

**Inter-Korean Economic Relations -  
The Political Goals of Economic Engagement**

**By**

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Over a recent lunch discussion, an ardent liberal and critic of President George W. Bush exclaimed how foolish and futile it is for South Koreans to try to sell cars in North Korea. Of course, he was referring to *Pyonghwa* (Peace) Motor's investment in an automobile assembly plant west of Pyongyang. I countered, "The purpose is not simply to sell cars. The endeavor has a much longer term objective – using capitalism to transform a communist economy." Stunned, he admitted superficial knowledge of reality on the Korean Peninsula.

### **“Soft” and “Hard” Landers**

Frankly speaking, I do not fault him for his lack of knowledge about Korea related issues. Americans generally misunderstand South Korea's current policy of economic cooperation with North Korea. The same can be said of influential officials within the Bush Administration and most American journalists. Both rely heavily for their view of Korean issues on the interpretations of a small cadre of "Korea specialists." This group divides itself into either advocates of North Korea's "soft" or "hard" landing. During the Clinton Administration, champions of the "soft landing" were in the political ascendancy. They believe that North Korea could be transformed peacefully and gradually by engaging it diplomatically and economically.

Their antagonists eventually won the collective label "neo-conservatives," and achieved ascendancy when President Bush moved into the White House in January 2001. Ever since, they have dominated Washington's think tanks (the American Enterprise Institute, CATO, the Heritage Foundation and the Hudson Institute, National Endowment for Democracy, among others) and served as the Bush Administration's "brain trust." Generally speaking, they share the belief that North Korea was on the verge of collapse, economically and politically. Many also promote regime change in North Korea, i.e. a "hard landing," as the ultimate solution for the Korean Peninsula's woes.

### **Frustrated Expectations**

Throughout President Bush's first term in office, 2001-04, we often heard the president and his closest advisers voice the neo-conservative experts' catch phrase, "North Korea is a failed system on the verge of collapse." But such predictions have themselves failed to fulfill expectations. North Korea a decade later has not collapsed. On the contrary, it is making gradual but steady progress away from the brink of bankruptcy.

Rather than admit their shortcomings, the "neo-conservative experts" have sought to deflect attention away from their failed predictions. They have blamed North Korea's survival on international humanitarian aid, Kim Dae-jung's "Sunshine Diplomacy," President Roh Moo-hyun's policy of economic cooperation with Pyongyang, and China's extensive economic assistance. Recently they have become more vocal in accusing the North Korea regime's durability on "illicit trade" in counterfeit currency, illegal drugs and other international contraband. All the while, neo-conservatives have also sought to discredit their political adversaries by accusing them of having "appeased" Pyongyang, "rewarded its nuclear blackmail," and "propped up" Kim Jong Il's totalitarian regime

while ignoring the plight of North Koreans under his iron fisted rule. From this rhetorical approach has sprung such now famous phrases as “axis of evil” and “outpost of tyranny.”

### **Seoul’s “Neo-cons”**

South Korea’s proponents of the Kim Jong Il regime’s “hard landing” share much in common with their American counterparts. They too see themselves as “compassionate conservatives” intent upon democratizing North Korea by removing its totalitarian ruler. They harbor contempt for Kim Dae-jung’s “Sunshine Diplomacy” and President Roh Moo-hyun’s policy of economic cooperation because they believe these policies promote Kim Jong Il’s goal of regime survival. They, along with their American colleagues, have gone so far as to accuse Korean presidents Kim and Roh of being “pro-Kim Jong Il” and “pro-communists,” all labeled as “anti-American” Koreans who criticize President Bush’s approach to North Korea. .

All citizens share, in any democratic society, the right to criticize constructively their government’s policy for the purpose of making it more effective in promoting the national interest. Obviously, the debate over how to deal with North Korea has become too much a war of words, too little an exercise in constructive pragmatism. After all, both camps share the same goal – peace and stability in Northeast Asia and on the Korean Peninsula. The issue is how to achieve this shared goal, not how best to belittle one’s political and intellectual adversaries. The purpose of this essay is to elevate the current level of debate over the best strategy for dealing North Korea.

### **The Starting Point**

Inter-Korean economic relations are not a “for profit” commercial enterprise. President Roh Moo-hyun’s policy of economic cooperation with North Korea is primarily a political strategy for dealing with North Korea. His goals are no different than those of his predecessors, nor of South Korea’s primary ally the United States. He endeavors to sustain peace and stability on the Korean Peninsula by promoting South-North reconciliation while maintaining, with the United States’ assistance, a compelling posture of armed deterrence aimed at North Korea. His tactics for pursuing these goals, however, is the source of domestic political friction and strain in the US-South Korea alliance.

To better comprehend Roh’s goals and methods, we should view them in the broader historical context and the fundamental characteristics of international relations. Economic policy underlies the two primary strategies that democratic, capitalist societies have used since 1947 to deal with authoritarian communist societies. These strategies are either containment or engagement. Investment and trade are at the core of both strategies. Containment denies a government normal diplomatic intercourse and strives to impede its ability to conduct commerce in the international market for the purpose of undermining its political legitimacy and economic vitality.

## Containment verse Engagement

Containment and engagement were both formulated in Washington during the Cold War. The Democratic Administration of President Truman applied the strategy of containment to North Korea at the beginning of the Korean War. It was rooted in an idealistic and moralistic Christian approach to international relations. In the case of North Korea, it was deemed an illegitimate nation unworthy of diplomatic and commercial relations because of its invasion of South Korea. Containment also assumes that intense economic pressure will eventually compel any nation to succumb to the will of other nations. Truman rallied global support, centered in the United Nations, for an extensive regime of economic and diplomatic sanctions. His aim was to discredit and isolate North Korea diplomatically and commercially in the hope of undermining its government. Containment was reinforced by deterrence, a military strategy which relies on armed might superior to that of an adversary as to discourage an armed attack. South Korea during the Cold War understandably became an ardent practitioner of both containment and deterrence in its dealings with North Korea.

As a consequence of Truman's containment strategy, the People's Republic of China (PRC or "Red" China) and North Korea were labeled "an international outlaw," was denied international legitimacy and normal diplomatic relations. They were also excluded from most politically influential and economically potent international organizations. This included the United Nations, which denied it access to the UN Development Program and other economic development agencies, the World and Asian Development Banks, the International Finance Corporation (IFC) and the International Monetary Fund (IMF). Additionally, the United States imposed multiple layers of economic sanctions on North Korea, and urged its allies to do likewise. Most of these sanctions remain in place more than a half century after they were first imposed. "North Vietnam" was treated much the same way until it successfully and forcefully reunited Vietnam after 25 years of war.

But in 1972, the Republican Administration of President Nixon, on the advice of Secretary of State Henry Kissinger, initiated a new strategy. At the time it was commonly labeled "*rapprochement*." This is the antecedent of the engagement strategy which the Republican Administrations of Presidents Reagan and Bush applied to the Soviet Union and China during the 1980s. "Rapprochement" shares with engagement the same fundamental assumption – economic incentives can induce a government to comply with another government's wishes. This is exactly the opposite of containment which relies on the coercive tactic of denying one's adversary access to economic benefits. Concern for morality set aside. Instead, capitalism is used to penetrate a communist economic system and transform it gradually into a more open society which condones individual enterprise. But like containment, engagement also relies on deterrence to discourage an adversary from possible armed attack.

The Nixon Administration's initial aims in 1972 were:

- to induce China to distance itself from its primary ally the Soviet Union,

- to convince it to discard its hostility and isolation in favor of engaging the international community and,
- to induce China to transform itself into a respected and prosperous member of the world community.

American advocates of containment in 1989 contested former President Bush's continuation of engagement with China after the *Tiananmen* Square incident. The foes of engagement protested that China's immoral abuse of China's champions of democracy should not go unpunished. Then President Bush ignored his critics and instead intensified his diplomatic and commercial engagement of China. Consequently, the pace of China's opening to the outside world and economic transformation was hastened rather than retarded. China today is dramatically different from China just fifteen years ago.

### **Engagement and “*Nor Politic*”**

Initially, as the engagement strategy slowly opened China in the 1970s and 1980s, South Korea clung to containment for dealing with North Korea. Subsequently, for almost two decades, South-North Korea relations alternated between peaks of tension and brief periods of reconciliation. President Roh Dae-woo in 1988, however, decisively discarded containment in favor of engagement. He called his form of engagement “*Nor politic.*” He approached all communist states in the hope of isolating North Korea by enlisting its allies' participation in the 1988 Seoul Olympiad. His impressive success garnered South Korea respect around the world and greatly expanded its diplomatic and commercial relations with other nations. A surge of South Korean exports and investments followed, even including North Korea's most ardent supporters the Soviet Union and China. By 1992, Seoul had leaped ahead of North Korea militarily, diplomatically, economically and technologically.

Seoul's success may well have convinced Pyongyang's leaders to discard their preference for isolation and to launch their own form of engagement. This set the stage for a surge in successful South-North dialogue between 1990 and 1992. Washington played a supporting role while Seoul forged a series of “basic agreements” with Pyongyang. Seoul's efforts even contributed to Pyongyang's willingness to jointly enter the United Nations and to accept international inspection of its nuclear facilities.

But by 1992, the pace of engagement's success may have unnerved North Korea. In August 1992, Seoul and Beijing normalized their diplomatic and commercial relations. Pyongyang's leaders reacted with a profound sense of insecurity. While Seoul had won diplomatic relations with Moscow and Beijing, Pyongyang had failed to normalize relations with Washington and Tokyo, Seoul's primary champions. While Pyongyang was exposing its nuclear weapons development program to international inspection, Washington's nuclear umbrella over South Korea remained secret. Between 1992 and 2000, Pyongyang vacillated between isolation and engagement of the international community. Seoul under President Kim Yong-sam similarly alternated between containment and engagement.

## **“Sunshine Diplomacy’s” Bright Side**

President Kim Dae-jung moved assertively in 1998 to restore engagement as South Korea’s preferred strategy for dealing with North Korea. Journalists labeled his brand of engagement, “Sunshine Diplomacy.” This strategy shares with engagement the preference for diplomacy over confrontation, economic cooperation rather than rivalry, and humanitarian concern instead of animosity. The combination of these elements applied consistently finally convinced North Korea to respond positively to South Korea’s overtures. The huge cash payment, rumored to be as much as one billion US dollars, undeniably served as a significant enticement to get North Korea’s leader to agree to the first South-North Summit of 2000. At the same time, however, money alone could not have convinced North Korea to facilitate the first South-North Summit.

Ever since, the two Koreas have achieved greater progress toward reconciliation than they were able to do during the previous 50 years. This progress is not a consequence of money. Rather it has been nurture by an unprecedented array of successful joint South-North ventures. During the past five years, Koreans on both sides of the De-militarized Zone (DMZ) have engaged in various types of political and military dialogue. This dialogue has reduced tensions and clashes along the DMZ, and set the precedent for the resolution of differences through dialogue rather than armed competition. Economic integration is making gradual but steady progress. Trade continues to grow. During the first half of 2005, inter-Korean trade totaled USD 454.1 million, a 39.5% increase over the same period of 2004 (USD 305.8 million in commercial trade and USD 148.3 million in non-commercial trade). The Kaesong Industrial Park and the Mt. Kumgang Tourist project have convinced both sides to penetrate the DMZ with roads and eventually railroads. Humanitarian assistance has improved the quality of life for the North Korean people and facilitated person-to-person contact on a massive scale. An impressively diverse array of social and cultural exchanges remind North and South Koreans that they are all Koreans with a shared ancestry, history, culture and language.

## **The Dark Side of “Sunshine Diplomacy”**

But President Kim Dae-jung made a profound error that has almost discredited engagement in the eyes of Koreans. Prior to the June 2000 summit, he authorized the payment of at least US \$500 million, and possibly as much as US \$1,000,000,000 to the Kim Jong Il regime. When I visited Pyongyang three months after the summit, even North Korean officials complained that the payment was inappropriate. They claimed that none of the money went to the national treasury. Instead, these responsible and ranking officials told me that Party Secretary for International Affairs Kim Yong-sun and his cronies pocketed most of the money. Kim Yong-sun’s apparent action aroused North Korean leader Kim Jong Il’s suspicions about his possible rival’s intentions. Eventually, Kim Yong-sun died in an automobile accident, according to official reports.

Nevertheless, Seoul’s shortsighted reliance on cash payments to promote reconciliation eroded public support for President Kim and his “Sunshine Diplomacy.” The cash payments and North Korean leader Kim Jong Il’s failure to fulfill his pledge to visit

South Korea became rallying points for critics of engagement, both in Seoul and Washington. The ensuing political debate tarnished Kim Dae-jung's gains toward reconciliation and contested engagement's effectiveness. Kim's successor appears to have learned that payments in hard currency are not the most effective way to promote reconciliation, peace and stability on the Korean Peninsula, nor smooth relations with the United States. But President Roh's "economic cooperation" strategy has other, potentially equally counterproductive shortcomings.

### **Washington's Adopt Neo-containment**

When President George W. Bush assumed office in January 2001, he dismissed engagement's success and concentrated instead on its shortcomings. Bush promptly re-oriented his government's strategy from engagement to "neo-containment" of North Korea. Bush sought to secure the United States through assertive and decisive unilateral action, going so far as to rely on "preemptive" armed attack of those who posed a threat to the United States. He pushed aside multilateral diplomacy and the concept of collective security. The tragic "9/11" terrorist attack only seemed to convince him of the righteousness of his convictions. He determined that he alone could lead the assault on the "axis of evil" and pursue the war on terrorism. Others were "either with or against" the United States, and had to follow and support his campaigns, or become their target.

He dismissed North Korea as unworthy of diplomatic dialogue and faulted it for the 1994 US-North Korea Agreed Framework's collapse. Loudly he chastised Pyongyang for failing to fulfill its international commitments while threatening it and other members of his self-proclaimed "axis of evil" with a "pre-emptive" strategy of nuclear counter proliferation. President Bush also confronted then President Kim Dae-jung and urged him to cease "appeasing" North Korea, and subsequently urged Kim's successor Roh Moo-hyun to stop "pandering" North Korea. In Washington and Seoul, advocates of neo-containment inappropriately labeled President Roh's continuing preference for engagement as "anti-American."

Frankly speaking, however, President George Bush's neo-containment approach toward North Korea has failed to achieve substantive gains during the past four and one half years. Militarily and economically, North Korea today is stronger than when he entered the White House. His strategy of "pre-emptive counter proliferation" has failed to deter North Korea's development of nuclear weapons. If anything, one can argue that this strategy crystallized Pyongyang's conviction that it needed its own nuclear arsenal. The Bush Administration's refusal to engage North Korea in diplomatic dialogue has severely retarded progress in the Six Party Talks toward his avowed "peaceful diplomatic" solution. In short, achieving a peaceful, diplomatic solution to the nuclear problem without engaging in diplomacy is a contradiction. Nor has the Bush Administration's efforts to undermine North Korea's economic vitality achieved any concrete results. On the contrary, this strategy appears to have convinced China and South Korea to intensify their efforts to prevent North Korea's economic collapse.

## **South Korea's "New" Brand of Engagement**

Fortunately for Korea, and all of Northeast Asia, President Roh Moo-hyun has persisted in his government's preference for engagement of North Korea. This strategy is rooted in the South-North Joint Declaration of June 2000. Article 4 reads:

The South and the North have agreed to consolidate mutual trust by promoting balanced development of the national economy through economic cooperation and by stimulating cooperation and exchanges in civic, cultural, sports, public health environmental and all other fields.

At subsequent Inter-Korean ministerial meetings, the two Koreas formed the Committee for the Promotion of Inter-Korean Economic Cooperation "to discuss and implement various issues to expand exchange and cooperation in the economic area. While these and similar inter-Korean accords were reached during President Kim Dae-jung's era of so-called "Sunshine Diplomacy," they remain current today.

President Roh Moo-hyun, who succeeded Kim Dae-jung in the Blue House on February 23, 2003, has refined these accords' implementation with his "Policy of Peace and Prosperity" toward North Korea. He has set the ambitious goals of promoting Korea's unification and making the Korean Peninsula a hub for commerce in Northeast Asia. Toward these ends, he pledged that his economic program would promote reconciliation and cooperation with North Korea and other governments in the region. All the while, he cautioned, South Korea would maintain a potent defense posture, one obviously designed to deter North Korean armed confrontation.

### **On the Plus Side**

President Roh's policy of "economic cooperation" has achieved several laudable results. They have sustained Pyongyang's confidence in the sincerity of Seoul's efforts to promote national reconciliation. Also, this policy has nurtured Pyongyang's sense of security by demonstrating that Seoul is in fact asserting a significant degree of independence from President Bush's preference for what has been a much more confrontational and coercive approach to North Korea. At the same time, Roh's reliance on engagement has restrained Bush's ability to unilaterally pursue his "neo-containment" of North Korea, both in terms of economic sanctions and possible military action.

Also, President Roh's preference for engagement over containment has profoundly affected both the United States' and North Korea's approach to resolving the nuclear issue. As recently became evident, President Bush and North Korean leader Kim Jong Il have both felt compelled to adjust their respective strategies regarding the Six Party Talks. This process has taken one year of intense quiet diplomacy, but Seoul's patience persistence, in conjunction with China's collaboration, appears to have finally paid some dividends in the form of Washington and Pyongyang agreeing to halt their tension producing war of words and instead to demonstrate reciprocal flexibility to restart the Six Party Talks.



## **On the Minus Side**

The South Korean government, however, continues its struggle to find a balance between its nationalistic and unilateral impulses, and between “carrots and sticks” or “inducements and sanctions.” One of the most glaring shortcomings is its continuing preference for unilateral action rather than multilateral cooperation. This became blatantly clear during Unification Minister Chong Dong-yong’s meeting with North Korean leader Kim Jong Il. At the meeting he promised that South Korea would provide North Korea a huge amount of electricity, if and when it promised to discard its nuclear weapons. He did so in the hope of inducing North Korea to return to the Six Party Talks. Only after having met with North Korea’s leader did Minister Chong consult with the United States about the idea. Ranking Bush Administration officials termed the offer “creative” to avoid any appearance of friction between Washington and Seoul.

Seoul’s handling of the offer, however, demonstrated its preference for unilateral action and a lack of appreciation for the potential benefits of multilateral cooperation. By going first to Pyongyang, Seoul revealed its eagerness to minimize the risk of Washington’s opposition while also demonstrating its sense of political insecurity at home by striving to garner political credit for itself. Although North Korea has yet to respond to Seoul’s offer, Seoul has already loudly claimed, without any supporting evidence, that the offer helped convince Pyongyang to return to the Six Party Talks. On the other hand, had Seoul presented its offer in as part of a multilateral package in conjunction with Washington and Tokyo, the impact in Pyongyang arguably could have been both more profound and productive over the long run.

Similarly, Seoul continues to lavish inducements on Pyongyang while receiving marginal dividends in return. Every time a North Korean delegation attends talks with their South Korean counterparts, Seoul rewards Pyongyang with impressive amounts of “humanitarian aid.” In May, Seoul promised Pyongyang would soon receive 200,000 metric tons of chemical fertilizer for engaging in Vice Ministerial Talks. After Pyongyang send a Ministerial level delegation to Seoul a month later, the Roh Administration announced it would ship 500,000 metric tons of rice to North Korea. What these inducements have achieved concretely remains to be seen.

Meanwhile, such practices encourage Pyongyang to continue its “shopping chart” diplomacy. Every time it needs food, fuel, investment, etc., it refuses to engage in dialogue with South Korea or to stay away from the Six Party Talks. The more adamant Pyongyang’s refusal to remain aloof, the more inducements Beijing and Seoul put in its shopping chart. When North Korea decides it has achieved maximum gains in terms of commodities, etc. it returns to talks. Since June 2004, when North Korea last attended the Six Party Talks, China has greatly increased its investment in North Korea’s economy, improved selective sectors of its infrastructure, sustain the supply of most of its crude oil needs and substantial increased its imports of minerals and other commodities from its ally. Meanwhile, Seoul has likewise continued its substantial investment in the Kaesong Industrial Park, the Mt. Kumgang Tourist Project, and the provision of fertilizer, food, medicine and clothing.

Alas, the Roh Administration is struggling to demonstrate what it has gained in return. Pyongyang thus far has adroitly avoided giving Seoul anything durable, other than access to the Kaesong Industrial Park. North Korea has yet to restrain its development of nuclear weapons and ballistic missiles, to improve the quality of life for its citizens, to take steps to improve relations with South Korea's foremost allies, the United States and South Korea. Eventually, one can expect the people of South Korea to become disillusioned with Roh's "economic cooperation" strategy, unless it accomplishes concrete results in the near future.

In this regard, however, the Roh Administration appears to rely on Koreans' historical inclination to distrust superpowers, i.e. the United States and Japan, to deflect criticism at home away from himself and his strategies' shortcomings. Like President Bush, President Roh expects his allies to follow his lead and to support his strategy. When it serves his purposes, he is quick to cite either or both allies as the reason of his strategy's shortcomings. When North Korea remained reluctant to return to the Six Party Talks, despite Seoul's repeated inducements, the Roh Administration pointed the finger at the Bush Administration's rhetoric and inflexibility toward North Korea. Roh expects Washington and Tokyo to be flexible, when South Korea's wants to give Pyongyang "carrots," but tries to use his allies as "sticks" once negotiations resume. Understandably, this has produced friction between Seoul and its allies, something that Pyongyang has adroitly manipulated to receive maximum material gains from South Korea.

At the same time, Seoul has vacillated between Pyongyang and Tokyo. It wants Tokyo to be touch when dealing with Pyongyang, but then teamed up with Pyongyang against Japan when Dokdo Island again exploded as an issue. The Roh Moo Hyun Administration, like its predecessors since President Roh Dae-woo, has shifted from using shrill warnings about the "North Korean threat" to loud complaints about Japan's colonialism as a club to still its domestic critics.

Seoul's contradictory tactics in dealing with its allies impedes confronting North Korea with a united front consistent of South Korea, the United States and Japan. Instead, Pyongyang benefits by playing Seoul against Tokyo or Washington. This is a serious impediment to progress toward a peaceful diplomatic resolution of the nuclear and other issues to be negotiated in the Six Party Talks.

In short, the Roh Moo-hyun Administration, like the two previous administrations, has yet to firmly establish it's near and long term priorities, and to refine implementation of its engagement strategy toward North Korea. Unless it does this soon, public and ally support for its "economic cooperation" policy will wane, and along with it progress toward national reconciliation and the attainment of a peaceful, nuclear free Korean Peninsula.

### **Toward a Durable Peace**

Peace and stability on the Korean Peninsula is the cornerstone for peace and prosperity throughout East Asia. Northeast Asia today is at peace, and has some of the world's most

prosperous and dynamic economies. Ultimately, sustaining the region's peace and stability hinges on the Korean Peninsula's fate. Inevitably, the path to a durable peace requires Korea's unification. But abrupt unification, either via regime collapse or forced change, is not in the interest of Korea or its neighbors. It could mean political chaos, even civil war, and the possible undermining of the region's prosperity. On the other hand, gradual unification will remain a distant hope because it is certain to be a highly complex and contentious political process.

Koreans came to recognize this on the eve of the first South-North Summit in Pyongyang in 2000. Ever since, both Koreas have wisely focused on national reconciliation and economic cooperation and integration. Both sides appear to have agreed, after a tumultuous half century of confrontation, that economic engagement better promotes their common interests rather than rivalry, containment and confrontation.

Current South Korean government policy toward its former primary adversary has contributed substantially to Northeast Asia's continuing stability since the Cold War's end. But national reconciliation and a peaceful, diplomatic resolution of the Korean Peninsula's nuclear woes remains a distant hope. South Korea cannot expect to achieve either or both these goals without substantial help from its allies, the United States and Japan. As it strives to refine its engagement strategy and increase its effectiveness vis a vis Pyongyang, the government in Seoul would do well to consult and collaborate more closely with Washington and Tokyo. Otherwise, it could ultimately fail to achieve both its primary goals.