

Kim Jong Il's Southern Tour: Beijing Consensus with a North Korean Twist?¹

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From January 10 to 18, North Korea's paramount leader Kim Jong Il paid a remarkably conspicuous "unofficial" visit to China. As some have already noted, Kim's itinerary (including Wuhan, Guangzhou, Zhuhai, and Shenzhen) was reminiscent of Deng Xiaoping's famous Southern Tour in January-February 1992 (covering Wuchang, Shenzhen, Zhuhai, and Shanghai), which reaffirmed Beijing's commitment to economic reform in the post-Tiananmen era. Encouraged by this historical precedent, some North Korea watchers regard Kim's "Southern Tour" as a prelude to extensive reform in the near future. To corroborate their case, they add that Kim's previous visits to China were followed by economic opening and reform measures. In particular, they point to Kim's trip to Shanghai in January 2001, when he exclaimed that Shanghai had undergone a cataclysmic transformation and "changed beyond recognition"—a remark he repeated on his latest visit. Kim subsequently circulated an internal memo in October 2001, emphasizing "New Thinking" and laying out the basic principles for the July 2002 reform.³

Skeptics have a different view. To them, Kim Jong Il's Southern Tour is largely theater for foreign consumption, designed to reinforce Chinese and South Korean perceptions that he is someone they can do business with. Skeptics believe that Kim's trip is not a prelude to fundamental reform, but rather an attempt to draw political support and economic assistance from China and South Korea.

With the emergence of Iran's Mahmoud Ahmadinejad as a new poster boy for the axis of evil, there indeed would be some logic for Kim Jong Il to present himself in a positive light at this time. However, it would be a stretch to argue that his Southern Tour is basically for foreign consumption when it has been clear for some time that he has a voracious appetite for foreign news, films, and fashion trends. At a grand banquet hosted by Hu Jintao during his visit, Kim readily acknowledged that he was pleased to fulfill the "long-cherished hope to visit the southern part of the Chinese land." That said, it would also be rather imprudent to predict that North Korea will now undertake "Chinese-style" reform, based on superficial similarities between Deng's and Kim's tours. Before jumping to either conclusion, it would be wise to examine closely what Kim actually said and did on his recent trip to China and draw implications for North Korea's reform prospects.

In a nutshell, three inferences can be drawn from Kim Jong Il's Southern Tour. First, his control on power is secure. He feels sufficiently confident about his regime security to take more than a week off from Pyongyang and travel around in a foreign country. This may be an obvious point

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³ For details, see Wonhyuk Lim, "North Korea's Economic Futures: Internal and External Dimensions," forthcoming in *Korea: The East Asian Pivot*, edited by Jonathan Pollack (Newport, RI: Naval War College Press), accessible at http://www.brookings.edu/fp/cnaps/events/lim_20051102.pdf, pp.6-12.

to most North Korea watchers, but it may be news to those who read much into any odd development in North Korea such as Kim's pictures being taken down last year. Second, the relationship between China and North Korea is far deeper and more extensive than many casual observers realize. Third, while North Korea will pursue further economic opening and reform, its path is likely to be somewhat different from China's, as indicated by Kim's emphasis on developing an economic model suited to "the specific conditions of the country."

The close and multi-dimensional nature of the PRC-DPRK relationship was in full display during Kim Jong Il's visit. He saw all nine members of the Standing Committee of the Politburo and held separate talks with Wu Bangguo and Wen Jiabao as well as with Hu Jintao. Although some North Korea watchers had speculated that Kim's visit would basically focus on the Six-Party Talks in conjunction with the counterfeiting issue, economic and technical cooperation were critical components of bilateral discussions. In addition to having an in-depth exchange of views on "important international and regional issues of mutual concern," Kim Jong Il and Hu Jintao talked enthusiastically about economic matters. According to Hu Jintao, "mutually beneficial cooperation between the two countries in the field of economy and trade has registered fresh success in recent years." Hu and Kim even visited the Crop Research Institute in Beijing together, with Kim expressing a keen interest in raising agricultural productivity through variety improvement. Wen Jiabao and Kim exchanged their views on boosting economic cooperation between China and North Korea. The Chinese premier also explained to the North Korean leader about the current economic situation in China and "the relevant content of the 11th five-year plan" (2006-2010). This exchange may be of more than passing interest for the two leaders given that North Korea is about to implement a multi-year economic plan (three-year basic industry and agriculture plan from 2006 to 2008) for the first time since 1996, when its economic difficulties made multi-year planning infeasible. Not only does China provide North Korea with an example of an economy where "plan" and "market" co-exist, but there also is ample room for coordination between the two sides especially with regard to bilateral investment projects.

In fact, since Kim Jong Il visited Beijing just before the inter-Korean summit in 2000 to restore North Korea's relations with China, their economies have become increasingly integrated. Their bilateral trade has increased from \$0.49 billion in 2000 to \$1.39 billion in 2004, raising China's share in North Korea's total trade from 20 percent to 37 percent (Figure 1). In comparison, South Korea's share in North Korea's total trade has stayed around 18 percent while Japan's share has plummeted from 19 percent to 7 percent over the same period. Furthermore, prices in North Korea's informal markets track those in China's northeastern provinces as professional merchants and ordinary citizens are increasingly engaged in cross-border trade. Long gone are the days when Chinese companies were reluctant to invest in North Korea. According to Chinese statistics, in 2004, China's non-financial foreign direct investment flow into North Korea was \$14.1 million, more than a ten-fold increase from \$1.1 million in 2003. Some South Korean estimates of China's FDI deals in North Korea are larger by an order of magnitude.⁴ In March 2005, China and North Korea signed an investment promotion and protection accord. In December 2005, the two governments reached an agreement on joint exploration of seabed oil in the Yellow Sea. Perhaps geopolitical considerations as well as commercial incentives influence China's investment in North Korea, and an element of hyperbole is apparent, but some are even beginning to declare that "China yesterday is North Korea today, and China today is North Korea tomorrow."

⁴ See, for instance, Myung-Chul Cho and Moon-Soo Yang, *The Increase of North Korea's Economic Dependence on China and Its Implications for South Korea* (Seoul: KIEP, 2005) [in Korean]. Based on various sources, including newspaper articles on newly signed FDI deals, their estimate for China's FDI in North Korea in 2004 is \$173.5 million.

Of course, regional security issues continue to be of great concern for North Korea and China even as their bilateral relations deepen on all fronts. China is likely to do what it can to get North Korea back to the negotiating table and resume the Six-Party Talks. During their summit meeting, Kim and Hu in effect agreed to work together to “overcome the difficulties” and get the process going again. However, Chinese pressure on North Korea with regard to the Six-Party Talks should not be overstated. When the United States and North Korea signed the Agreed Framework back in 1994, China was quite concerned about the possibility of the United States establishing a foothold in North Korea. After five years of weak U.S. engagement in East Asia under the Bush Administration, however, China enjoys a much stronger position. Its influence in North Korea and the rest of East Asia is rising, and China is in no hurry to put heavy pressure on North Korea as long as the Six-Party Talks process continues. The next round of the Six-Party Talks is likely to resume in the near future lest the whole process falls apart. However, unless the United States and North Korea miraculously come to a shared understanding of the Joint Statement of Principles agreed on September 19, 2005, it is unlikely to produce any substantive result.

With respect to North Korea’s reform prospects, Kim Jong Il’s recent visit to China offers some interesting clues. Kim made it clear that he was interested in seeing for himself the results of China’s reform. Clearly, his intellectual curiosity and openness to new ideas are positive attributes conducive to reform in North Korea. Yet, before proclaiming he is “a bold reformer,” one should look at his other attributes as well. First, although he may be genuinely curious about the world outside North Korea, he tends to focus on technological marvels themselves rather than the institutional infrastructure that has made these technological developments possible. He displayed this tendency during his visits to high-tech factories in Shenzhen as well as the Crop Research Institute in Beijing. Second, Kim Jong Il is extremely concerned about his personal safety and regime stability given the precarious external environment. His cautious attitude serves as a brake on his willingness to implement reforms based on new ideas. As a result, the kind of reform he is likely to undertake is a mixed one marked by a stop-and-go pattern.

As for the North Korean leader’s emphasis on developing an economic model suited to “the specific conditions of the country,” a historical perspective would be useful. Back in the first half of the 1990s, the term “unique North Korean characteristics” or its equivalent was basically used as a code word for “no reform” in North Korea. Lengthy articles in North Korea’s official propaganda channels argued that the reforms undertaken by former socialist countries led to their demise and that North Korea with its “unique characteristics” had no need for fundamental reform. Even when Pyongyang opted for some economic opening in this period, such as the establishment of the Rajin-Sonbong Free Economic and Trade Zone in 1991, the emphasis was on limiting the influx of foreign influence rather than ensuring commercial viability. Since the food crisis in the second half of the 1990s exposed serious problems in the North Korean economy, however, this policy approach has become untenable. Today, when Kim Jong Il speaks of the need to design an economic model suited to North Korea’s specific conditions, he actually seems to mean what he says. In his banquet speech during his recent visit to China, Kim said: “The astonishing changes that have taken place in the vast land of China have been possible because the CPC (Communist Party of China) laid down a new line and policies to suit the specific conditions of the country.” He also praised various special economic zones for making a great contribution to “the socialist modernization drive with Chinese characteristics.” For his part, Hu Jintao said China would support the North Korean comrades in shaping out “the road of development suited to the specific conditions of their country.”

In essence, Kim Jong Il is in search of a model that would bring about economic development and political stability given North Korea's conditions, which are different from China's in terms of geography and geopolitics as well as economics. Smaller than a typical Chinese province, North Korea has limited room to conduct economic experiments on the periphery without having to worry too much about their side effects. Also, unlike China, which embarked on extensive reform after normalizing relations with the United States, North Korea has yet to normalize relations with the United States and Japan. Whereas China was able to adopt a "dual-track" strategy and develop "market" around "plan" in a relatively orderly fashion, North Korea had a serious economic decline and uncontrolled marketization after the collapse of the Soviet Bloc in the early 1990s, and is now struggling to attract foreign capital and strike a new balance between the formal and informal sectors in the economy. In addition, while China was a predominantly agricultural country when it launched extensive reform and enjoyed a large productivity increase after breaking up collective farms, North Korea has a relatively small agricultural sector and probably should rely more on improvement in labor-intensive manufactures. Although Kim Jong Il recognizes the merits of "the Beijing consensus," or maintaining state leadership and political control while undertaking market-oriented reform, he is well aware of these differences and is adding a North Korean twist. To him, the Russian alternative of political decompression and economic liberalization followed by the emergence of oligarchs is not acceptable, although he may draw some lessons from Vladimir Putin's attempt to reassert state leadership after a period of uncontrolled marketization.

Pyongyang has begun to adopt policy approaches suited to North Korea's specific conditions in recent years. With regard to experimentation on the periphery, Pyongyang has made decisive moves to ensure commercial viability, acknowledging that there are few venues in North Korea that are both commercially attractive and far away from the center. Although skeptics might argue that the Kaesong Industrial Complex is "a limited export enclave" just like Rajin-Sonbong, an hour drive from Seoul to Kaesong would show that this assessment is off the mark. Few companies wanted to go to Rajin-Sonbong in the remote northeastern corner of North Korea. It was *not* an export enclave, not even a limited one. By contrast, while Pyongyang is still concerned about regime stability for obvious reasons, it has made serious efforts to ensure commercial viability for companies in Kaesong. The industrial complex is already employing 6,000 North Korean workers, and planning to hire 100,000 in the first stage of development, or close to 10 percent of the North Korean work force in South Hwanghae Province.

With regard to normalization of external relations, Pyongyang is making do with countries that are willing to engage with North Korea, although it would be nice to normalize relations with the United States and Japan as well. The year 2000 marked a watershed as North Korea repaired relations with China, entered a new era with South Korea following the summit, and began to re-engage with Russia after Putin's election. North Korea's external trade soared in 2000, and has been on an upward trend since. When tallied up, North Korea's trade volume in 2005 is likely to be on a par with its 1990 level (Figure 2). Although it would have been better for North Korea to adopt extensive reform before the collapse of the Soviet Bloc, North Korea has come a long way since its "arduous march" days and can seriously think about alternative reform paths. Kim Jong Il's economic diplomacy in recent years also suggests that North Korea is playing China off against South Korea and Russia so as not to become overly dependent on any one country.

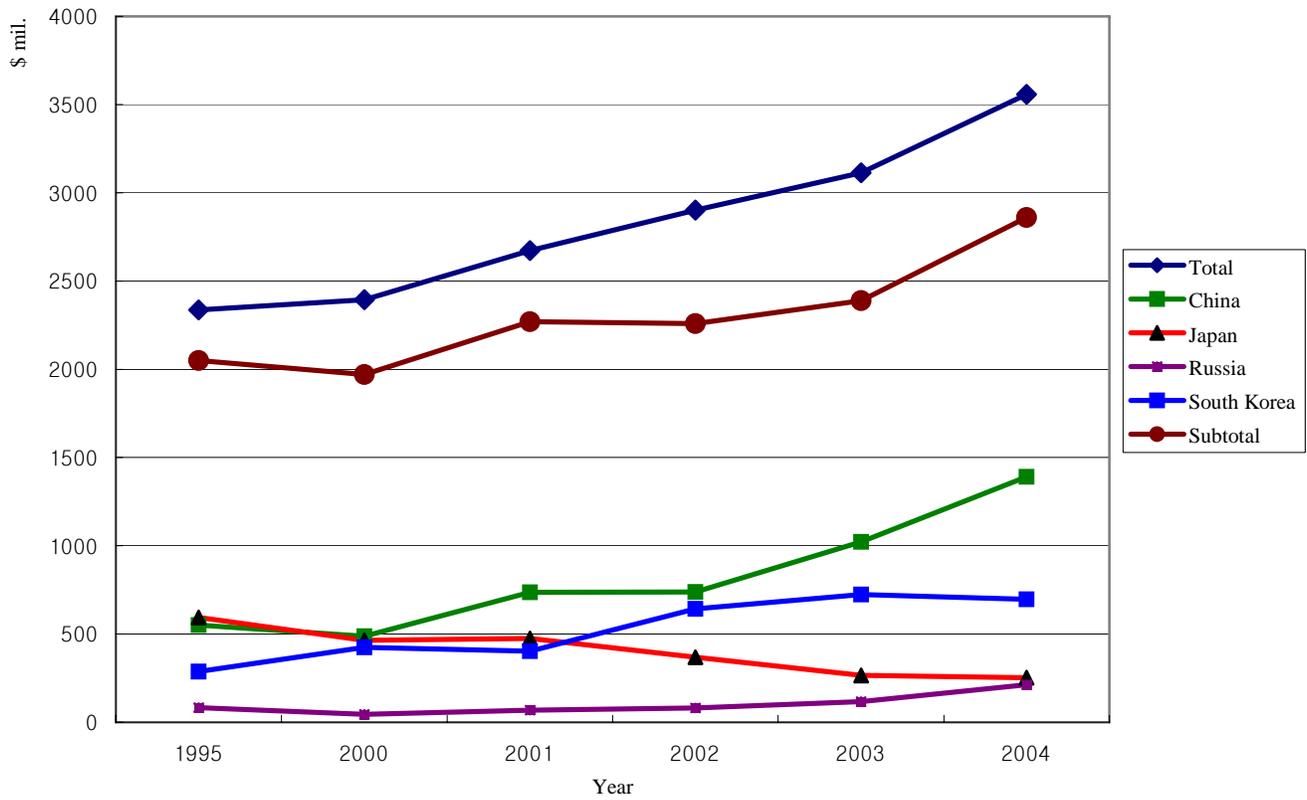
With regard to reasserting state leadership after a period of uncontrolled marketization, North Korea's moves have been less clear-cut. Last fall Pyongyang took some measures to reverse private food sales, particularly in border areas, and attempted to revitalize the public distribution system by selling rice at below-market prices to full-time workers. Although some observers have interpreted these developments as a major "U-turn" in economic policy, the real picture is

likely to be more complex, especially in light of the fact that, if anything, North Korea's economic engagement with the outside world intensified last year. In fact, rather than a retrogression to the semi-autarkic command economy of the past, the recent move may just be an ineffective attempt to attract workers back from the informal sector and put economic growth on a more stable trajectory. Although North Korea's informal sector has expanded a great deal since the outbreak of the food crisis, its relevance is basically limited to food and other distribution services. In manufacturing, which requires large capital and secure property rights, the role of the informal sector remains insignificant. However, as long as there are profitable sales opportunities and readily available food in the informal sector, workers' absenteeism is likely to remain a significant problem in the formal sector. In short, due to marketization without secure property rights, there is a capital-labor coordination problem in the informal and formal sectors.

Now, if the North Korean authorities had little concern about regime stability, they might think about liberalizing the establishment of private enterprises, but they are unlikely to be so confident. Instead, they are trying to lure back workers into the formal sector by offering full-time workers food at below-market prices. This is somewhat reminiscent of South Korea's decision to raise the interest rate on one-year time deposits from 15 percent to 30 percent in 1965 to attract savings into the formal sector and increase the amount of financial resources under state control. As far as reported restrictions on private food sales are concerned, such measures are likely to be ineffective in North Korea today and would risk triggering a policy-induced food crisis if fully enforced. In fact, it is doubtful there ever was an effective nationwide ban on private food sales in North Korea last fall.

Although Pyongyang might have hoped that selling food at below-market prices would provide a sufficient incentive for workers to remain in the formal sector, uneven food supply and low capacity utilization due to lack of essential inputs constrain its effectiveness. Here it might be useful to recall that although the July 2002 reform was extensive, it failed to generate a sufficient supply response because of limited domestic resources. After a decade of economic crisis, only the infusion of external capital would provide a substantive solution to the capital-labor coordination problem and put economic growth on a more stable trajectory. Clearly, the Kaesong Industrial Complex shows that it would not be difficult to persuade North Korean workers to stay in the formal sector if factories are run as they are supposed to and food is readily available. Special economic zones in southern China essentially underscore the same point, as they demonstrate the importance of combining foreign capital and market principles to generate economic growth. After his Southern Tour, Kim Jong Il should have a much better idea about how to develop an economic model suited to North Korea's specific conditions.

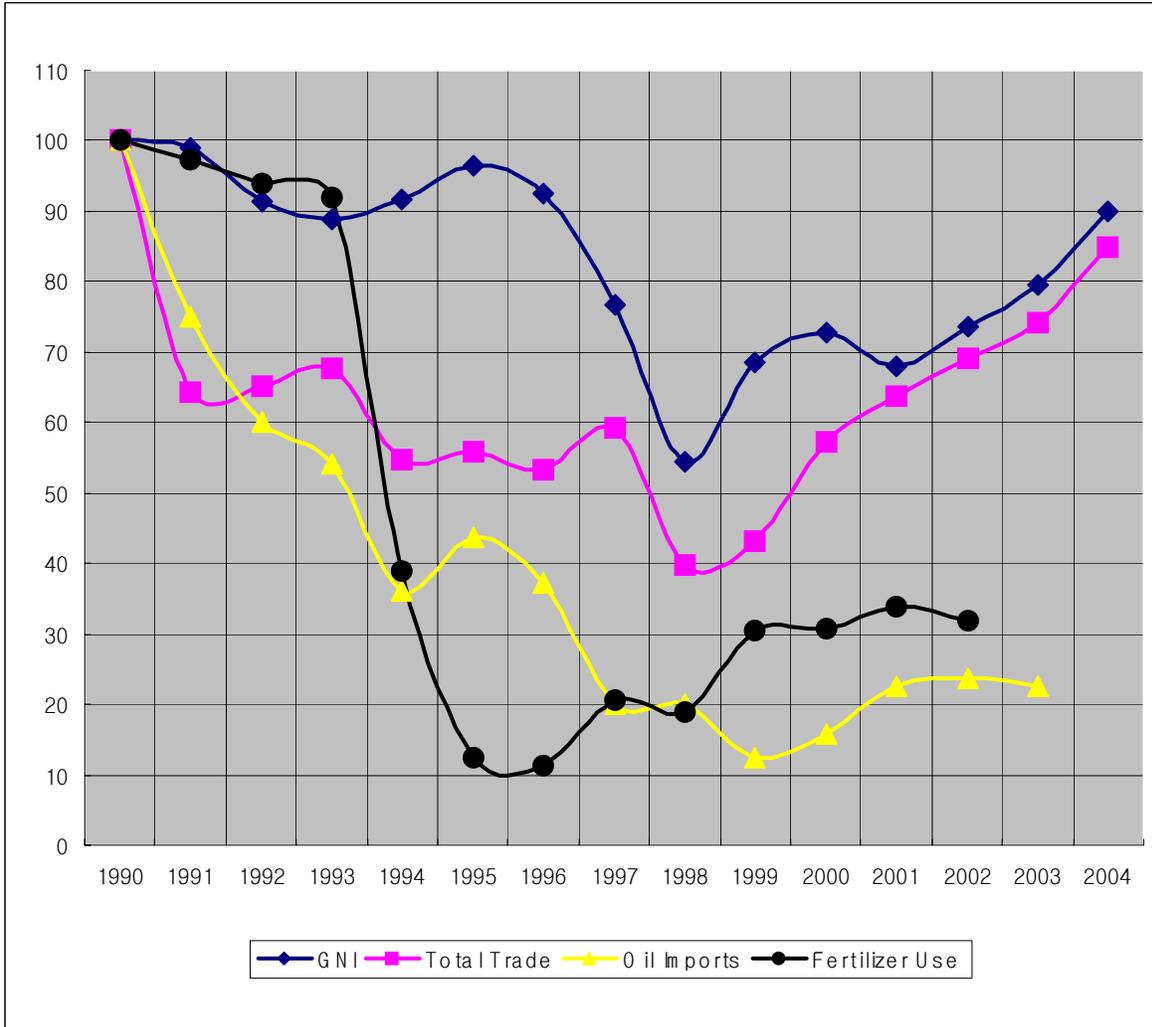
Figure 1. Composition of North Korea's Trade



Source: Kotra (www.kotra.or.kr); Ministry of Unification (www.unikorea.go.kr)

Note: "Subtotal" sums up all North Korea's external trade except its trade with South Korea.

Figure 2. Economic Trends in North Korea, 1990-2004



Source: North Korea's GNI, trade volume, crude oil imports, and fertilizer use estimates are provided by the Bank of Korea, Kotra and the Ministry of Unification, Korea Energy Economics Institute, and FAO, respectively.

Note: Level values are converted to index numbers and normalized at 100 in base year 1990. Base-year values are as follows: GNI, \$23.1 bil.; trade volume, \$4.2 bil.; oil imports, 18.5 mil. Barrels; and fertilizer use, 832,000 tons.