

”Binding Up the Nation's Wounds: An Economic Analysis of the Korean Reunification”

Sang Yoon (Tim) Lee

Yongseok Shin

We develop a multi-sector occupational choice model with two-dimensional individual skill heterogeneity. Sectors are different in terms of minimum skill requirements. Individuals are heterogeneous in terms of managerial skill and efficiency units of labor, and decide whether to become a manager or a worker and in which sector. Individual skills are accumulated over the lifecycle according to a stochastic learning-by-doing technology. This lifecycle effect generates non-trivial transition dynamics such as lagged responses of both TFP and labor productivity that were important characteristics of the growth miracles of East Asia and the post-communist transitions of Eastern Europe. We characterize the theoretical model and apply it to the economic integration process that results from a hypothetical reunification of North and South Korea. The model is used to project the transitional dynamics of a unified Korea under various integration scenarios and policy regimes.