended in a stalemate, intensified mutual distrust between South and North Korea, and led to the extremely anti-democratic political culture of labelling dissident groups as "spies" from the other side.

The development dictatorship established after the May 1961 coup in the South and the isolationist dictatorship of the North only accelerated the centralization of power and mass mobilization. Neither the anti-Japanese guerrilla fighter credentials of the North Korean leadership nor the spectacular economic growth achieved under the South Korean leadership failed to justify the respective dictatorial system. However, the outward-oriented "wealthy nation, strong army" policy pursued by the military regimes in the South produced a large middle class which demanded democratic reform commensurate with economic growth, and the long-continued democratic struggle in the South was finally able to put away the dictatorial system in the late 1980s.

The democratic revolution of South Korea will provide an impetus for the building of a unified democratic system in the Korean Peninsula. It must be noted, however, that the popular election of a president every 5 years by itself does not mean that the transition toward democracy has been completed. If unaccompanied by the decentralization of power, popular election can give rise to absolutist rule by a president whose legitimacy, based as it is on people's will, is more secure than ever before. What is supposed to be a democracy can degenerate into a system of directly electing a legitimate dictator every few years.

Although power is being gradually devolved from the center, authoritarianism, that arch-enemy of democracy, is still alive and well in the Korean Peninsula. In fact, as

long as feudalistic elements in Confucian values and the confrontational structure of inter-Korean relations hold sway, Korea's democratic revolution will remain unfinished.

Within this historical context, the unification of South and North Korea will have the effect of removing "the external enemy" which has frequently been used by both governments to stifle dissent and justify the centralization of power. Moreover, Korean reunification will make it no longer possible for other countries to employ a "two-Korea policy" and play one against the other, and thereby contribute to the enhancement of national independence and self-determination. Thus, Korean reunification will not only serve as an impetus in banishing authoritarianism and establishing a genuine democracy based on decentralization and participation, but will also provide a sound basis for a strong independent nation. Herein lies the true historical significance of Korean reunification.

III. Economic Agenda for Korean Reunification

In order to achieve unification within this historical context, it is necessary to devise an economic system which will provide the material basis for a strong independent nation and vibrant democracy. The recent experiences of the Communist Bloc countries and other developing countries seem to show that neither the socialist system nor the development dictatorship can serve as a foundation for a dynamic economy and vibrant democracy, both of which is characterized by respect for individual autonomy. Although it is somewhat premature to declare the final winner in the competition of systems, the social market economy-- or, what may be called "capitalism with a human face"-- may be judged to be the best economic system to provide opportunities for individuals to pursue self-development, the natural basis of a strong independent democratic nation.

Within this context, this section examines the set of tasks that must be accomplished to establish such a social market economy in the Korean Peninsula. While the attention of economists so far have been focused on system transformation in Eastern Europe, economic integration in Germany, and economic development in low-income countries, this section will examine all three tasks in order, for they are closely interrelated problems in Korea's case.

1 System Transformation

The socialist system was originally proposed as an alternative to the early capitalist system characterized by its unorganized and exploitative nature. Although Karl Marx, the founder of "scientific socialism," made few detailed suggestions about the daily

operation of the socialist economy, "real socialism" constructed by the likes of Joseph Stalin, Mao Tse-tung, and Kim Il Sung was a command economy founded on the principle of mobilizing idle labor and raw materials. This extensive growth strategy based on mobilization of resources led to significant economic gains in early stages, but began to lose its effectiveness as the structure of the socialist economies became complicated and horizontal relationships among economic agents became important. Unable to generate meaningful productivity gains-- as opposed to output increases, many of these economies stagnated for over a decade before finally being overthrown in 1989. Most scholars now agree that the structural problems of the socialist system could be resolved only through system transformation.

System transformation, however, is not a partial reform of a system, but rather a replacement of a coherent system by another coherent system. As the socialist system too is a coherent system with its own internal logic, carrying out system transformation without a proper accounting of its interrelated elements will only create serious disruptions. The transformation of a socialist economy thus first requires an intimate understanding of the characteristics of the socialist system.

The fundamental structural problem of the socialist system is that there is a systematic separation between information and decision authority, with little incentive to connect these two critical elements. If the socialist system of extensive central planning is to operate smoothly, the decision authorities at the center must have detailed information on the productive capacity of each subordinate. In the case of the former Soviet Union, this task involved keeping track of prices and quantities of over 24 million goods. [Ericson(1991)] Maintaining a planning economy on such a scale would certainly be a formidable task; however, if information provided by subordinates is accurate and information flow among subordinates smooth enough, preparing a comprehensive production plan would not be an impossible task given the increasing power and sophistication of modern computers.

From the perspective of an individual plant, however, it would be an act of self-flagellation to provide accurate information on its productive capacity and respond positively to requests from related factories. As the state retains rights to economic output and little material reward is given for increased production under the socialist system, it is only natural that each individual production unit under-report its productive capacity and exaggerate its need for labor and raw materials. Information provided by such economic agents cannot be accurate.

Moreover, since each production unit escapes blame as long as it fills the production quota within the prescribed specifications, it has little incentive to consider whether its products are really appropriate as capital or consumption goods for other economic agents. For example, even if ball-bearings supplied to a tractor factory are so

unsuitable that an alternation of production has to be made, it is not a concern of the ball-bearing factory. [Ericson(1991)] Instead of promoting smooth horizontal and vertical information flow among production units, the plan, in short, tends to create isolated pockets of information.

In the end, what forms the basis of the central plan is highly inaccurate and disjointed information provided by subordinates. Given such conditions, it is perhaps not an exaggeration to say that what preserves the socialist planning system is not the economic rationality of the plan itself, but the center's urge to command and control the economy. Under such a system, the economic consideration of incorporating continually changing information becomes secondary to the political consideration of stable control, and the central plan becomes a reflection of the existing production relationship. Planning from the previously achieved level, the center thus demands from each production unit a percentage increase in its output. The plan in effect "freezes" the existing structure of production and impedes technological innovation, blocking the exit of inefficient plants and the entry of new firms. [Estrin(1991)]

Much like the production structure itself, prices are frozen to minimize variability within the system and facilitate central planning. Since prices fail to reflect supply and demand conditions under the socialist system, they merely exist as accounting entries.

In administratively fixing prices, socialist countries adopted a rather interesting policy. They commonly pursued a policy of pricing "basic necessities" below cost and "luxuries" above cost. This characteristic of socialist pricing policy is clearly shown in the following table which compares East and West German prices for various goods as of May 1990. [Ahn(1992), p.89]

Item	East/West Price Ratio	Item	East/West Price Ratio
tape recorder	600	kindergarten fees	5
pineapple	550	streetcar fare	10
camera	530	haircut	15
women's nylons	510	bread	16
calculator	490	newspaper	17
refrigerator	390	coal(for heating)	17
coffee beans	390	housing	18
chocolate	310	electricity	24

On the surface, it may seem sensible to restrict the consumption of such "luxuries" as cameras, refrigerators, pineapples, and coffee beans by overpricing these

commodities, and guarantee minimum living standards by underpricing such "basic necessities" as education, transportation, and food. Such a pricing policy, however, leads to distortions in economic activities and delays the advent of the economic stage in which growth is achieved through the mass consumption of durable goods.

For example, the below-cost pricing of coal made it possible for florists to grow tropical flowers for export in Poland(!) [Wellisz(1991)], and its overuse directly contributed to the air pollution problem in Eastern Europe. Moreover, in the case of the former Soviet Union, artificially low food prices made it cheaper for peasants to buy and feed bread and potatoes to their livestock than to use unprocessed grain. [Kennedy(1987), p.491]

If the underpricing of basic necessities leads to "bizarre" economic activities and increases the subsidy burden of the state, the overpricing of luxuries restricts consumption and impedes economic growth. To make a leap to a higher value-added stage, the most natural course of action for any country to follow is to encourage the consumption of durable goods and novel products which, up to that point, have been considered "luxuries." All socialist countries, however, failed to make a transition to this stage. Since durable goods were so exorbitantly priced, the general public had nothing but basic necessities to buy, and were forced to save much of the money they could not spend. These "forced savings" created a wedge between their income and actual quality of life. As the consumption of such durable goods as refrigerators and automobiles was restricted, these industries could not develop, and having a taste of the "affluent living" of the West became a dream in these countries. It would not be an overstatement that this all-too-human desire played a critical role in the mass exodus of East Germans and the eventual unification by absorption.

Now, when prices bear little relation to costs as shown above, the profitability of an individual production unit will have little connection with its productive efficiency. If, for instance, the underpricing of a factory's output leads to heavy losses, then it should be the responsibility of the state to provide subsidies to prop up this innocent victim of the system. As such practices become common, however, the budget constraint will lose its binding power, and will become "soft." Together with guaranteed employment, unrealistic prices under the socialist system thus produce the phenomenon of "soft budget constraint," in effect allowing factories to spend beyond the limit set by their original budget. [Kornai(1990)]

What kinds of implications does this socialist combination of concentrated market structure and fixed prices have for system transformation? Suppose that prices are liberalized and autonomy granted to individual production units without first addressing the market concentration problem. In all likelihood, the existing state enterprises will take full advantage of their market power and raise prices way above

costs. This is precisely what the Polish state enterprises did when subsidies were cut off and prices were liberalized in 1990, as they only raised prices and reduced output, taking no measures to improve their productivity. [Economist(1993), p.19] In contrast, if autonomy is granted to individual firms without price liberalization, even the most efficiently operated plants may make heavy losses and will have to appeal to the state for subsidies. The experience of economic reform in Hungary and Poland before 1989 clearly demonstrates that such uncoordinated, halfway measures cannot work. [Wolf(1991), Seo et al.(1993a)] The tripartite system of unrealistic prices, guaranteed employment, and social ownership of means of production must be attacked in a coordinated manner.

What, then, would be the most effective way to redefine property rights and sequence industrial restructuring and price liberalization? In an ideal world, a competitive market structure would be created simultaneously with price liberalization; in the real world, however, it is extremely doubtful that viable domestic competitors to gigantic state enterprises can be created in a short time. The alternative of opening up the market and exposing state enterprises to international competition, on the other hand, runs the risk of huge business failures and massive unemployment. Under these circumstances, the most effective and realistic course of action may be to employ a modified version of antitrust policy: Instead of liberalizing prices outright, control prices so that they reflect production costs, but not market power, and impose a price cap to promote cost reduction and productivity improvement. Also, break up gigantic state enterprises into smaller firms of optimal efficiency scale, and have them compete against one another and eventually against foreign producers. Designed to transform bloated state firms into efficient public enterprises like POSCO, this gradual approach may be preferable to the "big-bang" privatization scheme advocated by many economists.

Certainly, wholesale privatization still may be recommended, if only to increase state revenue and to avoid the politicization of problems associated with the management of state enterprises (e.g., layoffs). Even in such a case, however, one must be careful not to fall into the trap of the black-or-white dichotomy of market ideologues who claim that the continued existence of state enterprises means the preservation of the socialist order while privatization means genuine reform toward market economy. As in the case of privatizing public enterprises in market economy, both efficiency and equity must be accorded careful consideration. [Fischer and Gelb(1991)]

Among various property assignment schemes, the simplest and least controversial of all may be the equal distribution of ownership, for all means of production under the socialist system can be thought to be owned by the people. For example, the state can issue vouchers, and when a market for vouchers is formed, individual citizens can

dispose of their vouchers as they wish. This scheme has the attraction of being faithful to the socialist principles of equity at the time of distribution, and market principles of efficiency after distribution. As long as accurate information is provided to individual investors to guide their decisions in the unfamiliar terrain of market economy, the voucher scheme will generate a widespread public support for system transformation.

Instead of this equal distribution scheme, a policy of returning property to original owners may also be considered. By recognizing the rights of property owners prior to the imposition of the socialist order, this scheme seeks to establish the principle of the sanctity of property. However, since it is impossible to return land or other types of property whose shape or use has been changed through the years, this policy of restoring property rights may degenerate into a legal battle over the appropriate amount of compensation. Moreover, as it is often difficult to establish the identity of the original owner, new investment projects may have to be delayed while the question of ownership is sorted out. [Ahn(1992)]

In practice, the policy of returning property to original owners is often combined with considerations for social equity. Rumania, for instance, has returned land to original owners within 10 hectares and allowed each household to purchase a maximum holding of 100 hectares. [Brooks et al.(1991)] This hybrid approach can be compared with what amounts to a limited voucher scheme in China. Instead of returning land to original owners, the Chinese government has in effect opted to play the role of a landowner and grant land leases to peasants, and collect taxes in lieu of tenant fees.

Unlike in the case of land, the assignment of property rights in factories usually does not have to deal with the question of prior ownership, since most of these were built anew during the socialist rule. Instead, efficiency considerations become supreme, and separation of ownership and management may take place as a result. In order to achieve a desirable outcome, the state may have to sell a sizable proportion of its shares to large private companies with technical and managerial expertise, retain some shares to monitor the management, and distribute the rest to the people to gain a broad popular support for economic reform.

Efficient assignment of property rights and liberalization of prices is a critical element in the establishment of a market economy. The assignment of property rights makes it possible for the holder of local information to make decisions on his or her own, and assume the responsibility for the consequences. By thus decentralizing the authority to make decisions, it lays the groundwork for system transformation, and secures the foundation for an economic and political system that values individual initiative. Korea's unification process cannot proceed smoothly without such system transformation measures.

2 Economic Integration

Economic integration is a process through which two or more countries form a single economic entity by removing barriers to the free flow of goods and factors of production and by eventually establishing a unified system of economic institutions. This section briefly reviews the experience of the European Union and Germany to compare gradual and sudden paths to economic integration, and draws relevant lesson for Korean reunification.

The origin of the European Union can be traced back to Jean Monnet's May 1950 plan. In proposing this plan, Monnet sought to arrest the relative decline of Europe in the postwar U.S.-Soviet bipolar system and to prevent the outbreak of war in Europe, especially between France and Germany. Accordingly, when France, West Germany, Italy, and the Benelux countries established the European Coal and Steel Community (ECSC) in 1951, they not only sought to pursue common economic interests, but also intended to contribute to peace in Europe by jointly overseeing the production, distribution, and consumption of basic raw materials for the manufacture of heavy weapons-- namely, coal and steel. In 1957, the foreign ministers of these six nations signed a treaty to establish EURATOM, and by signing the Treaty of Rome, they created the European Economic Community (EEC). [Byun(1982)]

Having secured a solid foundation for peace and prosperity in Europe, the six member nations integrated EEC, ECSC, and EURATOM into a single organization and formed the European Community in 1967. In order to guarantee the free flow of labor as well as finished goods, the member nations coordinated their job training and social security policies, and established the European Social Fund for the retraining and reemployment of laid-off workers.

Although the EC member nations had already agreed in 1969 to establish a single economic and monetary policy by 1980, the two oil shocks in the 1970s impeded their progress toward complete economic integration. With the adoption of the Delors Report in 1989, however, the member nations reasserted their desire to create a single Europe, and by signing the Treaty on European Union in Maastricht in December 1991, they declared that their dream of creating one Europe was within reach. However, as the delegation of monetary authority to the European Central Bank and the issuance of a single European currency are almost certain to compromise the economic sovereignty of member nations, the movement for European integration is running into significant resistance at this point. [Kim & Lee(1992), Economist(1994)]

In contrast to the gradual approach of the European Union, Germany is a case where the sudden approach toward economic integration *had to* be taken to complete political unification: what had been economic cooperation *without* a clear blueprint for

the future had to be suddenly transformed into complete economic integration. Even after the division of Germany and establishment of separate governments in 1949, East and West Germany continued to engage in trade with each other. In fact, in order to facilitate this trade and reaffirm its legitimacy, when West Germany joined the GATT (General Agreement on Tariffs and Trade) in 1951, it went so far as to secure an international agreement to treat West-East German trade as intra-national transactions. [Hwang(1992)] Thus, while East and West Germany politically and diplomatically took a Cold War stance against each other, they maintained their economic relations--unlike in the case of Korea.

Inter-German relations underwent a dramatic change when the Social Democrats came to power in West Germany in 1969. Under the policy of *ostpolitik*, West German Chancellor Billy Brandt sought to improve relations with the Soviet Union and East European countries, and adopted a conciliatory approach toward East Germany. After holding the the first summit meeting in March 1970 and signing the Basic Agreement in December 1972, West Germany recognized East Germany as a legitimate state. In return, it was promised increased exchanges between the two sides. The two Germanys simultaneously joined the United Nations in 1973, and established missions in Bonn and East Berlin in March 1974.

In order to preserve a sense of national unity, Bonn provided generous assistance to Berlin, and directly supported the annual exchange of visits and correspondences by millions of East and West Germans by paying, for instance, user fees on inter-German roads and railways. The West German government even put up bail on political prisoners in East Germany. It is unclear whether West Germany had a "masterplan" to topple the East German regime through these measures, but collapse it did, and Bonn was faced with a new problem of full-scale economic integration. [Kim & Lee(1992)]

In contrast to the European Community whose original member nations had similar income levels but different ethnic and cultural heritages, Germany was faced with the exact opposite problem of pursuing economic integration based on identical heritage and drastically different income levels. Under such circumstances, the most economically rational plan might have been to block the inflow of East German workers, who would have a depressing effect on West German wages, and to raise East German living standards by promoting the outflow of West German capital. However, it would have been considered against the spirit of unification to control the movement of East Germans and tell them to wait until their economic situation improves.

In the end, Germany resolved the economic problem of labor market integration with the political slogan of "One Nation, One-to-One Exchange Rate." Prior to unification, the effective exchange rate between East and West German currencies had

been approximately 4.4 to 1. The 1-to-1 exchange rate had the effect of raising East German wages by more than four times. In the short run, this dramatic wage increase boosted the purchasing power of East Germans and led to a 20% increase in the number of automobiles that they owned. In the long run, however, this unrealistic exchange rate and the ensuing wage rise aggravated the competitive weakness of East German firms and produced a 30% unemployment rate. [Collier(1991)] It must be noted, in passing, that unemployment insurance payments to laid-off workers have more the character of irrecoverable subsistence cost than long-term investment in productive capacity.

The experience of the European Union and Germany demonstrates the difficulty of creating a supra-national community out of existing countries. Not only does such a supra-national community require the member nations' ideological consensus on the single unified system, but it also demands a similar cultural background so that conflicting economic interests between member nations would not develop into racial animosities, for instance. Even when these conditions are met, drastic differences in income levels may hinder economic integration.

In Korea's case, although its ethnic homogeneity seems to provide the basic foundation for a single unified community, the lack of ideological consensus on the shape of the unified system has tended to block any serious efforts toward economic integration. As North Korea has begun to show signs of experimenting with some elements of the market economy, however, hopes for gradual economic integration are not totally unjustified. In order for such a process to get on track, South Korea must *consistently* promote inter-Korean economic exchanges in such a way as to support the North's tentative moves toward economic reform and to restore the sense of national unity that is being gradually lost due to the long division of the Korean Peninsula.

Unfortunately, Seoul's recent policy toward North Korea has suffered from lack of consistency. Certainly, some confusion in inter-Korean relations may be inevitable given Korea's peculiar situation: South and North Korea fought a war and their heavily armed troops face each other across the DMZ; at the same time, they have to be the eventual partners for unification. It is, however, still very feasible *and* necessary to have a consistent policy with a clearly defined objective.

In the late 1980s, South and North Korea seemed to follow the same steps taken by East and West Germany in the early 1970s. Inter-Korean relations, however, soured again before the two sides could move to the stage of having human and economic exchanges on a regular basis. In order to restart the unification process, the South should maintain a consistent policy along the lines mentioned above, rewarding the North's move toward market economy and democracy and withholding support when the North moves in the opposite direction. Before making further demands on North

Korea, the South must first make its policy consistently and transparently unification-promoting.

3 Economic Development

In thinking about Korean reunification, an economic task that must be considered together with system transformation and integration is that of development. Characterized by underinvestment in infrastructure and lack of market mechanisms, North Korea has the characteristics of a typical underdeveloped economy, which seeks economic growth through mobilization of resources rather than capital investment and technological development. [Choi(1992)] It is a characteristic of an underdeveloped economy to be caught in a low-equilibrium trap that it requires a big push of investment in infrastructure and productive capacity to pull the economy out of this trap and create employment opportunities for a massive number of unemployed and underemployed workers [Rosenstein-Rodin(1961)]

In order to pull an underdeveloped economy out of stagnation, it is absolutely essential that surplus labor, usually in agriculture, be redeployed in more productive sectors. It is important to note, however, that the assignment of property rights through privatization and reliance on market forces alone do not provide sufficient incentive for private investment, for private investment requires prior provision of public goods of both material and institutional nature. In the absence of basic infrastructure such as power grids and transportation networks, private investments in productive capacity will suffer. Even state-of-the-art machines, for example, will not function properly if electricity cannot be provided on a stable basis.

The economic development of South Korea demonstrates this need to provide public goods of both institutional and material nature. In 1963, the per-capita GNP of South Korea was less than 60% of the Philippines' and is estimated to be about 55% of North Korea's. In fact, having successfully reconstructed the economy from the ashes of the Korean War, Kim Il Sung boasted of North Korea's achievements, and proposed a confederation scheme on the occasion of the 15th anniversary of Korea's liberation from Japan. He confidently declared:

The most urgent problem today is to rebuild the South Korean economy and to improve the living conditions of the people who have fallen into great misery.... This problem cannot be solved without economic exchanges between the South and the North. It is a simple truism of economics that no country can develop light industries and agriculture and improve people's lives without heavy industries. In our country, only the northern half has such industries..... We also have a plenty of experience with economic development.

After staging a successful coup in 1961 in South Korea, Park Junghee confronted the cold reality that the South was facing a formidable adversary who was winning "the economic war which comes ahead of military or political battle," and channeled all national energy into economic build-up. Deploring that South Korea had to depend on U.S. assistance for 52% of the government budget in fiscal year 1961, he summarized the South's economic conditions as follows:

From 1956 to 1962, economic assistance averaged about \$280 million per year, and military assistance, about \$220 million per year. Add to this total an average trade deficit of \$50 million per year, and the conclusion is that we must earn anew an average of \$550 million per year. And, what are we going to do with the additional pressure from a population growth rate of 2.88%, namely 720,000 people per year? [Park(1963)]

As he had already made clear at the outset, in the Revolutionary Pledges of May 16, 1961, he was determined to "focus all energy into developing capability to confront communism, in order to realize the people's long-standing wish for national unification."

Although some commentators have defined Park's economic development policy as "export-led unbalanced growth strategy," it would be more accurate to say that South Korea's development policy prior to the mid-1970 was really a balanced growth strategy accounting for the development of both agricultural and manufacturing sectors. In order to channel surplus labor into productive uses, the Park government decided to pursue an export-promotion policy centered around labor-intensive industries. The previous policy of import substitution was scrapped around 1964 with the introduction of (partial) import liberalization policy, and a new financial and industrial policy regime was established to encourage South Korean firms to grow through competition in domestic and international markets. [Lin(1989)]

In addition to providing institutional public goods, the South Korean government secured claims from Japan and loans from foreign countries to provide material public goods such as power plants, highways, and industrial complexes. The chronic power shortage problem which had impeded economic growth was finally solved in 1968; a series of new highways were constructed in the 1970s according to the logic of the "build first, fix later" principle; and coastal industrial complexes were constructed to attract private investment in productive capacity. [Kim(1994)] In less than 10 years after launching such a comprehensive program of economic development, South Korea became one of the leading members of developing countries, and began to surge past North Korea in such economic indices as per-capita GNP.

In Vietnam's case, too, it took less than 10 years of systematic reform for the country to make a leap from the depths of economic troubles and become one of the

rising stars among late developing countries. For Vietnam, the first decade after unification was marked by a gradual economic decline. After achieving unification by force in 1975, Hanoi sovietized the former South Vietnam. After signing a 25-year friendship treaty with the Soviet Union in 1978, Vietnam invaded Cambodia in the same year, provoking hostile responses from China and the United States. [Dotae Kim(1993), *Economist*(1995)]

Vietnam reached its economic nadir in 1986, with food shortages and rampant inflation threatening to destroy the very fabric of the society. Recognizing that they had erred, the Vietnamese leaders declared economic reform at the party congress in December of that year. After taking measures to liberalize trade and encourage joint ventures with foreign companies, the Vietnamese Communist Party dissolved collective farms, freed food prices, and cut off subsidies to state enterprises in 1988. When Vietnam withdrew its main forces from Cambodia in 1989, foreign investment began to trickle into the country. Although Vietnam lost a Soviet aid of billion rubles a year from 1990, it was able to expand trade with market economies and record an average growth rate of around 10% per year. [*Economist*(1995)] Currently, the per-capita GDP of Vietnam is estimated to be around \$1,200 on purchasing power parity basis. This is below the \$2,500 level of China, and lower even than the per-capita GDP of North Korea, which is around \$2,000.

Another example of socialist market economy, China too provides some valuable lessons for North Korea's economic development. In the initial stage of economic reform, which was launched in 1978, China accorded priority to agriculture and trade. Collective farms were scrapped, and prices of secondary crops, and eventually those of grain, were freed up to provide peasants with material incentives. In order to promote exports, the monopoly on foreign trade held by the state corporations was broken up, and special economic zones were set up along the coast. In addition, China's currency was devalued to the dollar, from 1.7 yuan in 1981 to 4.8 yuan in 1990. These industrial and trade policies had the effect of exposing domestic producers to international competition and forcing them to improve their productivity. Lured by the dynamism of the Chinese economy, foreign investment began to pour in, especially from overseas Chinese. The overseas Chinese share in total foreign investment was so pronounced that in 1990, 55 percent of all realized foreign investment came from Hong Kong and Macao. [Perkins(1994)]

The decollectivization of agriculture, export promotion, and the massive investment by overseas Chinese provided a solid foundation for a spectacular growth of the Chinese economy. From 1978 to 1993, China grew at an average growth rate of 9% per year, and recorded a trade surplus every year except for four years. Although China has yet to resolve the problems posed by inefficient state enterprises and latent

inflationary pressures, it would not be an exaggeration to declare that China's market socialism has been a resounding success. [Yusuf(1994)]

4 Lessons for South and North Korea

What lessons can Korea draw from this survey of economic theory and historical experience of various countries? First, the experience of China and Vietnam suggests that there is no need to despair over the economic prospects of North Korea. Although North Korea is estimated to have recorded a minus economic growth for four straight in the 1990s and has to be provided with food imports or assistance, it has one of the highest per capita income among less developed countries. Perhaps more to the point, North Korea seems to have accumulated a great deal of growth potential while trying to build a self-sufficient economy. After all, it does have the ability to build its own missiles.

At present, the most pressing economic task faced by North Korea is to revive foreign which suffered a catastrophic decline after the collapse of the Socialist Bloc. The former Soviet Union not only accounted for 60% of North Korea's total trade in the late 1980s, but was also providing a de facto aid of hundreds of million dollars by recording a large trade surplus with North Korea. With the disintegration of the Soviet Union, this trade all but vanished. [National Unification Board(1992)] However, if North Korea, like Vietnam, can expand trade with Asian and Western countries, it should be able to fill the vacuum left by the collapse of the Communist Bloc.

A more detailed evaluation of North Korea's current economic conditions is as follows. Although it varies depending on the exchange rate applied, North Korea's per capita income is estimated to be around \$2,000. [Hwang(1992), National Unification Board(1992), Seo et al.(1993b)] This figure does not deviate significantly from an estimate produced by regressing per capita income on more easily measurable quantities such as per capita energy consumption and average life expectancy. On purchase power parity basis, this econometrically derived result is around \$2,200, similar to the per capita income of the Philippines. [Noland(1995)] It is interesting to note that these estimates roughly agree with Pyongyang's own announced figures of \$2,200 in 1982 and \$2,460 in 1991. [National Unification Board(1992)] Even taken at face value, these announced figures seem to confirm that the North Korean economy stagnated in the 1980s. Of course, given that military industries are estimated to account for as much as 30% of North Korea's total output, an average North Korean's living standards are likely to be quite lower than what the per capita income of \$2,000 seems to imply. Nevertheless, it must be emphasized that North Korea's current economic conditions are little worse than those of Vietnam in the mid-1980s and South

Korea in the early 1960s.

Similar to the role played by Hongkong Chinese in China's economic development, South Koreans have the ability to assist in the North's economic transformation by making investment and transferring know-how. In particular, at least in the short run, the South can transfer its labor-intensive sunset industries to the North to create employment opportunities-- to the benefit of both sides.

Certainly, North Korea's economic transformation has its share of problems. As previously stated, without Pyongyang's willingness to dissolve its "one-and-only" system, genuine economic reform cannot be launched. Moreover, North Korea's industrial structure, with its undue emphasis on heavy industries, may serve as an obstacle to economic development. When South Korea, China, and Vietnam was about to launch their economic development program, about 70% of the total workforce was in the agricultural sector. In contrast, only about 25 % of North Korea's workforce is in agriculture, and 60% is estimated to be in manufacturing. [Park(1963); Eberstadt(1994); Economist(1995)] While predominantly agricultural China and Vietnam were able to secure popular support for economic reform by dissolving collective farms and simply handing land leases to peasants, North Korea thus faces an unenviable task of pursuing system transformation through industrial restructuring, which may lead to significant dislocations and layoffs.

In short, among socialist economies, North Korea represents a rather unique hybrid: While having the industrial structure of relatively advanced economies like the former Soviet Union and Czechoslovakia, it also has the per-capita income of developing economies like China and Vietnam. This combination of advanced industrial structure and low per-capita income (and hence low wages) seems to imply that a promising development strategy for North Korea may consist of creating export-oriented labor-intensive industries to soak up surplus labor and ease the pain of industrial restructuring. This scheme for economic development will require Pyongyang's willingness to carry out genuine system transformation.

The North's economic development is closely connected not only with its system transformation, but also with its economic integration with the South. The closely intertwined nature of these three tasks calls for a comprehensive approach.

First, the South and North should build up mutual confidence and promote economic cooperation by establishing a Korean version of ECSC or EURATOM. By jointly overseeing the production and consumption of nuclear energy and basic raw materials through such an organization, the two sides should be able to have more informed discussion on energy and military issues. In this stage, the South could help alleviate the North's power shortage problem by jointly developing energy resources, including the North's estimated uranium reserve of 26 million tons. Energy joint

ventures between the two sides will not only provide a sound basis for further economic cooperation and integration, but also lay the groundwork for North Korea's economic development.

In this early stage, Pyongyang should make clear that it has made a solid commitment to system transformation. Although North Korea has made such dramatic gestures as declaring a free trade zone in the Rajin-Sonbong Area, this area is more like an isolated enclave to produce exports and earn hard currency than a testing ground for genuine reform. As long as Pyongyang displays no willingness to scrap its socialist system, it is unlikely that foreign investors would seriously consider putting their money in North Korea.

Once that North Korea makes an unswerving commitment to genuine system transformation, the scope of inter-Korean economic cooperation can be expanded. In this stage, investment should be channeled into absorbing North Korea's underemployed labor in inefficient state enterprises. Two channels seem to be immediately available: massive investment in public works and creation of labor-intensive industries, supported by consignment training and joint ventures.

Also, in this stage, South Korean firms may serve as partners or management consultants for North Korean enterprises, and share their insights into the workings of market economy. POSCO, for instance, may become "a sister company" of the North's Kim Chaek Steel Corporation, and directly improve the productivity of this state enterprise by transferring its technical and managerial know-how.

By raising the productivity of North Korean workers and thus reducing the inter-Korean income gap, Korea could begin to prepare for eventual reunification. If, however, unification is achieved without prior resolution of the income gap, the Korean people may be confronted with more serious post-unification traumas than Germans. If the labor market is rapidly integrated through a massive influx of North Korean workers into the South, the North will suffer from premature "de-industrialization," and the South will have to deal with the downward pressure on wages exerted by the new army of underemployed workers. If South Korean workers have to suffer significant wage cuts and layoffs due to the presence of cheaply available North Koreans, a new internal conflict may develop within Unified Korea. If rapid economic integration leads to massive unemployment in either the South or the North, the unification process will encounter a serious resistance from workers.

In regard to the income gap, South Korea's own experience provides a valuable lesson. As of 1985, by which time the phenomenon of "reckless exodus to Seoul" had largely disappeared, the per capita income of Cholla Provinces amounted to 65% that of Seoul. Similarly, if there is to be no "reckless exodus to the South," it seems to be reasonable to assume that the North's per capita income should reach at least 50% of

the South's. [Korea Development Institute(1991)] At present, the North's per capita income is estimated to be only around 20% of the South's. Ironically enough, the divided situation of Korea offers an ideal physical setting for the two sides to resolve this income-gap problem, for the free movement of labor across the border is prohibited under the present circumstances. South Korea should take full advantage of this situation and help to raise the living standards of North Korean workers. Just as overseas Chinese in Hongkong, Taiwan, and other places are contributing to the improvement in Chinese workers' living standards, South Koreans should go into the North with capital before North Korean workers come down to the South in search of higher wages.

A comprehensive analysis of economic conditions in South and North Korea suggests that the most serious economic obstacle to unification is likely to be the widening income gap between the dynamic South and stagnant North. If the per capita income of South Korea is assumed to grow at an average of 7% per year, the North's per capita income must grow at an average of 23% for the two figures to converge in 10 years. Even for a more modest goal of 50% convergence within 10 years, the North's per capita income growth should still average around 16%. If the North's per capita income grows at a more realistic rate of 10% per year, only 27% convergence is achieved in 10 years. In other words, the inter-Korean income gap is not a problem that could be resolved in a short period. In order to reduce the shock of unification, the North should make a solid commitment to system transformation and economic development, and the South should support the North's economic growth on a long-term basis.

IV. Conclusion

In order to provide a historical rationale for Korean reunification and a hopeful vision for the future of Unified Korea, this paper has first criticized the optimistic and pessimistic extremes of conventional views on unification, and proposed an alternative framework based on the twin principles of self-determination and decentralization. Reviewing the experience of the former Communist Bloc countries and other developing countries from an economic perspective, the paper has argued that South and North Korea should jointly solve the much-intertwined problems of system transformation, economic integration, and economic development if they are to secure a solid material foundation for national independence and genuine democracy.

Since the late 19th century, the Korean people have tended to liken their fate to that of "a shrimp among whales," who must be constantly on guard lest its little back be squished amidst the pandemonium of a fight between the giants. This fatalistic and

fundamentally negative way of thinking on Korea affected even foreign scholars. One comprehensive survey of Korea, for example, ends in what is claimed to be an "optimistic" tone by suggesting that Unified Korea may become the Switzerland of Asia. [Economist Intelligence Unit(1992)] In other words, becoming a small neutral, albeit prosperous, nation among regional powers is the best hope that these experts offer to the Korean people.

By no stretch of imagination, however, will the Unified Republic of Korea be a small nation. Even now, South Korea by itself ranks among the world's top 12 countries in terms of GDP. Unified Korea will easily be among the 10 largest economies in the world, and its total population of more than 70 million will surpass that of Russian Far East and will amount to about half the total population of China's northeastern provinces as well as that of Japan. In short, Unified Korea will not be "a shrimp among whales," and will wield influence comparable to that of the existing powers in Northeast Asia, as the nations in this region undergo gradual economic integration.

As previous argued, however, the mere expansion of national power will not be the sole, nor even the primary, consequence of Korean reunification. By striking at the very roots of political and economic authoritarianism, unification will facilitate the transition toward a genuine decentralized democracy and market economy, and will go a long way toward realizing the Korean people's dream of building an independent democratic nation.

Notes

- 1) Formally titled "the Agreement on Reconciliation, Non-Aggression, and Exchanges and Cooperation Between the South and the North," the Basic Agreement characterizes the inter-Korean relationship as "a special interim relationship" to be creatively dissolved through reunification.
- 2) Seoul envisages a three-stage process through which the present regime of no unified central government, two separate regional governments, and two different systems (0-2-2 formula) evolves first into a commonwealth (0.5-2-2) and eventually into a single unified state (1-0-1); whereas, Pyongyang proposes to create a confederation of one central government, two separate regional governments, and two *different* systems (1-2-2 formula). Note that a commonwealth, based as it is on the free association of separate political entities, does not include a formal structure of central government with binding powers.
- 3) For a historical perspective on various unification schemes, see Park and Choi(1993).
- 4) For a thought-provoking survey of modern Korean history, see Kang(1994).
- 5) Under the Hallstein principle, West Germany cut off diplomatic relations with any country that established formal relations with East Germany throughout the 1950s and early 1960s.

- 6) Some West Germans attacked this policy, likening it to paying a ransom for hostages, and they argued that Bonn's economic assistance was merely propping up a corrupt and oppressive regime in East Germany. It must be acknowledged, however, that West Germany's conciliatory policies helped to maintain a sense of national unity among the German people, and led East German citizens to expect generous treatment should they flee to West Germany.

References

- Ahn, Dusun(1992), *Unification of the Korean Peninsula and Economic Integration* (Seoul: Korea Economic Daily Press).
- Brooks, Karen, J. Luis Guasch, Avishay Braverman, and Csaba Csaki(1991), "Agriculture and the Transition to the Market," *Journal of Economic Perspectives* 5(4): 149-161.
- Byun, Doun(1982), *The European Community* (Seoul: Pyongmin Press).
- Choi, Juhwan(1992), *A Study of North Korea's Economy* (Seoul: Daewang Press).
- Collier, Irwin L., Jr.(1991), "On the First Year of German Monetary, Economic and Social Union," *Journal of Economic Perspectives* 5(4): 179-186.
- Eberstadt, Nicholas(1994), *Korea Approaches Reunification* (Seoul: Korea Economic Daily Press).
- Economist(1992), "A Survey of Germany: Not as Grimm as it looks," 23 May 1992.
- Economist(1993), "Poland's Economic Reforms: If it works, you've fixed it," 23 January 1993, pp.19-21.
- Economist(1994), "A Survey of Germany: model vision," 21 May 1994.
- Economist(1995), "A Survey of Vietnam: The road to capitalism," 8 July 1995.
- Economist Intelligence Unit(1992), *Korea and Its Future* (London: Business International).
- Ericson, Richard E.(1991), "The Classical Soviet-Type Economy: Nature of the System and Implications for Reform," *Journal of Economic Perspectives* 5(4): 11-28.
- Estrin, Saul(1991), "Yugoslavia: The Case of Self-Managing Market Socialism," *Journal of Economic Perspectives* 5(4): 187-194.
- Fischer, Stanley, and Alan Gelb(1991), "The Process of Socialist Economic Transformation," *Journal of Economic Perspectives* 5(4): 91-106.
- Hwang, Uigak(1992), *A Study of North Korea's Economy* (Seoul: Nanam Press).
- Kang, Mangil(1994), *Modern and Contemporary History of Korea* (2 vols.), revised edition (Seoul: Changjak-gwa-Bipyong Press).
- Kennedy, Paul(1987), *The Rise and Fall of the Great Powers* (New York: Vintage).
- Kim, Chung-yum(1994), *Policymaking on the Front Lines: Memoirs of a Korean Practitioner, 1945-79* (Washington, D.C.: World Bank).
- Kim, Dotae(1993), "Unification of Vietnam: A Case Study," Research Paper 93-14 (Seoul: Research Institute for National Unification).
- Kim, Kukshin, and Yujin Lee(1992), "A Plan for the Formation of a Korean Economic Community," Research Report 92-17 (Seoul: Research Institute for National Unification).
- Kim, Kukshin(1993), "Unification of Yemen: A Case Study," Research Report 93-19 (Seoul: Research Institute for National Unification).
- Korea Development Institute(1991), *A Basic Framework for Improvement in South and North*

- Korean Economic Relations* (Seoul: KDI Press).
- Kornai, Janos(1990), *The Road to a Free Economy* (New York: W.W. Norton).
- Lee, Jongsok(1995), "The Content and the Limitations of 'Our-Style Socialism'-- with a Focus on the Economic Effects of the One-and-Only System," *The Stagnation of North Korea's Socialist Economy and Its Responses* (Institute of Far Eastern Studies, Kyungnam University), pp.187-216.
- Lin, Ching-yuan(1989), *Latin America vs East Asia* (New York: M.E. Sharpe, Inc.).
- McKinnon, Ronald I.(1991), "Financial Control in the Transition from Classical Socialism to a Market Economy," *Journal of Economic Perspectives* 5(4): 107-122.
- National Unification Board(1992), *An Overview of North Korea, 1992* (Seoul: National Unification Board).
- Noland, Marcus(1995), "The North Korean Economy,"
- Park, Sunsong, and Jinuk Choi(1993), "The Evolution of Discussions on National Unification, 1945-1993," Research Report 93-30 (Seoul: Research Institute for National Unification).
- Park, Junghee(1963), *Country, Revolution, and I* (Seoul).
- Perkins, Dwight(1994), "Completing China's Move to the Market," *Journal of Economic Perspectives* 8(2): 23-46.
- Rosenstein-Rodan, Paul N.(1961), "Notes on the Theory of the 'Big Push,'" in *Economic Development for Latin America: Proceedings of a Conference Held by the International Economic Association* (New York: St. Martins), pp.57-67.
- Schonbohm, Jorg(1994), *Two Armies and One Nation*, trans. from German to Korean by Hanhong Lee et al. (Seoul: Republic of Korea Army Headquarters).
- Seo, Jaejin et al.(1993a), "A Comparative Analysis of Reform and Open-Door Policy under the Socialist System," Research Report 93-23 (Seoul: Research Institute for National Unification).
- Seo, Jaejin et al.(1993b), "A Comparative Analysis of National Power Trends Between South and North Korea," Revised Edition, Research Report 93-24 (Seoul: Research Institute for National Unification).
- Wellisz, Stanislaw(1991), "Poland Under 'Solidarity' Rule," *Journal of Economic Perspectives* 5(4): 211-217.
- Wolf, Thomas A.(1991), "The Lessons of Limited Market-Oriented Reform," *Journal of Economic Perspectives* 5(4): 45-58.
- Yu, Jiho(1994), "Problems after Yemen's Unification-- Focusing on Political and Military Issues," *Problems with Yemen's Unification*, Seminar Series 94-03 (Seoul: Research Institute for National Unification), pp.33-56.
- Yusuf, Shahi(1994), "China's Macroeconomic Performance and Management During Transition," *Journal of Economic Perspectives* 8(2): 71-92.