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## US Leadership in the Rebuilding of the North Korean Economy

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*“ . . . not only to give emergency food aid—because people are terribly hungry—but to work with them in restructuring their entire economy and helping make it more functional again.”*

—President Bill Clinton, 25 April 1997

### The Problem

One of the problems in assessing the probabilities of military conflict, implosion, or gradual change with or without integration in the Democratic People’s Republic of Korea (DPRK) is that we tend to accept at face value the caricature of North Korean society that North Korea itself in years past has encouraged the outside world to draw. The picture we are given is of a fiercely self-reliant, even fanatical, people who are unalterably opposed to attempts to change their system from either within or without and who would prefer under almost any circumstances to fight it out to the bitter end rather than to compromise.

In his first “foreign policy work,” published on 4 August 1997, Kim Jung Il, the North Korean leader, wrote that “if the South Korean authorities show positive changes through acts in the future, we will meet with them anytime to have open-hearted negotiations on the destiny of

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the nation.” Similarly, if Japan “repents its past” and abandons its hostile policy toward Pyongyang, “we will treat Japan, a neighboring country of ours, in a friendly manner, and the abnormal DPRK-Japan relations will improve as well.” As for the United States, “we do not want to regard the United States as an enemy of a hundred years; we want DPRK-US relations to be normalized.”

What is interesting about such North Korean statements is not whether they “contain anything new,” a question that is in any case unanswerable unless put to the test, but whether they reveal anything about the underlying architecture of Pyongyang’s foreign policy today, a subject that has received much less attention. That is, after decades of close political relations with Moscow and Beijing, why does North Korea’s foreign policy now appear to revolve almost entirely around its relations with Seoul, Washington, and Tokyo? Does a shift of this magnitude—one might term it a reorientation from the socialist East to the capitalist West—not suggest an ability to change policy? If so, what does the suggestion that North Korea’s future somehow lies wrapped up in its relations with its chief ideological adversaries imply about its domestic policy?

Our ability to answer the question of North Korea’s future depends intimately on a clear understanding of this new strategic architecture. All questions relating to the food and energy shortage, economic decline in general, prospects for foreign trade and investment, political reform, and a reduction in military tensions can be understood only in the context of the strategic imperatives dictating North Korean foreign and domestic policy today.

## **Brief History of the Shift**

In 1987, in his famous speech of 7 July, South Korea’s Roh Tae Woo announced his “Northern Policy,” a policy of forcing the North to come to the table for inter-Korean talks by normalizing relations between Seoul, on the one hand, and Moscow and Beijing, on the other. The basic strategy was that by going beyond mere containment, the earlier policy, to one of encircling and eventually forcing the North to submit to the South, Korea would be reunified on South Korean terms. South Koreans viewed this move as the first serious departure away from their decades-old alliance with the United States; but flush with a decade of spectacular economic growth and increasing world attention paid to Seoul, they felt it was a price worth paying for the prospect of bringing the Korean question to a final conclusion.

North Korea’s response to this move, little noticed at the time, was to produce its own *Sudpolitik*, that is, to normalize relations with the United States and Japan so as to counter the South Korean move. Yet for Pyong-

yang, more was at stake than geopolitical balance on the Korean peninsula. The North Korean decision to improve relations with Washington and Tokyo was not merely rooted in the old “cross-recognition policy” (under which Seoul would normalize relations with Moscow and Beijing in exchange for Pyongyang doing so with Tokyo and Washington). Threatened by the abrupt ending of the Cold War, by the subsequent loss of its trading partners in Eastern Europe and the former Soviet Union, by China’s turn toward market economics and increasing acceptance of South Korea as a legitimate political entity, and by South Korea’s own record of rapid economic growth, North Korea went considerably further. It cooled its relations with both Moscow and Beijing, a situation that remains unchanged today; it began to move toward a political accommodation with South Korea (the high-level talks leading to the 1991 inter-Korean accords), and it took steps to revitalize an economy suddenly deprived of food and energy inputs (the establishment of the Rajin-Sonbong Free Economic and Trade Zone). Most surprisingly, it reached out to the United States to forge a new political and security relationship. As early as 1991, a high-level Foreign Ministry official explained to a visiting US delegation the need for the United States and North Korea to jointly check Japan’s future advances into the region.

## Two Wrong Views

In recent months two articles have appeared in a single publication (*Foreign Affairs*) that together define the current parameters of the debate on North Korea’s future. Nicholas Eberstadt, in “Hastening Korean Reunification” (1997), presents the “sick man of Asia” thesis—that is, North Korea today is in its death throes and the sooner Asia’s statesmen put it out of its misery and force a reunification of the peninsula on South Korean terms, the better. The five governments of South Korea, the United States, China, Japan, and the Russian Federation should work together to bring about North Korea’s early downfall, he argues. “The Pacific powers,” writes Eberstadt, “can no longer classify the Korean question as a problem that can be postponed and then muddled through.” To this end, the United States should consider abandoning the US-North Korean Agreed Framework, which merely prolongs North Korea’s agony, and South Korea should embark on far-reaching reforms of its agricultural, financial, and trading systems as well as of its civil and administrative legal regimes. Japan should use international financial and multilateral institutions to exert a positive influence on the coming developments in North Korea, since “it has never had a ‘normal’ foreign policy” and “[cannot] play a role on the international stage in the same manner as other industrial democracies.” Curiously, Eberstadt argues that “neither China nor Russia can be counted on to cooperate in multilateral

deliberations about what follows the end of North Korea,” despite his earlier prescription for a five-way cooperative process. In short, muddling through is less preferable than coordinating an early finish to the North Korean state.

Muddling through is exactly what Marcus Noland thinks may happen to this Romania-like economic basket case, unable either to reform itself or even to simply collapse, since the external powers will not permit it. In “Why North Korea Will Muddle Through” (1997), Noland suggests that with Chinese or others’ assistance, North Korea is capable of developing a Romanian-style “apparatchik capitalism” and hence ensuring its survival at least for the time being.

## Perception Gap

In addition to such views, there remains a considerable gap between reality and international perceptions of North Korea. The events of 19 August 1997 reveal much about this gap. Together with over 100 diplomats from 10 different countries, reporters from around the world gathered in Sinpo, North Korea, to witness the groundbreaking ceremony for the first of two light-water nuclear reactors being constructed by the Korean Peninsula Energy Development Organization (KEDO)—a US-led consortium formed as a result of the October 1994 Geneva Agreed Framework between the United States and the North. Many of the background media reports about the ceremony described North Korea as “closed,” “unyielding,” or even “hostile.” Ironically, the very event about which these reports were issued was evidence to the contrary.

Since the conclusion of the Agreed Framework, North Korea has fully observed its commitments under the agreement and the implementation of KEDO has proceeded smoothly. More remarkable still are the many historic protocols reached between the North and KEDO. Unfortunately, however, international perceptions have not kept pace with actual developments in North Korea. It is portrayed as a land frozen in time—unable to respond to the dramatic changes taking place in the surrounding world. A recent South Korean book was even titled *North Korea: The Land That Never Changes*. Though widespread, such a view is inaccurate. North Korea is adjusting at an unprecedented pace and in many arenas is making real progress.

The complement to this view of the North as stagnant is the “collapse” theory. In the face of severe external economic shocks, a faltering economy, and growing food shortages, many analysts argue that a collapse of North Korea is inevitable and even imminent. If one examines only the surface of the situation, this scenario may seem logical. However, those scholars who dig deeper have a much clearer understanding of the strengths of the regime, and they come to a different conclusion.

The resulting, more informed view is represented by scholars such as Marcus Noland, mentioned earlier. Yet even this line of thinking does not fully capture the reality of the situation in North Korea today.

Despite significant challenges, the North is not merely “reacting” to external changes; it clearly intends to do more than simply “muddle through.” A short overview and assessment of recent diplomatic and economic developments should provide a clearer view of North Korean policy and prospects.

## **Recent Diplomatic Developments**

One of the perceptions of North Korea that has been slowest to change is that the country is “closed.” The North maintained close ties with its allies throughout the Cold War era and beginning in the late 1980s has actively pursued improved relations with the West. North Korean diplomats are quick to point out that their country has been not so much “closed” as “isolated” by countries such as the United States and through actions such as the US economic embargo.

### **North Korean-US Relations**

After 40 years of hostility, North Korean-US relations have made dramatic strides in the past four years. Though relations remain inherently difficult due to the continuing division of the Korean peninsula and the US alliance with South Korea, bilateral ties today are fundamentally different than they were just five years ago.

#### **Agreed Framework**

North Korean and US officials alike have frequently described the Geneva Agreed Framework as the foundation of the current bilateral relationship. Although much of the agreement focuses on freezing the North’s nuclear program, it also provides a road map for normalizing US-North Korean relations and for lifting the US economic embargo.

The North Korean response to the agreed framework provides some of the clearest evidence of a willingness to engage the United States and to participate more fully in the international community. The North has allowed international inspectors from the International Atomic Energy Agency (IAEA) to remain in the country on an ongoing basis, has shut down its existing nuclear reactors and stopped construction on planned reactors, and has fully cooperated with the US Department of Energy in the process of canning spent fuel rods. Moreover, it has actively engaged KEDO, both in receiving heavy fuel oil in exchange for the

closure of North Korean nuclear power plants and in constructing two light-water reactors (LWRs). The degree of contact necessitated by the agreed framework has not been insignificant. Moreover, the agreement has moved from the realm of speculation to actualization. With the groundbreaking ceremony for the light-water nuclear reactors in Sinpo in August 1997, the Geneva Agreed Framework has arguably reached the stage of full implementation.

The principal elements of this agreement alone make it quite clear that US-North Korean relations are fundamentally different in 1997 than they were in 1993. However, the agreed framework also called for progress in “other areas of concern” to the United States.

### Missile Talks

Although the talks scheduled for last month were postponed because of the defection of the North Korean ambassador to Egypt, the North has shown a clear willingness to discuss the disposition of its missile program openly with the United States. More important, as that missile program is currently assumed to be a source of revenue, any discussion of its cessation is likely also to consider measures that may be of economic benefit to North Korea.

### MIA Talks

With the possible exception of KEDO, the most dramatic progress in US-North Korean relations has been in the North’s willingness to allow several US military search and recovery teams into the country to locate and recover the remains of US servicemen listed as missing in action (MIA) during the Korean War. The significance of the actual presence of US military personnel on the ground in North Korea cooperating with the Korean People’s Army (KPA) should not be minimized.

### Focus on the Embargo

While the US focus has been upon MIAs and missiles, the North has consistently pushed the United States to live up to its commitment under the Geneva Agreed Framework to ease the economic embargo on North Korea. The United States, despite making token moves in January 1995, has yet to fully live up to its agreement. The North Korean government argues that with the groundbreaking of the LWR project in Sinpo, the Agreed Framework has reached the state of full implementation; the United States should therefore now fulfill its promise.

On the whole, North Korea and the United States have demonstrated a willingness and an ability to engage on a broad variety of fronts and

to overcome potential threats to this process, such as the helicopter incident of 1994 and the submarine incident of 1996.

### **North Korean-Japanese Relations**

The recent decision by the North to allow Japanese wives of North Koreans to visit Japan marks an important breakthrough in relations between the two countries. Japan will not only contribute food aid but has agreed to resume normalization talks with North Korea at the ambassadorial level.

Japan has been criticized in recent months for having essentially forfeited any significant role on the Korean peninsula. The political weakness of the Hashimoto administration, coupled with pressure from South Korea not to get ahead of their policy and with claims that the North has been responsible for kidnapping Japanese citizens in the past, has made the task of improving North Korean-Japanese ties more difficult. However, it now appears that Japan is prepared to resume a more constructive role.

### **North Korean-South Korean Relations**

Though negative events in inter-Korean relations such as friction along the Demilitarized Zone (DMZ) or the September 1996 submarine incident tend to linger in the public consciousness, there has also been significant progress in North-South ties. Most recently, meetings between the respective Red Cross organizations of the North and South have met with relative success; and South Korea has consistently contributed to the international relief effort targeted to the North's flood-damaged provinces. South Korea has also actively participated in the KEDO process, and international officials frequently remark about the smooth cooperation and relatively friendly contacts that have taken place in this forum. The four-party talks proposal has provided another venue for North-South contacts, and in such meetings North Korean officials have indicated their willingness to return to and implement the inter-Korean accords of 1991 and 1992.

On the political front, the December 1997 presidential elections in the South offer the possibility of a fresh start in inter-Korean ties. As mentioned above, Kim Jung Il has already expressed a willingness to reengage the South; and with the departure of Kim Young Sam, the prospects for a inter-Korean summit might be reexamined.

On the economic front, inter-Korean trade and cooperation continue to outpace diplomatic and political developments. As of 1996, the South was North Korea's third-largest trading partner, second-largest export market, and, by most counts, largest source of hard currency. The Daewoo group is currently operating a joint-venture clothing factory in Nampo,

and the amount of trade on commission between North and South has been steadily increasing.

### **Four-Party Talks**

Though initially skeptical (perhaps rightly so, as the proposal for four-party talks was issued jointly from South Korea by President Clinton and Kim Young Sam), North Korea agreed to attend a preparatory meeting for the talks in New York in August 1997. While the first round did not go as well as some had hoped, the very fact that the four parties sat down together marks a new stage in the peace process. Now that the process has been engaged, the questions facing the participants are arguably more matters of pace and form than of whether such talks will really occur. Though starts, stops, and various distractions can be expected to be the rule rather than the exception in the process, the beginning of the four-party talks signals a fundamental shift.

### **Participation in International Forums**

Since joining the United Nations in 1992, North Korea has been an active participant in numerous UN agencies, including the United Nations Industrial Development Organization (UNIDO), the United Nations Development Program (UNDP), and the United Nations Children's Fund (UNICEF). The North is also seeking membership in more highly politicized organizations, such as the Asian Development Bank, the World Bank, and the International Monetary Fund. In fact, a delegation from the IMF visited North Korea in early September 1997. The North continues to seek out new relationships and increased participation in international organizations and conventions.

### **Economic Developments**

Perhaps the greatest evidence that North Korea is indeed adjusting to a changing international environment can be seen in its economic sector. Though there are various opinions and interpretations regarding the cause and the degree of economic decline, analysts generally agree that the North's economy has suffered considerably over the past five years. Putting questions of domestic policy aside, the country has experienced severe external shocks to its economy that have fundamentally altered its international economic relations. The collapse of the socialist bloc deprived North Korea of its principal market, and the reforms in China and the former Soviet Union have inalterably affected the North's relations with its two primary patrons.

North Korea's reaction to these changes has taken many forms. Recent food shortages have led it to accept assistance from the international community. It has put forth and actively promoted a free trade zone, has campaigned vigorously for the lifting of the US economic embargo, and more recently has begun to seek trade and investment on a much broader scale.

## **International Food Aid**

The North's admission that it had suffered considerable loss as the result of flooding in August 1995 was in itself remarkable. More important still was the decision to turn to the international community for assistance, which marks a significant change in policy. Regardless of the causes and the extent of the food shortage, it is clear that North Korea has now begun to interact fully with an ever-growing list of international agencies and organizations in an attempt to deal with the problem. Many such agencies are now beginning to address some of the underlying problems in the North's agriculture and planning as they work to engage the regime in broader development efforts.

## **Rajin-Sonbong**

In 1991 North Korea, in close cooperation with the UNDP, declared the area surrounding its northeastern cities of Rajin and Sonbong a Free Economic and Trade Zone. This zone abuts the border with Russia and China and is closely linked to the greater Tumen River Area Development Program. Over the past six years the North has promulgated an impressive body of law dealing with the zone and has become increasingly sophisticated in its efforts to promote investment.

In September 1996, North Korea hosted an international business and investment forum that was attended by some 400 foreign businessmen and that produced nearly \$300 million in contracts. Infrastructure improvements continue in the zone and groundbreaking on a major hotel has reportedly taken place. While the broader prospects for the zone as an industrial and manufacturing center may be less hopeful, its very location will likely bring it success as a transshipment and service center—particularly given the rapid growth in northeastern China and that region's lack of access to the sea.

## **Mining Sector**

North Korea is currently considering the creation of a new free trade zone, focused on the mining industry, in South Hamgyong Province.

This potential “Danchon Free Trade Zone” would mark a significant step forward in the North’s willingness to entertain significant investment outside the Rajin-Sonbong zone. The Danchon area boasts a considerable concentration of precious metals and ore and is close to the new port and transportation facilities being built in Sinpo for the construction of the light-water nuclear reactors. US firms have received special licenses to import magnesite from North Korea, and several shipments have already taken place.

## **KEDO**

Perhaps the most significant progress on the economic front has been the success of KEDO in negotiating the many protocols necessary for the construction of the LWRs. As the LWR project is extremely large-scale (early estimates of costs are at least \$4 to \$6 billion), involves several different countries, and includes numerous contractors and subcontractors, the protocols have been very carefully negotiated and set forth. They thus provide an excellent model and possible starting point for future investment projects. A summary review of the protocols completed to date reveals the degree to which North Korea is willing to recognize and accommodate international norms and legal requirements.

## **Domestic Economic Adjustments**

It is perhaps in the domestic economy that the greatest experimentation with new ways of producing economic output is taking place. Too little has been made of North Korea’s acknowledgment of the failure of its last Seven-Year Economic Plan in 1993, caused by the loss of socialist inputs from its traditional trading partners. No new economic plan has been announced, and if the West, particularly the United States, can push it in the right direction—away from a total command economy to a mixed one giving greater rein to material incentives and decentralized economic decision making—North Korea may permanently abandon that rigid, centralized approach.

Indeed, instead of announcing a new plan in 1994, North Korea opted for a new emphasis on agriculture, light industry, and trade, a switch that represents a drastic restructuring of the domestic economy away from its earlier Stalinist orientation. As part of this process, the government has been urging elements in the lower levels of the economic system, which are still under tight restrictions, increasingly to assume economic responsibility and make decisions on their own without reference to national goals. Local industry is now required to conduct its own export market studies, for example, and to identify for itself those products that it thinks can be competitive in overseas markets. Trade is

to be conducted directly at the local level, without the intervention of state trade organizations.

Moreover, individual organizations at local levels are required to find the materials necessary to increase output. Such required inputs include not only energy but food. A little-known aspect of the current food shortage is the government's use of the problem to encourage local organizations to become more self-reliant instead of depending on the center. It would be interesting to see if there is a direct correlation between the incidence of hunger and the inability to fend for oneself under the new circumstances. If this theory is correct, perhaps the "arduous march" that the North Korean people have been subjected to for over a year now is actually a way to make the economy more rational and efficient.

What enables the North Korean leadership to effect these changes in the domestic economy is of course the *juche* ideology itself. Frequently translated as "self-reliance," the term actually has a broader connotation that is often overlooked. *Juche* is primarily a philosophical term (deriving from Western philosophy) that means "acting subject," as opposed to "object acted upon." Man, as North Korean announcers are so fond of pointing out, is the master of his own fate and can direct the course of history as he sees fit. No philosophical system can be so antithetical to historical materialism as North Korea's *juche* ideology. (One of the divisions between the first and second generations in North Korea today is their degree of commitment to scientific socialism, with a number of older cadres wistful about the old days, their training in Marxist-Leninism in Moscow and elsewhere, and their deep skepticism about the much greater pragmatism of the second generation.)

Urban markets are now everywhere. While still limited to individual stalls selling baked goods, their numbers have been increasing dramatically. Agricultural products from surpluses produced by collectives are showing up in these markets.

## Future Prospects for Cooperation

An initial hypothetical package of measures designed to integrate North Korea into the international community might consist of the following actions:

- In the field of agriculture: the provision of emergency food aid at the level of 1 million tons per annum for a period of five years; assistance in upgrading the production capacity of the urea plant in Namhung from its current 300,000 tons per annum to 500,00 tons; the introduction of 100,000 tons of modern seeds (maize, beans, vegetables, and rice) per annum for five years; the provision of 5,000 tractors and a

supply of fuel for their operation; and the dispatching of 500 agricultural technicians abroad for training.

- In the field of energy: the construction of a 1 million kWh capacity thermal power plant outside of Pyongyang operating on coal and mixed coal/oil or possibly two 500,000 kWh capacity units.
- In the field of light industry and exports: the provision of textile machinery by the United States, along with the extension of a textile quota in the amount of 3 million dozens per annum. Until such industry begins to thrive, North Korean citizens will require a variety of consumer goods, including clothes and daily necessities.

## Conclusion

Suppose the United States and others, principally China, were to be successful in persuading North Korea to enter into a “genuine” political dialogue with South Korea; what would they have to say to each other across the table? Would there be anything in common beyond comments about the weather? A common Korean future? Very unlikely. National reconciliation and mutual forgiveness? Hardly. A rational understanding of the mutual threat and an agreement to move gradually toward normalizing relations? Possibly, but only after a decade or more of such discussions, during which time incidents of various kinds are bound to offset any modest gains achieved. In the meantime, military buildups would continue, creating the conditions for another full-scale confrontation involving millions of lives.

The North Korean drive to normalize relations with the United States represents the single greatest opportunity to truly stabilize the situation on the Korean peninsula. Since 1988, when this policy was formulated, North Korea has shown itself prepared to compromise and make concessions when necessary, although it has often done so reluctantly. KEDO is but one example. The freezing of the North’s nuclear reactor program has remained in place, and the facilities for the canning of spent fuel rods are well on their way to completion. Inter-Korean trade, though conducted quietly, has been under way for close to a decade. Signs of a major economic readjustment in the domestic economy are now visible. Above all, there is a new willingness to discuss military and security measures trilaterally (with the United States and South Korea), along with a new interest in a US security posture that encompasses the whole of the peninsula.

The proper US response under such circumstances is to forge a comprehensive policy consisting of security discussions that include South Korea, economic assistance on a large scale, and extensive people-to-people exchanges in a wide variety of fields (technical, professional,

academic, and educational). Simply extending diplomatic recognition to Pyongyang is not enough. A policy that encourages friendship and mutual respect along a broad front of cultural relations is the key to unraveling the tightly wound knot that is the Korean peninsula today. This approach is our best hope for the current generation. If the opportunity is missed, it may not come around again for generations.

What of South Korea? Can there be any doubt that South Korea would be the greatest beneficiary of a genuine improvement in relations between Pyongyang and Washington? Suppose for a moment that North and South Korean exchange students were studying side by side at a US university. Over time they would become friends, as each came to understand that the other party was not some creature from Mars. What better means are available for a reduction in tensions than these? In fact, the process, thanks largely to North Korean strategy and US leadership, has already begun in Simpo, a remote location in South Hamgyong Province in North Korea, where engineers are building two light-water reactors. Far better to encase this strategy in a rapid normalization of relations with Pyongyang than to continue the current state of high tensions in the world's most dangerous place.

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