

U.S.-Korea Relations:
**Good Sense in Washington,
A Big Question Mark in Pyongyang**

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This quarter opened with many unanswered questions about the direction of diplomacy on the Korean Peninsula. As the U.S. reviewed its policy toward North Korea, the South Korean government nervously watched and waited. South Korea worried especially that the suspension of inter-Korean talks – ordered by Pyongyang until the U.S. policy review was complete – could become permanent. North Korea, for its part, contributed to the chilly diplomatic atmosphere by threatening to drop its ban on missile testing or to pull out from the 1994 U.S.-DPRK Agreed Framework, which froze Pyongyang's suspected nuclear weapon program, if the U.S. maintained a "hard line."

By early June, the direction of the new Bush administration's policy toward North Korea became clear. President Bush decided to "undertake serious discussions" with Pyongyang in an attempt to reach a resolution of outstanding security issues, including, for the first time, North Korea's conventional force posture. While the North agreed to pursue the U.S. offer of talks, it did not publicly signal any flexibility on the issues under discussion. And Kim Jong-il continued to avoid making any commitment on a return summit visit to South Korea during 2001. Now that U.S.-North Korea diplomatic talks are underway, Pyongyang's true diplomatic intentions will soon become clear, and we will learn how far Pyongyang is willing to go to settle issues that are crucial to future peace and stability in Northeast Asia.

The Regional Context

During most of April, the international political news, from a Korean perspective, was dominated by the controversy over a new Japanese textbook that seemed to distort or cover up war crimes committed by the Japanese Imperial Army in Korea and elsewhere in Asia. South Korea recalled its ambassador from Tokyo in protest and later postponed joint naval exercises with Japan scheduled for June. For its part, Tokyo denied government responsibility for the new textbook and did not express any sympathy for the substance of the South Korean position. As this controversy festered and gathered momentum in South Korean public opinion, observers worried about its deleterious impact on U.S.-South Korea-Japan trilateral coordination toward North Korea.

In early May, a delegation from the European Union, led by Swedish Prime Minister Goran Persson, achieved the first diplomatic breakthrough in negotiations with North Korea in 2001. During two days of talks in Pyongyang, Persson made clear the EU's serious concerns about North Korea's weapons proliferation as well as its dismal human rights conditions. He strongly supported South Korean President Kim Dae-Jung's policy of engagement and explored various ways of increasing North Korea's trade and investment activities with the EU. As result of the talks, North Korea announced that it would extend its moratorium on missile testing until 2003 and enter into discussions on human rights with the European Union. This was the first time that North Korea had ever agreed to discuss human rights with any outside government.

Presumably as a follow-up to the May 2-3 talks between Kim Jong-il and Prime Minister Persson, the EU announced in mid-May that it was establishing diplomatic ties with North Korea. This announcement was the culmination of an approximately 18-month effort by North Korea to establish diplomatic relations with the member states of the EU. It was symbolic of North Korea's strategy to break out of its perceived diplomatic isolation and build political and commercial relations to overcome its serious domestic economic problems. Nonetheless, observers noted both the limits of European influence on North Korea and the limited extent to which the EU could actually assist North Korea, so long as U.S.-North Korea ties remained strained.

The larger effect of the EU-North Korea talks was to restore some positive momentum to the reconciliation process on the Peninsula. By putting the EU squarely behind President Kim's engagement policy, Prime Minister Persson ratcheted up the pressure on Washington to produce a new North Korea policy that did not move in contrary directions.

The late May visit of Chinese leader Li Peng to South Korea seemed to reflect South Korea's urgent need to build support for its engagement policy while the U.S. policy review was still underway. Li publicly proclaimed China's strong endorsement of North-South reconciliation and said China would urge North Korea's leader to move forward with that process. The visit served as a reminder that the only powerful country that had good relations with both South and North Korea is China. The implication that China could foster the inter-Korea reconciliation that Seoul was seeking – in the absence of a meaningful U.S. negotiating initiative – undoubtedly focused the minds of U.S. policy makers.

An IAEA team went to Pyongyang on May 22-26 to discuss North Korean compliance with the international safeguards regime. Compliance is a necessary precondition for the hand-over of key components of light water reactors, as outlined in the 1994 Agreed Framework. The IAEA did not reach any agreement with North Korea and subsequently announced that it was still unable to begin the process of verifying DPRK compliance. Since the process of IAEA certification is expected to take two to three years, it is critical that the process begin.

The U.S. Takes the Hint

The first indication of the new direction in U.S. policy toward North Korea came during the visit of Deputy Secretary of State Richard Armitage to Seoul on May 9. Armitage ostensibly visited Seoul to provide a briefing on U.S. plans for missile defense; he did not seek South Korea's endorsement of the policy. But the headlines in Seoul stressed Armitage's statement that he expected the U.S. to resume its negotiations with North Korea in the near future. The deputy secretary also brought a letter from President Bush strongly endorsing President Kim's engagement policy. Armitage's message had a leavening impact on public diplomacy at a time when impartial observers wondered whether the Bush administration would continue its "hard line" and refuse further negotiations with North Korea altogether.

At trilateral talks with Japan and Korea in late May, the U.S. briefed its close allies on the results of its North Korea policy review and the outlines of Washington's new North Korea policy. Led on the U.S. side by recently confirmed Assistant Secretary of State James Kelly, the trilateral talks also served to re-establish the importance of the Trilateral Coordination and Oversight Group (TCOG) process itself, which some conservative Bush advisers had called into question during the presidential campaign.

The long-awaited announcement of the Bush administration's new policy toward North Korea came on June 6. President Bush directed his national security team to "undertake serious discussions with North Korea on a broad agenda to include: improved implementation of the Agreed Framework relating to North Korea's nuclear activities; verifiable constraints on North Korea's missile programs and a ban on its missile exports; and a less threatening conventional military posture." The new policy sets forth a "comprehensive approach" toward North Korea, includes a strong endorsement of President Kim's "Sunshine Policy," and seeks "to encourage progress toward North-South reconciliation."

According to the Bush administration, if "North Korea responds affirmatively and takes appropriate action, we will expand our efforts to help the North Korean people, ease sanctions, and take other political steps."

In several respects, the new Bush policy represents a continuation of the Clinton administration's policy toward North Korea. It affirms that the U.S. intends to pursue a diplomatic solution to security issues with North Korea. It specifically continues President Clinton's efforts to negotiate limits on North Korea's long-range missile development program and to ban its missile exports altogether. And it endorses the Agreed Framework, which froze and will ultimately serve to dismantle North Korea's nuclear weapons program. The Framework provides the foundation for U.S. diplomatic engagement with North Korea in the broadest sense.

The Bush administration policy also contains two important new elements. It explicitly calls for progress in North-South reconciliation and it introduces the question of conventional force deployments into the U.S.-North Korea talks. The first element

should significantly diminish the concerns of some South Korean officials and observers that the U.S. does not consider inter-Korean reconciliation important or even desirable from a strategic standpoint. An exclusive U.S. focus on North Korea's nuclear and missile threat – together with the national missile defense (NMD) program as a means of defending against those threats – had the potential for undermining South Korea's engagement policy and creating a split between Washington and Seoul.

The new Bush policy also stresses the importance of negotiating “a less threatening conventional military posture” of North Korean military forces on the Peninsula. During the Clinton administration, the U.S. took a minimalist approach to conventional force issues. Under the rubric of “tension reduction,” U.S. participants at the Four-Party Talks (U.S., China, the ROK, and the DPRK) addressed aspects of conventional forces, but they broadly deferred to their South Korean colleagues who had the “diplomatic lead” on this issue. The U.S. approach of moving from “easy to hard” confidence building measures fit well with the Pentagon's general unwillingness to discuss the “status of U.S. forces” on the Peninsula, which North Korea repeatedly demanded.

In keeping with its new “comprehensive approach,” the Bush administration evidently believes it is essential to address the conventional threat from North Korean forces before the U.S. can fully normalize diplomatic relations. If handled correctly, this new policy would allow the U.S. and South Korea to discuss far more effective arms control and confidence building measures with North Korea than were considered in the past. The parties may be able to negotiate a mutually beneficial monitoring regime that would reduce the risk of surprise attack to both North and South Korea. Moreover, the new policy could eventually allow the parties to reshape the deployments of *all* military forces on the Peninsula, with an eye to increasing stability and significantly lowering the risk of war.

Shortly after Washington announced its new policy, President Kim renewed his call for Kim Jong-il to visit South Korea by the end of 2001 for a second summit. North Korea had earlier suspended talks with the South and said it could not make a decision on a second summit, so long as U.S. policy was in limbo. To underscore this point, North Korea castigated the United States in propaganda broadcasts during April and May for taking a “hard line” and trying to perpetuate the Cold War on the Peninsula.

North Korea and South Korea's Hyundai Group did agree in early June to open an overland route to Mt. Kumgang, through the DMZ, during the second half of 2002. The announcement took on particular significance since North Korea had previously stopped construction on its portion of the new rail link through the DMZ that was agreed upon at the June 2000 summit.

The effect of the newly announced U.S. policy and President Kim's appeal to Kim Jong-il was not clear at the end of the quarter. Many observers argued that the ball was now in Pyongyang's court whether to seek a fundamental transformation in relations with both Washington and Seoul. It seemed to these observers that a second Korean summit meeting that addressed core political, economic, and military issues could make the

North-South reconciliation process irreversible.

North Korea's public reaction to the new U.S. policy reiterated its standard negotiating positions, while welcoming the general prospect of dialogue with the U.S. Pyongyang said it would seek compensation from Washington for delays in building two light water reactors under the 1994 Agreed Framework. The DPRK also indicated it would not agree to discuss its own conventional forces until the U.S. withdrew all troops from South Korea. Pyongyang's willingness to resume negotiations with the U.S. was also reflected in its agreement to a mid-June diplomatic meeting in New York on "procedural issues" that the State Department called "productive."

Economy and Politics

In April, the extent of South Korea's economic slowdown became clearer. The International Monetary Fund, which had earlier estimated a relatively modest 6.5 percent growth rate in 2001, lowered its projection to 3.5 percent. Most observers attributed the drop to the effects of a global slowdown and the adjustments due to restructuring in the domestic economy. Since April, there have been mixed signals on the direction of the economy, but the slowdown seems to have moderated.

Nevertheless, it is difficult to tell whether the economy has hit bottom, since exports continued to shrink during the quarter and corporate capital investment has remained weak. Seoul seems to believe that a global economic rebound and continuing domestic reforms will return the economy to a growth path of 5-6 percent in the second half of 2001.

Particularly disconcerting, especially to foreign observers, were the apparently successful efforts of large *chaebol* to weaken reform measures adopted after the 1997-98 economic crisis. Under the guise of demanding further "reform," the Korean Federation of Industries effectively lobbied the government in mid-May to ease ceilings on the amount of payment guarantees that a parent company can grant overseas subsidiaries. The payment guarantee, imposing limits on the overseas subsidiaries of South Korea's 30 largest business units, was enacted in late 1998 to discourage excessive borrowing.

In mid-June, Deputy Prime Minister Jin Nyum said the government might reverse its financial regulation that limits *chaebol* ownership of shares in local banks. That limit was a way of preventing the *chaebol* from unduly influencing the lending decisions of banks. Critics now fear that *chaebol* may use their increased ownership of the local banks to obtain easy access to cash in order to fund unwise investments. In the big picture, giving *chaebol* greater ability to dominate South Korea's financial institutions could significantly retard overall reform efforts since the 1997-98 crisis is often attributed to the poor health of the banking and finance sector.

Labor reacted with more protests and demonstrations this quarter to restructuring efforts that it considered to be unfairly targeting workers. Unions pressed for more job security as well as higher wages and shorter work hours. On June 12, 55,000 workers including

employees of South Korea's two major national airlines stayed away from their jobs and caused short-term disruptions. But the labor action ended shortly thereafter as the majority of strikers returned to work.

President Kim's political popularity remained low throughout the quarter. The South Korean public focused on weakness in the economy and could see little silver lining in North Korea's suspension of inter-Korean talks during the Bush administration's policy review. The credit and popularity President Kim earned from his initiatives toward North Korea seemed largely to have dissipated. Compounding President Kim's popularity problem was an embarrassing appointment of a new minister of justice, which had to be withdrawn within 24 hours. That mishap almost led to a mutiny by members of his own political party.

At the end of June, South Korean prosecutors began a criminal investigation of six leading newspaper companies for tax evasion and failing to report over \$400 million in corporate income. The opposition party charged that the tax inquiry was intended to muzzle President Kim's domestic critics. But the head of the National Tax Service strongly denied any political motivation for the probe.

More broadly, politicians of all parties are now looking ahead to the December 2002 presidential election and prospective candidates have already begun jockeying for position. Recent polls show opposition leader Lee Hoi-chang ahead of the pack with the so-called "seven dwarves" from the ruling and opposition parties trailing behind. Leaders of President Kim's party are particularly worried about finding a new candidate from among their ranks to successfully retain control of the presidency.

Analysts predict that regional loyalties will again play a major role in South Korea's presidential election. Since President Kim's election in 1997, critics have accused him of unfairly appointing numerous officials from his home province of Cholla-do, which had suffered from strong discrimination in the past. This has created resentment and visceral opposition in South Korea's other major provincial areas. In addition to regionalism, the ideological divide between rich and poor, which deepened as a result of the 1997-98 financial crisis, will have a major impact on the upcoming election.

Trade Issues

Conflict between the U.S. and South Korea on trade issues flared at the end of the quarter, as the Bush administration called for an International Trade Commission (ITC) "Section 201" investigation of Korea's exports of steel to the U.S. The investigation will focus on whether the South Korean government gave unfair assistance to its steel industry, allowing it to undercut domestic U.S. steel producers. The ROK currently has an approximately 7 percent market share in the U.S.

The Section 201 investigation could result in a U.S. decision to impose punitive tariffs on South Korean steel. The South Korean government strongly objected to the investigation, which could cause a loss of approximately 40 percent of ROK steel exports generally, if

tariffs are ultimately applied.

In late May, members of Congress passed a concurrent resolution calling on South Korea to adopt “practical measures” to increase the number of foreign cars that are sold in the ROK. Last year, while the U.S. bought approximately 500,000 South Korean cars, less than 1,000 American cars were sold in Korea. Compared to Japan, where U.S. companies hold a 6-8 percent share of the domestic auto market, in the ROK, that share is 0.4 percent.

Under pressure from Seoul, Hyundai is reportedly planning to import large numbers of American cars from Chrysler, its strategic partner, and then lease them to local businesses for use as taxis and commercial vehicles. The goal is to mollify American automakers, who point to the asymmetry in U.S.-South Korea auto sales as an example of unfair Korean import barriers.

Finally, the U.S. kept the ROK on the Priority Watch List at the end of April, despite South Korea’s enactment of fairly draconian measures in February to enforce intellectual property rights. Microsoft and the Business Software Alliance reportedly lobbied the United States Trade Representative (USTR) heavily to keep Korea on the Priority Watch List until the longer-term impact of the new measures could be ascertained. South Korea’s Ministry of Foreign Affairs and Trade, which pushed for greater enforcement of intellectual property rights, privately expressed great disappointment that USTR had not reacted positively and decisively to its efforts.

Future Prospects

Now that the U.S. policy review on North Korea is complete, the hard diplomatic work begins – negotiating the terms of agreements with Pyongyang. The U.S. has committed itself to “undertake serious discussions” with North Korea, despite the skepticism of hardliners in the Bush administration. From a U.S. domestic political standpoint, the burden now falls on the pragmatists and moderates to show that their preferred approach works – and that the North Korean threat to both South Korea and the United States can be dealt with in a diplomatic fashion. Fortunately for the Bush administration pragmatists, the new political make-up of the Senate ensures stronger support for their efforts from Capitol Hill – a luxury that the Clinton administration did not have as it weathered years of Republican right-wing attacks for “appeasing Pyongyang.”

Of course, the main responsibility for progress in U.S.-North Korea talks as well as in inter-Korean relations now falls on Pyongyang. Or, as leading commentators have pointed out, the ball is in Kim Jong-il’s court. North Korea previously attacked the U.S. for Bush’s apparent “hard line” and justified its suspension of talks with the South on the basis of the pending U.S. policy review. Now that the policy review is over – and the U.S. has agreed to seriously negotiate – Pyongyang no longer has any excuse for failing to pursue an engagement policy of its own. By the end of the next quarter, we should know North Korea’s real intentions – whether it really means to reach a settlement of outstanding security issues with the U.S. and South Korea or whether it’s simply playing

for time and more untied humanitarian aid.

Chronology of U.S.-Korea Relations **April – June 2001**

Apr. 11, 2001: South Korea indicates plan to import U.S. autos to relieve trade friction.

Apr. 25, 2001: IMF lowers South Korea's economic growth forecast from 6.5 percent to 3.5 percent for 2001.

May 1, 2001: Bush administration targets South Korea for possible trade sanctions.

May 2, 2001: EU delegation led by Swedish PM Persson visits Pyongyang for talks.

May 3, 2001: North Korea extends ban on missile testing until 2003 and agrees to human rights talks with EU.

May 9, 2001: U.S. Deputy Secretary Richard Armitage visiting Seoul says U.S. will resume talks with North Korea.

May 11, 2001: Armitage and Assistant State Secretary James Kelly in Seoul, meet with Kim Dae-jung.

May 14, 2001: EU establishes diplomatic ties with North Korea.

May 18, 2001: South Korean government loosens restrictions on 30 large *chaebol*, allowing them greater access to overseas financing.

May 20, 2001: Ruling and opposition parties agree on economic restructuring measures.

May 23, 2001: Chinese leader Li Peng, visiting Seoul, calls for closer inter-Korean relations.

May 23, 2001: President Bush designates Thomas Hubbard as ambassador to South Korea.

May 24, 2001: President Kim urges Kim Jong-il to set date for visit to South Korea.

May 26, 2001: U.S., South Korea, and Japan conduct trilateral talks on North Korea in Hawaii.

May 29, 2001: North Korea proposes North-South civilian "grand symposium" to celebrate summit anniversary.

May 30, 2001: GM submits takeover proposal for ailing Daewoo Motor Company.

May 31, 2001: South Korea announces “deregulation” measures for *chaebol*, giving in to their demands.

June 3, 2001: Several North Korean cargo vessels violate South Korean coastal limits.

June 5-12, 2001: ROK FM Han Seung-soo meets with Secretary of State Colin Powell in Washington.

June 6, 2001: South Korean FM requests UN secretary general to visit two Koreas to promote peace.

June 6, 2001: President Bush announces results of U.S. policy review – to undertake comprehensive and “serious negotiations” with North Korea on Agreed Framework, missiles, and conventional forces.

June 9, 2001: U.S. DPRK resume joint MIA search.

June 10, 2001: Hyundai Group announces agreement with North Korea to build an overland route to the Mt. Kumgang tourist site.

June 12, 2001: 55,000 workers strike to protest corporate restructuring and to improve working conditions.

June 13, 2001: U.S. and North Korea resume diplomatic dialogue in New York City.

June 15, 2001: On North-South summit anniversary, President Kim calls for Kim Jong-il return visit to South Korea.

June 18, 2001: Rejecting arms reductions, North Korea says compensation for light water reactor delay is top agenda item for U.S. talks.

June 19, 2001: U.S. refuses to provide compensation to North Korea for reactor delay.

June 21, 2001: U.S. defense secretary and South Korea defense minister meet in Washington.

June 22, 2001: U.S. requests Sect. 201 investigation of South Korean steel imports.

June 24, 2001: South Korean Navy fires warning shots at intruding North Korean fishing boat.

June 26, 2001: U.S. envoy Jack Pritchard meets with DPRK counterpart Li Hyong-chol in New York.

June 29, 2001: National Tax Service refers six media firms to prosecutor's office for tax evasion.

June 30, 2001: Seven North Korean defectors, all family members, arrive in Seoul from Beijing via Manila.