

June | 2018



Marketization of the North Korean Economy

**A Virtual Think Tank (ViTTa)[®]
Report**

Produced in support of the
Strategic Multilayer Assessment (SMA) Office
(Joint Staff, J39)

Deeper Analyses
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What is ViTTa®?

NSI's **Virtual Think Tank (ViTTa®)** provides rapid response to critical information needs by pulsing a global network of subject matter experts (SMEs) to generate a wide range of expert insight. For this Strategic Multilayer Assessment (SMA) Strategic Outcomes on the Korean Peninsula project, ViTTa was used to address eight key questions provided by the Joint Staff project sponsors. The ViTTa team received written response submissions from 50 subject matter experts from academia, government, military, and industry. Each Korea Strategic Outcomes ViTTa report presents 1) a summary overview of the expert contributor response to the ViTTa question of focus and 2) the full corpus of expert contributor responses received for the ViTTa question of focus. Biographies for all expert contributors are also included in each report.

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ViTTa Question

[Q7] Many analysts indicate that due to the partial marketization of the North Korean economy, the economy has stabilized somewhat. What were the key reasons the regime made the decision to marketize? What factors inhibit a broader marketization of the economy?

Subject Matter Expert Contributors

Dr. Bruce Bennett, RAND; **Dean Cheng**, Heritage Foundation; **Dr. Richard Cronin**, Stimson Center; **Ken Gause**, CNA; **Shihoko Goto**, Wilson Center; **Dr. James Hoare**, Chatham House; **Dr. Gregory Kulacki**, Union of Concerned Scientists; **Soojin Park**, Wilson Center; **Dr. James Platte**, United States Air Force Center for Strategic Deterrence Studies; **Anthony Rinna**, Sino-NK; **Brig Gen Rob Spalding**, United States Air Force; **Yun Sun**, Stimson Center

Summary Response

This report summarizes the input of 12 insightful responses from the Korea Strategic Outcomes Virtual Think Tank (ViTTa) expert contributors. While this summary response presents an overview of the key expert contributor insights, the summary alone cannot fully convey the fine detail of the contributor inputs provided, each of which is worth reading in its entirety. The expert contributors identify factors that explain the apparent condoning of controlled marketization in North Korea, as well as factors that appear to be inhibiting broader marketization in the country. This summary first discusses the key *drivers* of North Korean marketization and then considers the primary *inhibitors* to broader North Korean marketization efforts.

Key Drivers of North Korean Marketization Efforts

Four key reasons emerge from the expert contributor responses as primary *drivers* of North Korean marketization efforts.

- The economic downturn and famine that engulfed North Korea and eventually led to the collapse of the country's Public Distribution System in the 1990s.
- The rising expectations and aspirations of North Koreans that have started acclimating to marketization.
- The emergence of Kim Jong Un and new economic development policy.
- The reassuring precedent from China integrating itself into the international system in a way that promotes significant economic growth and development while preserving the security and legitimacy of its political system and regime.

Economic Downturn, Famine, and the Collapse of the Public Distribution System

The reason most frequently cited by the contributors to explain marketization in North Korea is the significant economic downturn and famine that engulfed the country in the 1990s and early 2000s, what

Dr. James Hoare of Chatham House describes as North Korea’s “economic meltdown.”¹ A weak North Korean economy was struggling, as economic infrastructure and equipment decayed and agricultural land wore down. Environmental challenges (e.g., flooding, drought) only made the situation more difficult. All of these obstacles, interacting together, put serious strain on the economy, making an already troubling economic situation even more problematic.² The situation eventually grew even more dire when, unable to withstand the economic downturn, the regime’s central ration system for providing food and other necessities to its people, the Public Distribution System, collapsed, sparking widespread famine and desperation across the country, with many North Koreans left by their government to survive on their own.³

Several contributors point to this collapse of the Public Distribution System as the proximate cause of North Korea’s initial shift toward marketization.⁴ The collapse meant that the regime was no longer capable of providing basic necessities. No longer able to rely on the regime for basic needs and survival, North Koreans took desperate measures including turning to informal markets for sustenance.⁵ Despite concerns over the legality of such informal markets, and an overall ideological opposition to marketization and capitalism in general, the regime did not move to quash these activities, seemingly concluding that the seriousness of the situation warranted concession. Soojin Park of the Wilson Center explains that the regime was ultimately left with “no choice but to tacitly condone” and tolerate the spread of commercial activity and marketization across the country, as it offered a means of survival for many North Koreans.⁶ Thus, an informal market economy emerged to help fill the void left by the failure of the regime’s Public Distribution System.

Importantly, this progression suggests that North Korean marketization initially resulted from what appears to be largely a bottom-up, rather than top-down, process.⁷ Park states this point directly: “North Korea’s marketization did not come about by design, but rather as a result of the state’s failure to sustain the livelihoods of its population.”

Rising Expectations of North Koreans Acclimating to the Market Economy

The rising expectations and aspirations of North Koreans who have started to benefit from marketization is also cited by contributors as a key reason for the regime’s decisions to allow limited marketization.⁸ The failure of the regime’s Public Distribution System unintentionally opened the door to private enterprise in North Korea, and introduced many North Koreans to the idea of a market economy. It also provided many North Koreans with an opportunity to witness first-hand some of the advantageous aspects of marketization. Since the regime’s initial limited opening to the idea of individual citizens profiting from informal market segments outside strict government controls, marketizing activity across the country has increased as North Koreans acclimate to the market economy. These activities, in fact, have created a new class of wealthy elites (“Donju”) who have been able to use their new-found wealth to purchase influence in the country’s economic and political institutions, further adding to their gains.⁹ Seeing the advancements that have emerged from marketization has driven higher the economic expectations and aspirations of many North Koreans, and

¹ See contributions from Cheng; Gause; Hoare; Park; Bennett; Platte; Rinna

² Cheng; Hoare; Park

³ Bennett; Hoare; Gause; Park; Platte; Rinna

⁴ See contributions from Bennett; Gause; Hoare; Park; Platte

⁵ Gause; Park; Platte; Rinna

⁶ See also the contributions from Hoare; Park; Platte; Rinna

⁷ See contributions from Park; Platte; Rinna

⁸ See contributions from Bennett; Cronin; Gause; Goto; Park

⁹ Gause; Goto; Park

has increased curiosity about the kinds of economic advancement opportunities that could arise from further broadening marketization within the country.¹⁰

Any attempt by the North Korean regime to significantly curb marketization, therefore, is likely to face some degree of pushback from the North Korean population.¹¹ Park reminds us of the regime's unsuccessful attempts to curb private entrepreneurship and decelerate marketization in 2007 and 2009. She explains that "such attempts, including the currency reform measure in November 2009—redenominating 100 won for 1 won—angered the people and were met with direct resistance, though short of rebellion." This pushback, Park suggests, helped the regime "realize that it would need to tolerate and allow market activities and marketization as a way to counter the people's complaints."

North Koreans with rising economic aspirations are likely to look to the Kim regime to establish and maintain an economic environment that will empower them to achieve their ambitions. The onus, therefore, is on the regime to stimulate and develop the North Korean economy. Not doing so, and diverging from popular expectations, could hurt the regime's legitimacy even more so than maintaining tight centralized control. In fact, Ken Gause of CNA suggests that the Kim regime is already feeling pressure from North Korean elites on this front:

The idea that Kim Jong Un came to the notion of diplomacy and engagement as a result of the Maximum Pressure Campaign is a fallacy. He has been preparing the country for this moment since 2012. That said, he doesn't have a lot of time. He is on a clock. By opening up the markets, he has exacerbated the differences in economic classes. The so-called moneyed elite ("Donju") have rising expectations and have suffered as a result of the sanctions. This class of elite is particularly critical to Kim's hold on power. Only through opening to the outside world, albeit in a controlled fashion, can he satisfy this demand. If left unsatisfied, his legitimacy will begin to suffer.

The Emergence of Kim Jong Un as the Leader of North Korea

Contributors also consider Kim Jong Un's emergence as the leader of North Korea to be a key driver of the country's economic decentralization.¹² The contributors generally believe that Kim has exhibited noticeable interest in economic development and marketization since taking over control. For example, he frequently discusses economic development in public, has initiated several highly-visible economic development initiatives (e.g., sparkling new apartment blocks in Pyongyang, the Masikryong Ski Resort in Kangwon Province, and a new international terminal at the Kalma Airport in Wonsan), and has instituted market reforms in the interest of promoting development and growth.¹³ Moreover, Kim appears willing to both accept some degree of marketization in North Korea and capitalize on markets within the country for economic and political gain. Gause even goes so far as to assert that Kim "gave free reign to the markets" upon taking over control. Kim's objective in doing so, Gause explains, was to help stabilize the North Korean economy by capitalizing on the markets to supply much needed goods and services, as well as to start acclimating the North Korean population to the market economies.

Ultimately, contributors appear to agree with the assessment from Dr. James Platte of the United States Air Force Center for Strategic Deterrence Studies that Kim appears to be "serious about improving the

¹⁰ Bennett; Cronin; Gause

¹¹ Park

¹² See contributions from Gause; Platte; Spalding

¹³ Gause; Platte

North Korean economy” and is willing to “stake some of his personal legitimacy on economic development.”

Reassuring Precedent from China’s Approach to Reform

Several contributors suggest that China’s approach to reform might be perceived by the North Korean regime as a reassuring precedent.¹⁴ Some of the same factors that drove economic reform in China are likely to be behind North Korea’s efforts to reshape its economic policies. Therefore, North Korea may find reassurance in, and be encouraged by, China’s ability to integrate itself into the international system in a way that promotes significant growth and development of its economy while also preserving the security and legitimacy of its political system and regime. China’s success on this front may entice North Korea into employing a similar approach. Brig Gen Rob Spalding of the United States Air Force emphasizes this point, offering a concise assessment of the dynamics:

Many Asian leaders have witnessed China’s stunning growth and realize you can develop economically yet remain authoritarian because the West will open their societies to you if you act peacefully. It is probable that Kim has finally seen the wisdom of the Chinese approach. This will encourage them to copy China’s economic development model.

Hoare, on the other hand, raises doubt about just how far the North Korean regime would be willing to follow any sort of Chinese model. North Koreans, Hoare argues, “have a very ambivalent relationship with China and resent being told that they should follow a Chinese model. And, of course, they were an industrialized nation well before China.”

Key Factors Inhibiting Broader North Korean Marketization Efforts

There are also three key factors that expert contributors cite as *inhibitors* to broader North Korean marketization efforts.

- The Kim regime’s perception of economic liberalization and broad marketization as a serious and direct threat to its fundamental interest, the security and survival of the regime.
- The Kim regime’s tight grip on the flow of information in the country and its desire to create ideological purity.
- Structural factors (e.g., productive capacity is severely lacking, the economy is severely constrained by limited foreign investment, there is currently no financing mechanism for providing capital at the individual level, legal protections for foreign businesses are quite weak, markets are still technically illegal and rife with corruption, and international sanctions have prevented the benefits afforded by globalization).

Fear of Economic Liberalization Threatening the Regime’s Fundamental Interests

The Kim regime appears to view economic liberalization and broad marketization as a serious and direct threat to its fundamental interest, the security and survival of the regime.¹⁵ Thus, while Kim has demonstrated a willingness to accept some degree of marketization inside North Korea, he is not likely

¹⁴ See contributions from Kulacki; Spalding; Sun

¹⁵ See contributions from Bennett; Cheng; Cronin; Goto; Park; Platte; Sun

to tolerate any sort of political reform or interference coinciding with economic reform initiatives. Nor is Kim likely interested in fully opening the North Korean economy to broad marketization, as doing so could risk the kind of significant economic and social change that could spark political instability. It would also likely reduce the regime's ability to maintain absolute control over the population and undermine the regime's legitimacy.¹⁶ As Park explains, "a totalitarian state like North Korea which is maintained under strict control over its people and society becomes increasingly vulnerable when it allows greater liberalization...while willing to accommodate some marketization, the regime is still very vigilant to keep it at a manageable level."

The Kim regime seems to ultimately be facing an interesting dilemma between balancing its political aspirations, which seemingly best align with a centrally planned and controlled economy, and its economic aspirations, which may be best served by great economic liberalization. Dr. Bruce Bennett of RAND offers further reflection on this dilemma: "the regime knows that if it allows too much market activity, the legitimacy of the regime will be undermined. But if the regime cuts the markets back too much, the North Korean economy will begin to fail."

Tight Control Over the Flow of Information

The Kim regime's tight control over the flow of information across the country is cited by contributors as a key factor inhibiting broader North Korean marketization efforts.¹⁷ The Kim regime strives to maintain absolute control over the population. In North Korea, this also extends to having absolute control over the flow of information. This information control is a part of Kim's initiative to create what he calls "ideological purity" across North Korea.¹⁸ Platte explains that "to enforce ideological purity and reduce chances for bottom-up political reform, Kim Jong Un likely will retain or strengthen controls meant to limit external influence on North Korean people. News, pop culture, and other media from the outside world, especially from South Korea, will be limited to trusted classes, as will interaction with outsiders." The current, fully controlled information environment that provides most North Koreans with little to nothing in terms of information freedom, together with the regime's ideological purity initiative, create conditions that are fundamentally contradictory to the idea of broader marketization.

Structural factors

Finally, the contributors also reference several structural factors that further inhibit broader North Korean marketization. These structural factors are listed below.

- Productive capacity is severely lacking.¹⁹
- The economy is severely constrained by limited foreign investment.^{20 21}
- There is currently no financing mechanism for providing capital at the individual level.²²
- Legal protections for foreign businesses are quite weak.²³

¹⁶ Gause; Cheng; Park; Platte

¹⁷ See contributions from Park; Platte

¹⁸ Platte

¹⁹ Park

²⁰ Park

²¹ Goto expounds on the role of aid and increased competition among donors in light of the Singapore Summit. She contends that, "by backing off on sanctions, the next step for growth would be to incorporate foreign aid and private capital down the line, beginning with infrastructure development. Pyongyang would undoubtedly be able to leverage the competition between key donors, especially from China, South Korea, and Japan, to maximize potential assistance by dividing the three powers."

²² Goto

²³ Rinna

- Markets are still technically illegal and rife with corruption.²⁴
- International sanctions have prevented the foreign direct investment, resources, and markets afforded by globalization.²⁵

²⁴ Hoare

²⁵ Cronin; Spalding

Subject Matter Expert Response Submissions

Dr. Bruce Bennett

Senior International/Defense Researcher (RAND)

25 May 2018

North Korea has gone back and forth on allowing markets for two decades. In the mid- to late-1990s, North Korea experienced a famine of extreme magnitude in which perhaps 1 to 3 million North Koreans starved to death despite the fact that the regime had the money to pay for the needed food. While there were likely some market activities before the famine, most food and other resources were provided by the regime's public distribution system before the famine. But desperation forced many North Koreans into finding a way to survive; market activity was the option chosen by many. Expert sources disagree on whether the public distribution system survives and the degree to which it provides needed food and other goods. It appears that increasing markets replaced the public distribution system as the leading source of food and other goods. When the regime has cut back on markets, famine has returned to the country, forcing them to allow more market activity. Ironically, this is more true in Pyongyang, apparently, where the elites live than it is true in the rest of the country. Many of the senior elites in North Korea have become capitalists, creating stores and restaurants and markets where goods can be exchanged. Still, the regime and its control system maintain some degree of control on the markets, fearing that the markets are a major source for importing foreign information that jeopardizes the regime. This is certainly true of the foreign media, and especially true of the South Korean soap operas that the North Korean people so much love and the regime fears. The regime knows that if it allows too much market activity, the legitimacy of the regime will be undermined. But if the regime cuts the markets back too much, the North Korean economy will begin to fail.

Dean Cheng

Senior Research Fellow, Heritage Foundation

30 May 2018

While there have been some steps towards allowing private markets, such measures, as in Cuba under Castro and even in NK under Kim Jong-il, are always subject to political moves. Kim Jong-un could reverse steps towards accepting the market at any time. This is most likely if/when North Korean merchants gain sufficient power and influence to be seen as a threat to the Kim family's hold on power.

Kim Jong-un accepted these measures in part because of the de facto collapse of the North Korean economy. At some point in the late 1990s and early 2000s, North Korean money ceased functioning (as a signal of resource accessibility and scarcity). Coupled with various demands for resources (maintaining the NK military, nuclear weapons research), as well as ongoing sanctions which at times affected NK access to China (e.g., after the Banco Delta Asia sanctions of 2005), NK was compelled to allow some market measures. As with the Soviet Union, once allowed, market measures proved to be far more effective at generating and sustaining capital and economic activity. (Soviet private plots, while a fraction of Soviet land use, was a major source of grain and other staples in the USSR.)

Private plots and private property, however, reduces the ability of the state to maintain absolute control over the population. A populace that is dependent on state-issued rations is one that will be far less likely to engage in protests or otherwise question the authorities. (In NK, this is backed by a massive security apparatus, prison camps, the family responsibility systems, etc.) Thus, the state is unlikely to allow a full flowering of private enterprise.

Dr. Richard Cronin

Distinguished Fellow, Stimson Center

7 June 2018

The increasing leakage via the internet of news from the real world, more North Koreans working in or fleeing to border areas of China and elsewhere, the impact of tougher sanctions all have had an impact. China has long leaned on Kim to undertake "Deng Xiaoping-type domestic market opening if for no other reason than supporting stability and reducing its own burden of shoring up the economy.

Whatever the economic data may show—and there is not much that is at all reliable—the visible signs of actual growth are evident in Pyongyang. All of this plays into the regime's self-confidence but also creates a positive slippery slope. The aspirations of at least the economic and political elite and probably most of the population of Pyongyang cannot be met without a growing economy. But so far, liberalization is solely domestic. Statements by US officials such as Secretary of State Mike Pompeo about how much US business and capital will roll into NK if a deal is struck are likely to be more chilling than encouraging. It's all about the survival of the clan and the regime. Domestic-led growth is supportive but any serious foreign—especially western or Japanese investment, except totally on the regime's terms and isolated from the general population would be politically dangerous. It seems Pompeo was talking from his congressional, pro-business and ideological perspective, not from any real understanding of the NK regime and system.

Ken Gause

Director, International Affairs Group, Center for Strategic Studies, CNA

4 June 2018

Early on in the KJU era, he gave free reign to the markets. This was designed to do two things. First, it helped stabilize the economic situation inside the country. The markets were able to backfill the goods and services lost with the collapse of the Public Distribution System. Second, it slowly began to acclimatize the population to an incentive-based economy. Over time, the population has been prepared to deal with a growing interaction with the outside world. The idea that KJU came to the notion of diplomacy and engagement as a result of the Maximum Pressure Campaign is a fallacy. He has been preparing the country for this moment since 2012. That said, he doesn't have a lot of time. He is on a clock. By opening up the markets, he has exacerbated the differences in economic classes. The so-called moneyed elite (*Donju*) have rising expectations and have suffered as a result of the sanctions. This class of elite is particularly critical to Kim's hold on power. Only through opening to the outside world, albeit in a controlled fashion, can he satisfy this demand. If left unsatisfied, his legitimacy will begin to suffer.

Shihoko Goto

Senior Northeast Asia Associate, Asia Program, Wilson Center

7 June 2018

Assuming that North Korea's aspiration is to follow the Chinese model for growth, the question is where Pyongyang draws the line in incorporating market mechanisms. Clearly, Kim Jong-un's regime has seen improved living standards as a result of allowing enterprising individuals to profit from transactions to a limited extent, and for technologies—particularly mobile phones—to be used so long as they were not used for subversive political activities. Easing of sanctions is expected to lead to a return in market activities. Whether or not these fledgling entrepreneurial activities could be encouraged to be scaled up is a different matter altogether.

There is currently no financing mechanism available in North Korea that would allow commercial activities as the restricted, individual level to expand. Whether or not Pyongyang would allow access to capital for individuals will give an indication on whether the regime is prepared to green light broader marketization of the economy.

Additional feedback from Shihoko Goto provided on 27 June 2018

One comment I would add would be about the role of aid and increased competition among donors. This is of course after the Singapore summit, but by backing off on sanctions, the next step for growth would be to incorporate foreign aid and private capital down the line, beginning with infrastructure development. Pyongyang would undoubtedly be able to leverage the competition between key donors, especially from China, South Korea, and Japan, to maximize potential assistance by dividing the three powers.

Dr. James Hoare

Associate Fellow, Asia-Pacific Programme, Chatham House

4 June 2018

I am not sure that there was a key decision to marketize the DPRK economy; it happened despite the ideological opposition to markets as a symbol of capitalism because the state could no longer provide the means of life to its people. This was not a sudden development. By the 1980s, there were clear signs that equipment was getting old and agricultural land becoming worn out. While exhortations to workforce continued, there was little improvement. Changes in East Europe and the Soviet Union also began to have a negative impact, which became a torrent after 1991. Changes in China also led to the Chinese ending special treatment for the DPRK. All these, together with floods and drought, led to an economic meltdown. The Public Distribution System, which had feed the urban workforce, collapsed. People died and the state gave up trying to control the economy. There had always been markets, sometimes tolerated more openly than was normal, but now they became essential to provide the basic necessities. They were clearly visible when I first visited Pyongyang in 1998 and even more when I came to live there in 2001-02. Many were well organized within enclosures and with guarded access. Others were on the streets and one sometimes came across them. Officially they did not exist. The MFA desk officer for the UK told my number two that she should stop asking to see a market because if she did it would show that the socialist economy was not working...

Markets were thus forced on the state because there was little alternative. They are still technically illegal and so can be closed down at any time. They are also a major source of corruption – bribes paid to officials etc. They probably also encourage smuggling – those who have visited them have reported masses of Chinese goods. Some will have come in legally, others clandestinely. They have allowed some to become wealthy, often in foreign currency holdings and therefore a target for the state.

Additional feedback from James Hoare provided on 26 June 2018

I have some doubts about how far the North Koreans are willing to follow a Chinese path in doing anything. The Koreans as a whole have a very ambivalent relationship with China and resent being told that they should follow a Chinese model. And, of course, they were an industrialized nation well before China.

Dr. Gregory Kulacki

China Project Manager, Union of Concerned Scientists

22 May 2018

I do not believe there is sufficient information about DPRK decision-making to answer this question. If, however, you see the DPRK as following the Chinese model, some of the same factors that prompted Chinese economic reforms are likely to be behind the DPRK's efforts to reshape its economic policies.

Soojin Park

Public Policy Fellow, History and Public Policy Program & Asia Program, Wilson Center

8 June 2018

1. Collapse of the state's ration distribution system

The collapse of central ration system of food and other necessities during North Korea's economic crisis in the 1990s, widely known as the "Arduous March" was the main driver of marketization. As the situation only aggravated further with major famine hitting the country in the mid to late 1990s, individuals were virtually left on their own to ensure their livelihoods. Unable to provide for its population, the state had no choice but to tacitly condone black marketeering and individuals taking up commercial activities for survival. So North Korea's marketization did not come about by design, but rather as a result of the state's failure to sustain the livelihoods of its population.

But to prevent growing economic and social disorder stemming from extensive black markets, North Korea under the new leadership of Kim Jong-il set out to overhaul its system that in essence meant a more utilitarian and practical socialism. The July 1 Economic Management Improvement Measures in 2002 allowed for partial acceptance of a bottom-up marketization, a phenomenon already in progress on the ground. By legalizing black markets, consumer markets were now officially allowed and those participating in market activities grew notably. In fact, some state-owned stores converted to such markets as well or were leased to enterprises and trading companies to sell imported products from China directly to the public. Hence, marketization spread throughout North Korea with a sharp increase in the number of individuals taking up market economic activities, and paving the way for the growth of a merchant class.

2. The state as well as people become heavily dependent on markets and marketization

Beginning in 2007, there were attempts by the authorities in North Korea to curb burgeoning markets and decelerate marketization out of concern and fear that growing individualism and mercantilism as well as more information seeping in along with foreign goods--by-product of market forces-- will have negative fallouts on the North Korean society politically and socially and ultimately, result in the regime's loosening of the power grip over its population.

But such attempts, including the currency reform measure in November, 2009 --redenominating 100 won for 1 won--angered the people and were met with direct resistance, though short of rebellion. North Korea realized that it would need to tolerate and allow market activities and marketization as a way to counter the people's complaints.

The rise of a new class of '*donju*', meaning 'money owner' have become instrumental in North Korea's economy. Having become the nouveaux riche financiers, these individuals were able to use private capital to establish partnerships with state institutions and factories by paying loyalty donations to further their business and economic activities for greater profit. So bluntly put, they have come to conduct business under the pretext of official trade with the cover by the authorities, effectively serving as a kind of the buttress for the ailing state-owned companies and providing a means of living for officials at institutions and authorities.

So the markets and marketization in North Korea not only feed the people where the state has failed, but have also made the state increasingly dependent on it for the sustenance of the institutions and its employees.

3. Political and structural factors that inhibit a broader marketization

While Kim Jong-un has granted more autonomy in factories and introduced measures resembling market-oriented reforms, Pyongyang continues to label capitalism as the source of all evil in society or the "hotbeds of anti-socialism." Instead, North Korea encourages and lauds efforts to conduct economic management "in our own style". This appears largely out of fears that an open shift to and full-fledged marketization would inevitably accompany greater economic and social changes creating risks of political instability.

A totalitarian state like North Korea which is maintained under strict control over its people and society becomes increasingly vulnerable when it allows greater liberalization. With enterprises and individuals conducting trade by appropriating state assets and resources, there is growing fear that the physical foundation of the state's planned economy is fast eroding and consequently weakening its authority and status in the sphere of people's economy. And broader marketization would inevitably result in more autonomy of economic actors with greater footing and independence from the perimeters of the

state, all perceived detrimental to the interests of the dictatorship in North Korea. So while willing to accommodate some marketization, the regime is still very vigilant to keep it at a manageable level.

Besides concerns for social and political ramifications, there's also structural factors that inhibit broader marketization. Development of markets and marketization in North Korea have been marked largely by that of trade and distribution, without comparable expansion in its productive capacity. Set aside resources poured into nuclear and missile development, money earned from trade has been poured largely into construction and service sectors—i.e., building high-rises, large public swimming pools, aquarium, and ski resorts—rather than production facilities to enhance its manufacture industry. The absence of institutionalization of personal property rights is among the reasons for such a phenomenon. For North Korea's economy to grow further with broad marketization, proper investment and allocation of resources must be made.

Lastly, but more fundamentally, North Korea's economy remains severely constrained by limited foreign investment. Although North Korea since 2013 has designated some two dozen economic development zones to attract foreign investment promising favorable environment for economic activities, they remain such zones only in name. In the absence of necessary infrastructure and rule-of-law to protect the investors, not to mention its record of seizing assets from investors, not to mention sanctions in place all make investors reluctant to venture in to North Korea.

Dr. James Platte

Assistant Professor, United States Air Force Center for Strategic Deterrence Studies (CSDS)

1 June 2018

The marketization of the North Korean economy began in the 1990s in response to the widespread famine that struck the country then. The state was not able to provide for people's nutritional and economic needs through its public distribution system, so people turned to other means just to survive. This included setting up informal markets and smuggling goods in from China. The central government was too weak to totally clamp down on these activities outside of Pyongyang, so an informal market economy began to develop. Economic reforms instituted after the famine ended in the early 2000s mostly just recognized the new reality of the North Korean economy. Thus, these reforms were more bottom-up reforms than top-down reforms.

As North Korea recovered from the famine and economic collapse of the 1990s, the state occasionally tried to reassert control over the economy and crack down on the emerging merchant class, sometimes termed the *donju*. Some measures, such as the 2009 currency reform, were quite draconian and ended up failing, while other reforms had less impact. In general, Kim Jong Il, father of current North Korean leader Kim Jong Un, did not seem committed to economic reform and marketization and only reluctantly allowed some market activities to not be punished.

Current North Korean leader Kim Jong Un has spoken often of economic development since taking power in 2012. He borrowed a phrase, *byungjin*, from his grandfather, Kim Il Sung, to characterize his development strategy. Kim Il Sung's *byungjin* strategy was to simultaneously develop the economy and the military, while Kim Jong Un's *byungjin* strategy is to simultaneously develop the economy and nuclear weapons. Kim Jong Un has instituted several showcase economic projects, such as sparkling new apartment blocks in Pyongyang, the Masikryong Ski Resort in Kangwon Province, and the new international terminal at the Kalma Airport in Wonsan.

In addition to these showcase projects, Kim Jong Un also has instituted some market reforms to help develop the North Korean economy. These reforms are a combination of top-down reforms initiated by the central government and bottom-up reforms that mostly acknowledge or decriminalize already ongoing market activities. Kim Jong Un seems serious about improving the North Korean economy and has staked some of his personal legitimacy on economic development. It is unclear whether he is promoting economic development out of true concern for the North Korean people or to help stabilize his rule by removing a potential source of instability.

Regardless of Kim Jong Un's true intentions or development goals, he likely will not tolerate any political reform to coincide with economic reforms, and he has emphasized ideological purity and the authority of the Workers' Party of Korea in his public speeches. Thus, he likely will want to retain state control over key industries, which will inhibit broader marketization of the economy. Additionally, to enforce ideological purity and reduce chances for bottom-up political reform, Kim Jong Un likely will retain or strengthen controls meant to limit external influence on North Korean people. News, pop culture, and other media from the outside world, especially from South Korea, will be limited to trusted classes, as will interaction with outsiders. These

measures will inhibit further marketization, as Kim Jong Un tries to maintain absolute rule over the country. They also will make it difficult for regional actors to cooperate economically with North Korea, as Pyongyang likely will balk at anything that they feel may be opening up their country too much or too quickly.

Anthony Rinna

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28 May 2018

Initial marketization did not occur in North Korea due to deliberate government policies. The end of the Cold War led China and Russia to stop providing subsidies for the North Korean economy. A famine struck the country in the mid-1990's, leading to widespread death. The partial marketization of North Korea's economy occurred from the bottom up, as people used whatever means they could to survive, such as bartering on informal markets. The North Korean authorities have tolerated this partial marketization as it provides a means for people to survive, and have amended the North Korean constitution to permit limited private economic activity.

The international sanctions regime currently in place against the DPRK is not in and of itself a reason why North Korea has not undertaken further marketization. It is not clear the Pyongyang regime was interested in pursuing further market liberalization in the first place. Sanctions, nevertheless could certainly inhibit the prospects of marketization. The current climate of reconciliation between North and South Korea has caused a wave of optimism not only among Koreans along both sides of the DMZ, but also in areas bordering North Korea. Real estate prices in the Chinese city of Dandong, for example, have recently risen, corresponding to hopes that reconciliation will lead to closer economic interconnectedness between North Korea and the northeast border provinces of China. If, however, sanctions remain in place - and if China elects to enforce them - then hopes for greater openness and economic exchange in the border areas will be misplaced.

At the same time, sanctions could propel further privatization in North Korea, albeit outside of official government permission. As North Korea has been prohibited from purchasing fuel on the international market, the hardship cutting off North Korea's fuel supplies causes for average DPRK citizens may lead to an increase in fuel smuggling. This could take the form not only of government-approved sanctions evasion, but also private citizens taking advantage of the lopsidedness in supply and demand.

Weak legal protections for foreign businesses also inhibit marketization. There are a select few limited cases of firms that are jointly-owned between the North Korean government and businesspersons from other countries - a case-in-point is the joint North Korea-Russia firm RasonKonTrans. In these cases there are regulatory guidelines for which side of the partnership (the North Korean or foreign) is responsible for what. RasonKonTrans, however operates within the Rason special economic zone near the border between the DPRK and Russia. In general, however a number of firms (mostly Chinese firms, ones not jointly-owned), despite long-standing contacts with North Korean counterparts, express fears of issues such as corruption and asset appropriation in North Korea. The lack of arenas for dispute settlement between North Korean and foreign firms is also a problem for Chinese businesses.²⁶

Brig Gen Rob Spalding

Special Assistant to the United States Air Force Vice Chief of Staff, United States Air Force

15 May 2018

Disagreement in philosophy between DPRK and Chinese Communists has prevented more market opening in recent past. Kim has a new view which will force him to abandon conventional military force for a nuclear deterrent thus freeing up resources to

²⁶ Having no prior knowledge of North Korea's marketization, the author of this report is indebted to Marcus Noland and Stephan Haggard, co-authors of "Hard Target", "Sanctioning North Korea: The Political Economy of Denuclearization and Proliferation" and "Integration in the Absence of Institutions" (sources from which these insights were generated) for their insights on North Korea's business environment; Jennifer Lee is also a co-author with Haggard and Noland in "Integration in the Absence of Institutions"; the author of this report is grateful to her as well for her contributions.

grow the economy. US-led trade sanctions inhibit the required foreign direct investment, resources and markets afforded by globalization. Many Asian leaders have witnessed China's stunning growth and realize you can develop economically yet remain authoritarian because the West will open their societies to you if you act peacefully. It is probable that Kim has finally seen the wisdom of the Chinese approach. This will encourage them to copy China's economic development model.

Yun Sun

Co-Director, East Asia Program, Stimson Center

Director, China Program, Stimson Center

29 May 2018

Black market with the Chinese is beyond the regime's control. China's reform and opening up serves as a reassuring precedent. China is willing to provide security guarantee. The fear of political liberalization, or the uncontrollable social movement as the result of opening up, is the key factor that inhibits broader marketization.

Subject Matter Expert Biographies

Dr. Bruce Bennett

Senior International/Defense Researcher, RAND

25 May 2018



Bruce W. Bennett is a senior international/defense researcher at the RAND Corporation who works primarily on research topics such as strategy, force planning, and counterproliferation within the RAND International Security and Defense Policy Center and the RAND Arroyo Strategy, Doctrine, and Resources Program. Bennett's work applies war gaming, risk management, deterrence-based strategy, competitive strategies, and military simulation and analysis. He specializes in "asymmetric threats" such as weapons of mass destruction (WMD) and how to counter those threats with new strategies, operational concepts, and technologies. He is an expert in Northeast Asian military issues, having visited the region more than 110 times and written much about Korean security issues. He has also done work on the Persian/Arab Gulf region. His Northeast Asian research has addressed issues such as future ROK military force requirements, the Korean military balance, counters to North Korean chemical and biological weapon threats in Korea and Japan, dealing with a North Korean collapse, potential Chinese intervention in Korean contingencies, changes in the Northeast Asia security environment, and deterrence of nuclear threats (including strengthening the U.S. nuclear umbrella). He has worked with the Office of the Secretary of Defense, the Defense Threat Reduction Agency, U.S. Forces Korea and Japan, the U.S. Pacific Command and Central Command, the ROK and Japanese militaries, and the ROK National Assembly. Bennett received his B.S. in economics from the California Institute of Technology and his Ph.D. in policy analysis from the Pardee RAND Graduate School.

Dean Cheng

Senior Research Fellow, Heritage Foundation

30 May 2018



Dean Cheng brings detailed knowledge of China's military and space capabilities to bear as The Heritage Foundation's research fellow on Chinese political and security affairs. He specializes in China's military and foreign policy, in particular its relationship with the rest of Asia and with the United States. Cheng has written extensively on China's military doctrine, technological implications of its space program and "dual use" issues associated with the communist nation's industrial and scientific infrastructure. He previously worked for 13 years as a senior analyst, first with Science Applications International Corp. (SAIC), the Fortune 500 specialist in defense and homeland security, and then with the China Studies division of the Center for Naval Analyses, the federally funded research institute. Before entering the private sector, Cheng studied China's defense-industrial complex for a congressional agency, the Office of Technology Assessment, as an analyst in the International Security and Space Program. Cheng has appeared on public affairs shows such as *John McLaughlin's One on One* and programs on National Public Radio, CNN International, BBC World Service and International Television News (ITN). He has been interviewed by or provided commentary for publications such as *Time* magazine, *The Washington Post*, *Financial Times*, *Bloomberg News*, *Jane's Defense Weekly*, South Korea's *Chosun Ilbo* and Hong Kong's *South China Morning Post*. Cheng has spoken at the National Space Symposium, National Defense University, the Air Force Academy, Massachusetts Institute of Technology (MIT) and Eisenhower Center for Space and Defense Studies. Cheng earned a bachelor's degree in politics from Princeton University in 1986 and studied for a doctorate at MIT. He and his wife reside in Vienna, Va.

Dr. Richard Cronin

Distinguished Fellow, Stimson Center

7 June 2018



Richard P. Cronin is a Distinguished Fellow at Stimson. Until July 2016 Cronin directed Stimson's Southeast Asia Program and Mekong Policy Project. Cronin joined Stimson in 2005 after a long career as an Asia Specialist with the non-partisan Congressional Research Service. At Stimson, he works on transboundary and nontraditional security issues in Southeast Asia and the South China Sea from a political economy perspective. Among numerous publications he is the author of "Hydropower Dams on the Mekong: Old Dreams, New Dangers," (Asia Policy, July 2013) and the lead co-author of numerous Stimson reports, issue briefs, and presentations, including Mekong Tipping Point (2010), "After Xayaburi and Don Sahong: Time for a New Narrative on Mekong Hydropower," (March 2015), a series of four first-hand "Letters from the Mekong" issue briefs, "After Xayaburi and Don Sahong: Time for a New Narrative on Mekong Hydropower" (Oct 2016). He is a co-author of a Stimson briefing, "A Call for Strategic, Basin-wide Energy Planning in Laos" (Jan 2017). Cronin has testified at US Congressional hearings on Mekong hydropower issues and the South China Sea. Senior US officials have credited Cronin and Stimson with awakening the US Government to the growing threat to peace and stability in the Lower Mekong because of dam development on the Mekong's mainstream. He has been a non-official member of US delegations to several regional meetings of the Lower Mekong Initiative (LMI) and the Friends of the Lower Mekong donor group. Cronin earned a B.S. in economics and history, and an M.A. in European history from the University of Houston. He holds a Ph.D. in modern South Asian history from Syracuse University. He served in Vietnam (1st Lt) with the US Army's 1st Infantry Division in 1965-66.

Ken Gause

Director, International Affairs Group, Center for Strategic Studies, CNA

4 June 2018



Ken Gause is the director of the International Affairs Group, a part of CNA's Center for Strategic Studies. He is CNA's senior foreign leadership analyst and has spent the last 20 years developing methodologies for examining leadership dynamics of hard-target, authoritarian regimes. In particular, he is an internationally respected expert on North Korea who has written three books on North Korean leadership. His latest book is "North Korean House of Cards: Leadership Dynamics Under Kim Jong-un." Leadership and opposing force (OPFOR) analysis are core areas of expertise within CNA Strategic Studies and Gause has personally directed studies on the North Korean, Iranian and Russian leadership and decision-making. His work on foreign leadership dates back to the early 1980s with his work on the Soviet Union for the U.S. government. Over the last three decades, he has devised analytical techniques used to understand adversary decision-making. These techniques span a five-tier set of methodologies that range from biographical analysis to studies on how to impact and shape an authoritarian or totalitarian regime's actions. These studies include a range of approaches from sophisticated game design to proprietary analysis based on a "virtual network" of researchers around the world dedicated to providing analysis on regimes of interest, their leadership, and how they make decisions. Gause has also published numerous articles on leadership structures for such publications as Jane's Intelligence Review, Jane's Defense Weekly, and the Korean Journal of Defense Analysis. He has a B.A. from Vanderbilt in Russian and Political Science and an M.A. from The George Washington University in Soviet and East European Affairs.

Shihoko Goto

Senior Northeast Asia Associate, Asia Program, Wilson Center

7 June 2018



Shihoko Goto is the senior Northeast Asia associate at the Woodrow Wilson Center's Asia Program, where she is responsible for research, programming, and publications on Japan, South Korea, and Taiwan. She is also a contributing editor to *The Globalist*, and a fellow of the Mansfield Foundation/Japan Foundation U.S.-Japan Network for the Future for 2014 to 2016. Prior to joining the Wilson Center, she spent over ten years as a journalist writing about the international political economy with an emphasis on Asian markets. As a correspondent for Dow Jones News Service and United Press International based in Tokyo and Washington, she has reported extensively on policies impacting the global financial system as well as international trade. She currently provides analysis for a number of media organizations. She was also formerly a donor country relations officer at the World Bank. She received the Freeman Foundation's Jefferson journalism fellowship at the East-West Center and the John S. and James L. Knight Foundation's journalism fellowship for the Salzburg

Global Seminar. She is fluent in Japanese and French. She has a BA in Modern History from the University of Oxford, and an MA in international Policy Theory from Waseda University.

Dr. James Hoare

Associate Fellow, Asia-Pacific Programme, Chatham House

4 June 2018



Since retiring from HM Diplomatic Service in 2003 - where his last post was establishing the British Embassy in North Korea - Dr. Hoare has pursued a second career as a broadcaster, writer and occasional teacher on East Asia. Much of his work concerns North Korea but he also has expertise on China and Japan. He has published several books, some with his wife, Susan Pares, also a former diplomat. He is a graduate of Queen Mary University of London (BA 1964) and the School of Oriental and African Studies (PhD 1971).

Dr. Gregory Kulacki

China Project Manager, Union of Concerned Scientists

22 May 2018



Gregory Kulacki is an expert on cross-cultural communication between the United States and China. Since joining UCS in 2002, he has promoted dialogue between experts from both countries on nuclear arms control and space security and has consulted with Chinese and U.S. governmental and non-governmental organizations, including the U.S. House China Working Group, the Senate Armed Services Committee, the U.S. National Academies, NASA, and the Office of Science and Technology Policy. Over the last decade, Kulacki has been cited by a number of U.S. and Chinese news organizations, including the *Christian Science Monitor*, *Nature*, *New York Times*, *NPR*, *Washington Post*, and *Washington Times*. Dr. Kulacki, who is fluent in Mandarin Chinese, has lived and worked in China for more than 20 years. Prior to joining UCS, he served as an associate professor of government at Green Mountain College, director of external studies at Pitzer College, and director of academic programs in China for the Council on International Educational Exchange. Dr. Kulacki

earned a doctorate degree in political theory and a master's degree in international relations from the University of Maryland in College Park. He also completed graduate certificates in Chinese economic history and international politics at Fudan University in Shanghai.

Soojin Park

Public Policy Fellow, History and Public Policy Program & Asia Program, Wilson Center
8 June 2018



Soojin Park is a Public Policy Fellow in residence at the Woodrow Wilson Center's History and Public Policy Program and Asia Program. Park served as Deputy Spokesperson for the Ministry of Unification in the Korean government from 2011 to 2016. During her tenure, she attended numerous inter-Korean talks to resume operations at the Gaeseong Industrial Complex, a symbol of inter-Korean cooperation, as well as reunions of the separated families in the North's Mount Geumgang. Prior to her post in civil service, Park was a journalist and host to "Diplomacy Lounge" at Arirang TV, Korea's first English show focusing on the country's diplomatic front where she interviewed many visiting heads of state from around the world. Park has a bachelor's degree in English Language and Literature from Yonsei University in Korea and a master's degree in Communication with emphasis on Public Affairs & Issue Management from Purdue University.

Dr. James Platte

Assistant Professor, United States Air Force Center for Strategic Deterrence Studies (CSDS)
1 June 2018

Dr. James E. Platte is an assistant professor with the USAF Center for Strategic Deterrence Studies (CSDS), and he is the course director for the Deterrence Research Task Force elective cross-listed with the Air War College and the Air Command and Staff College. Prior to joining CSDS in 2017, Dr. Platte was an intelligence research specialist with the U.S. Department of Energy, and he also has worked on nuclear counterproliferation with the Defense Intelligence Agency and the National Nuclear Security Administration. He received his PhD in international relations from the Fletcher School of Law and Diplomacy at Tufts University and has held research fellowships with the East-West Center, Pacific Forum CSIS, the Council on Foreign Relations, and the Harvard Kennedy School. Dr. Platte broadly is interested in the military and commercial applications of nuclear energy, and his research particularly focuses on nuclear issues in East Asia, including North Korea's nuclear program, U.S. extended deterrence, and the proliferation of nuclear technology across the region.

Anthony Rinna

Senior Editor, Sino-NK
28 May 2018



Anthony V. Rinna is a Senior Editor at Sino-NK, a research organization dedicated to the study of the Korean Peninsula and Northeast Asia. Rinna is a specialist in Russian defense and economic policy in Northeast Asia, and regularly publishes on those topics in academic journals and policy forums. He also frequently gives commentary to the media on Russia's North Korea policy. He has a working knowledge of Korean, Russian and Spanish. A US citizen, Rinna has lived in South Korea since 2014.

Brig Gen Rob Spalding

Special Assistant to the United States Air Force Vice Chief of Staff, United States Air Force
15 May 2018



Brig Gen Robert S. Spalding III assumed the duties of Special Assistant to the U.S. Air Force vice chief of staff in February 2018. General Spalding received his commission through Fresno State University's Reserve Officer Training Corps program in 1991. He earned his doctorate in economics and mathematics from the University of Missouri at Kansas City in 2007. The general attended undergraduate pilot training in 1993, and was subsequently assigned as a B-52 Stratofortress co-pilot in the 5th Bomb Wing at Minot Air Force Base, North Dakota. He subsequently transitioned to the B-2 Spirit at Whiteman AFB, Missouri. In 2001, he was selected as one of three Air Force Olmsted Scholars, and was a distinguished graduate of Mandarin Chinese language training at the Defense Language Institute in Monterey, California. Afterward, the general attended Tongji University in Shanghai as a graduate research student. He then returned to Whiteman AFB as a B-2 evaluator pilot and assistant director of operations for the 393rd Bomb Squadron. The general was then assigned to the Office of the Secretary of Defense's Prisoner of War Missing Personnel Office as the military assistant for the deputy assistant secretary of defense. During the Iraq surge in 2007, General Spalding deployed to Baghdad and directed the Personal Security Coordination Center. After a stint at the Air War College at Maxwell AFB, Alabama, he was reassigned to the B-2 at Whiteman AFB. While at Whiteman AFB, he was the chief of safety, operations group commander and vice wing commander. He was then selected as a Military Fellow at the Council of Foreign Relations in New York. General Spalding then served as the chief China strategist for the chairman of the Joint Chiefs, the Joint Staff at the Pentagon, Arlington, Va. Prior to his current assignment he served at the White House as the Senior Director for Strategic Planning at the National Security Council, Washington, D.C. General Spalding speaks Chinese-Mandarin and Spanish.

Yun Sun

Co-Director, East Asia Program, Stimson Center
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29 May 2018



Yun Sun is co-Director of the East Asia Program and Director of the China Program at the Stimson Center. Her expertise is in Chinese foreign policy, U.S.-China relations and China's relations with neighboring countries and authoritarian regimes. From 2011 to early 2014, she was a Visiting Fellow at the Brookings Institution, jointly appointed by the Foreign Policy Program and the Global Development Program, where she focused on Chinese national security decision-making processes and China-Africa relations. From 2008 to 2011, Yun was the China Analyst for the International Crisis Group based in Beijing, specializing on China's foreign policy towards conflict countries and the developing world. Prior to ICG, she worked on U.S.-Asia relations in Washington, DC for five years. Yun earned her master's degree in international policy and practice from George Washington University, as well as an MA in Asia Pacific studies and a BA in international relations from Foreign Affairs College in Beijing.