Prospects for eventual reunification of North and South Korea appear brighter than at any time in the past several decades. Yet it is premature, if not naïve, to assume that reunification will occur smoothly, let alone peacefully.

To be sure, the recent signs are encouraging, as well as unusual: the much publicized embrace by the two Presidents Kim and their amicable discussions in June, followed by exchanges of visits between 100 selected North and South Korean families, by the release by South Korea of several dozen convicted North Korean spies, and by the joint appearance of the South and North Korean Olympic teams in Sydney on September 21.

Nevertheless, in the past there have been numerous occasions where indications of an impending relaxation of tensions were followed by blatant North Korean acts of hostility and violence, including sabotage in the South, attempted assassinations, and infiltration of guerrilla units into the South.

If this explosive pattern from the past is not repeated this time around, one issue that still might—but should not—be allowed to impede progress toward reunification is fear by South Korea (and its ally, the United States), as well as exaggerated expectations by the North, of the enormous costs to South Korea (benefactions, from the

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standpoint of North Korea) that reunification would entail. In fact, contrary to much conventional lore and questionable calculations on the subject, the costs of reunification can be held within moderate bounds by a combination of sensible negotiations and effective management of the reunification process.

In the recent past, the costs of Korean reunification have been plausibly, but misleadingly, estimated by several sources including the World Bank to be as high as $2–3 trillion, about five or six times South Korea’s gross domestic product! Such exorbitant economic costs, quite apart from the enormous political and social problems that reunification would present, have made reunification at any time in the next few decades seem chimerical.

The seeming plausibility of these estimates has been driven by the experience of German reunification in the past decade, and its huge (still continuing, and originally underestimated) costs. At first glance it might appear that the costs of Korean reunification would impose even larger relative burdens than those that materialized in the German case. For example, the population of North Korea is about half that of the South, while that of East Germany was only one-quarter that of West Germany. Moreover, per capita GDP in North Korea is perhaps only one-fifth to one-tenth that of South Korea, while per capita GDP in East Germany was believed in 1991 to be about two-thirds to three-quarters that of West Germany. (In the event, the East German per capita GDP actually turned out to be more like one-quarter that in West Germany, hence not that different from the comparison between North and South Korea.)

So, if the relative income disparity and the relative population magnitudes between North and South Korea are assumed to be much larger that the corresponding comparisons in East and West Germany, the plausible inference has been drawn that the costs of Korean reunification would be relatively even greater than the costs actually experienced in the German case—"plausible," but unwarranted.

Several offsetting considerations lead to quite a different conclusion.

If the process of reunification in Korea is negotiated sensibly and managed carefully, the ensuing cost burden imposed on the South
and its allies can be limited to a sum that is less than one-tenth of the conventional estimates!

The principal offsets include the resource savings and reallocations to be gleaned by substantial military downsizing, as well as by prudently limiting the economic goals that reunification should seek:

- North Korea continues to support a huge military establishment: 1.1 million men in its regular armed forces plus about four times that number in its reserves, as well as a large defense industry which undergirds these forces and generates North Korea’s principal exports. The economic burden this imposes amounts to between 30 and 40 percent of the country’s GDP. (In East Germany, the military consisted mainly of Soviet forces, largely representing a cost burden on the Soviet Union not on East Germany itself.) If and as progress toward reunification in Korea occurs, substantial savings and reallocations of resources can be realized by a commensurate downsizing of the North Korean military establishment. My initial calculations suggest that savings from this source should be between 13 and 15 billion U.S. dollars annually, provided downsizing of North Korean military forces is negotiated as an integral part of the reunification process.

- Additional, but smaller, savings can also be realized by a reduction of South Korea’s own military forces of 600,000 men. These savings could be between 2 and 3 billion dollars annually, envisaging a total military force on the peninsula of perhaps 400,000, instead of the 1.7 million armed forces that currently face one another across the 54th parallel.

- While resources can be saved by a significant military build-down, the quantity of resources needed for North Korea’s economic build-up can be bounded by establishing reasonable, limited, and realistic targets for reunification. For example, economic targets should be considered that are sufficient, but not excessive, for preventing a large population flow from North to South Korea. (Incidentally, Korea’s location and topography make the goal of controlling excessive population flows much more practicable than in the German case.) With this goal in mind, it would be reasonable, for example, to aim at a doubling of per capita income in the North over a five- to seven-year
period. It would be quite unnecessary as well as unreasonable to seek to equalize per capita income levels between North and South in any short period of time. (It is worth recalling that, for political reasons, German reunification was launched with overambitious economic and financial targets: for example, equalizing the par values of the ostmark and the deutschmark, standardizing the package of social entitlements between the East and the West, etc.) If the reasonable goals mentioned above are established for Korean reunification at the outset of the process, the total capital costs of achieving them should not exceed four or five times North Korea’s estimated GDP.

So, setting the resource reallocations from the military build-down in both North and South Korea—about $75 billion over a five-year period—against a rough estimate of the costs of reconstruction in the North of $200 billion (assuming a capital-to-output ratio of four; hence, four times North Korea’s GDP), would still leave a large but much more manageable cost of $125 billion. It is not unreasonable to assume that, say, half this sum could come from private foreign capital motivated by profit considerations. The residual would require public capital transfers—bilaterally from South Korea, Japan, and the United States, and multilaterally from the World Bank Group and the Asian Development Bank—of between $60 and $65 billion over a five-year period.

Although these numbers are substantial, they are about the same as the bailout funds provided to South Korea to relieve its short-term financial crisis in 1997 and 1998.

The costs of Korean reunification are much more manageable than has usually been assumed. Exaggerated estimates of these costs should not be allowed to hinder or delay reunification.

Postaudit

While some of the parameters have changed, the essential points about how the costs of Korean reunification can be held to manageable amounts remain valid.