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Master Thesis



North Korea and a potential economic opening-up strategy for the future

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“On my honour as a student of the Diplomatic Academy of Vienna, I submit this work in good faith and pledge that I have neither given nor received unauthorized assistance on it.”

Abstract

English:

This thesis focuses on North Korea and the country's potential in the future. It aims to find answers to North Korea's political and economic development and whether or not an opening-up strategy to the international community could be expected or not. As the country has much in common with its most important trading partner – which is China – there is the assumption that North Korea could follow a similar foreign policy ever since Mao Zedong. In order to get a better understanding of what made the North Korean state what it is today, a closer look at the history since the Japanese colonialism has been provided in this thesis. By using secondary data and statistics the main part of this thesis focuses on North Korea's political regime and provides a glimpse into its socialist command economy. Comparisons to China are provided consistently in order to set up a relevant benchmark. Finally, an expert interview has been conducted in order to understand the future direction of North Korea and what one can expect within the next 25 years. North Korea's way out of an introverted socialist system could potentially be achieved through easing its nuclear programme, restricting power on the highest level of government and involving leaders into multilateral peace and trade talks internationally. In economic terms, North Korea needs to abandon its "military first" policy and better manage its imports and exports, since the country has much to offer.

German:

Der nordkoreanische Machthaber Kim Jong Un gilt als der bisher weltoffenster Führer in der Geschichte des Landes. Im Jahr 2018 standen sowohl Treffen mit dem südkoreanischen Präsidenten, als auch dem amerikanischen Präsidenten am Programm. Dies könnte ein Startschuss für eine wirtschaftliche und politische Öffnung des Landes bedeuten. Diese Arbeit analysiert daher eine potenzielle Öffnungsstrategie Nordkoreas und zieht Vergleiche mit dem wichtigsten Handelspartner – China. Nach einem geschichtlichen Überblick geht diese Arbeit insbesondere auf das politische Regime und die wirtschaftliche Situation ein. Den Schluss bildet ein Experteninterview, in welchem auch Ausblicke für die nächsten 25 Jahre prognostiziert werden. Nordkoreas erfolgreiche Öffnung könnte über eine atomare Abrüstung, Einschränkungen des Machtapparates, sowie ein besseres Management von Im- und Exporten in Zukunft durchaus Potential haben.

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List of Abbreviations

CIA	Central Intelligence Agency
DPRK.....	Democratic People’s Republic Korea
FDI.....	Foreign Direct Investment
GDP.....	Gross Domestic Product
IAEA	International Atomic Energy Agency
IT	Information Technology
KPI.....	Key Performance Indicator
MIT	Massachusetts Institute of Technology
NSC.....	National Security Council Report
NPT	Non-Proliferation Treaty
OEC.....	Observatory of Economic Complexity
OECD	Organization for Economic Co-operation and Development
SAIS	School of Advanced International Studies
SEZ.....	Special Economic Zone
SOE	State-Owned Enterprise
UN	United Nations
US	United States
USD.....	United States Dollar
WTO	World Trade Organization

1. Introduction

In this introductory chapter, the author would like to introduce the main research question of his master thesis and point out why it appears to be relevant studying this respective area more closely. Finally, a theoretical framework as well as a methodological approach will be introduced for studying this topic.

1.1. Research Question and Objective

In the course of this master thesis, the following research question should be answered and elaborated on:



What could a North Korean economic opening-up policy look like?

Apart from offering insights into impacts that a North Korean opening-up policy might have, the objective of the author's research work is to test whether or not the following main hypothesis can be found true or not:



"North Korea's economic opening would be similar to that of China"

1.2. Relevance of Research Topic

After reviewing the existing literature, the author of this thesis has identified three main arguments in favor of studying this topic:

First and foremost, the last 18 years have reflected continuing rising tensions between North Korea and the rest of the world, thus, representing a **period of little progress**. In June 2000, a historic handshake between the North Korean leader Kim Jong-Il and South Korean president Kim Dae-Jung marked a moment of re-opening borders and re-uniting separated families. However, shortly after, this surprisingly sparkling relationship deteriorated again rapidly and eventually turned into many years of fear until 2018. One could identify North Korea's ongoing nuclear provocations, especially after 2009 when the country started testing various long-range missiles. Following tight tensions of the UN Security Council (e.g. capping North Korea's oil imports, stopping joint ventures with other nations, banning textile exports¹), North Korea continued even further to test long-range missiles and undertake nuclear tests in 2017. It was exactly

¹ Zachary, C. and Richard, R. (2017): UN passes fresh sanctions on North Korea

the year when Kim Jong-Un announced that his country had successfully developed missiles carrying nuclear warheads which could potentially reach United States mainland. In contrast to the years before, 2018 really has brought about significant differences to North Korean relations than the years before. In January 2018, North Korea decided to send a team to the Winter Olympics in South Korea. Only three months later, Kim Jong-Un became the first North Korean leader ever to meet the South Korean president Moon Jae-In in order to hold talks. These talks ended in agreeing on finishing hostile actions and reducing nuclear weapons on the Korean peninsula. Finally, in June 2018, the historic meeting between US president Donald Trump and North Korean leader Kim Jong-Un took place in Singapore in order to end the nuclear tensions, which have lasted for so many years.² Obviously, this contrast to many previous years without any real progress at all, makes it relevant to study a North Korean opening-up scenario more closely at this point.

Second, the future development of North Korean relations appears to be interesting for **international security matters**. What could the region expect from a North Korean opening-up? Are there indications that it could be as peaceful as the recent Chinese rise? Among others, China has a vast interest in peace on the Korean peninsula. This is because of the country's grand strategy, which basically developed out of a history of numerous wars (e.g. South Korea, Japan and India). As China is moving from a regional mid-level power to a global superpower, it has defined strategic 5-year plans that also state its interest in peace and stability. In 2015, the 16th 5-year plan has turned into effect and will last until 2020. One may find China's goal to rise peacefully among the most important ones.³ Regional security cooperation in Asia has become extremely important and China has participated in many security talks thereafter. Especially with regards to the North Korean issue, China has taken a different role than its counterparties like the US, Japan or South Korea in the recent years, in that it drives a more passive/defensive approach towards North Korea.⁴ This is because China cannot afford nuclear disputes right in front of its door, as this would not be in favor of its strategic plans, its economy and the country's inhabitants of course.⁵ Furthermore, with peace on the Korean peninsula, China would maintain an important buffer zone between itself and the west, as American troops are stationed right at the border to

² BBC News (2018): North Korea profile - Timeline

³ Robert, K. (1971): The big influence of Small Allies, pp. 166-168

⁴ Bjorn, J. and Linus, H. (2012): Rethinking Japan's China Policy, pp. 224-239

⁵ Ester, F. (2017): What is China's role in the North Korean crisis?

South Korea for example. In general, North Korea cannot really be seen as having served as intrinsically valuable to China as a trading partner, but truly did so as a military ally.⁶ Thus, researching what a potential North Korean opening-up policy could look like in the future may provide valuable insights into international security cooperation with regards to the Korean peninsula.

Finally, the author's research topic seems interesting to research on because looking at a North Korean country that would be willing to develop its economy through opening up measures, also other countries might find complementary sectors they could potentially invest in and link their economy more closely to the North Korean one. In short, the topic of this thesis could suggest for new **economic co-operations**, which have not been identified as such in previous research work. The North Korean economy seems to be the most unknown one in the world and from an outside perspective it is almost impossible to get a detailed glimpse into the country's economy. This is mainly because the North Korean government has suppressed economic and social data in order to not let outsiders make a valid estimate of its economy.⁷ Though, in order to talk about complimentary economic possibilities, one must at least understand what the main features of the economy look like. This thesis will try to bridge this gap by using an economic mirror analysis of North Korea's economy.

1.3. Literature Review

Having outlined why it makes sense to research further on this topic, the author has collected various academic material in order to find an answer to the research question stated above. The current state is to be described through the strengths and weaknesses of the literature that already exists.

In terms of the strengths of the existing literature, one may find several previous work that helps to answer the research question. First, the current literature offers a very concrete and **solid picture of China**. This is particularly true for historic moments (Guoqiang, T.), the country's internationalization process and market development since 1978 (Guang, T. et al), as well as data about the economy (National Bureau of Statistics of China). Especially one can infer detailed information about each internationalization step towards opening-up China's economy and allowing for more

⁶ Victor, C. (2012): The Impossible State: North Korea, past and Future. p. 318

⁷ Nicholas, E. (2015): North Korea's „Epic Economic Fail“ in International Perspective, p. 10

international trade. Peter Buckley for example has divided this process into five major steps – cautious internationalization, government encouragement, expansion and regulation, implementation of a “go global policy” and the post-WTO period. This information will be supportive in determining similarities and differences between the two countries profiles, but could also allow for establishing an appropriate theoretical framework for dealing with the case of North Korea.

Second, the existing literature provides surprisingly much information about the **North Korean history** ever since the Korean War. In his book “A History of Korea: From Antiquity to the Present”, Michael Seth uncovers the contemporary North Korea between 1953 and 1993. This picture helps to better understand why the situation in North Korea is as worse as it appears and one can also infer from this a potential future state by using estimations, like Il-Dong, K. in his article “Korea’s Reunification from the Perspective of Northeast Asia’s Economic Integration”. Among others he looks at a united Korean peninsula and describes disparities between North and South Korea based on historic events. For example, he suggests that differences in income would be almost 20% after a re-unification, but only 2.4% 30 years later. Also he mentions, that it would take at least 25 years for the North to catch up on a similar GDP per capita level with the South. This detailed information about a future state could be used to describe potential North Korean economic reforms once introducing an opening up policy.

Another strength of the existing literature would be that it offers much insights into **North Korean living standards**, which makes them comparable to other standards abroad. This information would be particularly important when comparing the North Korean standards to the Chinese ones before its opening up measures in 1978 under Deng Xiaoping. One can infer data about the food supply, GDP per capita, infant mortality rates, number of doctors, life expectancies, number of hospital beds, refugees etc. In his paper, “Height and living standards in North Korea from the 1930’s to 1980’s”, Pak, S. infers from the development of heights the underlying socioeconomic, nutritional and epidemiological factors within the society. For example, before the Korean division the North Korean cohort used to be taller than the South Korean one. This changes drastically after 1948 and confirms, contrary to some socialist propaganda, that North Koreans are not enjoying the same standard of living like their Southern counterpart (approximately 2cm in difference). Hare, P. adds up to this in his

paper “North Korea: Building the Institutions to Raise Living Standards”. He talks about the issue of lacking food supply in North Korea and that farmers there do not feel confident that any gains in their income will not be confiscated by the political regime. Furthermore, Hare, P. even draws a comparison to the case of China and suggests that Chinese measures during their previous economic-opening could work similarly with North Korea.

Finally, previous research has explained **trade between China and North Korea**. In their paper “Trade between North Korea and China: Firm-Level Analysis”, Seung-Ho Jung and Byung-Yeon Kim found that Sino-North Korean Trade has increased substantially between 2000 and 2013, when even that was a period of tough economic sanctions on North Korea from other countries. As the following graphic depicts, around 80% of North Korean foreign trade is with China (unit: million USD):

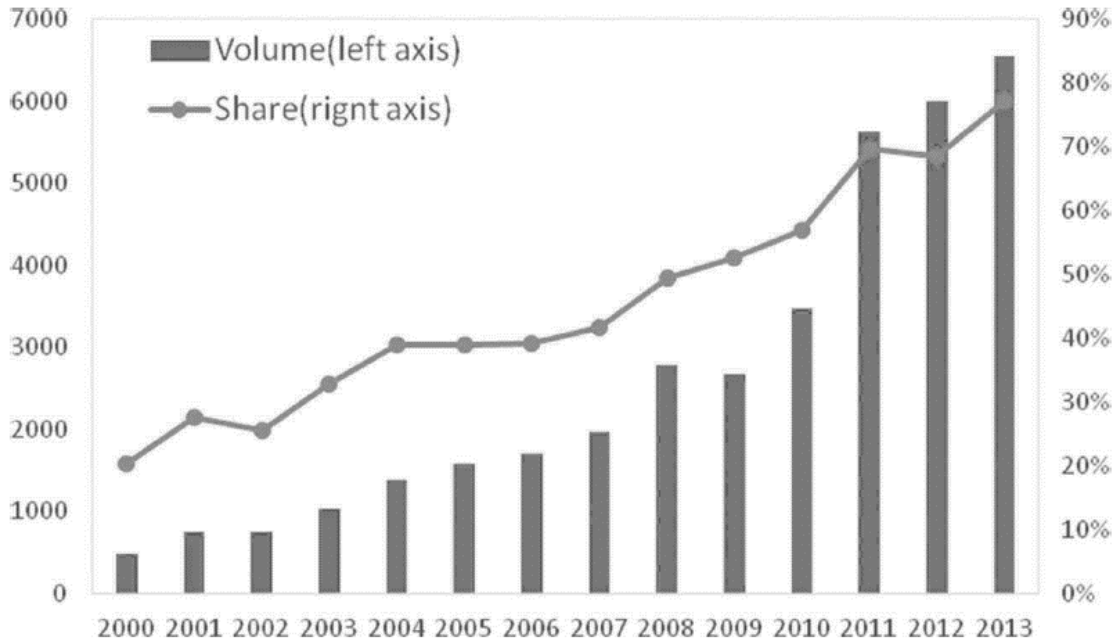


Figure 1: Trade between North Korea and China: Firm-Level Analysis
 (Source: Seung-ho, J. and Byung-Yeon, K., p. 1487)

Obviously, the North Korean economy depends heavily on China. Also, the authors state that North Korean firms do see China as an example with regards to its business activities and its economy as such. Therefore, could China serve as a role model for the North Korean economy and a potential opening-up?

In contrast to the strengths of the existing literature described above, the author of this thesis has also identified some limitations. First and foremost, the **reliability of**

economic data about North Korea remains to be an open question and leads to a research gap. The North Korean socialist regime usually suppresses any social and economic data in order to deprive persons from other countries of an independent ground for taking a measure of its country's performance. As mentioned earlier, Nicholas Eberstadt has dedicated himself to this issue and tried to make use of "mirror statistics" on North Korean international merchandise trade. For example, he found that North Korean trade performance is even worse than the one of Haiti or Argentina and that meaningful long-term economic progress should not be expected. However, "mirror statistics" will probably not provide a 100% accurate overview about North Korean economic key performance indicators.

Second, as much as economic data from North Korea remains quite unreliable, we also do not know much about the **country's strategy**, main intentions and grand plans. Of course, we do know that North Korea's centrally planned market economy has established various plans (e.g. two year plans, three year plans, five year plans, seven year plans), but details and insights remain to be deficient. In their paper "The Evolution of the Informal Economy in North Korea", Byung-Yeon Kim and Min Jung Kim talk about this issue by pointing to the fact that much information about the country's intentions has been received from surveying refugees only and not from official sources. In addition, much of the information received by refugees is about living standards and their view on the economy but less about North Korea's intentions. Thus, knowing nothing or only little about North Korea's intentions with regards to its economic future makes it more difficult to arrive at an accurate conclusion to how exactly their potential opening-up policy could look like.

1.4. Theoretical Framework

The research question “What could a North Korean economic opening-up policy look like?” will be the center of the authors’ theoretical concepts. For conducting his work, the author uses key concepts and theories within three main areas:

1. Concept for gathering insights about North Korea

In order to make North Korea comparable to China, one has to gather relevant information about the political command economy of North Korea and interesting economic facts. As aggregated data is quite difficult/impossible to receive directly from the country, one has to use other concepts to make the best accurate estimations. One concept the author would like to suggest is the so-called concept of “mirror statistics”. In his paper “North Korea’s Epic Economic Fail in International Perspective”, Nicholas Eberstadt has introduced such a concept in 2015 when trying to put the North Korean economy into numbers. Basically, he reconstructed the trade of North Korea on the basis of data reported by trading partners, especially China. For example, the construction of economic data has shown that North Korea has been more dependent on economic aid than the least developed countries classified by the UN and Sub-Saharan Africa (e.g. between 1990 and 2000: more than twice as aid dependent).⁸

2. Theories for comparing the North Korean with the Chinese system

There are quite a few economic theories this thesis will use in its argumentation. First and foremost, there is the Heckscher-Ohlin theorem. As the critical assumption of this model is that the two trading countries are more or less similar (except for the resource endowment), this would follow the idea of this work because North Korea and China will be compared not just in political terms, but to a wide extent in terms of their economy as well. Also, in relation to this, one has to take a look at the two country’s economic output (in terms of products, services etc.) and therefore consider the Heckscher-Ohlin theorem for determining the comparative advantage of each country. This model considers the differences the factor endowment and the technological progress.

Furthermore, in order to understand whether or not an economic opening-up strategy of North Korea could be similar to that of China, one has to understand the main theories of the Chinese one. One quite interesting theory by Lee Branstetter and

⁸ Nicholas, E. (2015): North Korea’s „Epic Economic Fail“ in International Perspective, p. 50

Nicholas Lardy describes that a country with decentralized internal structures allows regional leaders to have a greater influence on privatizing sectors of a respective state as well as energize the regional economy.⁹ Particularly, this can be observed once local governments were allowed to solely regulate both domestic and foreign joint ventures that were within their jurisdiction.¹⁰ Another theory is about incentives provided by the Chinese government. Certain officials presiding over important regions of substantial economic growth were very likely to become promoted over time.¹¹ What is more, Loren Brandt and Thomas Rawski also suggest another theory for China's opening-up success. They believe that the success of the reforms conducted in China can be attributed to Deng Xiaoping's cultivation of all his governmental followers, meaning to shape a common picture of the countries objectives and roadmap.¹²

3. Ongoing international security through a North Korean opening

Given North Korea's nuclear provocations and threats to international security, the author considers it important to come to a conclusion whether or not a potential opening-up strategy bears a risk to the region. A suitable theory that describes this risk would be the regional security community theorem introduced by Karl Deutsch in 1957. It describes a group of countries that have achieved a high level of corporation. In general, three major characteristics can be identified by looking at this theorem: members share the same identities, they have direct relations and a long term interest in each other. It appears to be interesting to see whether or not a North Korean opening-up strategy fulfills the requirements of this theorem. So far, the current literature suggests that all three elements of this theory are true for the relationship between North Korea and China (the security theorem still holds)¹³ but does not provide an insight if this could change during economic policy adaptations in the future.

⁹ Loren, B. and Thomas, R. (2008): China's Great Economic Transformation. p. 17

¹⁰ Lee, B. and Nicholas, L. (2006): China's Embrace of Globalization. pp. 9-11

¹¹ Lee, B. and Nicholas, L. (2006): China's Embrace of Globalization. p. 13

¹² Loren, B. and Thomas, R. (2008): China's Great Economic Transformation. pp. 18-19

¹³ Peter, J. (2008): South Asia: Is a Regional Security Community Possible?, pp. 188-190

1.5. Approach and Methodology

In general, for his thesis the author would like to mainly use qualitative methods. Therefore, the author will mostly use secondary literature (e.g. books, academic research articles) and descriptive statistics (e.g. National Bureau of China, Statista) for his work. For the gathering more up-to-date insights, filling gaps of any data deficiencies as well as making further estimations with regards to the topic of this thesis, the author also will conduct some expert interviews and transcript them in writing. The author will not use a deductive way of arguing, but rather an inductive one. This is because the findings of each chapter will be relevant to come up with an own theory in the end and answer the research question. Generally, the disciplines involved will to the greatest extent deal with subjects of economics as well as international relations.

In order to begin writing the thesis, the author would first like to look at the history of the Korean peninsula ever since the Korean War during the mid-20th century by using secondary literature. The divergence of North and South Korea shall be explained on the basis of adequate books, like “A History of Korea: From Antiquity to the Present” or “The North Korean revolution 1945-1950”. Additional information on the development of the North Korean economy shall be gathered through suitable academic articles. In general, within chapter 2 “North Korean History” the author aims to collect limitations and strengths for a possible North Korean opening-up policy. Also, the author would like to identify contributing factors that made the North Korean economy what it is today.

For the third chapter, the author would like to provide a glimpse into what a command economy in North Korea looks like. He wants to gather detailed information about the country’s socialist regime and economy through using academic articles, statistics, and estimations. Suitable research articles would be “Understanding the North Korean Regime”, “International Isolation and Regional Inequality: Evidence from Sanctions on North Korea” or “Market Socialism in North Korea: a Comparative Perspective”. Also, interviews with North Korea experts should help to fill gaps between what is already know about the economy and research deficiencies. What is more, this chapter also aims to provide a detailed glimpse into the Chinese system. By using secondary literature and descriptive statistics, the author aims to arrive at a current state of China’s political and economic situation in order to compare these findings with the ones from North Korea in the end of this chapter.

Finally, the fourth chapter aims to connect with the findings of chapter 2 and chapter 3 in that it suggests a potential similar opening-up strategy for North Korea as with China. Also, this chapter makes a research contribution by identifying possible complimentary economic sectors between North and South Korea. In order to gather the right data for this economic comparison, the author will dedicate much of his work analyzing statistics and country reports about South Korea. In addition, expert interviews will help to pick up on any data that is not available or deficient.

2. North Korean History

This introductory chapter focuses on the modern historic developments on the Korean peninsula starting from the early 20th century. It aims to find limitations as well as strengths with regards to an economic opening-up strategy in the future. Apart from that, this chapter will also talk about contributing factors, which make North Korea what it is today.

2.1. The Roots of a Divided Korea (Prior to 1945)

With the Japanese empire collapsing on August 15 1945, also its long lasting colonial power over Korea did come to an end. In fact, Japan had major colonial power over Korea since 1910.¹⁴

In the early 20th century many Western powers, and Japan, wanted to increase their trade performance abroad and, thus, wanted to also gain more influence in Far East Asia. Through Japan's successful Meiji restoration, which took place between 1868 and 1912, and which represented a modernization of the government, the country eventually turned into becoming a westernized society. Shortly before Japan's colonial influence in Korean, Japan put much pressure on Korea in 1876 in order to gain extensive territorial rights there. In fact, Japan aimed to enforce the signing of the so-called Japan-Korea Treaty in that respective year. This treaty gave more rights for Japanese citizens on Korean territory and also allowed for the opening of three Korean ports in order to boost Japanese trade.¹⁵

After Japan's annexation of Korea in 1910 and given the overcrowded rural areas in Japan, a massive amount of Japanese inhabitants settled in Korea between 1910 and the Second World War. This brought about huge land purchases by the Japanese, which lead to a strong increase in land ownership too. In fact, Japanese owned more than 50% of the available land in Korea.¹⁶ These purchases aimed to confiscate any available land, which has not been owned by farmers. Voices against the Japanese ideology were big and in the course of these events, a Korean guerilla movement was established harassing Japanese authorities. Among the most important leaders of this movement was the Communist Kim Il-sung. Literature suggests, that he was

¹⁴ Mitsuhiro, K. (1999): From fascism to communism: continuity and development of collectivist economic policy in North Korea. pp. 69-70

¹⁵ Peter, D. (1995): The Abacus and the Sword, pp. 19-20

¹⁶ Edward, C. (1970): Japanese Colonialism in Korea and Formosa: A Comparison of The Systems of Political Control, pp. 138-139

profoundly shaped by the experiences he made during growing up in a colonial Korea.¹⁷ Also, during the time of Japanese colonialism (1910-1941), Japan developed an extensive heavy industry in the northern part by installing steel mills, manufacturing plants and hydro-electric dams. As a result, the North could be described as more industrialized, whereas the agricultural sector was to be found more towards the Southern part of Korea. Japanese influence was extremely high, for example they claimed that Koreans were now Japanese. What is more, all public and official documents, job applications and school records had to state the level of origin. This means that it should have been clearly visible whether a person corresponds to a “homeland Japanese” or a “peninsular Japanese”.¹⁸ After the collapse of the Japanese empire, the Korean peninsula was then politically divided into the North (influenced by the Soviet Regime) and the South (influenced by the United States). In the South, Koreans who used to work closely together with the Japanese were confirmed in their respective positions and could even grow to become political influencers and leaders. Also, these people were allowed to keep their economic properties and ownership of farm land. In contrast to this, the North was characterized by the exact opposite. Former Korean elites, who used to work together with the Japanese, were expelled from the country without any hesitation. Furthermore, the heavy industry (including all the mines), which was mainly built by the Japanese and accounted to approximately 63% of the GDP¹⁹, was put under state ownership and management.

2.2. Korean Division and a New North Korean Government (1945-1949)

The previous sub-chapter 2.1 “The roots of a divided Korea” introduced that Korea was liberated from the Japanese rule both by the Soviets and the Americans. There were several developments during the final hours of the Second World War, which turned out to be important in creating the division of North and South Korea. Though, among the most outstanding ones was the emerging rivalry and conflict between the Soviet Union and the United States on the other hand.

First and foremost, one can identify the Tehran Conference in 1943 as a crucial moment in modern Korean history. Basically, this conference was a meeting carried out in Tehran between November 28 and December 1 between the U.S. President

¹⁷ Michael, S. (2010): A History of Korea: From Antiquity to the Present. pp. 289

¹⁸ Michael, S. (2010): A History of Korea: From Antiquity to the Present. pp. 289

¹⁹ Stewart, L. and Gavan, M. (1993): Korea since 1850. pp. 184-185

Franklin Delano Roosevelt, the Soviet Premier Joseph Stalin and the British Prime Minister Winston Churchill. The main intention of this conference was to discuss and coordinate the three leaders' military strategy with regards to Germany and Japan as well as to make certain key decisions on the area after the Second World War.²⁰ The main decision made was a consensus to construct a second front against Nazi Germany to be initiated by May 1944. In 1945, the Soviet Union declared war on Japan and the United States became quite concerned that they would also want to occupy the whole territory of Korea, as Soviet troops were advancing into the country substantially fast. This movement was not in accordance with what was discussed two years earlier at the mentioned Tehran Conference, namely that military moves should be coordinated and agreed on by consensus between the Soviet Union, Great Britain and the United States. This incident really marked the moment when Korea was being divided, without actually being involved in the decision making process. This is true, as the Soviet Union and the United States jointly decided to divide Korea into two separate occupation zones between 1945 and 1948. During that time, the Soviet Army and its allies initiated a communist regime in the northern area of the 38th parallel. In the southern part of this line, US military troops were stationed in order to support the South and its military capabilities. It is important to mention that the 38th parallel was an arbitrary line only and did not correspond to any cultural, geographical or historical division of Korea. This cutting point was between the two provinces Kyonggi and Kangwon and was never proposed to set up by any Korean in history ever. It was the decision of the two big players only – the United States and the Soviet Union – to set up such a division.²¹ In total, 16 million Koreans were placed within the zone of the United States, whereas 9 million Koreans were placed within the zone of the Soviet Union.²²

²⁰ Office of the Historian (2018): The Tehran Conference, 1943

²¹ Michael, S. (2010): A History of Korea: From Antiquity to the Present. pp. 307

²² Adrian, B. (2007): The Making of Modern Korea, p. 53



Figure 2: The 38th Parallel Separating the North from the South

(Source: <http://geoawesomeness.com/top-20-maps-charts-explain-north-korea/>)

Given the Soviet influence in the North, a Communist regime was being put in place quite quickly in 1946. By the time Soviet troops entered the North Korean capital Pyongyang, they were happy to see that a local People's Committee was already established. Since Kim Il-sung entered North Korea shortly after, he was celebrated as a national hero who could identify extremely well with Soviet ideologies and strategies. Also, as he had fought against the Japanese in the previous years, he was a highly respected person. On February 8 in 1946 a Provisional People's Committee started to carry out a number of reforms under close surveillance of the Soviets and their hero Kim Il-sung. Even though the Committee used to be a broad coalition of various groups, it was strongly dominated by the Communists, who aimed to increase their dominance over the country. The following months were characterized by carrying out the nationalization of the Japanese industry. According to the Law and Land Reform in March 1946, any land that used to be owned by Japanese was confiscated. Indeed, this was a distribution from bigger landlords to smaller families. Taxes corresponded to a given rate of 25% of the crop. A number of other quite popular measures were conducted by the regime in summer 1946:²³

- Granting equality to woman

²³ Michael, S. (2010): A History of Korea: From Antiquity to the Present. pp. 313-314

- Creating large scale social organizations
- Mobilizing peasants and workers with little previous power
- Implementing universal primary education
- Establishing rudiments of a defense force

Also in summer 1946, the Korean Communist Party, which was led by Kim Il-Sung, turned to become the North Korea's Workers' Party. During elections in 1947, this party received 97% of the votes. Step-by-step, Kim Il-Sung succeeded in establishing a centralized government with influencers and branches at each and every local level. The new government under the guidance of the North Korean Workers' Party organized youth, woman, intellectuals and labor in support of a different economic order. Given all these events, the proud Soviets kept promoting Kim Il-Sung as the leader and placed his picture publicly next to the one of Stalin. Also, a national university was named after Kim Il-sung in late 1946.²⁴

In the meanwhile, unlike the Soviet Union, the United States still wanted to come to a conclusion on what to do with Korea. Therefore, in 1948 the United States requested a United Nations vote for the inhabitants of the Korean peninsula to determine on the future by themselves and not let anyone else take their decision. Shortly after, the North did not accept to participate, which lead the South to initiate its own government. The response of the North resulted in the installation of the former communist guerilla Kim Il-Sung to be appointed the first president of the Democratic People's Republic of Korea (DPRK).²⁵ By 1949, North Korea has turned completely into a fully Communist state, with a government moving extremely quickly to create a political system reflecting the Soviet style.²⁶

2.3. The Korean War (1950-1953)

We learned from the previous sub-chapters that North Korea has highly benefited from Soviet support with respect in building infrastructure, creating a defense force and also establishing a certain mindset against the old Japanese ideologies. Given this information and North Korea's ongoing willingness to re-unite the two Koreas, in late 1949 North Korea sought support from the Soviet Union for a war of re-unification.²⁷ In the beginning Stalin did not appear to be too happy about this decision but changed

²⁴ Charles, A. (2003): The North Korean Revolution, 1945-1950, pp. 56-58

²⁵ Sarah, P. (2018): Why are North and South Korea divided?, p. 2

²⁶ Adrian, B. (2007): The Making of Modern Korea, p. 67

²⁷ Adrian, B. (2007): The Making of Modern Korea, p. 72

his mind in 1950, once nuclear weapons were successfully tested and China announced that they would be willing to support Kim Il-Sung's initiative.²⁸

On June 25, North Korean troops finally crossed the 38th parallel to the South with approximately 75,000 soldiers. This invasion can be referred to as the first military action of this Cold War. Only one month later, American troops also entered the war to come help their South Korean friends. From their point of view it really was a war against the spreading of Communism worldwide and that's why it actually captured their interest as well. Nonintervention was not an option for the United States and there was even a National Security Council report²⁹ (NSC-68) that recommended to use military force against the spreading of Communism if necessary to do so. Once North Korean troops occupied the South Korean capital Seoul in late 1950 the United States prepared theirs as well for fighting against Communism there. In the beginning, the war could be described as a rather defensive one, meaning that the ultimate goal was to throw the Communists out of the South. However, this did not work out as planned due to a North Korean army that had much knowledge in fighting and extensive war equipment given their Soviet support. In contrast to that, the South Korean army turned out to be rather frightened and helpless under their president Syngman Rhee.³⁰

In late 1950, former president of the United States Truman and his General Douglas MacArthur, agreed on a new set of war goals. Instead of pursuing a strategy of a defensive war, they now aimed to turn the war into an offensive one. This means that their strategy was to liberate the North from the Communist influence. In the beginning, this strategy was quite successful as North Koreans were pushed out of Seoul again and back to the 38th parallel. However, as American troops kept moving forward towards the North and towards the border between North Korea and China, the Chinese began to become frightened about this American intervention and saw their territory in danger as well. Therefore, the former Chinese leader Mao Zedong sent troops into North Korean territory and warned the United States of a full-scale war.³¹ It is important to mention here that the whole war itself was strongly based on the involvement of the United Nations, even though the United States controlled these

²⁸ Martin, B. (2006): Under the Loving Care of the Fatherly Leader: North Korea and the Kim Dynasty, pp. 85-87

²⁹ National Security Council (1950): NSC68: United States Objectives and Programs for National Security, IX.

³⁰ History (2018): Korean War

³¹ History (2018): Korean War

supplied forces (no control over combat forces by the UN). In fact, during the Korean War military forces of several UN member states (e.g. United Kingdom, Australia, France, Belgium, Netherlands, and Canada etc.) were sent off to Korea in order to support the South and push back communism to the North. Among all involved UN member states, the US represented the largest contributor, deploying around 140,000 personnel in Korea. Additionally, several countries, like Denmark, Sweden or Norway, provided direct humanitarian support for soldiers and individuals in need.³²

Until 1953, heavy fighting continued along the 38th parallel including an extremely high number of casualties. As a result of this heavy fighting, much of the infrastructure in North Korea (including its heavy industry and manufacturing plants) was destroyed.³³ After two years of peace negotiations, the so-called Korean Armistice Agreement was signed on July 27, 1953. This agreement drew new boundaries close to the 38th parallel and allowed South Korea additional 1,500 square miles of territory. Furthermore, the well-known “demilitarized zone”, which still exists today, was created at this point.³⁴ The following illustration depicts the four main phases of the Korean War, starting with the mentioned North Korean invasion of South Korea:

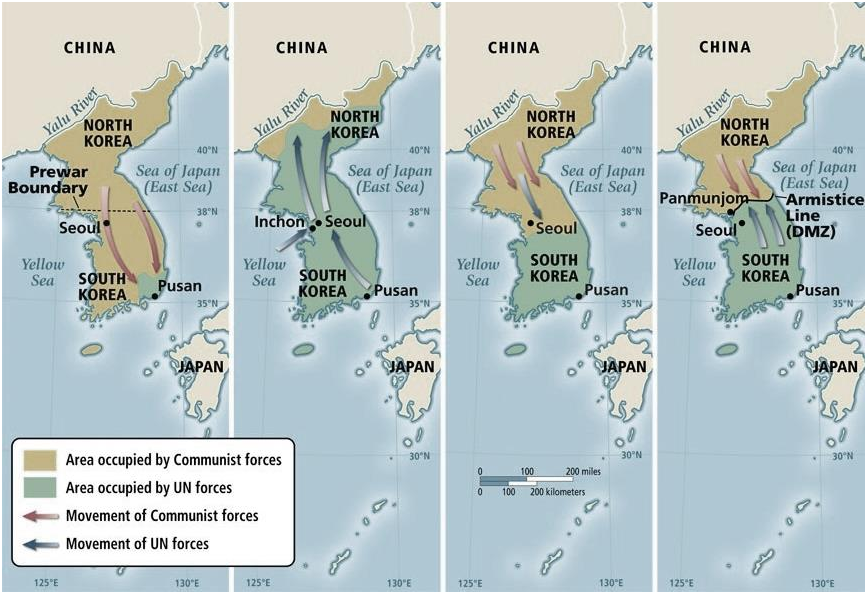


Figure 3: Phases of the Korean War

(Source: <https://www.quora.com/Why-was-the-Korean-War-so-different-from-the-Vietnam-War>)

The agreement followed a ceasefire, but until today no peace treaty has come into

³² ANZAC (2018): United Nations Forces in the Korean War
³³ Bruce, C. (2005): Korea’s Place in the Sun: A Modern History, pp. 297-298
³⁴ History (2018): Korean War

action. In a nutshell, the Korean War was rather short but characterized through extreme violence and bloody actions. Almost 2.5 million civilians and another 2.5 million soldiers lost their lives during this war. The rate of civilian casualties (approximately 50%) turned out to be even higher than the one during the Second World War and the Vietnam War. Even today, one can identify some hostile acts, but obviously at a much lower rate than during the time of the Korean War.³⁵

2.4. The Post-War Upwind

After the end of the Korean War in 1953 it could be observed that North Korea took a completely different path than their counterpart South Korea. The government, which had communist characteristics, strongly focused on the collectivization of agriculture and aimed to reduce small-scale industries as well as commerce by re-organizing them into consumers and producers cooperatives. This plan was accomplished in collaboration with the Soviets and China and eventually was finished in 1960. By then, a system of strict state control over the North Korean economy and all social activities by its individuals was successfully established.³⁶ In fact, these measures were described also in North Korea's first Five Year Plan, which had been in force between 1957 and 1961. This plan also sparked huge mobilization campaigns, which addressed an extremely high amount of people. Among one of the most important socialist movements in history represents the so-called Chollima Movement. Countrywide more than 227,000 people took part in this movement and helped to speed up socialist construction and economic development enormously. Basically, "Chollima" originates from China and the movement emphasized ideological incentives to work harder under the supervision of Kim Il-Sung.³⁷ One could argue that this movement had some similarities with a Chinese movement at almost the same time, namely the Great Leap Forward, which took place in China between 1958 and 1962. Likewise, it aimed to rapidly transform China from an agricultural based economy into a socialist society.³⁸

This North Korean system of strict state control over the economy was exactly what the Japanese rightists before 1945 had in mind with the country too. Thus, after the

³⁵ Bruce, C. (2005): *Korea's Place in the Sun: A Modern History*, p. 298

³⁶ Mitsuhiro, K. (1999): *From fascism to communism: continuity and development of collectivist economic policy in North Korea*. p. 83

³⁷ James, P. (2009): *New Evidence on North Korea's Chollima Movement and First Five-Year Plan (1957-1961)*, p. 66

³⁸ Michael, R. (2007): *Korea's Twentieth Century Odyssey: A Short History*, p. 151

Korean War, it can be observed that North Korea inherited much of the Japanese ideas and economic policies but expanded them even further through Chinese role models (e.g. through socialist mass campaigns like the Chollima movement). One might argue that this development was in fact a consequence of the collectivist philosophy dominating North Korea already since the 1930's. In addition to the Japanese influence it was further influenced by Stalinism and, of course, Maoism in China. From a general point of view, it can be said that the system was quite successful until the 1970s. Indeed, North Korea's economy and GDP growth were said to be almost equivalent to the South Korean one until that time.³⁹ ⁴⁰ Even though North Korea's economic conditions picked up substantially during the 1960's and 1970's, this did not lead to a relaxation of state control. The case was quite the opposite as Kim Il-Sung pursued an extensive militarization of the economy. That's how the country's main slogan "Arms in one hand and hammer and sickle in the other" finally evolved. And even abroad North Korea's system of a militarized planned economy caught attention, as it was the case with Cuba's president Che Guevara in the early 1960's, who saw the whole system as a role model for his country.⁴¹

2.5. The North Korean Turnaround after 1973

As mentioned in the previous sub-chapter, until the mid-1970's North Korea's economy developed similarly to the South Korean one. However, 1973 marked a turning point in this development phase. In order to accumulate North Korea's massive economic growth the country has taken out loans abroad to build upon its military industry, infrastructure and mining industry. Once the world oil crisis in 1973 started to set-in, North Korea was unable to pay for its debts and defaulted on basically all of the payments until somewhat 1985. In addition to the economic downfall through the economic crisis of 1973, some of North Korea's most important allies turned their back on the country. This is true, given that the dissolution of the Soviet Union (1991) and the Eastern bloc (1989-1990) caused severe additional damage to the North Korean economy as they used to strongly support the country through financial aid before. By that time, North Korea was left with China as its one and only ally left. Shortly after these major events, North Korean leader Kim Il-Sung died in 1994 and was succeeded

³⁹ Mitsuhiro, K. (1999): From fascism to communism: continuity and development of collectivist economic policy in North Korea. p. 84

⁴⁰ Bruce, C. (2005): Korea's Place in the Sun: A Modern History, p. 434

⁴¹ Mitsuhiro, K. (1999): From fascism to communism: continuity and development of collectivist economic policy in North Korea. p. 84

by Kim Jong-Il in 1994. The new leader faced an economic struggling country and started to radicalize the country's military even more. He constituted a new policy called "Songun Chong 'chi" or military first. This led to the establishment of the Korean People's Army, which can be seen as the leading economic and political force in North Korea until today. This new measure brought about additional inequalities between the military and the vast majority of ordinary citizens. Also, during the 1990's poor agricultural policies, flooding and economic mismanagement in general resulted in a period of famine. It is estimated that hundreds of thousands of people died of starvation and malnutrition.⁴²

Given North Korea's poor economic management and vast military expansion, the country has tried to demonstrate its rigorous power to the West numerous times ever since 1990 through its quest for nuclear weapons. In fact, this has led to even more tensions between contemporary North Korea and western countries and has brought about four main nuclear crisis occurring in 1990, 1994, 1998 and 2002.⁴³ The following table briefly depicts these major crisis (from an American point of view):

<p>1990: First Nuclear Crisis</p>	<p>Already during the 1970's Kim Il-Sung decided that North Korea should build an atomic bomb by itself. The country could not hope to get assistance from the Russians or Chinese, but, given the know-how and the research reactor which the Soviet Union once had provided, North Korea initiated construction. In 1989, American satellites provided evidence that this plan was reaching fruition. In fact, the satellites detected an advanced construction site near Yongbon, which had the means to build an atomic bomb. As the Americans appealed to both the Chinese and the Russians, the IAEA got permission to inspect this construction. After a thorough inspection, the IAEA came to the conclusion that North Korea had produced more plutonium than a small amount they had declared earlier.</p>
<p>1994: Second Nuclear Crisis</p>	<p>North Korea announced that it would withdraw from the Non-proliferation treaty (NPT) in May 1994 and ordered international inspectors to leave the Yongbon reactor.</p>

⁴² History (2018): North Korea

⁴³ William, P. (2006): Proliferation on the Peninsula: Five North Korean Nuclear Crisis, p. 79

	<p>Once again the country began to re-process the fuel, which would have made it possible from them to produce at least half a dozen nuclear bombs. As the United States, Japan and Korea stated their intend to impose severe actions, North Korea responded by saying that it's million-man army would turn Seoul into a "sea of flames". As this was not an option for security in this region, another solution had to be found. Fortunately, Kim Il-Sung finally agreed to shut down the reactor and began serious negotiations with the Clinton administration. In the end, this crisis was resolved by an agreement known as the "Agreed Framework". In turn, Japan and South Korea agreed to build new light water reactors for North Korea.</p>
<p>1998: Third Nuclear Crisis</p>	<p>In 1998 North Korea had designed two long-range missiles which could easily reach United States mainland as well as Japan. From a western point of view, this created serious concern that North Korea was working on enriching plutonium again for these nuclear warheads. The "Agreed Framework" was terminated again and the United States offered North Korea two options. First, if North Korea would forgo its missile program including its nuclear one, western powers would move to a comprehensive normalization of economic and political relations. Alternatively, if North Korea would not comply, this could result in necessary actions to contain that threat. In this case, the North Koreans were seriously interested in choosing option one, as they were hoping for economic support from the west, which they desperately needed. In 2000, Kim Jong Il even followed an invitation to Washington by sending a senior emissary.</p>
<p>2002: Fourth Nuclear Crisis</p>	<p>Once again, North Korea started to begin its nuclear program in 2002. Unlike the previous ones in Yongbon, this one was based at a covert location somewhere else. In the course of time, the Bush administration decided to</p>

	<p>cut off the fuel the United States provided to North Korea (under the “Agreed Framework”) and also persuaded Japan and South Korea to stop helping out with a light water reactor. At this point, the “Agree Framework” was basically nullified. During this crisis, China’s voice became more prominent as security challenges did interfere with its aim to rise peacefully. Thus, China pressures North Korea for ongoing multilateral meetings to solve the dispute. Finally, an agreement was reached that North Korea would stop its nuclear program, whereas the United States would not prepare military actions against it.</p>
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Table 1: Major North Korean Nuclear Crisis

(Source: own representation based on William, P. 2006)

After Kim Jong-Il died in 2011, Kim Jong-Un became North Korea’s new leader. However, evidence suggests that this did not significantly improve North Korea’s economic and political reputation. In fact, in addition to the nuclear issues mentioned before, North Korea was also accused by the United Nations of the most severe crimes according to international criminal law, for example crimes against humanity.⁴⁴

Based on the content of this chapter, the following sub-chapter would like to summarize the main strengths and limitations for a potential North Korea opening-up strategy and sum-up the main factors that made North Korea to what it is today. This evidence will be used for moving over to chapter 3 “North Korean Economic Assessment”.

2.6. North Korean History: Resume

With regards to North Korea’s history, one could identify strengths and weaknesses that would have to be considered in a potential opening-up scenario. First and foremost, the country possesses quite an extensive know-how in operating and building heavy industry. This is true, as North Koreans have learned a lot from Japan and the Soviet Union during the first half of the 20th century. Of course, it remains questionable whether or not this knowledge can still keep up with today’s fast moving

⁴⁴ North Korea: UN Commission documents wide-ranging and ongoing crimes against humanity, urges referral to ICC

economies, but technical know-how could still play an important role in introducing new foreign policies. What is more, originally, the country seemed to be much more people oriented than one might think. This is shown, for example, by the introduction of economic measures shortly after the Second World War (e.g. equality rights for woman, investment in primary education etc.) but also during its economic peak times until the 1970s. Also, this shows that a centralized government does not necessarily aim to do wrong on its people.

On the other hand, there are several points taken from history that would nowadays interfere negatively with ideologies abroad and in more modern countries. First, due to its strong historic relationship with the Soviet Union, North Korea obviously possesses a strong communist way of thinking. This form of government has become quite unpopular, given the fall of the Soviet Union in 1991, and many countries would probably be concerned to engage in a diplomatic, economic or business relationship with North Korea therefore. In addition to the communist North Korean command economy, there is the inherited rightist Japanese way of thinking, which originated from Japan's actions on the peninsula starting in 1910. What is more, one could observe the various nuclear crisis North Korea has triggered. This did and still represents a massive security issue for the whole region and the world. Additionally, the military, which plays an extremely important role in North Korea (e.g. Korean People Army) seems quite dangerous from an outside perspective. On top, history has shown that as North Korea's economic situation has worsened, the country defaulted on almost all of its payments and is currently not able to feed its population accordingly, thus, making negative news with starvation and malnutrition.

To sum up, history clearly shows that the more negative associations about North Korea outweigh the positive ones. The following chapter 3 "North Korean Economic Assessment" will draw a comparison between North Korea and China and will include the aspects found in this chapter for further evaluation and drawing of an opening-up path.

3. North Korean Economic Assessment

This chapter will now focus on analyzing the state of North Korea. It will talk about the political regime and will go into what a socialist command economy looks like in more detail. In addition, economic and political factors should be explained in the light of the Heckscher-Ohlin theorem in order to understand the country's abundant and scarce factors (politically and economically). At the various points, comparisons to China will be provided in order to analyze whether or not the prospects for an economic reform could be any consistent with the Chinese approach.

3.1. The North Korean Regime

In general, the political system in North Korea since the 1980's can be described through the concept of a leader system ("Suryong system"). In today terms this would described a system which aims to allow for the guidance of a leader through hereditary succession.⁴⁵ The North Korean Constitution has been restructured several times, which the most recent one in 2016, but the term "leader" appears to be relevant in most of its articles. For example, article 11 of the North Korean Constitution states that "the Democratic People's Republic of Korea shall conduct all activities under the leadership of the Worker's Party of Korea"⁴⁶, which means that the supreme leader of the Worker's Party gives guidance and direction to the country as a whole. As chapter 2 "North Korean History" has described, this role has been passed over from Kim Jong-Il to Kim Jong-Un after his death 2011.⁴⁷ Kim Jong-Un also severs as the Chairman of the State Affairs Commission, which duties are defined through Article 103 of the Constitution. Among these duties are some of the following:⁴⁸

- Direct the overall affairs of the State
- Appoint and remove important officials of the country
- Declare a state of war or emergency
- Ratify or terminate important treaties with other countries

In short, North Korean leader Kim Jong-Un basically has the sole power to manage the entire state by himself and enjoys **absolute authority** through the positions held by him. One might refer to this by using the term "Kimilsungism-Kimjongilism", which

⁴⁵ Takashi, S. (2013): North Korea's Political System, p. 1

⁴⁶ Atsuhito, S. (2017): Understanding the North Korean Regime, p. 11

⁴⁷ Dean, K. (2016): Analysis of contributing factors behind Pyongyang's belligerent stance and threats of instability in North Korea, p.599

⁴⁸ Atsuhito, S. (2017): Understanding the North Korean Regime, p. 12

describes an ideology of two important areas – Juche and Songun. Juche means self-reliance and includes aspects of ideological autonomy and political independence. On the other hand, Songun encompasses the military-first idea, which has already been established through Kim Jong-Il. In short, the term “Kimilsungism-Kimjongilism” centers on these two aspects and underlines North Korea’s political system, which is strongly based on a **military first policy** (Songun) as well as adopting **independent policies** which disregard other states (Juche). Even though the system has its political roots in the ideology of Leninism, it is now based on a combination of these two self-made ideas.⁴⁹ Thus, one might argue that the North Korean regime adapts socialism as a continuous form of government, which makes it difficult to estimate what the country has in mind for its people. However, given the democratic aspect within the constitution of North Korea (e.g. Democratic People’s Republic of Korea), one might wonder whether or not democratic elections could change the political system in North Korea or not.

Between its founding in 1948 and 2014 elections were held 13 times. In general, citizens who are 17 years and older are eligible to vote. What is interesting to mention, the elections use a system of confidence, wherein only one candidate is proposed in each constituency. The last election in 2014 showed that a total number of 687 candidates were proposed for the respective constituencies and all of them were also elected, with an approval rate of 100 percent. Throughout the voting process, citizens would present their identification cards and receive a ballot paper with the respective names of the candidates on it. Two options exist for the medium voter: (1) do not mark anything on the paper if you approve and (2) cross of the candidate’s name if you disapprove. In fact, if a voter only picks up the pen, it is clear that he or she would like to vote against the political regime. This example shows one of the functions of the political regime in North Korea, which is about **controlling its residents**.⁵⁰ One concrete example of how surveillance and control is being carried out becomes visible when looking at the extensive network of organizations and organizational membership. Generally, every North Korean citizen has joined an organization and is controlled through this organization (except infants and toddlers). For example, members of the Worker’s Party are part of the Central Committee, which represents an organization at the highest level. Organizations at lower levels are for example the

⁴⁹ Takashi, S. (2013): North Korea’s Political System, pp. 1-3

⁵⁰ Atsuhito, S. (2017): Understanding the North Korean Regime, pp. 14-15

Union of Agricultural Workers of Korea (for women), the General Federation of Trade Unions (for workers) and the Youth League (for children). It is exactly these various organizations that play a prominent role in controlling citizens by providing rewards for members who inform others about any incompliances. Any behavior that is against the current regime will be reported by someone, which helps to preserve the socialist system. Even oppression, starvation or poverty would not be enough to trigger an anti-establishment movement under the current conditions. In addition methods of restricting communication and looking into inter-person communication are being extremely well executed in North Korea (e.g. regulations on the communication between farmers and workers).⁵¹

Now, let us draw some comparisons to the Chinese model. Literature suggests that in China one finds a similar political framework, though, with some modifications. For example, the Chinese authoritarian regime aims for “**good governance**”, which cannot be supplied through the ideologies of pure communism.⁵² Under “good governance” one might associate the following words with: consensus oriented, transparent, participatory, effective and efficient, follows the rule of law, transparent and accountable.⁵³ Also, unlike in North Korea, it is worth mentioning that Chinese central rulers have less control on local government agents in general. This aspect is also found in the composition of interest groups. In China, central rulers may be able to implement institutional changes that have a direct effect on private firms, but they cannot eradicate interest group opinions and there is no enforcement of participating in such organizations.⁵⁴ As the utopian communistic form of government is still very strong in North Korea, leaders there do not have a desire for “good governance”. But, one has to admit that the case was similar with China during most part of the 1980’s.

In fact, China did represent a quasi-totalitarianism regime, which did not correspond to the characteristics of “good governance” at all. Loyalty was high in spite of the fact that the enormous repression would be relaxed. Though, Deng Xiaoping did not aim to maximize leadership under a totalitarian system. His primary goal was to enhance economic performance, thus, leading to improved supply of loyalty.⁵⁵ Even though he

⁵¹ Atsuhito, S. (2017): Understanding the North Korean Regime, pp. 25-27

⁵² Yingnan J., Z. (2016): Authoritarian governance in China, p. 5

⁵³ United Nations (2018): What is Good Governance?, p. 1

⁵⁴ Yongjing, Z. (2008): The Political Economy of the Evolution of China towards an Authoritarian Market Economy, pp. 5-6

⁵⁵ Guoqiang, T. (2016): China’s Reform: History, Logic and Future, pp. 214-216

had the chance to accumulate even more power through economic growth, he did not do so. Instead, he came up with the idea of a “term limited presidency”, which would relieve the **successor’s dilemma** and weaken his power as president. In short, Deng Xiaoping seemed to care about his legacy, changing the totalitarian Mao regime to a “free market communism”. Under resolving the successor’s dilemma Deng could not simply maximize political repression without losing prestige (e.g. Tiananmen Incident in 1976). With regards to North Korea, this dilemma does not seem to have been resolved yet.⁵⁶ However, one has to admit that things look once again different in China in 2018. Recent developments show that president Xi Jinping has removed term limits from the Chinese presidency. One reason could be to avoid space for political debates about certain policies. Now, this voting allows Xi Jinping to rule even beyond his 2023 retirement date.⁵⁷ Yongjing Zhang (2008) refers to this by using the term “soft authoritarianism”. Under this term one can understand the fact that rational growth-oriented leaders intend to maintain high loyalty on the one hand, but also reduce political repressions on the other hand, which are negatively related to economic growth. In short, the case of China shows that a country can change its political framework (positively and negatively) without having to give up economic growth and enhanced living conditions – this leads us directly to the next point.

3.2. Living Standards in the North

Having learned from chapter 2 “North Korean History”, the country used to treat its citizens quite well. Until the major crisis in the late 1970’s, North Korea had managed to combine both a command economy together with providing the adequate living standards for its people. However, when examining the country today one can say that North Korea has clearly failed as a state. About 40% of its inhabitants live below the poverty line (most workers earn between 2 USD and 3 USD per day) and most of its available resources have been directed to serve the interests of the Korean Worker’s Party and its military-first policy. In 2001 for example, North Korea has spent around 30% of its annual GDP on the military.⁵⁸ The situation in China looks different today. Only 3.3% of its inhabitants live below the poverty line, which was set at approximately USD 400 per month in 2011. In contemporary China only around 50 million people live

⁵⁶ Yongjing, Z. (2008): The Political Economy of the Evolution of China towards an Authoritarian Market Economy, p. 32

⁵⁷ Charlie, C. (2018): “More Opposition in Mai’s Time.” Why China’s Xi Jinping May Have to Rule for Life

⁵⁸ Humanium (2018): Children of North Korea

in poverty today, while this number amounted to over 250 million in 1978 still.⁵⁹ In North Korea, the incentive to produce nutritional products is missing. This is because of the country’s strong focus on increasing its military capabilities first and using the GDP left-overs then, to provide the inhabitants with food. Not surprisingly, there was a horrible famine from the early until the mid-1990’s, which caused the loss of at least one million lives. Also recently, refugees have reported famine conditions in some parts of the country. At various points, aid with regards to supplying food has been provided by some countries like China, the United States or South Korea. However, this food aid has shown enormous imbalances due to changing political factors and the country’s nuclear missile program.⁶⁰ The shortage of food in North Korea can also be explained through comparing the height of North and South Koreans. Research in this area has found that improvements in the average height of people serves as an indicator for improved economic conditions and living standards, but also includes aspects of health and nutrition. During the mid-1980’s researches have suggested to introduce the term “biological standard of living” for measuring the well-being of human in various countries worldwide. Time trends help to reflect changes with regards to the distribution of income, the amount of physical labor, food consumption.⁶¹ The following figure depicts such a trend for North and South Korea:

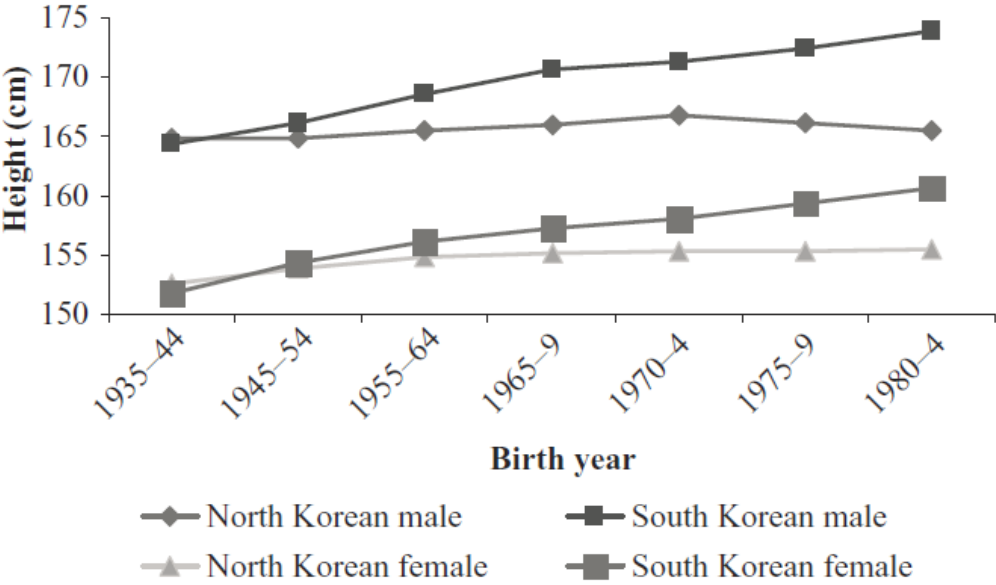


Figure 4: Comparing the Height of North and South Koreans
 (Source: Sunyoung, P. et al, p. 150)

⁵⁹ Index Muni (2018): China vs. North Korea
⁶⁰ Paul, H. (2012): North Korea: Building the Institutions to Raise Living Standards, p. 488
⁶¹ Sunyoung, P. et al (2011): Height and living standards in North Korea, 1930s – 1980s, pp. 142-143

It can be inferred from figure 4 above that until the beginning of the Second World War the height of North Korean people was very similar to the ones of people living in South Korea. However, after the formation of the Democratic People’s Republic of Korea in 1948, the situation worsened for North Korea and improved for South Korea. What appears remarkable is the divergence after the Second World War. One can identify a widening gap ever since 1945, but an even bigger gap (both countries going in the opposite direction) after the crisis that severely hit North Korea in the mid-1970’s. This fact is particularly interesting because we have learned in chapter 2 “North Korean History” that North Korea has established a number of popular measures in 1946 aiming to improve the situation of its citizens. Figure 5 clearly indicates that the popular measures did not come any close to measures taken in South Korea at that time and reflects a **substantial mismatch** between media propaganda and real term statistics. Further differences (and mismatches) between factors having an impact on living standards in the North and in the South are represented in the following figure:

	1960	1970	1980	1990	2000
Ann. GDP per capita (USD)					
South Korea	300.36	691.53	2,532.50	8,612.24	15,702.27
North Korea	-	112.44	557.66	1,487.87	1,378.95
Infant mortality rate (%)					
South Korea	90	43	16	8	5
North Korea	85	52	32	42	42
Life expectancy					
South Korea	51.1	59.8	62.7	67.4	71.0
North Korea	46	56	62.1	65.5	62.9

Table 2: Selected Social Indicators for South and North Korea
 (Source: own representation based on Sunyoung, P. et al, p. 144)

Again, table 2 clearly shows that North Korea is lacking behind South Korea with regards to various social indicators. While its GDP per capita has been somewhat to

1/6 in 1970, it amounts to only 1/11 today. Furthermore, North Korea has barely made a progress with regards to its infant mortality rate, which is more than eight times as high as the one in South Korea. Finally, life expectancy in North Korea appears to be around eight years lower today than in South Korea.

When looking at the Chinese example, similarly to North Korea, China was also characterized by poverty, insecurity of food and substantial income inequalities during the mid-20th century. In fact, back in 1949 the average life expectancy in China was around 44 years, while it increased to 68 years only a few years after Deng Xiaoping initiated his enormous economic opening-up efforts and stands at 75.7 years in 2017. Also today, China successfully managed to improve its annual GDP per capita enormously, which amounted to somewhat USD 16,600 in 2017 (USD 253 in 1980).⁶²

⁶³ What appears to be an interesting fact is that back in the 1980's China's GDP per capita was only around three percent of that in Europe. As China changed its political framework and moved towards a "free market communism" style economy, it did catch up with western living standards quite quickly and looks at around 30% of western living standards in 2018. On the other hand, when analyzing and comparing North Korea and China today, one finds that North Korea's GDP per capita is worth around 1/8 of that of China, which makes the starting position for an economic-opening up strategy much better than China's situation was during the 1980's. This fact would reflect Paul Hare's believe that some important North Korean reforms and policies could be carried out and fruit within a period of a few decades.⁶⁴ However, there are further aspects with regards to the living standards that one has to consider when looking at North Korea – this is human rights violations.

This is particularly true, as for example, a 2014 U.N. Commission Inquiry report stated that there are several **human rights abuses** in North Korea. This includes murder, rape, imprisonment, torture, forced abortion and constituted crimes against humanity. Moreover, access to information and freedom of expression is not allowed. Actions found in the respective matter are severely punished by the government.⁶⁵ Also, the country shows records of inhumane treatment in detention. Citizens accused of severe political offenses are normally sent to prison camps, which are operated by the

⁶² Index Muni (2018): China vs. North Korea

⁶³ Dan, S. (2014): Chinese Living Standards, International Perspective: The World Bank's PPP Debate

⁶⁴ Paul, H. (2012): North Korea: Building the Institutions to Raise Living Standards, p. 490

⁶⁵ Human Rights Watch (2016): North Korea. Events of 2016

country's National Security Agency. Within these camps one would find systematic abuses, such as no medical care, exposure to starvation, sexual assault and torture by the guards. According to the U.N. report, approximately 80,000 to 120,000 people are imprisoned within such camps at the moment. Moreover, the government systematically forces inhabitants to perform labor in order to keep its economy alive (e.g. fix roads, government construction, public beautification projects). Most of the North Koreans must perform forced labor without payment at some point in their lives. At this point, it is also worth mentioning that North Korea is one of only few nations worldwide that did not join the International Labor Organization. This means that workers are denied the freedom of association and they are not allowed to organize themselves into groups for collective bargaining.⁶⁶

Analyzing these human rights issues in the light of China again, one finds a similar picture there as well. Similarly to North Korea, the right for freedom of expression is strongly depressed by the government. In fact, access to major social media platforms (e.g. Facebook, Twitter etc.) is limited in China. The Ministry of Industry and Information Technology even issued a new regulation in 2017 by prohibiting circumvention tools and making it unlawful to access the uncensored global internet through them. Furthermore, in January 2018, Sun Yet-Sen University in Guangzhou admitted that it had banned personnel from criticizing the Chinese Communist Party and even fired some of their professors for speaking critically of the Chinese government. What is more, in August 2018, Cambridge University Press admitted that upon a request by the Chinese Communist Party it had to block access to more than 300 research articles published in one of its journals. This measure was carried out in order to comply with Chinese law. Apart from abuses against the freedom of expression, one may identify violations with regards to the freedom of religion. In this case, the Chinese government restricted the practice of five officially recognized religions in already approved premises. People still practicing one of these five religions have to fear harassment, imprisonment and torture. Apart from that, China ranks extremely bad with regards to taking care of women's and girl's rights in an international context (100th out of 144 countries). Major examples in this area represent sexual abuse and harassment, violence and discrimination (North Korea ranks the last

⁶⁶ United Nations (2014): UN Commission documents wide-ranging and ongoing crimes against humanity, urges referral to ICC

place within this ranking). In addition, China is not prepared to accept North Korean refugees into its country.⁶⁷

3.3. A Centrally Planned Socialist Command Economy

Before looking into the various aspects of the North Korean economy, one should understand the economic system under which the country is operating. In contrast to a free market economy, the North Korean one can be described as featuring characteristics of a centrally planned command economy. By this, one means that the government decides on the production of goods, the quantity and at which price they should be offered for sale on its own. Free-market competition simply does not exist in an economy like that. In addition, the government also takes over decision with regards to investments and incomes and it determines when economic growth should be generated. As described in chapter 2 “North Korean History” of this thesis, the government has become superiorly influential in putting businesses and entities into its own hands. This represents another example of what makes a command economy. Finally, under a central plan all relevant laws and regulations that impact the economy are set out by the government and all economic players have to follow this plan as well as its targets.⁶⁸

The North Korean economy heavily corresponds to the early Soviet model, which included highly centralized state planning and had an extensive focus on its heavy industry. As mentioned earlier, this model did yield substantial growth rates in the early days of the North Korean state but significantly slowed down in 1980. Apart from the massive oil crisis that struck North Korea a few years earlier, Paul Hare suggests several other factors, which led to this economic slowdown:⁶⁹

- Lack of innovation (resulting from an embargo on modern technology imports)
- Inefficient investment allocation (likely to happen in a command economy)
- Poor incentives for producing high quality products (within industry and agriculture)
- Labor force lacking modern skills (e.g. marketing, economic, IT, finance)
- Mismanagement of foreign trade

⁶⁷ Human Rights Watch (2018): China. Events of 2017

⁶⁸ Investopedia (2018): Command Economy. Overview

⁶⁹ Paul, H. (2012): North Korea: Building the Institutions to Raise Living Standards, p. 489

With the Soviet Union coming to an end in late 1991, North Korea experienced the probably most shocking moment in economic history. From one day to the other, Soviet trade deals, from which North Korea has benefitted until then, were stalled. Now, who should North Korea sell its products to? It turned out rather difficult for the country to find suitable trade partners, except China, which tried to limit relief by buying some of the North Korean goods. Also, since this time, North Korea does not have access to the world capital markets. Therefore, the country undertook serious economic reforms from the year 2002 onwards. But it appears to be interesting whether or not research provides evidence that North Korea has started to move towards the success story of the Chinese model. In fact, first, one has to ask what the Chinese model looks like.

In their research paper “Market Socialism in North Korea: A Comparative Perspective”, Gary S. and Sujian G. are providing a model, which is based on six key dimensions that make a market socialist economy like China:⁷⁰

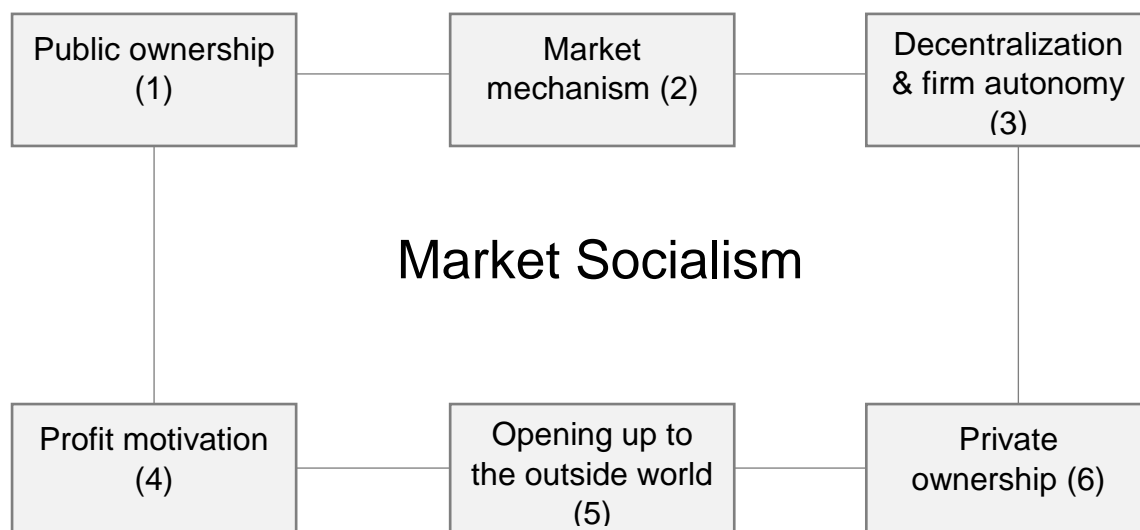


Figure 5: Key Dimensions of Market Socialism

(Source: own representation based on Gary, S. and Sujian, G., p. 192)

First, public ownership (1) corresponds to the fact that the economy pertains to a general system, which retains significant public ownership, thus, influencing the means of production in this economy. In this case, one would assume that in such an economy only state centralized corporations exist. However, this is not the case. Firms in a market socialist economy may be denationalized and not being controlled by the main

⁷⁰ Gary, S. and Sujian, G. (2007): Market Socialism in North Korea: A Comparative Perspective, pp. 192-195

party. But, one may not simply refer to this as privatization, because it rather reflects the holding of public property rights by a union or community. Public ownership also can be characterized in that citizen communities have certain control and income rights in the various enterprises. Especially in China, public ownership has shown great success throughout its opening-up strategy. For North Korea, literature does not support evidence that denationalization of enterprises and giving more rights to its citizens is under way.

Second, a very important element that makes a market socialist economy is the free interplay of supply and demand, thus, introducing a certain market mechanism (2). Therefore, the state should allow considerable freedom for markets to interact with each other. In North Korea, we have learned that this is not the case, as the government is setting production quantities, which leads to miscalculations and economic deficiencies in the medium run.

Third, decentralized planning (3) is crucial for allowing markets to operate freely and independently. For North Korea this would not mean that the state should give up its influence completely but rather engage in some other aspects, for example, providing consultation in the construction of economic plans or carrying out income and fiscal policies. Additionally, Yunker mentions that the more economic institutions act autonomously, the more the more a given system would reflect a market socialist approach.⁷¹ Neither is the case in North Korea.

Fourth, profit motivation (4) represents a further important aspect in a market socialist system. Given its purpose to improve the economic efficiency, it aims to set rewards towards higher productivity of firms, efficiency, entrepreneurship and innovation. Obviously, the North Korean system does not correspond to this dimension in that activities by firms and enterprises basically strive to fulfill plans and goals set by the central government (e.g. follow the main target of North Korea's central plan).

Fifth, opening-up to the outside world (5) is important to improve a country's economy. Of course, there are advantages (e.g. improvement of financial performance, market competitiveness, brain gain) and disadvantages (e.g. exchange rate risks, proprietary

⁷¹ James, Y. (1995): Post-Lange market socialism: an evaluation of profit-oriented proposals, 698-700

information theft, brain drain)⁷², but command economies like North Korea cannot expect strong economic growth without trading with the rest of the world.

Finally, private ownership of means of production (6) plays a prominent role in adapting an economy in a market socialist system. For North Korea, this is particularly important with regards to a land reform given the country’s dominant role of agriculture. A land reform would significantly help to increase productivity of agriculture and set out the basis for industrialization. Also, interests of peasants would be protected more severely, which could further boost productive forces in North Korea. In China, for example, such a land reform was carried out in 1950 already and marked the beginning of its industrialization progress (long before Deng Xiaoping even came to power).⁷³

One can infer from the above dimensions that North Korea still seems to be far away from becoming a market socialist economy like China but has started to make some progress in recent years. China did represent a perfect example of a centrally planned socialist economy but managed an enormous economic transformation from the late 1970’s onwards too. The timeline of its economic opening-up story (until joining the WTO) developed over approximately 20 years and looks as follows. For convenience reasons, comparisons with North Korea (if applicable) will be added into the table below.

Time	Description
1979-1985	<p>Under Deng Xiaoping China introduces the so-called “open door policy”, thus, introducing dimension two and five. Chinese state-owned-enterprises (SOEs) start to operate internationally. Around 189 of such internationalization projects were accepted by the government and amounted to USD 197 million.</p> <p>In North Korea, only a partial economic reform was carried out in 1984. The August Third People’s Consumer Goods Production Movement was established, which allowed some production outside of the central planning and created a Foreign Joint Venture law in order to attract foreign direct investment.</p>

⁷² Crystal Lombardo (2018): 12 advantages and disadvantages of International Trade
⁷³ China.org.cn (2009): 1950: The Land Reform

1986-1991	China starts to adopt the third dimension (decentralization & firm autonomy) under moving towards a market socialist economy. This is done by loosening its strict monetary and fiscal policies. After government consultations, foreign enterprises are given access to the Chinese market.
1992-1998	<p>This time is similar to the most recent financial crisis in 2008. Many enterprises engage in speculation (especially with stocks and bonds), which eventually leads to a major crisis in 1997 – that is the Asian crisis. The motivation for making big profit reflects dimension number four according to the model of market socialism.</p> <p>In 1998, North Korea started to amend its institution by allowing private non-productive properties to focus more on the aim of citizens. This included products from kitchen gardens as well as the income from legal economic activities. Also, at this point local governments were allowed to manage cooperatives and light industries.</p>
1999-2001	At this point, incentives (e.g. subsidies, tax rebates, and financial support) for enterprises lead to an even faster development of business activities abroad. Support is directed to a wide extent to the machine industry and agriculture. Providing these incentives may also be found in China’s 10 th Five-Year Plan. The total value of Chinese outward foreign direct investment amounts to USD 1.8 billion.
2001-2007*	After joining the WTO in 2001, China enhances its influence abroad by buying majority rights of foreign enterprises. This goal can be found in its 11 th Five-Year Plan. It is important to mention, that these projects are tied to several regulations set-out by the Chinese government (e.g. flow of capital). This fulfills the criteria of public ownership and therefore dimension number one, which makes China a fully-fledged socialist market economy by this time.

Table 3: China’s Internationalization Process

(Source: own representation based on Peter, B. et al., p. 504 and Gary, S. & Sujian, G., p. 201)

In short of table 3, it took China approximately 20 years to turn from a socialist command economy into a fully fledged socialist market economy, which operates globally. Long time after China made significant progress in opening-up economically, North Korea did not seem to have made significant progress in any of the six dimensions that make a socialist market economy, thus, the time frame for introducing a potential opening-up policy should amount to at least two decades (until 2038), when assuming that it takes a similar amount of time like for China. However, in 2002 and 2003 North Korea finally introduced some of the most prominent reforms in its history. Among them were the following:⁷⁴

- Official price increase: lead to a smaller gap between official prices and peasant markets
- Wage increase: wages were tied to the actual amount worked
- Devaluation of the Won: The exchange rate rose from 2.15 to 150 Won to the Dollar, which was much closer to the unofficial exchange rate (approximately at 230 Won per Dollar)
- No subsidies for state-owned firms: these firms were expected to cover for their own costs
- Decisional autonomy: Especially some SOEs were allowed to limited price-setting authority
- Special Economic Zones: Similar to the Chinese model, North Korea introduced five SEZs (e.g. Gumho, Sinuiju, Gaesung etc.)

But which economic features do we find when glimpsing into North Korea today? Have the economic reforms of 2002 and 2003 brought about significant improvements?

When looking at the **structure of the North Korean economy** today, one may find the following information. The GDP of the country's economy amounts to an estimate of USD 28 billion (official exchange rate) in 2015. On the other hand, GDP corresponding to the purchasing power parity amounts to USD 40 billion in 2015. Obviously, the exact number cannot be obtained through modern sources, but an estimate still provides a glimpse into the country suggesting that it might be somewhere between these two numbers. As North Korea does not publish any reliable data with regards to this KPI, this data is derived from the purchasing power parity GDP

⁷⁴ Gary, S. and Sujian, G. (2007): Market Socialism in North Korea: A Comparative Perspective, pp. 202-203

estimates that was conducted by Angus MADDISON in the course of a study for the OECD. According to this study, the GDP real growth rate has remained mostly steady, fluctuating between +1.1% in 2013 and -1.1% in 2015. The GDP per capita amounted to USD 1,800 in 2013 and USD 1,700 in 2015.⁷⁵ According to the World Factbook of the CIA, North Korean GDP per capita corresponds the one of the lowest levels on our planet (e.g. worst 5% of 229 countries)⁷⁶.

In more detail, the GDP is composed of **three main sectors** of origin. Agriculture makes up approximately 25.4% of the North Korean economy. The main agricultural products are rice, corn, pulses, wheat, potatoes, pork, beef, eggs, fruits and nuts. Then, the industrial sector accounts for roughly 41%. As mentioned earlier, its main focus is on the production of military products, chemicals, coal, iron, zinc, lead, textiles and heavy machinery. Finally, the service sector makes up around 33.6% of the overall GDP.

Now, according to the Heckscher-Ohlin theorem, a country shall export goods that use abundant production factors (e.g. land, labor and capital) and import goods that involve inputs the country is locally scarce of. With regards to North Korea, the most important import goods have been collected by the Observatory of Economic Complexity (OEC), which represents a project that was initiated at the MIT Media Lab Macro Connections group. The research team created a visualization breakdown of North Korean import and export data by using relevant data from the Center for International Trade at UC Davis as well as the UN Comtrade. For North Korean **imports** the situation looks as follows:

⁷⁵ Yong Suk, L. (2018): International isolation and regional inequality: Evidence from sanctions on North Korea, p.35

⁷⁶ Central Intelligence Agency (2018): The World Factbook. Economy of North Korea

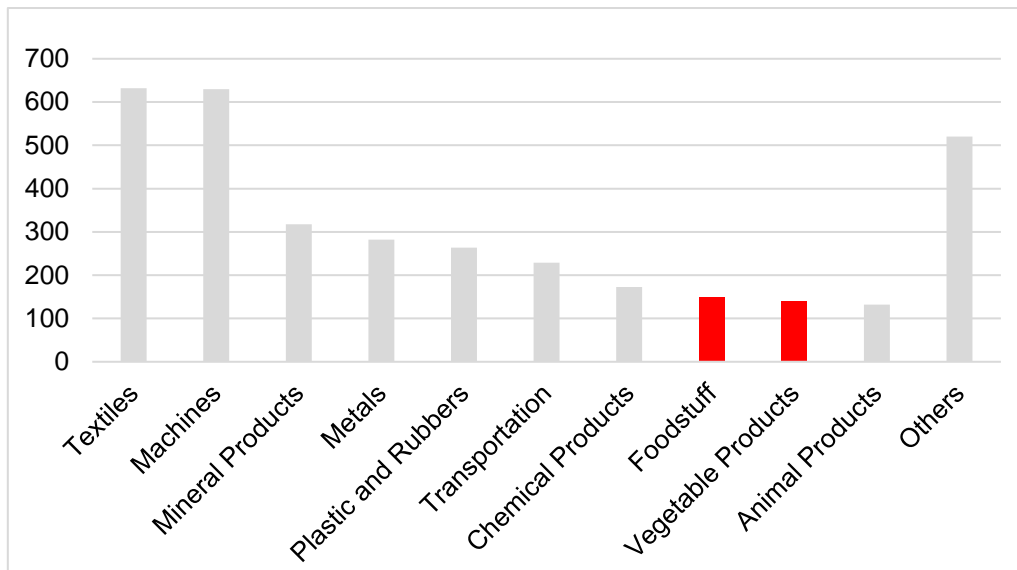


Figure 6: North Korean Imports (in million USD)

(Source: own representation based on OEC, Statista)

The figure above shows that textiles account for at least 18% of North Korean total imports (total: USD 3.47 billion in 2015). Among the most important products in this group are Synthetic fabrics, plastic coated textiles, knit t-shirts and packaging bags. The second most important import goods can be found in the area of machines. Similarly to textiles, this group also makes up around 18% of the total imports and accounts for approximately USD 630 million. Broadcasting equipment, video displays and computers hold the biggest share in this group. Then, mineral products (e.g. refined petroleum, gas and coal briquettes) and metals make up around USD 250 million each. It appears to be interesting that food is to be found more towards the end of prioritized import goods, while starvation and a lack of food are found to be a major problem in the Democratic People’s Republic of Korea (see chapter 2. “North Korean History”). In fact, foodstuffs and vegetable products together account for only 8.3%. On the other hand, the author’s research has shown that North Korea does possess an extensive heavy industry including vast machinery. Thus, it is interesting that North Korea imports even more of these, as they use abundant production factors, like especially labor (according to Heckscher-Ohlin).

In total, 85% of all imported goods are to be received from North Korean closest trading partners – China. This also leads to the conclusion that, because of the heavy/similar trade between the two countries, the Ricardian trade model seems more relevant for this case than Heckscher-Ohlin. India represents the second most important trading

partner (3.1%), followed by Russia (2.3%), Thailand (2.1%) and the Philippines (1.5%).⁷⁷ Given these facts, one might wonder what North Korea's trade performance looks like in a global perspective. Not surprisingly, the country's trade performance looks extremely poor when taking into account that global trade has been rising almost continuously over the past fifty years.

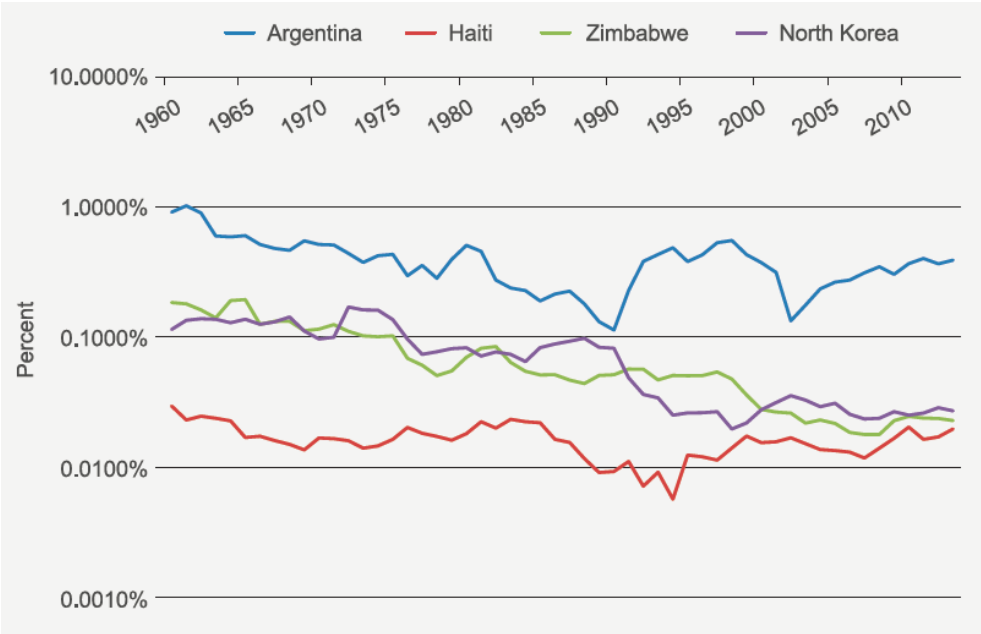


Figure 7: Share of World Merchandise Imports between 1960 and 2013, DPRK vs. Other Economies
(Source: Nicholas, E., p. 16)

In fact, as the figure 7 depicts, North Korea's share of world merchandise imports is extremely low and amounts to only as much as 0.03% in 2015. This number is comparable to countries like Zimbabwe or Haiti.⁷⁸

Now, in contrast to North Korea's import structure, let's have a look at the country's most important **export goods**:

⁷⁷ OEC, Statista (2017): North Korea's imports and exports by country
⁷⁸ Nicholas, E. (2015): North Korea's „Epic Economic Fail“ in International Perspective, pp. 16-18
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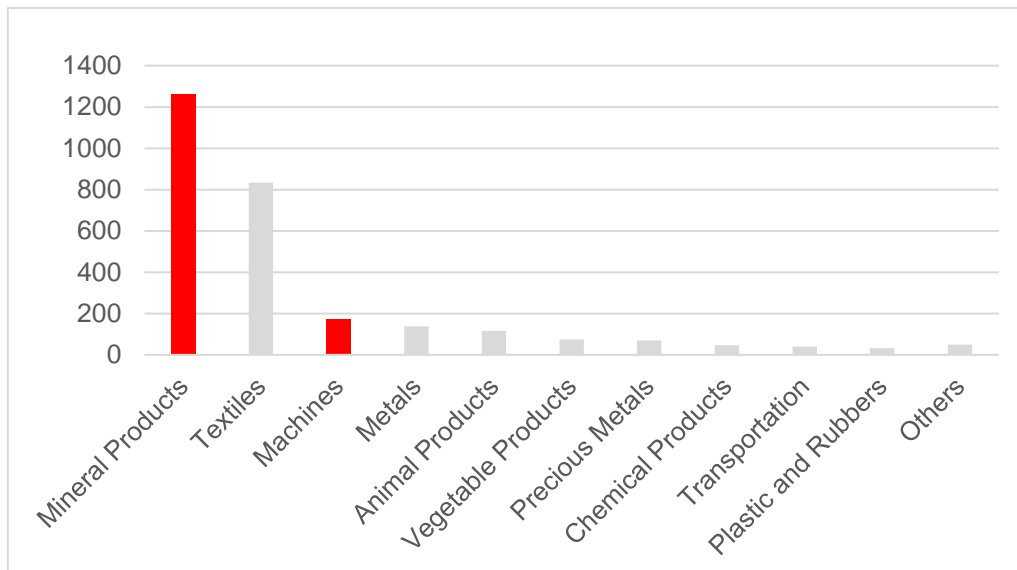


Figure 8: North Korean Exports (in million USD)

(Source: own representation based on OEC, Statista)

Figure 8 indicates that mineral products account for around 44% of North Korean total exports (total: USD 2.83 billion in 2015). In more specific, coal briquettes made up the most extensive part of all exports in 2015, namely 34%. Also in this group one may find refined petroleum, lead, iron and graphite. Then, the second largest group with regards to exported products makes textiles. In fact, textiles account for about 29% of all exports. In more specific, within this group one may find men's or women's coats and suits, as well as t-shirts. Furthermore, the country engages in exporting machinery equipment (e.g. insulated wire, electrical transformers, integrated circuits) metals and animal products like fish. By saying so, similarly to its import structure, 83% of all North Korean exports go to China. Then, the second most important trading partner for exports is again India (3.5%), followed by Pakistan (1.5%) and Burkina Faso (1.2%).⁷⁹ As for its export performance, North Korea's economic fail can probably best compared to the example of Zimbabwe between 1960 and 2013. During this time North Korea's share in world merchandise exports fell from around 0.11% to 0.019% and was even below Zimbabwe's performance for most of the time.

⁷⁹ OEC, Statista (2017): North Korea's imports and exports by country

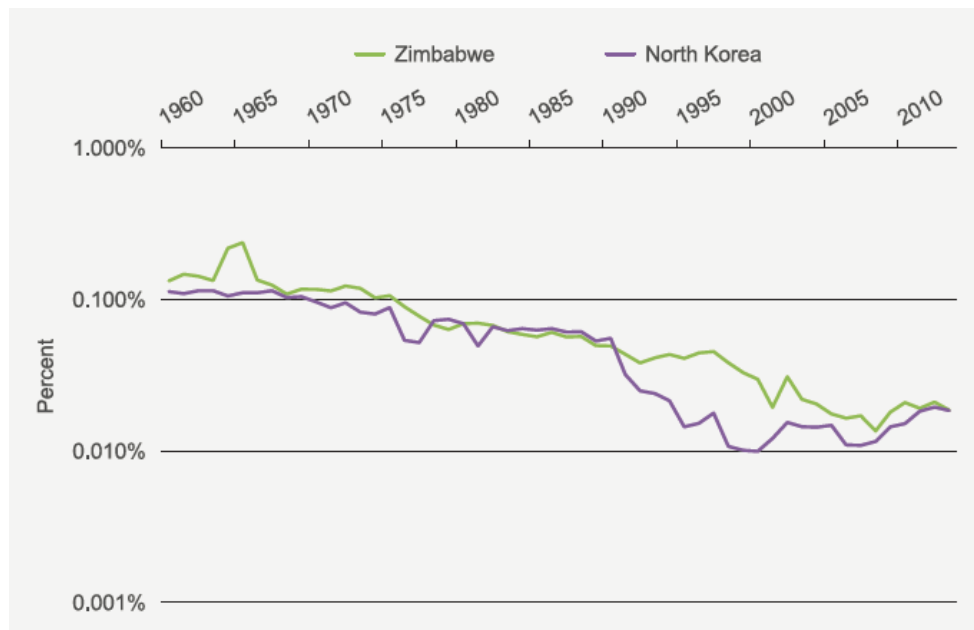


Figure 9: Share of World Merchandise Exports between 1960 and 2013, DPRK vs. Other Economies

(Source: Nicholas, E., p. 17)

It is important to mention that the decline in the share of world merchandise exports was a continuous one throughout the last 50 years and was not centered on a particular geopolitical event. Also, one can clearly see from figure 9 that North Korea's decline long preceded the Soviet end.⁸⁰ Another important aspect worth mentioning is that North Korea tends to be a much healthier, more urbanized, more educated and more populous state than Zimbabwe, and yet it has enormous difficulties to keep up with Zimbabwe's calculated merchandise import and export volumes. This truly is important because it underlines that the North Korean economy is even worse than what it looks like on certain graphics. Sanctions on North Korea by the international community obviously have made the situation even worse for the country.⁸¹

In terms of finding the right economic opening-up strategy, one has to tackle the most prominent economic issues first. Paul Hare suggests **three main areas for improvement** in order to bring the North Korean economy back on track:

1. Improve the performance of agriculture

In general, for countries that trade successfully, the performance of agriculture usually represents a second order issue. This is because food can always be imported

⁸⁰ Nicholas, E. (2015): North Korea's „Epic Economic Fail“ in International Perspective, p. 18

⁸¹ Nicholas, E. (2015): North Korea's „Epic Economic Fail“ in International Perspective, p. 19

if the agricultural functions at home failed. However, as we have seen that North Korea is unable to export enough to import food, the whole functioning of the area of agriculture is extremely important for the well-being of the population. In the case of North Korea, exactly the functioning of property rights and contract with regards to agriculture conflicts the most with the country's ideologies and its political regime. However, given the Chinese example, progress could also come gradual. In China, the change of the rule of law has started with informal understandings, which used to build on trust and shared responsibilities. Agricultural property rights in legal form were only formalized at a later stage. These rights would be a significant step towards the rule of law in North Korea and would allow for a faster technical and organizational progress. Hare estimates that an enormous difference in economic output could be reached certainly within five to ten years.⁸²

2. Reduce defense spending

In the context of investment and growth, North Korea's military spending represents a serious threat to both its economy and politics. Spending close to 30% of its GDP on defense makes it extremely difficult for the country to invest enough of the remaining GDP into its economy. Hare suggests that more financial means should be spent on productivity projects, for example projects that would have a positive impact (producing what is demanded) on the productive capacity of the economy as such. In North Korea one finds the situation that the Party supports the military, which leads to a loyal military towards the Party. Therefore, this repressive system holds for the benefit of the Party and the military. Only if the military started to realize that not enough funds or resources would be given to them, this would create an imbalance to this current system. Also, if the Party would want to make a progress towards serious economic reform and would less see itself as a partner of the military, this could help to improve the situation. Again, also in China this was not a deliberate choice right from the beginning but rather an evolutionary process. China had a rather pragmatic view on this but change its attitude throughout the 1970's once massive economic reforms were initiated.⁸³ The question is whether or not the North Korean Workers Party could achieve such a transition.

3. Adjust to the shock of the Soviet collapse in 1991

⁸² Paul, H. (2012): North Korea: Building the Institutions to Raise Living Standards, p. 490, 505

⁸³ Paul, H. (2012): North Korea: Building the Institutions to Raise Living Standards, p. 492

After the Soviet Union started to disintegrate into 15 independent successor states, North Korean exports fell even stronger as we have seen in figure 9. Normally, market economies adjust to economic shocks like this by, for example, devaluating their currency, re-setting their export activities by serving new markets, allowing new firms to access the export market or changing the composition of imports. All of these examples were not carried out by North Korea at all as the government did not put much work into adjusting production costs, enhancing enterprise profitability or making important steps in boosting foreign trade.⁸⁴ In the meanwhile, in 2001 China joined the rule-based trading framework (GATT) of the WTO, in order to facilitate an extremely quickly changing world economy. However, North Korea did not even choose to become an applicant of this international trading framework. Unlike China, North Korea has not yet managed to benefit from general trading rules or multilateral trade agreements of the WTO and, thus, must hope on bilateral or ad hoc arrangements for every single transaction it carries out with third countries. Obviously, advantages of multilateral trade agreements outweigh disadvantages by far. For example, multilateral trade agreements create less administrative work (avoiding the so-called “spaghetti-bowl effect) and lead to a trade creation rather than a trade diversion.⁸⁵

3.4. North Korean Economic Assessment: Resume

This chapter has provided an overview about the North Korean political regime, living standards and an assessment of the economy. Whenever possible, it drew some comparisons with China in order to provide room for discussion in the final chapter of this thesis.

First and foremost, North Korea’s political regime was found to be extremely authoritarian with a strong policy focus on enriching its military performance. It is heavily based on the Soviet model but goes even beyond that by having introduced the Juche and Songun ideologies. What is more, North Korea exercises a strong influence on its citizens. In fact, there is principally no way to forgo the participation in a community network, through which residents are controlled by others. What is more, with regards to elections, North Koreans have no or little freedom of choice with regards to their political preferences.

⁸⁴ Yong Suk, L. (2018): International isolation and regional inequality: Evidence from sanctions on North Korea, p.35

⁸⁵ Paul, H. (2012): North Korea: Building the Institutions to Raise Living Standards, p. 492

Second, living standards in North Korea remain poor. In 1978 the country has experienced one of the most serious famines in history, with ten thousands of casualties. Given the country's vast expenditure on military items, less money is directed towards the supply of food and, thus, represents a huge problem within the Democratic People's Republic of Korea. On average, 40% of the country's population live below the poverty line and make less than USD 2 per month. By assessing North Korea's performance with regards to living standards, the author has also considered the height of North and South Koreans. Interestingly, South Korean men were found to be almost ten centimeters taller than North Korean men in 1980.

Finally, one can infer from this chapter that North Korea has not made too much progress with moving from a command economy towards a socialist market economy, as many of the six dimensions are either not or only partially fulfilled. Furthermore, the Heckscher-Ohlin model does not seem to apply to the North Korea economy, as it imports things (e.g. machines, mineral products), which require production factors the country is supposedly rich of (e.g. raw material for production) and exports things (e.g. food), requiring production factors it is short of – given its lack in food supply.

This chapter has drawn some economic comparisons with the example of China. However, as one will find out in the next chapter, the way for opening up in the future could strongly depend on South Korea as an important trading partner within the field of foreign trade. Chapter 4 "Prospects for the Future" will review some modes and estimations for North Korea's future in the light of the main findings of chapter 2 "North Korean History" and chapter 3 "North Korean Economic Assessment".

4. Prospects for the Future

From 2018 onwards, in which direction could the North Korean regime and the country's economy develop? This question is difficult to answer, yet, it is possible to draw a picture, which considers North Korea's history and its current economic situation. Based on an interview with Michael G. Plummer, director of the Johns Hopkins University SAIS Europe, the author would like to steer this chapter based on three main thoughts and add these separate components on top of chapter 2 and chapter 3 of this thesis. The main thoughts of the interview are:

- The issue of a mindset of “control”
- A South Korean complimentary
- Security issues around the Korean Peninsula

4.1. Mindset of “control”

For the future, the questions remains whether North Korea needs to implement substantial changes with regards to its political regime first or start opening-up its economy. North Korea seems to not like the idea of engaging with the outside world too much. Through engaging with other countries, more influence from abroad can be expected, which would interfere negatively with the North Korean government ideology, which is about keeping control over its residents, its military, its expenditures and of course over its entire economy. The term “control” is within the government's mindset, thus, making a change of the game in the near future look far way on the time horizon.⁸⁶ However, one can again look into the Chinese case at this point because China also failed to achieve economic growth before its transformation in 1978.

In fact, the lack of industrialization (e.g. heavy industries and economic power) was to be seen as the root cause for China's backwardness. Similarly, Mao Zedong was scared of losing control and power and therefore primarily focused on building on the social and political level. After this was accomplished, in 1953 China initiated a serious of quite ambitious Five-Year Plans in order to speed up the Chinese economy and finally transform its industries into advanced ones. However, Mao Zedong planned to grow economically without fulfilling the dimensions of a market economy. Especially the fifth dimension of the market economy model presented in chapter 3 “North Korean Economic Assessment”, which is about opening up to the outside world”, did not

⁸⁶ Michael, P. (2018): Interview: „Thoughts on North Korea“, line 19-21

happen to be fulfilled during the 1950's. So, even though China's plan was to accelerate this building of modern industries, it could not do so because of **lacking a comparative advantage** over other countries.⁸⁷ Again, the Heckscher-Ohlin theorem about the principle of comparative advantage refers to this economic reality by stating that through international trade and differences in a country's factor endowment, some might be able to produce a certain good at a lower opportunity cost than others do.⁸⁸ In fact, during the 1950's China represented a low income agrarian economy, similar to North Korea today. Almost 85% of its total labor force was employed within the primary sector and Chinese firms were simply not viable to compete in an open market. Then, in order to achieve its strategic goals, China started to subsidize certain priority industries (e.g. price distortions, lower input prices, lower interest rates and undervalued exchange rate) and giving firms within these industries a monopoly. Through these measures, shortages were created and the government allocated resources directly to firms that were unviable. These interventions allowed China to move on quickly towards modernizing its industrial sector, but still, economic efficiency was low because of not opening up to the outside world. As the North Korean mindset is different to that of Deng Xiaoping starting from 1978⁸⁹, not much progress can be expected on a political level. However, in recent years North Korea seems to pay more attention to economic welfare and efficiency, probably more than ever before. Therefore, if the political mindset changed in the near future, what would one have to expect for a possible economic relation with South Korea?

4.2. A South Korean Complimentary?

In contrast to North Korea, South Korea has made an enormous economic progress ever since its separation with the North and represents an ideal trading partner for North Korea. In fact, it trades with the outside world and ranks 5th in exports and 8th in imports worldwide. In 2017 South Korean exports were worth more than USD 573 billion (around 200 times more than North Korean exports), whereas imports amounted to approximately USD 478 billion (around 140 times more than North Korean imports). Also South Korea shows a positive trade balance, which is about USD 95 billion in 2017, while North Korea's one is negative.⁹⁰

⁸⁷ Justin, L. and Zhou, L. (1998): *The China Miracle: Development Strategy and Economic Reform*, pp. 261-262

⁸⁸ C. Hidalgo et al. (2007): *The Product Space Conditions the Development of Nations*, pp. 483-484

⁸⁹ Michael, P. (2018): Interview: „Thoughts on North Korea“, line 65-66

⁹⁰ globalEDGE (2018): *South Korea: Trade Statistics*

The following figure illustrates the top ten **South Korean import goods**:

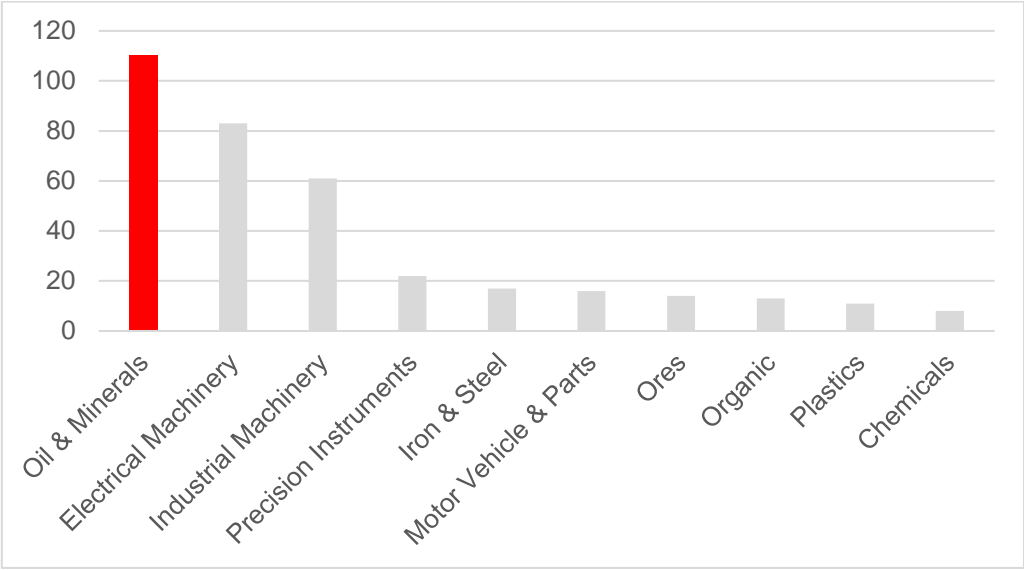


Figure 10: Top 10 South Korean Import Goods (in billion USD)
 (Source: own representation based on GlobalEDGE Trade Statistics)

One can infer from the figure above that Oil & Minerals, Electrical Machinery and Industrial Machinery stand out above the other import goods. Especially the import of mineral products amounted to almost USD 110 billion in 2017 and, thus, makes up around a quarter of South Korean total imports. Interestingly, minerals represents a category, which North Korea exports the most and South Korea imports the most of. It is difficult to say whether or not this could be a possible complimentary sector, but some literature provides possible hints that this could be an option. For example, one can learn from trade statistics that South Korea's most important trading partner is China (20%), followed by Japan (12%) and the United States (11%). More behind in terms of monetary value is Germany, Saudi Arabia, Australia, Vietnam, Russia, Qatar and Kuwait.⁹¹ Also interestingly, we have learned in chapter 3 “North Korean Economic Assessment” that China represents by far the most important trading partner for North Korea (85% of all trade) as well.

In their paper “Trade between North Korea and China: Firm-Level Analysis” Seung-Ho, J. and Byung-Yeon, K. found that, despite all sanctions, North Korean goods could have accessed the South Korean market through a circumvention of Chinese firms. By saying so, literature suggests that most of the Chinese firms North Korea engages in

⁹¹ GlobalEDGE (2018): South Korea: Trade Statistics

business activities with are Korean-Chinese, which means that the firm owners are ethnic Koreans but Chinese citizens. The same ideology applies to South Korea. In fact, South Koreans prefer to invest more heavily into the North-Eastern parts of China and into firms where they would find a Korean ethnic population.⁹² It is believed that there is a link between the South and North Korean market by re-labelling products in China and changing their place of origin from North Korea to “made in China”.⁹³ Now, how about South Korean exports?

The **South Korean export structure** in 2017 looks as follows:

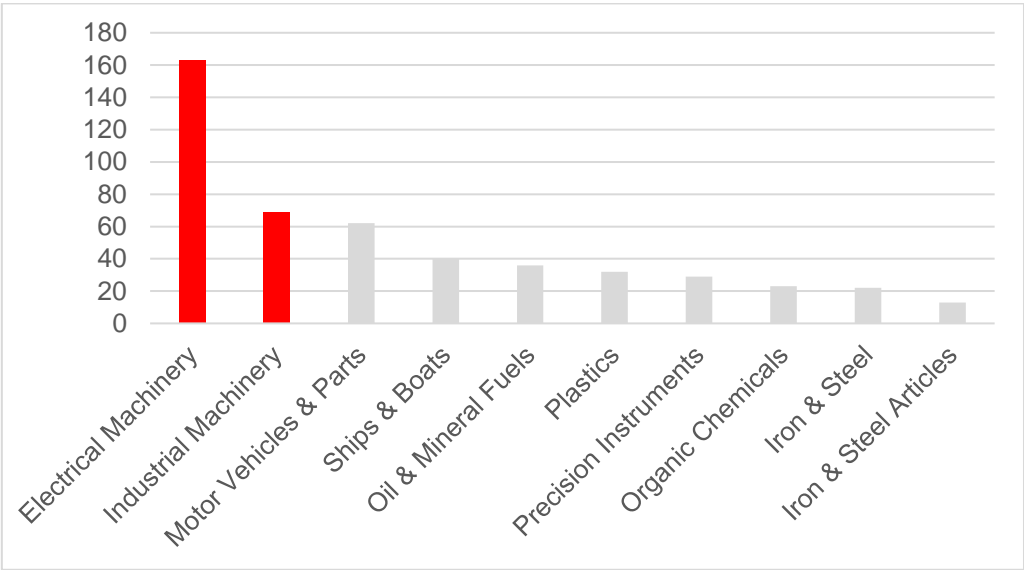


Figure 11: Top 10 South Korean Export Goods (in billion USD)

(Source: own representation based on GlobalEDGE Trade Statistics)

The graph above indicates that Electrical Machinery, Industrial Machinery and Motor Vehicles represent the most important export goods for the South Korean economy. Again, when looking into chapter 3 “North Korean Economic Assessment”, one can infer that North Korea imports machinery products heavily. Interestingly, this category leads South Korean exports on the other hand. In fact, the export of machinery makes up around 40% of all South Korean exports. When considering the most prominent trading partners of South Korea, we find that once again China ranks on the first place (25%), followed by the United States (12%) and Vietnam (8%). Similar as for imports, Seung-Ho, J. and Byung-Yeon, K. also found a reverse effect for exports. They argue

⁹² Michael, P. (2018): Interview: „Thoughts on North Korea“, line 49-50

⁹³ Seung-Ho, J. and Byung-Yeon, K. (2018): Trade Between North Korea and China: Firm-Level Analysis, p. 1483

that China with its Korean ethnic population is used to transfer products from South Korea to North Korea. Therefore, the most important goods directed towards North Korea are TVs, washing machines and other electrical home appliances. In short, it corresponds positively with what category leads South Korean exports (namely Electrical Machinery).⁹⁴ However, it is difficult to estimate how much of North Korean machinery imports really originate from South Korea or in fact from China. In sum, from looking at the import and export structure of both South and North Korea, one can learn that the two countries could potentially be of interest for each other economical wise and what they produce.

Now, in the following sub-chapter the author of this thesis would like to bring up North Korea's nuclear program once again. In chapter 2 "North Korean History" the main nuclear crisis have been explained already but at this point more focus should be given with respect to security in the region and what North Korea's nuclear program actually means for the country.

4.3. Security for the Future

Before markets could potentially open in the future, one probably has to expect great steps towards denuclearization. However, North Korea's nuclear program guarantees for the survival of the political regime in that it allows for executing control in negotiations with other states.⁹⁵ But what is happening at the moment with regards to denuclearization efforts?

2018 marked an interesting year with regards to developments on the Korean Peninsula. Kim Jong-Un seems to engage more with the outside world than his pre-successors and has also taken part in the 2018 North Korea – United States summit in Singapore. This event marked a meeting between him and the American president Donald Trump and was the first meeting ever between a North Korean leader and a US president. In general, they came together in order to sign a security agreement, in which security guarantees for North Korea on the one hand and its denuclearization plans on the other hand were discussed and agreed on. Even earlier in 2018, Kim

⁹⁴ Seung-Ho, J. and Byung-Yeon, K. (2018): Trade Between North Korea and China: Firm-Level Analysis, p. 1481

⁹⁵ Michael, P. (2018): Interview: „Thoughts on North Korea“, line 34-36

Jong-Un also met South Korean president Moon Jae-In in order to prepare for this North Korea – United States summit.⁹⁶

Later in 2018, a U.S. think tank announced on November 12th, that it had identified 13 new missile operating bases in North Korea, while the country had announced earlier the closing of others. This appears to be interesting because as obviously some of the missile operating bases are now closed (e.g. Sohae launch site in North Korea), others were opened. These sites identified were located in mountainous areas throughout North Korea and could potentially be used to house ballistic missiles with different ranges. It is believed that the largest ballistic missile could even reach mainland of the United States.⁹⁷ The following illustration shows one concrete example of how North Korea de-constructs a missile basis near the Sohae launch site:⁹⁸



Figure 12: Deconstruction Sohae Launch Site

(Source: Agencia EFE)

⁹⁶ Council on Foreign Relations (2018): The Korea Summit

⁹⁷ CNBC: North Korea keeps undeclared missile bases up and running: US think tank

⁹⁸ Agencia EFE: Pyongyang stalls dismantling of missile base, according to satellite photos

Obviously, one can understand that driving security improvements forward into a positive direction remains extremely difficult within this region. North Korea does not seem to be willing to give up its nuclear program immediately, unilaterally and unconditionally. Although its biggest trade partner China would favor North Korea's denuclearization, it would not push it through military means. In fact, security in the region around the Korean Peninsula is extremely important to China.⁹⁹ This is because the country is following a grand strategy, which aims to rise economically peacefully. This goal also influences its relationship with North Korea to a wide extent. Given the fact that China has experienced many wars throughout its existence (e.g. war with India and Japan), it now definitely wants to avoid the fact that economic allies could see China as a risk. Thus, it seems like it does not wish to threaten North Korea with a potential attack but rather support its political and economic decisions.¹⁰⁰ What is more, a North Korean immediate denuclearization could represent a potential risk to China as well. This is true, as literature suggests that China sees North Korea as a certain "buffer zone". In fact, North Korea was never neither intrinsically valuable to China with regards to international trade nor as a military ally. Its main intention was to use North Korea as an asset to keep other players – especially the United States – out of their reach.¹⁰¹

In sum, nuclear weapons do represent North Korea's leading negotiating tools with other countries. However, if the country wants to engage more with the outside world (what would help to transform North Korea more towards a socialist market economy) and improve its economic conditions, complete denuclearization probably has to be accomplished sooner or later.¹⁰² The question remains whether or not this can be expected any time soon as no big nuclear deal with the US has been struck yet, but rather small understandings on the issue itself (e.g. through the North Korea – Singapore Summit in 2018). What is more, the United States has only little experience with regards to negotiating deals with North Korea.¹⁰³

⁹⁹ Oriana, M. (2004): *Why China Won't Rescue North Korea*, p. 60

¹⁰⁰ Seung-Ook, L. (2014): *China's new territorial strategies towards North Korea: security, development, and inter-scalar politics*, p. 184

¹⁰¹ Victor, C. (2012): *The Impossible State: North Korea, Past and Future*, p.318

¹⁰² Viktor, C. et al. (2010): *North Korea's Provocations and Northeast Asian Security*, pp. 390-391

¹⁰³ Michael, P. (2018): Interview: „Thoughts on North Korea“, line 88

5. Discussion

In the following discussion the author of this thesis would like to highlight three major aspects, which appear to be relevant in finding an answer to what a potential North Korean economic opening-up strategy could look like. First, the author would like to discuss how much progress North Korea has made to move from a socialist command economy to a socialist market economy (similar to the Chinese example). Then, the implications of contradicting to the Heckscher-Ohlin theorem will critically be analyzed. Finally, future thoughts on free factor movement between North and South Korea will be discussed in order to clarify whether or not a potential peace treaty could drive North Korea's economic ambitions too.

5.1. Command Economy vs. Market Socialism

In chapter 3 “North Korean Economic Assessment” six dimensions were introduced for describing market socialism in the light of China. In fact, China has made an enormous economic progress ever since changing its political regime in the 1970s as well as its economic measures. But where do we find North Korea in this model?

The first dimension (**public ownership**) seems to be completely fulfilled, as North Korea keeps substantial influence over its production and most of the entities and cooperatives operating in the country. Also, this might be dedicated given the huge Japanese influence (see chapter 2 “North Korean History”) on the “control” thinking of the North Korean regime. The author agrees with Gary, S. and Sujian, G. that North Korea never actually abandoned this principle.

For the second dimension (**market mechanism**) the author of this thesis remains more skeptical. It is true that North Korea has put some major reforms under way in 2002-2003 (see chapter 3 “North Korean Economic Assessment”), which for example were increase in prices and wages and measures to devalue their currency in order to boost the economy. However, North Korea's strict state planning and its continuous execution of control functions (e.g. through various organizations) seems to contradict to the Chinese model that is in place today.

Dimensions three (**decentralization and firm autonomy**) seems to be partially fulfilled too. On the one hand, we have learned in chapter 3 “North Korean Economic Assessment” that North Korea initiated a small economic reform in 1984, which allowed for some firms and cooperatives to plan for their production independently. Also, we

have seen small movements towards decentralization in 1998 when local governments were allowed to manage cooperatives and light industries within their respective area. On the other hand, obviously the steps still seem to be too little to fruit. In the author's opinion the political regime yet is not prepared to accept an iterative bottom-up/top-down decision approach with regards to its economic planning. It is true that in China one cannot observe complete decentralization and firm autonomy either, but yet this iterative process seems to work better than in China today than for North Korea.

With regards to the fourth dimension (**profit motivation**) the North Korean system as of today could not meet the requirement. The author agrees with Peter Buckley's observations that market socialist schemes tend to reward innovation on the one hand and motivate firms for enhancing their production, efficiency and entrepreneurship on the other hand. For example, in China this had been the case shortly before joining the WTO in 2001. In fact, as mentioned in chapter 3 "North Korean Economic Assessment" the state offered subsidies and other rebates in order to promote individual cooperatives to perform even better. For North Korea this scenario obviously does not seem to be the case yet.

The fifth dimension (**opening-up to the outside world**) refers to what China has accomplished successfully since 1978. Here, the author would like to argue that North Korea has made little steps (e.g. setting up five SEZs) to attract FDI stream from abroad. However, the author agrees with Michael Plummer. that the country still does not do enough to grant foreign investors the right for accessing the capital and labor market. This is particularly true as North Korea remains the most closed economy on the planet.

Finally, the sixth dimension (**private ownership of means of production**) does not seem to be fulfilled either. As mentioned in chapter 3 "North Korean Economic Assessment", the country has yet failed to bring a successful land reform under way. A land reform could lead to significant improvements with regards to increasing the efficiency of production by allowing individual farmers to use their resources more ideal.

In short, the author comes to the opinion that as of today North Korea only fulfills two of the six dimensions mentioned in Gary, S. and Sujian, G. model (see table 4 below). When looking at the case of China, it took the country around two decades to move from a planned socialist command economy to a social market economy. Though, it

has to be admitted that the sixth dimension was already carried out much earlier, namely in the 1950s, when China conducted a substantial land reform within the agricultural sector.

	Dim. 1	Dim. 2	Dim. 3	Dim. 4	Dim. 5	Dim.6*
China	✓	✓	✓	✓	✓	✓
North Korea	✓	X	✓	X	X	X

Table 4: Comparing the six dimensions of a social market economy

A potential opening-up strategy could therefore include such a land reform before North Korea finally moves to granting foreigners access to its capital market. Substantial reforms on the **political level** (e.g. changing the mindset of “control”, allowing for more decentralized structures and firm autonomy as well as setting incentives for passive FDI streams) have to be undertaken prior to becoming a more open country in the future. Given the comparisons with China, the author would argue that 2018 marks a year that could have potentially initiated this opening-up process, but the journey will take at least 20 years.

5.2. Mismanagement of Imports and Exports

With regards to changes on an **economic level**, the author of this thesis would like to highlight the following finding. In chapter 3 “North Korean Economic Assessment”, it was found that North Korea imports what is rich of, while it exports what is rather scarce of. In fact, it seems interesting that the most important import goods are textiles and machines, while the country obviously has a lot of them at home (see chapter 2 “North Korean History”). On the other hand, it cannot be inferred that North Korea puts much attention to importing the goods which use the country’s scarce production factors extensively, which clearly are food raw materials. The Heckscher-Ohlin theorem suggests the exact opposite for the functioning of a normal market economy and leaves the reader wondering why a state like North Korea does not change its import and export structure accordingly. From the author’s point of view, one finds the result of a substantial economic mismanagement in North Korea.

If the country would want to open-up economically, the country probably would need to put more emphasis on importing nutritional factors in order to secure the living and support of its population. Once changes would be implemented on a political level, as mentioned before, this could lead to limitations with regards to the regimes “control”

factor. If this political change towards a more liberal market economy would happen, then the regime clearly has to expect to be overthrown by its own population if it does not change its import and export structure.

However, if at some point it also adopted measures that would lead to importing input factors what it is scarce of (e.g. raw food) and less of what it is rich of (e.g. disciplined labor for building machines and weapons), this could send a positive signal to its population as well. In chapter 2 “North Korean History” the author has analyzed that the regime did not necessarily mean to do bad on its people in history. Both Charles, A. and Michael, S. argue that the political regime in North Korea has shown evidence that it meant to support its people extensively (e.g. equality rights for woman, implementation of primary education etc.). Given the most recent events in 2018 (e.g. North Korea – United States summit), leader Kim Jong-Un shows some clear signals that one could hope for a change on the political level, which would bring about the economic changes hand in hand. In chapter 3 “North Korean Economic Assessment” Paul, H. described three main suggestions for an economic opening up strategy, which were (1) the improvement of the agricultural sector, (2) the reduction of defense spending and (3) overcoming the collapse of the Soviet Union in 1991 through economic reforms. In general, the author of this thesis agrees with these points, but would like to add at least two more points on top. First, as mentioned earlier, the **import and export structure** should be adapted towards what the Heckscher-Ohlin theorem suggests. And second, North Korea urgently needs to allow for an **iterative communication process** between the government and the country’s citizens. This includes free elections, joining organizations voluntarily and an improved mechanism for communication between cooperatives and high ranking government officials.

5.3. Relations with South Korea

As a final discussion point on what a North Korea opening-up strategy could look like, the author would like to include evidence from chapter 4 “Futuristic Prospects”. Given its geographical situation, North Korea could benefit from the South Korean market and its respective import and export structure to a great extent. This is because the author’s analysis show that North Korea owns a lot of material (e.g. raw material, minerals etc.) what South Korea imports the most. On the other hand, South Korea could potentially serve as a strong partner that would help to boost up North Korea’s economy through its advanced knowledge in technology. Experts like Michael, P. or

Seung-Ho, J. argue that after the signing of a peace treaty and free factor movement, South Koreans would be expected to invest heavily into North Korea's industrial sector, while cheap and well performing labor might immigrate to South Korea.

However, it is true that before a potential peace treaty will be signed, North Korea needs to abandon its extensive nuclear program. This is true, as we also have learned in chapter 4 "Futuristic Prospects" that while the country has shut down many of its nuclear missile stations, it has opened up others in more mountainous regions within North Korea. Once again, this reflects the need of the political regime for power and control and supports the hypothesis that North Korea's opening-up process will last longer than one would hope for and probably even longer than China's one. In sum, North Korea's unwillingness to stop its nuclear program and its fear of losing the political grasp might prolong the country's opening-up timeline in contrast to the Chinese example.

5.4. Implications and Future Research

This thesis has looked at prospects with regards to an opening-up strategy both on a political and economic level. If the North Korean regime decides to follow a change on both levels and implement new policies that would allow for the country to engage with the outside world more interactively, other separate studies should follow this thesis. For example, the author suggests to conduct an independent and empirical firm-level analysis on what businesses think of making North Korea their new destination for foreign direct investment (under the provisions of what this thesis has analyzed too). Also, the establishment of a legal framework for investments (e.g. providing details on SEZs, rules, business ethnics etc.) into North Korea could be interesting for exporters around the globe once clear signals from North Korea of moving towards a socialist market economy can be identified.

5.5. Conclusions

This thesis aimed to answer what a potential North Korean opening-up policy could look like and assumed that the country's strategy would be similar to the one of China under Deng Xiaoping during the 1970s. In general, an opening-up strategy should involve policy changes on both the political level and North Korea's economic management initiatives. Policy changes on the former level want to assist in transforming the North Korean command economy into socialist market economy and could therefore be represented through easing the country's nuclear program, giving a say to the

inhabitants (e.g. free elections), restricting power on the highest levels of government and involving leaders into multilateral peace and trade talks internationally (e.g. South Korea, United States). Also, in contrast to China, North Korea has not yet put underway an extensive land reform, which would be needed so much to make the biggest sector (agricultural) more competitive and prepared for trade.

On the economic level, much goes wrong in North Korea. Particularly, this is true for the country's import and export strategy as from an economic perspective it puts the focus on its government and military first policy rather than on building up competitive industries through motivated inhabitants. Factor wise North Korea has much to offer (e.g. raw material and disciplined labor) but it cannot yet leverage this comparative advantage due to its political regime that builds on the wrong morals.

In sum, a North Korean opening-up strategy seems to be under way now as Kim Jong-Un has started to interact with the outside world and drives forward political changes in his country (especially since 2018). It looks like the very first policy reforms will affect its nuclear program by reducing missile testing and reducing the enrichment of uranium. Once this is completely to the satisfaction of dominant players in this relationship (e.g. United States and South Korea), the country tends to be able to attract much attention from foreign investors and has already started to set up Special Economic Zones in order to accommodate this. Many aspects with regards to the country's history, its regime and its economic assessment appear to be similar to the former Chinese model, but, South Korea seems to be rather the main potential trading partner of North Korea in the future, while using the Chinese political way (still: a unification seems less likely, due to the big differences on a political level). This is because of South Korea's suitable import and export structure. China's WTO accession took place in 2001, thus, more than 20 years after Deng Xiaoping has started to liberalize the economy. For North Korea, a similar opening-up strategy can be expected. However, a missing land reform that would be so important for its agricultural competitiveness, as well as the – in comparison to China – even stronger conservative “Kimilsungism-Kimjongilism” ideology seem to prolong North Korea's opening-up strategy by at least a few years. In short, North Korea is set to go a similar way as China but is expected to arrive at its final destination (socialist market economy) not within the next 25 years.



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1 **Appendix**

2

3 Expert interview

4

5 Interviewee: Michael G. Plummer, Director John Hopkins University SAIS

6 Topic: Thoughts on North Korea

7 Date: 13 November, 2018

8 Location: Vienna and Bologna

9

10 **Author:**

11 When you think of what makes a socialist market economy like China (e.g. opening up
12 to outside world, profit motivation, decentralization, public ownership etc.), how far
13 away/close do you see the North Korean economy from this stage? Why? Does it make
14 any progress moving from a command economy to a market economy?

15 **Michael G. Plummer:**

16 Generally, there are some movements towards a socialist market economy, but on a
17 much more limited basis than it was the case in China during its initial economic-
18 opening up stages in 1978. To me, North Korea now seems to see the benefits of
19 greater economic efficiency and welfare more than ever in history. However, the term
20 “control” still remains in the minds of the North Korean government. Given this thinking,
21 North Korea is not expected to move quickly towards a socialist market economy. What
22 is more, the country simply does not appear to be very attractive for long term
23 investment from abroad. Though, small changes can have big effects. As the Chinese
24 example has shown, innovations in the agricultural sector have led to a substantial
25 increase in competitiveness and output. It is exactly these small changes that could
26 bring about a triggering “big bang” to the North Korean economy. It is important to
27 mention that the key for change is the political mindset, before bringing economic
28 reforms under way. It is true that the economy has to be liberalized, but steps towards
29 this scenario are yet too little. In fact, economic progress appears to be low because
30 on the political level one can identify little domestic change (even though it seems to
31 be the other way around to the outside world). This is particularly true for North Korea's
32 nuclear program. Recent articles suggest that while North Korea is shutting down some
33 of its nuclear plants (publically), it builds and opens up new ones on the other hand.

34 The country's nuclear program can probably be seen as its biggest asset in further
35 negotiations with other countries, thus, it is difficult to give up on and could still take a
36 lot of time.

37 **Author:**

38 What do you consider strengths of the North Korean economy?

39 **Michael G. Plummer:**

40 North Korea owns a lot of minerals and natural resources. Moreover, it has a cheap
41 and extremely disciplined military force. If the country would open up tomorrow, it would
42 have a strong comparative advantage over other countries (e.g. South Korea) in terms
43 of labor intensive goods. South Korea on the other hand has become a high wage
44 economy, thus, representing the opposite to North Korea these days. However, given
45 the differences, through an economic opening, North Korea would probably become a
46 quite interesting investment location for South Koreans. What is more, South Koreans
47 prefer to invest into large ethnic Korean regions. For example, South Korea invested
48 heavily into North-Eastern regions in China during its opening-up process. Also there
49 South Koreans would find a large Korean ethnic population, which made investment
50 into these areas more attractive. Of course, Special Economic Zones (SEZs) are very
51 important as well. In China, this has led to significant progress with regards to its
52 economic opening up progress. We see that North Korea has begun to set-up a few
53 SEZs as well and in order to attract foreign direct investment. However, many laws still
54 prohibit most foreigners to invest in North Korea, thus, making it difficult to integrate
55 the country into the world economy more smoothly.

56 **Author:**

57 Why could a North Korean economic opening-up strategy look similar to the Chinese
58 one under Deng Xiaoping? How could it be different?

59 **Michael G. Plummer:**

60 The difference turns out to be on the political level again. A North Korean economic
61 opening-up strategy could potentially be similar to that of China, but the political
62 mindset is different. The more North Korea would integrate with the global economy
63 (China, Russia and the US in particular), the less control it is going to have. This fact

64 seems to be scary to the North Korean government, as we know that the term “control”
65 is of utmost importance to the country.

66 **Author:**

67 What could an economic cooperation between North and South Korea look like? How
68 could the countries benefit from each other?

69 **Michael G. Plummer:**

70 It can be supposed that capital would probably flow into North Korea and cheap labor
71 into South Korea. However, what could be a difficult topic is the integration of people
72 with each other. Unlike the re-unification model of East and West Germany, Koreans
73 do not want such a model because the expenses of integration would probably much
74 higher than in Germany during that time. In North Korea we look at a population that is
75 completely brainwashed because thought control is much more dominant there than
76 in East Germany back in time. From my point of view, South Koreans would like to
77 integrate more with the North, but given the huge discrepancies, this could take a
78 significant amount of time.

79 **Author:**

80 What is your personal view on further developments on the Korean peninsula? What
81 future steps can be expected from North Korea?

82 **Michael G. Plummer:**

83 To me, denuclearization seems to be the most prominent topic for the future. Also, the
84 UN Security Council is focused on this, as the US appears to be extremely empathic
85 with regards to denuclearization and has vast influence in the region as well (e.g.
86 Japan, South Korea and China). Therefore, before markets are opening, one must
87 expect much bigger steps with regards to denuclearization. However, as already
88 mentioned earlier, its nuclear capabilities guarantee the survival of the political regime
89 in North Korea very much and have greatest priority. A peace agreement with the
90 South does not seem to come up any time soon. But North Korea needs to integrate
91 more with its neighbors in order to prepare the country for a prosperous future.
92 Potentially, it could allow for markets to emerge a little bit more and take a similar
93 approach to the Chinese model. Given the fast moving economies around North Korea
94 and North Korea's extreme stand-still, it will be difficult to pick-up on any progress soon.

95 For example, North Korea's GDP amounts to only around 1/20 of the US military
96 budget. Also, Samsung, which represents one of South Korea's most important and
97 biggest conglomerates is worth far more than USD 100 billion, which makes the value
98 of only one company much higher than North Korea's economy as such. From my point
99 of view, nuclear power really is one of the very few negotiation weapons North Korea
100 has and no really big deal with regards to denuclearization is to be expected any time
101 soon with the US either (little American expertise with regards to North Korea).

102 **Author:**

103 Thank you very much for the insights and the interview!