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**Inter-Korean Cooperation 2000-2008:
Commercial and Non-Commercial
Transactions and Human Exchanges**

by

Sabine Burghart and Rudiger Frank

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Introduction

Originally, this working paper was developed out of a small collection of numerical data on inter-Korean cooperation that we wanted to use in the context of another research project. We quickly found that while it was easy getting scattered information on this topic, it was surprisingly difficult to find updated numbers on all relevant subfields, such as trade, humanitarian aid, exchange of personnel etc. Journal or media articles are usually focused on a few specific areas, and broadly oriented books quickly become outdated. Access to databases tends to be restricted, and for many, there is the language barrier. So we thought that colleagues working on the two Koreas might find it useful if we shared the results of our data mining efforts and presented these in a handily available, compressed form posted online as a working paper.

Meanwhile, and to our surprise, this account of cooperation and exchanges has become much more than just a collection of numbers and dates. The change of the North Korea policy paradigm of the new administration in the Republic of Korea has added another reason of being to this paper. This data collection is a record of the tremendous developments during the past decade, starting from almost zero and having produced results such as a trade volume of US\$ 8.1 billion, tourism projects with 1.9 million visitors, an industrial zone with more than 30,000 workers and an output of US\$ 309.7 million, and a rapidly increased number of visitors from both sides.

This should not obstruct our view of the fact that what has been achieved so far is hardly enough, if the final goals are national unification, nuclear de-escalation, improvement of human rights and common prosperity. However, it would also amount to gross neglect to deny that the

past decade has seen dramatic changes as opposed to the past. The Sunshine Policy and its successor, the Policy for Peace and Prosperity, have occasionally been interpreted as naive. The opposite is true, as we would argue. In a way, they constitute the most vicious, aggressive and subversive policy vis-à-vis North Korea one could think of beyond a military attack.

Why is that so? Experienced scuba-divers know that air containers must never be emptied completely, since they need a minimum pressure to maintain their structural stability. In a way, North Korea is similar. The North Korean system is perfectly equipped, or actually built to resist the pressure stemming from open confrontation, demands for reciprocity, or attempts at outright manipulation. However, it is largely defenseless against seemingly unconditional aid from its adversaries. External pressure on the leadership in Pyongyang makes it stronger, helps to sustain the militarization of the North Korean society, and to justify conditions that remind of martial law. Selig Harrison (2002) called this the “rally-round-the-flag phenomenon”.

But it is much harder, if not impossible, to continuously decline aid that comes with no obvious strings attached. Few people would understand and back up such a policy. It is a widely prevalent misperception about autocracies that they can do without public consent. On the contrary, lacking the legitimacy granted by frequent elections, the leaders must either perform well or explain why their non-performance was still the best their people could expect. In some cases, propaganda and misinformation help. In other cases, fear can keep stability, at least for a while. But eventually, the temptation to accept unconditional aid gets too big for a country with such a malfunctioning economy as North Korea.

Refusing aid would arouse grumble among the masses. Crucially, this would not only be true for the suffering ordinary population of North Korea, but also for the largely invisible and underestimated, yet highly important enlarged leadership group, consisting of mid-level officials in government and party, military officers, and leaders of local communities. Once one accepts South Korean aid, it gets harder depicting the other side as poor and inferior; once contacts grow in number and intensity, it gets harder to explain that this is the enemy against whom one should defend at all cost. Everyone who has lived under socialism in Europe can confirm how this slow ideological poison spreads like cancer, how these cells grow and how they finally unfold their destructive, lethal power, hollowing out the system from within.

The North Korean leaders are perfectly aware of this danger; they have studied the Eastern European experience well but could do little against an opponent who reacted to provocations by sending even more presents. As Kim Jong-il said in 1995: "The most serious lesson of the collapse of socialism in several countries is that the corruption of socialism begins with ideological corruption...". There is reason to assume that the top leadership in Pyongyang released a deep sigh of relief after the election of a conservative President in South Korea in late 2007. Everything now seems to develop back to "normal". In fact, a worsened relationship with Seoul makes it even easier to have an improved relationship with the United States, since the last thing the North Korean leaders want is to run out of enemies, for adversaries are their and the Military First Policy's *raison d'être*.

There are many methodological challenges connected to the numbers that we have collected and commented upon. Obviously, dealing with North Korea is a political question. This does not mean that no

economic rationale exists; however, it is clearly subordinated to political considerations and constraints. This interplay of economic and political interests is very non-transparent, so that analysts at times have difficulties identifying causes and effects of observable actions. Repeatedly, the correctness of the numbers has been questioned.

Furthermore, the official classification of the single measures does not necessarily correspond with their actual nature. Unconditional aid is difficult to defend politically, as is payment for political rapprochement or for human rights improvements. Private companies can act on behalf of the state, as what Woo (1991: 179) has called "private agencies of public purpose". We were careful to avoid the many traps that these and other issues pose and hence have concentrated mostly on presenting the data and supplementing them with some context. We have deliberately refrained from drawing conclusions or developing a quantitative analysis based on these numbers. We hope, however, that this working paper will support other colleagues in doing exactly this: making sense of these numbers and helping us to better understand the relationship between the two divided Koreas. Important and heatedly debated contributions to this end have been made by Haggard and Noland (2007). Our understanding of North Korea would strongly benefit if such efforts at a professionalization of North Korea research were expanded further.

Ten Years of Engagement Policy in Korea

Since the inauguration of President Lee Myung-Bak on February 25th, 2008 the South Korean government's policy towards North Korea has undergone a drastic shift from the (seemingly unconditioned) engagement policies of Lee's predecessors, Kim Dae-jung and Roh Moo-hyun, towards a policy conditional on further progress in the denuclearization of the DPR Korea. Lee, who regards himself to be a pragmatic conservative, took office with the "Vision 3000" plan aimed at increasing economic growth in the DPRK and reaching a per capita GDP of 3,000 US\$ within the next decade – provided that tangible progress in the denuclearization is made (Lee MB 25.02.2008). So far, the ambitious policy goals have been thwarted and there are concerns that the policies pursued by the Lee government towards North Korea would lead to a setback in inter-Korean relations (Frank 2008). In addition, several incidents have challenged the process of inter-Korean cooperation: official visits between the two Koreas were halted, a production plant at the Kaesong¹ Industrial Complex (KIC) was shut down², and a South Korean tourist was killed by North Korean guards at the Mount Kumgang Resort on July 11th 2008. The rejection of the South Korean government's demand for a joint investigation by the North Korean authorities has led – until time of writing – to a suspension of the tours to the resort, and to the expulsion of South Korean staff.

¹ In this paper, the McCune/Reischauer method of transcription is applied (except for commonly used names and terms).

² According to Yonhap News, the South Korean factory shut down on 12 June 2008 due to a feud with the North Korean controller. Demands of the management to replace the controller were refused by the DPRK authorities (IFES 2008b).

Since national division and even more so the Korean War (1950-53), inter-Korean relations have been influenced by military threats, deep mistrust and domestic propaganda politics as well as great powers' geopolitical strategies. South Korea, a long-standing U.S. ally in East Asia, is in the difficult situation of being caught between various domestic and external interests. On the one hand, it depends on military deterrence provided by Washington, which shields Seoul not only from North Korea but also from other potential threats in the region and guarantees a certain degree of peaceful cooperation with the previous colonial master in Tokyo. Outbursts of nationalism related to territorial and history issues illustrate how fragile this relationship is. In addition, the South Korean economy becomes increasingly dependent on China but would not be able to exist without the decades-old close economic cooperation with the United States and Japan. On the other hand, South Koreans regard improved relations with the North as vital for their future, a certain decrease in unification enthusiasm notwithstanding. Analysts in Seoul have understood that unification will be very costly, and that it would be wise to pay these costs gradually in advance. They want to do so by raising the status of transportation and communication networks, industry and services closer to the South Korean level in a controlled fashion, rather than being faced with the herculean task of accomplishing all this within a limited period of time in order to avoid unrest, destabilization and massive migration after a possible collapse of North Korea.

The operating environment for implementing such a forward-looking strategy has been very complicated. The North Korean side has repeatedly disrupted the process by refusing to stop and dismantle its nuclear program. While one could ar-

gue that it would be naïve to expect Pyongyang to give away its only strong card, it is certainly difficult to argue in favor of continuous cooperation with a country that has gained such a disastrous international reputation. Serious human rights issues add to the problem and create ethical dilemmas. As a result, a number of international sanctions were issued, although their effects have been questioned (Frank 2006). The recent removal of North Korea from the list of state sponsors of terrorism points at a possible pragmatic change in U.S. policy, although its sustainability is not guaranteed.

In such an environment, it was particularly hard for the South Korean governments to adhere to their respective engagement policies. But against all these odds, inter-Korean dialogue and exchanges have developed remarkably since Kim Dae-jung's Berlin Declaration³. This paper reviews the development and current status of inter-Korean economic transfers and people exchanges. The first section analyses different forms of economic cooperation⁴ between the two Koreas, i.e. commercial and non-commercial transfers. Commercial transfers include general trade⁵, trade in processing on commission as well as transfers related to the economic cooperation projects (Kaesong Industrial Complex, Mount Kumgang Resort etc.). Non-

commercial transactions comprise humanitarian assistance, socio-cultural cooperation projects, and the KEDO light-water reactor project which was suspended in May 2006. The second section looks at the development of people exchanges at both the governmental and private level between 1995, when the DPRK appealed for international aid, and 2008, marking the shift from an unconditioned engagement policy towards a more conservative approach of containment. The conclusion gives a brief outlook on the further development of inter-Korean relations.

Inter-Korean Economic Exchanges – A Recap

The road towards the current status of inter-Korean exchanges has been a long and bumpy one. It took roughly fifty years for both Koreas to engage in high-level political dialogue and extended economic cooperation including (locally limited) investment projects. Although the first steps of cautious rapprochement were taken 37 years ago in 1971 under the impression of the Nixon shock, several efforts to reduce political and military tensions for the sake of confidence building measures on the Korean Peninsula ended up without tangible results. A certain breakthrough was reached after the collapse of socialism in the Soviet Union and Eastern Europe, which coincided with growing self-esteem in South Korea after two decades of successful development and the democratization process since 1987. In 1988, the Roh Tae Woo government unilaterally declared that it would promote economic exchanges with the North, issuing the *Special Declaration for National Self-Esteem, Unification and Prosperity*.

North Korea realized that it had to react, and agreed to separate membership of both Koreas in the UN. In 1992, the *Basic*

³ In the Declaration given by Kim Dae-jung in Berlin in March 2000, the former South Korean president formally renounced a unification policy aimed at absorbing the North. Kim stressed his administration's will to start inter-Korean economic cooperation.

⁴ For this paper the authors relied on documents and data from official South Korean sources such as the Bank of Korea, the Ministry of Unification, KOTRA and KITA.

⁵ In statistics provided by South Korean institutions, trade between the ROK and the DPRK is considered as intra-nation transfers. Instead of differentiating between imports and exports transfers are separated into "carry-in" and "carry-out" goods (Lim WH 2006:3).

Agreement was concluded, serving as the first institutional framework for inter-Korean trade. However, as the South was waiting for the North's collapse and the North explored the opportunities of nuclear blackmail and had to cope with the death of Kim Il-sung, through the mid-1990s, the relations between the two Koreas were characterized by minimal interactions going beyond the cooperation in the KEDO project. The development of inter-Korean economic cooperation can be divided into three major stages: 1989-1997, 1998-2002, and 2003-2007 (Lim SH 2007:10). During the first stage, economic cooperation consisted of general trade flows, and production orders from South Korean companies in the sectors of food processing, textile, and television assembly. In 1997, Hyundai initiated a relatively large-scale investment project at Mount Kùmgang. Until this moment, investment activities in the DPR Korea had been almost non-existent.

Despite public critique towards the Kim Dae-jung administration for having "bought" the meeting with the North Korean leader⁶, the first inter-Korean summit was held on 13-15 June 2000. It produced the *South-North Joint Declaration* and is still considered a milestone in inter-Korean relations (Kang 2007). With regard to economic cooperation, the politically highly symbolic event resulted in four major agreements⁷ aimed at easing business

activities. This second stage is characterized by increasing trade and humanitarian assistance due to a more favorable political, economic and legal framework.

With the construction of the Kaesòng Industrial Complex (KIC) since 2004, the third stage of inter-Korean economic cooperation includes direct investment in the DPRK by South Korean companies enjoying subsidies by their government. South Korean firms investing in the DPRK are exempted from paying taxes in the South. The second inter-Korean summit meeting held in October 2007 produced the *Declaration on the Advancement of North-South Relations, Peace and Prosperity* that includes a wide range of cooperation activities in the economic, social and cultural as well as humanitarian fields. With regard to the expansion of economic cooperation, both leaders agreed to create a "special peace and cooperation zone" in the West Sea, to complete the first-phase projects, and start construction of the second-phase at the KIC. Furthermore, infrastructure projects such as the modernization of the railway line between Kaesòng and Sinùiju, the highway between Kaesòng and Pyongyang, and the construction of shipyards in Namp'ò and Anbyòn were included in the agreement.

Although the engagement policies towards the North were labeled differently (Kim Dae-jung: *Sunshine Policy*⁸ and Roh Moo-hyun: *Policy for Peace and Prosperity*) they were more or less congruent and followed the same objective: to create a favorable environment for inter-Korean exchanges built on mutual trust and confidence. Both administrations were con-

⁶ The Kim Dae-jung administration faced allegations of having transferred US\$ 500 million to the North Korean leadership prior to the summit meeting. The money was transferred the DPRK government from the state-owned Korea Development Bank via the Hyundai group. Aides of the former South Korean president and Hyundai leaders were charged with bribery (Kirk 20.06.2003).

⁷ These include the Agreement on Clearing Settlement, the Agreement on Investment Protection, the Agreement on Procedures for Resolution of Commercial Disputes, and the Agreement on the Prevention of Double Taxation of Income. However,

the implementation of these agreements has been delayed by the DPRK authorities.

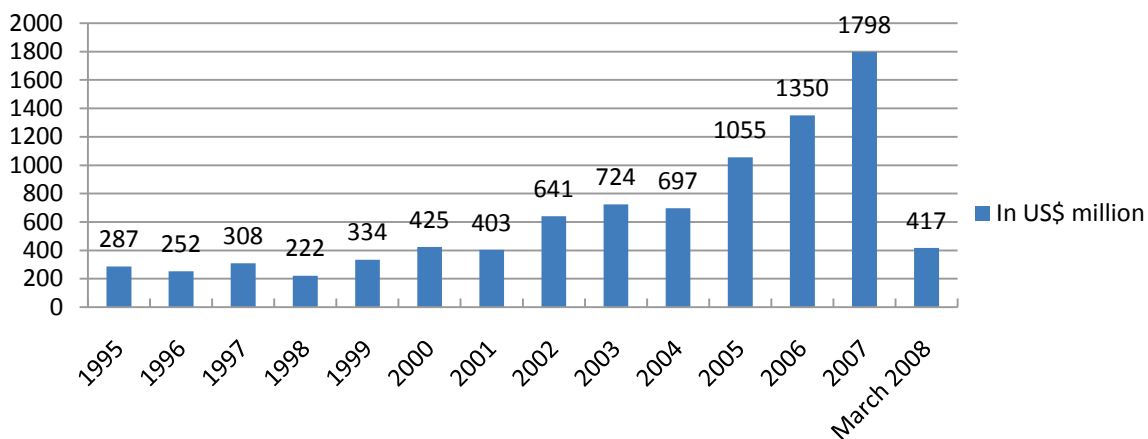
⁸ Referring to the fable of the Greek poet Aesop "The North Wind and the Sun", Kim Dae-jung argued that "sunshine is more effective than strong wind in making North Korea come out of isolation and confrontation" (Moon/Steinberg 1999:37).

vinced that continuous pro-active engagement with North Korea would promote economic reform, and facilitate the country's gradual integration into the international community and the world economy, eventually leading to peaceful Korean unification. The efforts of the South Korean leadership were not limited to inter-Korean affairs. Diplomatic persistency led other governments, for example the member states of the EU (with the exception of France) and the European Commission, to start diplomatic relations, and to engage in a dialogue with the DPR

Korea. Though on a relatively low scale, some European governments even actively supported capacity-building programs that were *de facto* projects of official development assistance (ODA).

The statement that the engagement policies had a certain impact is supported by empirical facts. Statistics show a significant increase of inter-Korean trade and people exchanges since the end of the 1990s. To put it in numbers, the value of transfers has steadily increased since 1995 from US\$ 287 million to US\$ 1,798 million in 2007 (Figure 1).

Figure 1: Inter-Korean Transfers (amount in US\$ million)



Source: Ministry of Unification (2008a): *Inter-Korean Exchanges and Cooperation*

It is also noteworthy that cooperation activities became more diversified, and increased at both the governmental and the non-governmental level. However, there is skepticism whether the “socializing effects” (Haggard/Noland 2008:20) of the engagement projects will spill-over to the rest of the DPRK’s economy. Acknowledging “considerable economic change” (Eberstadt 2008) in North Korea, critics of the *Sunshine Policy* argue that the South Korean government’s engagement policy failed because it had not stimulated economic reforms in the North, but instead

consolidated the power of the DPRK leadership. This highlights the major dilemma of economic cooperation with North Korea.

Facing a growing gap between the DPRK and ROK economy former South Korean policy makers have seen economic investment and assistance to the North as a means to stabilize and improve the economic situation in the country. Table 1 shows the South Korean estimates of North Korea’s Gross National Income, and the gap between both countries. In 2007, the estimated GNI of the DPRK amounted to US\$ 26.8 billion, which is about 36.4

times lower than the GNI of South Korea during the same year (US\$ 974.7 billion). The gap has been growing since 2000. In 2007, the per capita GNI in North Korea has been US\$ 1,155.6 or 17.4 times lower as compared to US\$ 20,120.4 in South Korea. Despite negative economic growth

in the DPRK for two consecutive years (2006, 2007), per capita GNI in the North has increased since 2000. Yet growth in the ROK has been even faster, widening the gap to factor 17.4 in 2007 from 14.3 in 2000 (all based on official South Korean estimates).

Table 1: The Development of the ROK and DPRK Economy, 2000-2007 (in US\$)

		2000	2001	2002	2003	2004	2005	2006	2007
GNI (in US\$ billion)	ROK (A)	509.1	484.4	554.9	609.3	687.5	793.1	900.2	974.7
	DPRK (B)	16.9	15.8	17.3	18.4	20.9	24.3	25.9	26.8
	A/B	30.3	30.6	32.2	33.1	32.8	32.6	34.8	36.4
GNI per capita (in US\$)	ROK (A)	10,909	10,230	11,654	12,735	14,309	16,474	18,635	20,120
	DPRK (B)	761.8	711.4	772.7	818.2	921.4	1059.4	1121.5	1155.6
	A/B	14.3	14.4	15.1	15.6	15.5	15.6	16.6	17.4
Growth rate (in %)	ROK	8.5	3.8	7.0	3.1	4.6	4.2	5.0	5.0
	DPRK	1.3	3.7	1.2	1.8	2.2	3.8	-1.1	-2.3

Source: The Bank of Korea (2008): 남북한의 주요경제지표 비교

Since the inauguration of the new president in South Korea, inter-Korean relations have, at least at the governmental level, dramatically cooled down. Recent trade statistics (Table 2) show a significant decrease of non-commercial transfers but also an increase of commercial transfers, suggesting that inter-Korean business is getting more independent from politics. As Foster-Carter puts it, both sides have been “careful not to let their current political quarrel prevent them from making money” (2008:3). However, we should not overlook that a large portion of commercial trade is trade on commission, i.e., semi-finished products that are exported to North Korea, processed there, and re-imported back to South Korea. Access for South Korean companies to North Korea is still heavily regulated by both sides, so making money by ordinary business transactions is still far away from being the only motive for participating in this kind of inter-Korean exchanges.

It is obviously too early to draw conclusions regarding the allegedly growing “immunity” of the business sector to un-

favorable developments in the political relations between the two countries. But it seems that, so far, (state-subsidized) business gained momentum. However, a further analysis of the detailed trade statistics, particularly data on trade in processing on commission would be necessary.

Indicating a certain return to a cooperative strategy after a rapid deterioration of bilateral relations since early 2008, President Lee has stressed in his speech at the opening of the 18th National Assembly on July 11th, 2008 that “full dialogue between the two Koreas must resume” (Lee MB 2008b). Lee also showed willingness to discuss about how to implement the summit agreements reached by his predecessors in 2000 and 2007. Related speeches have been given by the Minister of Unification. However, it remains to be seen whether the damage done by the attempts to pursue a hard line of strict reciprocity against North Korea during the first half of 2008 can be undone quickly.

Table 2: Commercial and Non-Commercial Transactions, January - June 2007 and 2008: A Comparison (in US\$ million)

	2008			2007		
	Commercial Transfers (change in %)	Non-commercial transfers (change in %)	Total Change (in %)	Commercial transfers	Non-commercial transfers	Total
January	134.3 (+50.9)	6.2 (+64.6)	140.5 (+51.5)	88.9	3.8	92.7
February	114.3 (+46.2)	4.6 (+12.8)	118.9 (+44.6)	78.2	4.0	82.2
March	150.3 (+60.3)	7.6 (-18.7)	157.9 (+53.1)	93.7	9.4	103.2
April	133.1 (+54.6)	11.2 (-76.1)	144.2 (+8.6)	86.1	46.8	132.9
May	153.1 (+46.1)	19.6 (-58.4)	172.7 (+13,7)	104.8	47.1	151.9
June	138.5 (+29.6)	7.9 (-83.5)	146.5 (-5.6)	106.9	48.4	155.2

Source: Ministry of Unification (2008b): Overview of Inter-Korean Exchanges and Cooperation

Table 3: Trade and Commercial Transfers between South and North Korea (in US\$ million)

Year	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
*Total Trade⁹	222	333	425	403	642	724	697	1,056	1,350	1,798
Exports (ROK -> DPRK)	130	212	273	227	370	435	439	716	830	1,033
Imports (DPRK -> ROK)	92	122	152	176	272	289	258	340	520	765
**Commercial trade (total)	n/a	n/a	265	244	355	425	437	690	928	1,431
Exports (ROK -> DPRK)	n/a	n/a	n/a	n/a	n/a	n/a	n/a	350	410	666
Imports (DPRK -> ROK)	n/a	n/a	n/a	n/a	n/a	n/a	n/a	340	518	765

Sources: *Total Trade (Data 1998-2004): Ministry of Unification (2004); (Data 2000-2006): Bank of Korea (2007:10); (Data 2007): KOTRA (2008)

**Commercial Trade (Data 2000-2006): Ministry of Unification; (Data 2007): KOTRA (2008)

⁹ Including commercial and non-commercial transactions between South and North Korea;

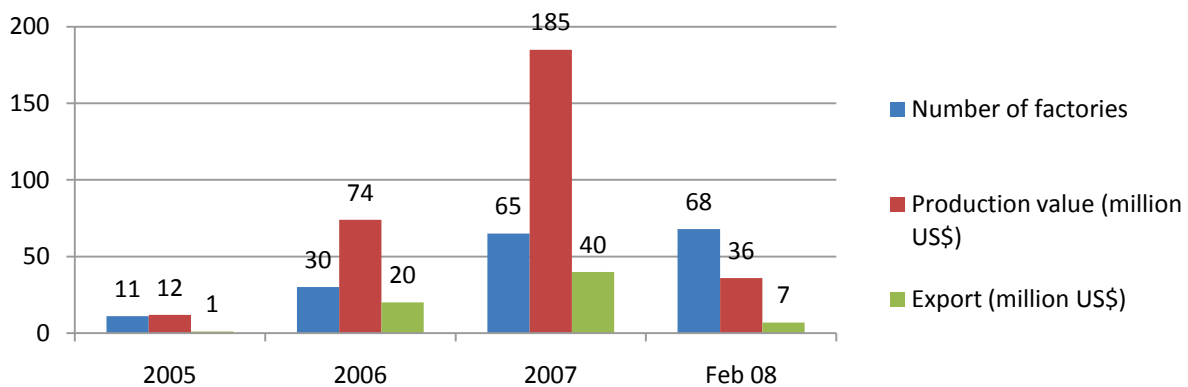
Commercial Trade

Inter-Korean business projects are gaining ground, as is evidenced by the steady increase of commercial transfers during the last decade. With the establishment of the Mt. Kùmgang tourism zone in 1998, the Kaesòng Industrial Complex (KIC) in 2004, and other smaller cooperation projects commercial trade has increased by 552 percent between 2000 and 2007, as Table 3 shows. Note, however, the conspicuous difficulties we had with finding data for trade that go beyond cumulative numbers

for total trade. Especially in the case of commercial trade, we were not able to do so for most of the past ten years despite sincere efforts.

The currently most prestigious inter-Korean economic project that creates the major increase of commercial trade is the KIC. Apart from the sector of light industry, smaller investment projects can be found in the mining and fishery industry.

Figure 2: Number of Factories and Production at KIC



Source: Ministry of Unification (2008a): *Inter-Korean Exchanges and Cooperation*

Kaesòng Industrial Complex (KIC)¹⁰

Covering an area of more than 350 hectares or 3.5 km², almost half of the first development stage of the complex was completed by the end of 2007¹¹. Whereas

11 South Korean companies were operating in the special economic zone in 2005, the number of production plants increased to 72 in July 2008. However, it must also be noted that some companies had to close shop in that same period. Goods such as textiles, cosmetics, chemicals, semi-conductors and cable loops produced at the KIC were worth a total of US\$ 309.7 million as of the end of February 2008. Particularly, small and medium-sized South Korean companies are investing in the KIC which is also open to foreign investors. In March 2008, the German car parts manufacturer Prettl began the construction of a plant, becoming the first non-Korean company investing at the KIC.

¹⁰ The construction of the Kaesòng Industrial Complex (KIC) was agreed upon during the first inter-Korean Summit in 2000, and started in 2004. Production began in 2005. The KIC operated by private Hyundai Asan (construction) and the state-owned Korea Land Corporation (design, leasing, and operations) is located 10 kilometers north of the Demilitarized Zone, and 70 kilometers from Seoul.

¹¹ The construction of the first development stage (2003-2010) has been delayed due to critical political developments (e.g. DPRK's missile tests, nuclear test). In October 2007, the construction of the infrastructure facilities was completed.

Prettl is expected to begin operations by spring 2009, when it will be employing more than 500 North Koreans (IFES 2008a). According to South Korean sources, two Chinese companies have also signed contracts to start production at the Complex (ibid).

As of July 2008, 30,084 North Koreans were employed in the KIC (MoU 2008a). The majority of them are women who are mostly working in factories and to a smaller number in infrastructure projects. The minimum monthly salary of US\$ 57.50 was increased by 5 percent in 2008 to US\$ 60.375; overtime is paid extra. The U.S. government and the EU have criticized that the North Korean employees are not paid directly by the companies. Instead, their salaries are transferred to the Central Special Direct General Bureau (CSDGB, 중앙특구개발지도총국), a cabinet-level administrative organization and constitute a growing source of income for the North Korean government. The CSDGB pays the workers in North Korean Won at the official exchange rate after deducting US\$ 7.50 for social security and other insurances. The 1,300 South Koreans at the KIC work mainly at the managerial level of the factories. On 16 March 2008, the South Korean government announced the introduction of special corporate tax benefits for companies that sign agreements for original equipment manufacturer products with firms in the KIC (IFES 2008a). Despite the government's efforts to promote investment in the KIC by providing financial incentives to companies, potential investors are still hesitant because of political uncertainties and unsolved legal problems. For investors, the issue of dual-use items and logistical shortcomings (infrastructure, energy supply, transportation) are of concern (Lim EC 2007:89-90). For example, due to the restrictions imposed

by the Wassenaar Arrangement¹² it is almost impossible to bring strategic materials into the KIC.

Furthermore, goods produced in the KIC are defined as products "Made in North Korea" on which high import tariffs are imposed, making many KIC products much more expensive, and therefore less competitive on the world market¹³. When negotiating the Free Trade Agreement with the United States (KORUS-FTA)¹⁴, the South Korean government tried to include goods produced in the Kaesong Industrial Complex but, so far, without success. Thanks to government subsidies and low wages, business opportunities for South Korean small and medium-sized companies are attractive, and opportunity costs (with regard to investment in China and Vietnam) apparently low.

The expansion of the KIC depends not only on the creation of an investment-friendly environment but is also a question of political will. The Lee administration declared that the improvement of the human rights situation in the DPRK was a precondition for the expansion of economic projects, in particular of the KIC's next development phase (Kim KS 2008).

¹² The Wassenaar Arrangement on Export Controls of Conventional Arms and Dual Use Goods and Technologies prohibits the export of dual-use goods and technologies to the DPR Korea.

¹³ As North Korea does not have Most Favored Nation (MFN) status, the U.S. imposes a 100% tariff on imports from North Korea.

¹⁴ The FTA was concluded in April 2007 between the United States and South Korea but – until time of writing – has not been ratified.

Mount Kùmgang Resort

Another major source of income and foreign currency for North Korea¹⁵ is the Mount Kùmgang Resort, also operated by Hyundai Asan. The decision of developing the Kùmgang Mountain area into a tourist destination was taken in 1998, and by March 2008 a total of about 1.8 million tourists had visited the resort¹⁶. After the opening of the land route that facilitates the access to the area, in 2003, the number of tourists using the new route increased by 778 percent (almost 8 times) in 2004. Since 2007, private cars of South Korean tourists are also allowed in the zone.

Table 4: Number of Mt. Kùmgang Tourists

Year	Number of tourists	By ship ¹⁷	By bus/private car
1998	10.554	10.554	-
1999	148.074	148.074	-
2000	213.009	213.009	-
2001	57.879	57.879	-
2002	84.727	84.727	-
2003	74.334	39.902	34.432
2004	268.420	449	267.971
2005	298.247	-	298.247
2006	243.446	-	243.446
2007	345.006	-	345.006
March 2008	62.405	-	62.405
Total	1.797.101	554.594	1.242.507

Source: Ministry of Unification (2008a): *Inter-Korean Exchanges and Cooperation*

¹⁵ Until August 2006, a total of US\$ 456.92 million were transferred to North Korea in form of entrance fees. (Lim WH 2006:14).

¹⁶ In addition, almost 100,000 tourists have visited the Kaesòng Industrial Complex (Korea Times 05.10.2008).

¹⁷ Until 2003, the area was only accessible by ship and tour prices were relatively high.

Visiting Mt. Kùmgang Resort allows South Koreans to get a glimpse of North Korea although free movement outside the official routes is restricted and contacts with North Korean employees in hotels, restaurants and shops are limited. These are well trained for the encounter with South Koreans, but experience from former European socialist countries suggests that such contacts would nevertheless have lasting effects. However, this possible source of change has dried out since after the shooting incident¹⁸ in July 2008, tours to Mt. Kùmgang have been suspended. The South Korean employees were expelled by the North Korean authorities. Long-term observers have also criticized that the tourism project has limited the access of North Koreans to the area.

Non-Commercial Trade

Non-commercial transactions between South and North Korea include, as mentioned above, transfers for the suspended KEDO light-water reactor project, humanitarian assistance and socio-cultural cooperation projects such as family reunions.

KEDO

Although the KEDO project has meanwhile been terminated, it is worth mentioning because the financial support contributed to the project constitutes a major part of non-commercial transfers to the DPR Korea in the past decade.

The Korean Peninsula Energy Development Organization (KEDO) was established by the U.S., Japan and South Korea in March 1995, and served as a vehicle to

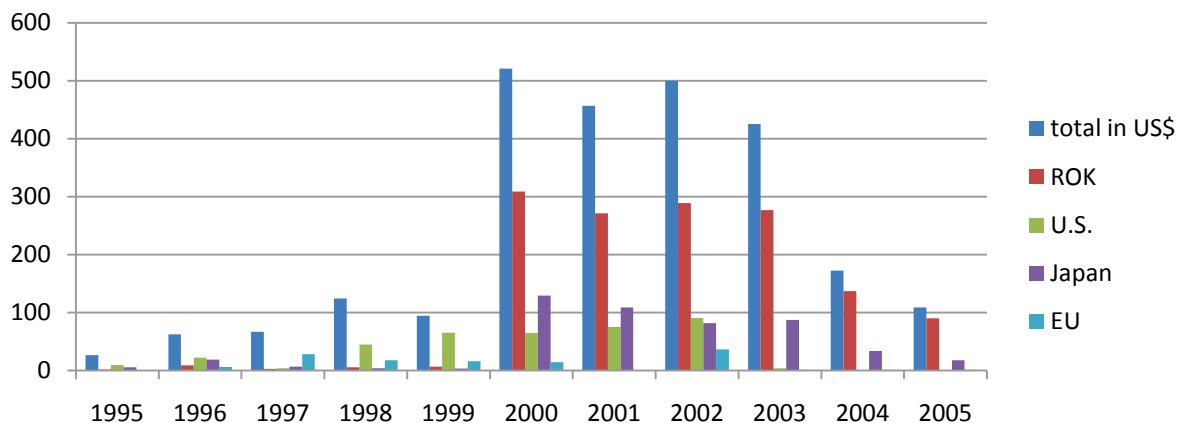
¹⁸ On 11 July 2008, a South Korean woman who had entered a military zone at the Mount Kùmgang area was shot and killed by a North Korean soldier (Lee JJ / Herskovitz 2008).

implement energy-related projects in the DPRK after the Framework Agreement between the U.S. and the DPR Korea was signed in 1994. The EU joined as a KEDO board member and provided about 10% of the KEDO budget.

In exchange for the freezing of older nuclear facilities that could produce weapons-grade plutonium, the international consortium agreed to build two light-water reactors (LWR) to compensate for the loss of energy production. To bridge the gap between freezing and the operation of the new power plants, North Korea would receive 500,000 metric tons of heavy fuel

oil annually as an alternative source of energy until completion of the project. South Korea, the U.S. and Japan were the largest financial supporters of the LWR-Project. The EU, represented by the European Atomic Energy Community (EAEC), joined KEDO in 1997. Contributions provided by EU member states amounted to about 10% of the KEDO budget. Various other countries also provided financial support to KEDO. Between 1995 and 2005 KEDO members contributed a total of US\$ 2.5 billion.

Figure 3: Financial Support of South Korea, Japan, the United States and the EU to KEDO (in US\$ million)



Source: KEDO (2005): Annual Report 2005

The largest individual share of the total costs of the LWR-project, about 55 percent, was borne by South Korea. In November 2002, KEDO's Executive Board decided to suspend the supply of heavy fuel to North Korea after the DPRK's engagement in an undeclared uranium enrichment program was reported (KEDO 2008a). The decision of the Executive Board to terminate the light water project on May, 31 2006 was "based on the continued and extended failure of the [...] DPRK to perform the steps that were required in the KEDO-DPRK Supply Agree-

ment for the provision of the LWR project" (ibid). It has to be noted that from early on there was fierce resistance in the U.S. government against the project. Especially after it became clear that North Korea would not collapse anytime soon as had been expected upon conclusion of the agreement, the new Bush administration showed little enthusiasm to keep KEDO intact¹⁹.

¹⁹ Based on off-the-record conversations of R. Frank with KEDO executives and high-ranking U.S. officials.

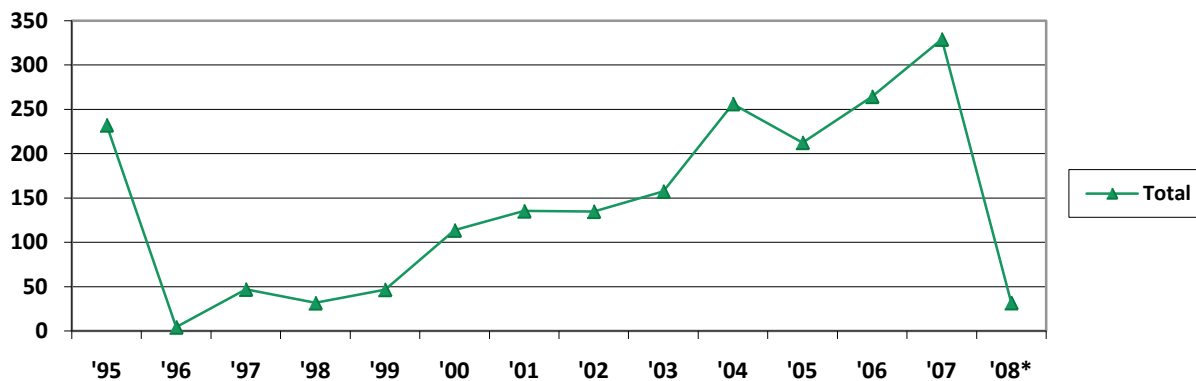
In the February 13 (2007) Agreement reached between the U.S., the DPR Korea, Republic of Korea, China, Japan and Russia within the framework of the six-party talks, the provision of light water reactors to the DPRK in exchange for denuclearization has not been mentioned. Recently, old plans are being resuscitated of providing energy compensation to North Korea in the form of natural gas through pipelines from Russia. The benefit would be obvious; in case of noncompliance with its commitments, North Korea could almost instantly be punished by cutting it off the gas supply. It is to be expected that Pyongyang will object for exactly this reason.

Humanitarian Assistance

Since the DPRK government's aid appeal at the United Nations in 1995 the South

Korean government has been sending food, fertilizer, construction materials and other items to the country. According to recent data from the ROK's Ministry of Unification, as of April 2008, the total assistance provided by the South Korean government and the private sector reached US\$ 2.82 billion, including food loans. The former political leaders of South Korea had emphasized that the provision of humanitarian aid to North Korea was based on a humanist decision delinking inter-Korean developments and political claims from the humanitarian cause. The new administration announced to continue in this respect. President Lee Myung-bak pointed out that the "Korean Government is ready to cooperate in efforts to help relieve the food shortage in the North as well as alleviate the pain of the North Korean people" (Lee MB 2008b).

Figure 4: Humanitarian Assistance Provided by South Korea to North Korea (in US\$ million)



Source: Ministry of Unification (2006; 2007)

*January to June 2008

Figure 4 shows that the volume of humanitarian aid has steadily increased since 1996 (with the exemption of 1995 when assistance reached almost US\$ 250 million as emergency aid during the famine). The sharp decline of the aid volume in the first months of 2008 illustrates the policy shift in the Lee administration with regard to its engagement in North Korea. One could

also conclude that successfully following a diversification strategy, the DPRK government can meanwhile rely on other international actors (governments, international agencies, NGOs etc.) that are willing to provide humanitarian aid to the country. While international aid was channeled through UN agencies such as the World Food Program (WFP), shipments from

South Korea including donations from both the government and non-governmental organizations were often directly sent to the DPRK and distributed by the North Korean authorities. This process was criticized by UN agencies and donor countries, especially the U.S., because of a lack of transparency and accountability, leading to the assumption that South Korean aid which was aimed to support the most vulnerable groups of society was diverted to the military or sold

on markets (for a discussion see Frank 2005c).

Table 5 shows that the ROK government's assistance was accompanied by an increase of private aid. Under the presidency of Kim Young-sam, private aid to the DPRK constituted about 7.9% of the total aid. Its share increased to 27.7% between 1998 and 2003 (Kim Dae-jung government). During the Roh administration, private aid contributions were worth US\$ 432 million, an increase by 44% compared to the previous period.

Table 5: South Korea's Humanitarian Aid to North Korea (in US\$ million)

Level	Administration in ROK			Total
	Kim Young –sam (1993-1998)	Kim Dae-jung (1998-2003)	Roh Moo-hyun (2003-2008)	
Government	261.72	499.77	1,402.53	2,164.02
Private	22.36	191.25	432.46	646.07
Total	284.08	691.02	1,835.00	2,810.10

Source: Ministry of Unification (2008c): *Humanitarian Cooperation: Facts and Figures*

Initially, there were attempts to channel private aid (particularly, under the presidency of Kim Young-sam) but the democratic governments “did not try to prevent civil society organizations from helping starving North Koreans” (Smith 2005:201). Although the National Security Law²⁰ (NSL, 국가 보안법) still limits many forms of private engagement with the DPR Korea, by the end of President Roh's term, private aid contributions to the DPR Korea were worth a total of US\$ 646 million.

Among the most prominent South Korean non-governmental organizations involved in inter-Korean humanitarian projects is the Korea National Red Cross. The organization has also played an active role in the negotiations and arrangement of family reunions. Negotiations between the Red Cross Societies of both Koreas led to the first exchange of hometown visiting groups held in October 1985. Official, i.e. government-level contacts were resumed in May 1997 to discuss relief assistance and the issue of separated families. The first shipments of relief aid arrived in the North shortly afterwards.

Exchange of people

As we have seen, the ROK's administration's engagement policies resulted in an increase of inter-Korean contacts and exchanges in various areas and on different

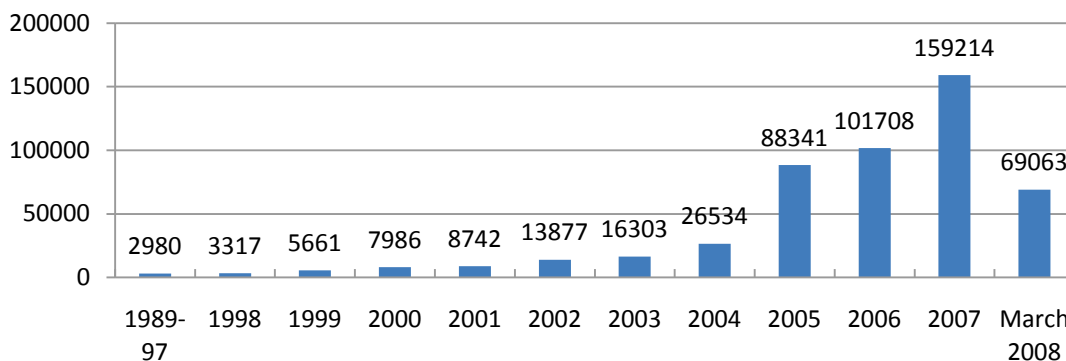
²⁰ The NSL bans South Korean citizens from having unauthorized contacts with the DPR Korea, and penalizes failure to report such contacts. Human rights organizations such as Amnesty International and Human Rights Watch have been criticizing the NSL as violating the rights to freedom of expression and association, i.e. fundamental human rights. The NSL with the often vaguely defined terms of “praising” or “benefiting” North Korea was used by former South Korean governments to imprison political opponents like Kim Dae-jung (AI 1999:2-3).

levels: governmental, semi-official and private. Despite limitations set by the NSL, people exchanges between the two countries have been increasing since the end of the 1990s. Since all non-governmental organizations and business corporations are required to report any form of contact with and activity in North Korea to avoid legal consequences, information about semi-official and private contacts as provided in Figure 5 seems relatively reliable.

Between 1989 and March 2008, more than half a million people crossed the border at the DMZ (Demilitarized Zone) for official and semi-official reasons (not including the number of South Korean tourists visiting Mount Kùmgang, Kaesòng or Pyongyang, which was another 1.9 mil-

lion people. Compared to the first quarter of 2007 the number of cross-border visitors increased by 182 percent to 69,063 in the same period of 2008. Not surprisingly, the number of South Koreans visiting the DPRK is much higher than the number of North Korean visitors to the South. In the first quarter of 2008, 69,033 South Koreans and only 30 North Koreans crossed the DMZ. Doing business in the KIC and being involved in other investment projects has led to the relatively huge number of South Korean visitors in the DPRK. Furthermore, since 2002, family reunions have been taking place at the Kùmgang Resort where the construction of the reunion center for separated families is almost completed (MoU 2008c).

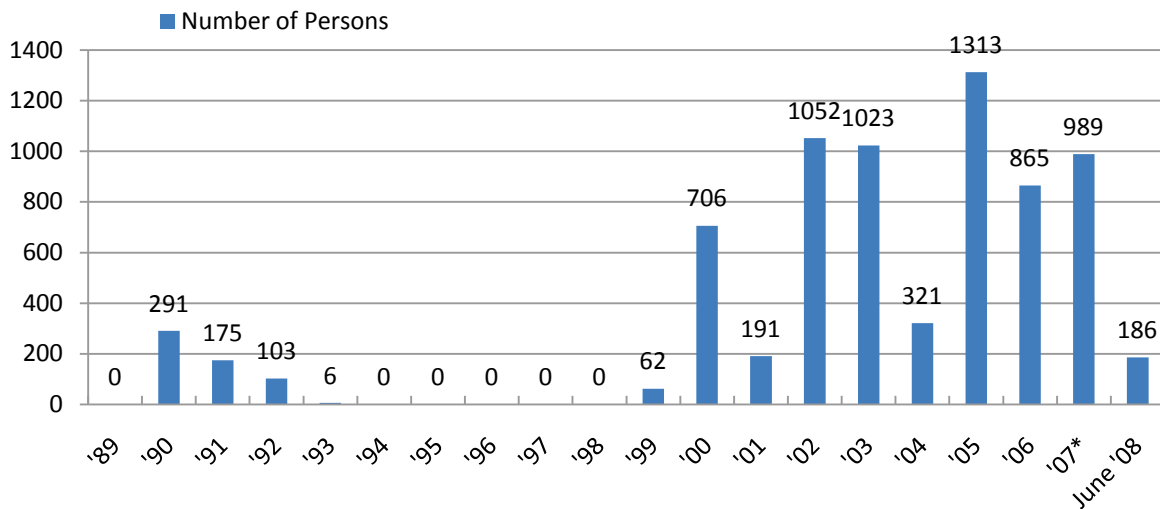
Figure 5: People Exchanges between South and North Korea



Source: Ministry of Unification (2008c): *Humanitarian Cooperation: Facts and Figures*

Although the number of cross-border visitors from the DPRK still constitutes a minor part of the total number of people exchanges it has been increasing within the last decade, as table 10 shows. Typi-

cally for socialist autocracies, travel regulations for DPRK nationals are already very strict in general; cross-border activity with South Korea is viewed with particular suspicion by the Pyongyang leadership.

Figure 6: Visits by North Koreans to South Korea

Ministry of Unification (1989-06/2008): Statistics (2007*: January-November)

Travel purpose for DPRK visitors was the participation in joint sport events, technical training in the framework of humanitarian aid programs, training in economics, cultural events, and in family reunions (until 2001). In the first half of 2008, the visits of 154 DPRK nationals to South Korea were related to inter-Korean trade affairs, which is 82 percent of the total number of visits in the same period. Cross-border visits and interactions with the other side allowed citizens of both parts of the divided Peninsula to form their own view about the neighboring country. A great number of South Koreans were able to gain first-hand information about the North. Smith argues that “[t]his intensified interaction contributed to a reformulation of a national attitude toward the DPRK” (2005:203).

Government-level talks

Government-level political and humanitarian talks between the two Koreas have been taking place since 1971 on a more or less regular annual basis, and there has been a number of social-cultural exchanges between 1971 and 1991, starting

with the inter-Korean Red Cross talks (KDI 2008: 40).

Whereas more than 135 political talks between South and North Korea were held between 1988 and 1994²¹, the number decreased to roughly 78 meetings between 1997 and 2008. Regular economy-related²² and military talks took place only since 2000.

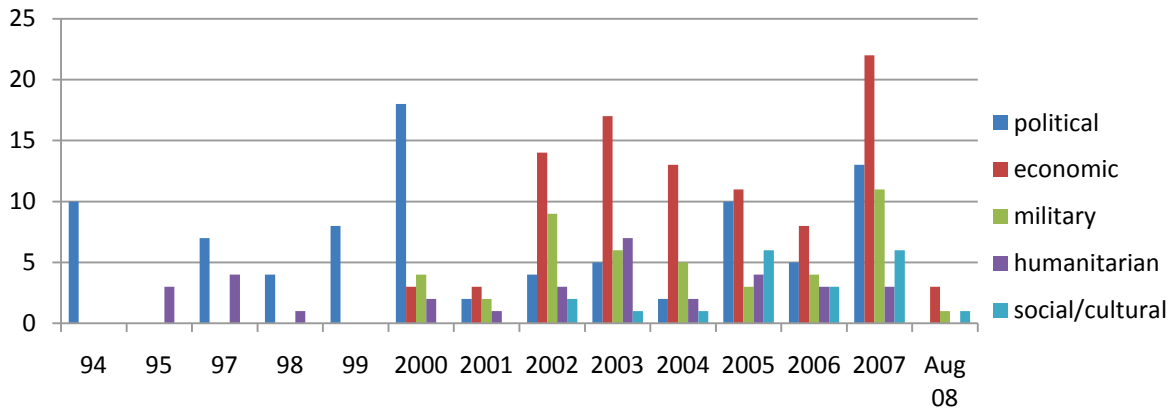
The partial increase in quantity and diversity of inter-Korean government-level meetings supports the argument that the South Korean government’s engagement policy towards the North has paid off. One could assume that without confidence-building measures the in total more than forty military-level talks and almost one hundred economy-related meetings would not have been possible. The effectiveness of these talks can be debated; however, given the lack of other contacts with North Korea, their very existence can be seen as

²¹ With a total of 88 inter-Korean talks (80 political, 8 humanitarian) the year of 1992 when the Agreement on Reconciliation, Nonaggression, and Exchanges and Cooperation Between South and North Korea was signed can be seen as an exception.

²² There were one and four economy-related meetings in 1984 and 1985, respectively.

having an intrinsic value, providing both sides with information that otherwise would not have been available.

Figure 7: Number of Inter-Korean Government-Level Talks (1994-2008)



Source: KDI (2008): *북한경제리뷰*, p.40

Family reunions

According to the (South) Korean Red Cross, more than 10 million Koreans have been living separated from their family members since the beginning of the Korean War. The issue of separated families served as a vehicle for inter-Korean rapprochement and was addressed at the inter-Korean Red Cross talks in August 1971.

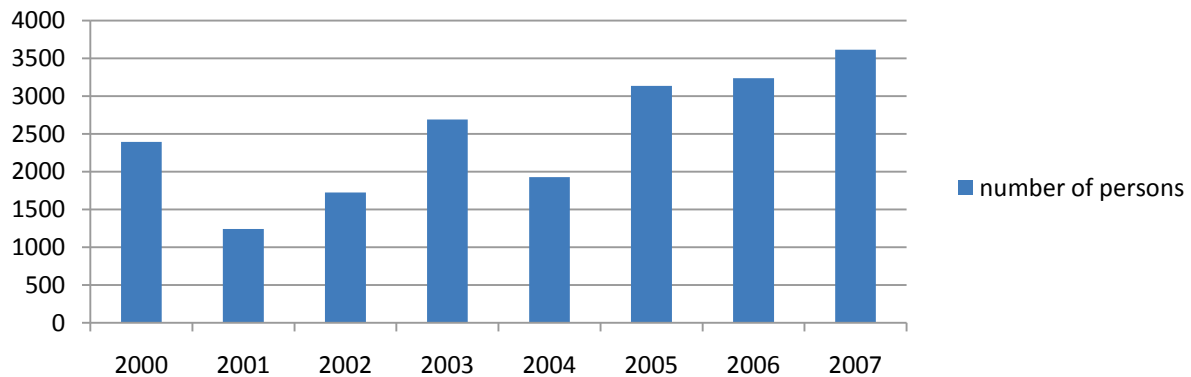
Fourteen years of negotiations on (temporarily) reuniting separated family members eventually led to the first exchange of hometown visiting groups held in October 1985 when 35 South and North Koreans visited their family members on the other side of the border. Since then, twenty-two more rounds of face-to-face and video family reunions with almost 20,000 participating persons were held in North and South Korea²³. Since 2000, more than 16,000 Koreans were given the chance to meet their relatives on the other side. On

17-22 October 2007, 396 South Koreans and 97 North Koreans participated in the, so far, last meeting at Mount Kumgang.

To facilitate the reunions of family members, and considering the advanced age of the participants, the scale and time limitations of the face-to-face reunions, so-called video reunions were introduced in 2005. These meetings are video conferences that take place in reunion centers at the Headquarters of the South Korean Red Cross and its branch offices and the reunion center in North Korea.

Until August 2008, seven rounds of video reunions were conducted. This version of a family reunion accommodates the security concerns of the North Korean authorities and hence has not been without criticism. In a video conference, the interaction between the families is easily controllable and direct contact is avoided. Supporters have argued that this procedure increases the number of such contacts and takes the physical state of the mostly elderly participants into consideration

²³ Since 2002, family reunions have been held in the DPR Korea.

Figure 8: Number of Reunited Family Members in Face-to-Face Reunions and Video Conferences

Source: Ministry of Unification (2008c): Humanitarian Cooperation: Facts and Figures

Table 6: Number of Participants of Face-to-face Family Reunions and Video Conferences (1985, 2000-2007)

Method of Reunion	Participants from ROK (number of families)	Participants from DPRK (number of families)	Total
Face-to-face (16 rounds)	10,673 (1,683)	5,539 (1,695)	16,212 (3,378)
Video conference (7 rounds)	2,257 (279)	1,491 (278)	3,748 (557)
Total	12,930 (1,962)	7,030 (1,973)	19,960 (3,935)

Source: Ministry of Unification (2008c): Humanitarian Cooperation: Facts and Figures

Table 7: Age of South Korean Applicants

	90 years and older	80-89 years	70-79 years	60-69 years	59 years and younger	Total
Number of persons	3,588	27,618	36,885	14,647	8,653	91,391
Percentage	3.9	30.2	40.4	16.0	9.5	100

Source: IICSF (2008)

Table 8: Relationship of Applicants to Family Members in the DPRK

	Couples/Parents/Children	Brothers/Sisters	3 rd degree	Total
Number of persons	43,810	36,029	11,962	91,801
Percentage	47.7	39.2	13.1	100

Source: IICSF (2008): [이산가족정보통합 센터] 신청자료 현황

The number of reunited family members constitutes only a small part of the general estimates about the persons concerned, which is provided by the Korean Red Cross.

According to the *Integrated Information Center for Separated Families* (IICSF, 이산가족정보통합센터)²⁴, it has received 127,285 applications for family reunions between 1988 and August 31st, 2008. Meanwhile 35,483 applicants died, leaving 91,801 South Korean nationals waiting to meet their families and kin in North Korea. The majority of the applicants, 70.6 percent, are in their 70s and 80s. Two-thirds of the applicants are male (65.6%), one third is female (34.4%).

The IICSF also provides statistics regarding the relationship of the separated families. Thus it appears that almost half of the persons concerned are married couples or parents and children (47.7 percent). 39.2 percent of the South Korean applicants look for their brothers and sisters.

Most of the applicants come originally from the North Korean provinces of Hwanghae (23.5%), South P'yòng'an (13.6%) and South Hamgyòng (11.9%). Since prospects of getting in touch with family members residing across the border via the official way are relatively low, more and more Koreans rely on privately organized exchanges through brokers. These middlemen forward letters and assist in organizing meetings of family members in a third country.²⁵

²⁴ The South Korean IICSF was established in 1998 in order to support exchanges between separated families and provide data related to this issue.

²⁵ Contrary to the situation in divided Germany where mutual visits and the exchange of letters were possible though limited, no mail or telephone service is available across the DMZ.

Conclusion

In this working paper, we have tried to take stock of how inter-Korean relations have developed since the second half of the 1990s, also considering the overall political framework and policy options of the governments of South and North Korea. As the numbers show, the engagement policies of the two previous South Korean leaders initiated an unprecedented era of *rapprochement* between the two countries. The effects of the new leadership in North Korea (Kim Jong-il since 1994) and the “arduous march” (food crisis 1995-1997) on inter-Korean exchanges are hard to quantify but have certainly been significant. The expansion of economic cooperation – though subsidized and directed by the South Korean government – was accompanied by an increase of people-to-people exchanges. These contacts helped demystifying North Korea in the South, especially among young citizens. Only future will tell if their (more positive) attitude towards North Korea will also result in financial or personal support of the work of South Korean NGOs in the DPRK. We have little evidence on the effect the intensified exchange had on North Koreans. However, experience from socialist societies in Europe and scattered observations in North Korea (see Frank 2005a, 2005b) seem to suggest that these effects are significant. After decades of having been exposed exclusively on mostly derogative propaganda about the other side, North Koreans learn quickly that South Koreans are much more affluent than themselves, and that they are willing to cooperate and lend a helping hand when needed. South Korean lifestyle has already established itself as the example to follow in many respects, leading the North Korean state as far as banning certain hairstyles. The battle over soft power supremacy is on, and the European experience suggests that once a regime lost the hearts of its people, its days are counted. As Kim Jong-il has stated in 1995: the corruption of socialism begins with ideological corruption.

Given the actual situation, further progress in inter-Korean economic cooperation clearly is a question of political will despite existing interest among private business circles. This dominance of political over economic motivation on the South Korean side leads to an abnormal situation and has to be duly considered when analyzing the status and prospects of inter-Korean exchanges. We would argue that in the long run, economic relations should be based on economic rationality to be sustainable, which does not exclude the implementation of political objectives. The current period can therefore be seen as transitory. One measure to better untangle the economic sphere from politics would be the introduction of a system of credit guarantees for South Korean companies that are willing to do business with the North. West Germany had done this quite successfully before unification in the form of so-called Hermes guarantees, leaving the core business decisions to the private sector but reducing the risk of these operations by covering a part of potential losses.

It is yet difficult to assess the effects of the dramatic policy shift during the first months of the Lee administration and how this relates to the achievements of the previous governments. So far, statistics imply a relative immunity of the business sector to the political developments. However, this assertion needs to be verified after some time. It also remains to be seen whether the return to an engagement policy vis-à-vis North Korea will be able to undo political damage, how long this will take, and whether the worsened political climate will show its effects on economic statistics with a time-lag.

Last, but certainly not least, we should note that the leadership in North Korea and its behavior regarding crucial security and human rights concerns will be primarily responsible for the future development on inter-Korean cooperation.

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