




Opinions

Economic Opportunities Amid Improving Inter-Korean Relations and Denuclearization Talks



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Summit diplomacy to resolve the denuclearization issue of North Korea is proceeding at a breathtaking pace. The negotiation progress up to now has far exceeded the expectations of experts. In a very short period of time, North Korea's denuclearization issue has rapidly evolved from a state of confrontation and antagonism to one of dialogue and compromise. North Korea conducted its sixth nuclear test in September 2017 and test-fired an intercontinental ballistic missile in November 2017. These actions naturally led to further deterioration in North Korea's relationship with the US and South Korea. The United States threatened to bomb North Korea in early February 2018, a so-called "bloody nose" strategy. The situation, however, suddenly reversed after the PyeongChang Olympic Games in late February. Since PyeongChang, subsequent summits have been held to solve the denuclearization problem. The highlights up to now have been the North-South Korean summits, held in Panmunjom, South Korea on April 27 and the North Korea-US summit, held in Singapore on June 12.

Denuclearization talks seem on the track of comprehensive agreements and phased implementation. However, there are some discrepancies in

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the concept of denuclearization, process, speed, and compensation.

It seems that North Korea is more inclined toward a step-by-step exchange of comprehensive denuclearization and security of the regime, together with the lifting of sanctions against North Korea, while the US wishes to make some progress in denuclearization first and ensure the security of the regime later. The key to addressing the agreement lies in the authenticity of North Korea's denuclearization process and the US's confidence in it. In the end the denuclearization talks will most likely result in an agreement being reached, though frequent frictions and misunderstandings could plague the negotiation.

The progress we are seeing in the denuclearization talks is leading to hopeful anticipation among North Korea's neighbors for prospective economic investments within the country. A successful conclusion to the denuclearization talks is likely to be followed by North Korea's economic transition to a market economy. North Korea has many advantages to attract foreign direct investment (FDI), such as its cheap labor, abundant mineral resources, and geographical location. At the initial stages of the economic transition, FDI to North Korea will likely suffer from the poor infrastructure conditions within the country and lack of understanding about laws and institution systems of market economies. However, FDI to North Korea will show high profits over the mid- to long-term. In the words of a Bloomberg report, "North Korea looks like Vietnam in 1986, and the economy is a bit more industrialized."¹ According to World Bank statistics,² Vietnam's GDP rose from 6.3 billion in 1989 to 205.3 billion US dollars in 2016, averaging approximately 13% annual growth in its GDP following the Doimoi economic reform policy carried out in 1986.

North Korea is expected to follow a similar economic growth path. First of all, the North Korean economy will likely show double-digit growth for at least 10 years after transitioning to a market economy. FDI to North Korea would be a channel to share the fruits of this rapid economic growth. Second, North Korea has abundant mineral resources and labor wages which are cheaper than Vietnam. These comparative advantages will boost the exports of North Korea and enable complementary relations with global value chains in Northeast Asia, relocating labor-intensive light manufacturing industries to North Korea and increasing imports

¹ Shuli Ren. 2018. *Kim Could Make North Korea Samsung's New Backyard*. Bloomberg. (May 15, 2018).

² World Bank Data Bank. 2018. GDP (Vietnam, Current USD), Available at <https://data.worldbank.org/indicator/NY.GDP.MKTP.CD?locations=VN> (accessed May 10, 2018)

and re-exports of intermediate goods from and to manufacturing industries in North Korea. Third, conducting FDI to North Korea carries the significance of entering the enormous markets of China, Japan, and Korea, due to cultural similarities and the geographical location of North Korea, which bridges China, South Korea, and Japan.

As for more concrete prospects, South Korea has positive expectations for inter-Korean economic cooperation projects, such as connecting the Trans-Korean Railway with the Trans-China Railway and Trans-Siberian Railway, and reopening the Kaesong Industrial Complex and Mount Kumgang Tourist Region. Russia is interested in railway connections with Korea, oil pipelines, and transmission lines through North Korea. In addition, the improvement in relations between the two Koreas seems to be having a positive effect on the development of Far East Russia. The Chinese and Japanese governments have yet to comment on whether they will be resuming economic cooperation with North Korea, but they are among the potential major stakeholders investing in North Korea. China's interest is in mining mineral resources and developing sea ports in Rason, North Korea. In particular, modernizing the sea ports in Rason is expected to lead economic growth in its land-locked provinces Heilongjiang and Liaoning, as access to China is improved through these sea ports. Japan will be able to improve logistics connections with the Eurasia continent through FDI to North Korea, and it could restart imports of agricultural and fishery products, which were imported before its bilateral sanctions against North Korea. In addition, England, France, Germany, and Australia are also interested in FDI projects in North Korea, such as in the area of railway construction, building infrastructure, power plants, water supply and sewerage systems, financial networks, and financing FDI to North Korea.

Even though potential FDI projects to North Korea are eliciting positive expectations, many obstacles will have to be overcome before the actual implementation of these projects. First, most economic sanctions against North Korea must be lifted to implement FDI. Economic cooperation simply cannot be achieved without lifting these economic sanctions. If the denuclearization talks come to a dead end, economic cooperation with North Korea will cease to be feasible. Second, North Korea has a very weak infrastructure. Most of the FDI to North Korea will concentrate in the coastal area, and it will be necessary to develop comprehensive industrial complexes, modern port facilities, power generation facilities and water and sewage facilities. Third, entering the North Korean domestic market in the form of FDI projects is unfeasible because the income level is too low. Instead, FDI should concentrate on the export of North Korean manufactured goods to overseas markets, leveraging the cheap labor in North Korea. Fourth, unfortunately, North Korea has no free trade agreement with any coun-

try except Korea. Lacking such trade agreements, it will be impossible for FDI to North Korea to forge links to GVCs in Northeast Asia. Fifth, North Korea's legal systems and institutional development remains at a low level, thus limiting the entry of FDI. The outcome of any dispute arising remains highly unpredictable and FDI firms have no choice but to rely on the arbitrary judgment of North Korean officials.

The North Korea denuclearization talks are making progress. There is much hope for the opening of the North Korean economy, but the conditions for this to happen are not favorable. Even in a positive scenario it will take at least two years to complete the denuclearization process, and this will lead to many uncertainties arising during the process of improving relations with North Korea. Nonetheless, the issue of FDI to North Korea is receiving much attention from other countries due to the potential for economic growth. We can safely conclude that progress toward the denuclearization of North Korea, and the subsequent resumption of economic cooperation, will serve as a significant factor contributing to peace and prosperity in Northeast Asia. **KIEP**