

## The Current Situation of Marketization in North Korea and Prospects for Change of Its Economic System

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### North Korea's Marketization and Its Informal Economy

The changes taking place in North Korea's political, military, and economic aspects since Kim Jong-un inherited power, are drawing the world's attention. In particular, as the Kim Jong-un regime places greater importance on the economy, there is a growing international interest as to whether the new economic measures will bring about positive changes in North Ko-

rea. Current policies of the North bear many startling resemblances to the reform policies of former socialist countries. At present, the time might not yet be ripe for predicting North Korea's full transition to a market economy. However, the Stalinist state has been placed in an abnormal situation where a planned economy and markets coexist in the country. As it is not likely that the socialist-planned economy would prosper in such a situation, for North Korea, the transition to a market economy is almost inevitable.

This report studies the marketization of North Korea and seeks to forecast the possibility of change in its economic system in commemoration of the advent of the new Kim Jong-un regime as well as the tenth anniversary of the “July 1st Economic Reform Measures” in 2012. The advances in marketization are likely to result in the weakening of the state control of North Korean authorities. In addition, the spread of markets suggests the high possibility of transition to a market economy, which occurred previously in socialist states in Eastern Europe and China.

## Estimation of the Size of North Korea’s Market

Most of the existing studies on estimations of the market scale in North Korea depended on surveys that involve North Korean defectors. These surveys can be distorted by the economic and social bias of the defectors. The researchers also sought to estimate the market scale of North Korea using macroeconomic data. However, the data they used had the possibility to be unsuitable in estimating the informal economy of the country. As a result, there appeared to be a significant gap between the estimations through surveys and macroeconomic data. In order to overcome such a problem, this study utilized the “2008 Census of Population of DPR Korea”. The census contains questions that can help infer the participation rate of informal economic activities in North Korea for the whole North Korean population, which is not limited to a certain number or regions of people.

Through an analysis of census questions, the study found that almost 83% of the North Korean population is involved in household economic activities, most of which are related to

growing vegetables and raising livestock or poultry. This participation rate in household economic activities can be deemed the same or very similar with that of informal economic activities. The study also found that the rate is affected by income and other market-related variables. Lee Suk conducted a survey, targeting North Korean defectors in the mid-2000s, and the result of the survey showed that approximately 86% of the North Korean households were involved in the informal economic activities.

**Table 1. The Participation Rate in Household Economic Activities for North Korean People Aged over 16**

		The Total Population (A)	The Population Participating in Household Economic Activities (B)	(B) / (A)
Total	Male	8,001,786	6,285,430	78.55
	Female	9,364,983	8,193,138	87.49
	Total	17,366,769	14,478,568	83.37
Urban	Male	4,939,085	3,725,953	75.44
	Female	5,747,438	4,791,884	83.37
	Total	10,686,523	8,517,837	79.71
Rural	Male	3,062,701	2,559,477	83.57
	Female	3,617,545	3,401,254	94.02
	Total	6,680,246	5,960,731	89.23

Note: The related census question is “Does \_\_\_ usually do any of the following mainly for own consumption during the last 6 months?”.

Source: DPRK, Central Bureau of Statistics, DPRK 2008 Population Census National Report, 2009.

As seen in Table 1, the participation rate of the household economic activities was higher in women than in men and higher in rural areas than in urban areas. When calculated by provinces, the participation rate was lowest in

Pyongyang, which was 56%. The reason the rate was low is believed that Pyongyang is a special city where people from the privileged class dwell and there is less need to be involved in household economic activities. In contrast, for South Hamgyong province, the rate marked a whopping 93%, which is the highest in North Korea. The participation rates were relatively higher in the Northeastern regions as seen in Table 2. The North Eastern regions were most severely affected by famine in the mid-1990s and it is likely that they had started participating in household economic activities earlier than other provinces in an attempt to survive the famine.

## Relation between Marketization and the Speed of a Transition to a Market Economy

In an attempt to figure out the effect of market experiences on the pace of a transition to a market economy, this study compared the degrees of transitions in their early stages and in 1997, when the transitions had ended in most Eastern European countries and former Soviet countries. As seen in Figure 1, the relation between marketization and the economic transition appeared as wedge-shaped.

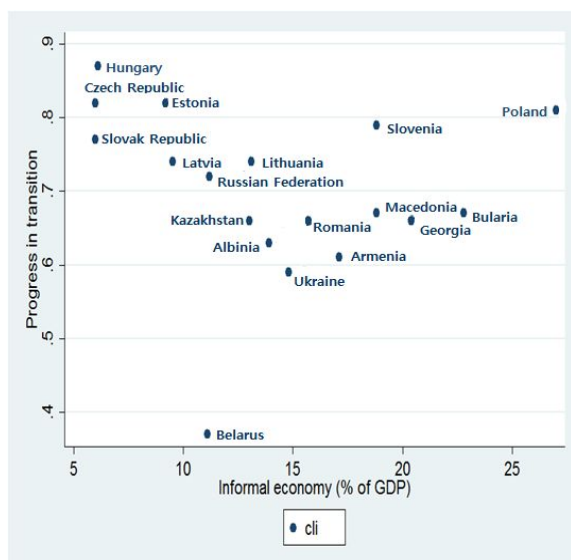
**Table 2. The Participation Rate of Household Economic Activities by Province**

	Total Population (A)			Population Participating in Household Economic Activities (B)			(B)/(A)		
	Total	Male	Female	Total	Male	Female	Total	Male	Female
Rygang	528,137	241,059	287,078	440,507	197,737	242,770	83.41	82.03	84.57
North Hamgyong	1,733,367	796,929	936,438	1,564,252	709,901	854,351	90.24	89.08	91.23
South Hamgyong	2,283,155	1,043,882	1,239,273	2,120,013	957,706	1,162,307	92.85	91.74	93.79
Kangwon	1,085,352	494,516	590,836	946,297	402,507	543,790	87.19	81.39	92.04
Jagang	969,291	447,819	521,472	824,014	356,948	467,066	85.01	79.71	89.57
North Phyongan	2,024,019	930,825	1,093,194	1,645,779	702,579	943,200	81.31	75.48	86.28
South Phyongan	3,039,228	1,411,434	1,627,794	2,685,280	1,157,719	1,527,561	88.35	82.02	93.84
North Hwanghae	1,561,562	721,450	840,112	1,390,505	611,298	779,207	89.05	84.73	92.75
South Hwanghae	1,688,310	772,359	915,951	1,495,192	637,410	857,782	88.56	82.53	93.65
Pyongyang	2,454,348	1,141,513	1,312,835	1,366,729	551,625	815,104	55.69	48.32	62.09
Total	17,366,769	8,001,786	9,364,983	14,478,568	6,285,430	8,193,138	83.37	78.55	87.49

Note: The related census question is "Does \_\_\_ usually do any of the following mainly for own consumption during the last 6 months?"

Source: DPRK, Central Bureau of Statistics, DPRK 2008 Population Census National Report, 2009.

**Figure 1. The Ratio of the Informal Economy in Socialist Countries and the Degree of Structural Reforms in 1997**



Source: The World Bank

In other words, socialist countries with small informal economies showed fast transitions and the speed of transitions decreases as the ratio of informal economy grows. However, when the ratio of the informal economy compared to its gross domestic production (GDP) rises over 15%, the informal economy and the speed of a transition show a positive correlation. This signifies that in the case where the informal economy is small, there tends to be an official institution, robust governance, and low corruption in place, thus leading to a rapid transition. In contrast, in the case of a large informal economy, households or businesses, which benefited from the informal economy, tend to be at the forefront of introducing a change geared towards capitalism. In addition, a large informal economy facilitates businesses at the early stage of transition. These effects, however, disappear with time. Therefore, it is important to come up with policies to promote transition in the early stages, if there is a large informal economy.

## Prospects for Change in North Korea's Transition and Its Constraints

The study goes on to divide 27 transition countries, including China and Vietnam, into three groups, including outstanding, fine, and poor reform groups through discriminant analysis based on the outcomes of economic reforms over the last two decades. According to the discriminant analysis, North Korea fell into the poor reform group. Most of the countries in the same group with North Korea belong to the Commonwealth of Independent States (CIS) that had strong planned economies and whose states showed a slow transition to market economies. These states share similarities in the sense that their former governments remained unchanged or they retained a government even after a new system was introduced.

North Korea is similar to those countries because it has a political structure unfavorable to reforms, hence, the North is likely to follow in the footsteps of the CIS states. Also, North Korea has a deficient initial condition in that the level of economic development, at the early stage of transition, is low. However, what is more significant is how the North sets up a favorable environment to reform with given initial conditions, as well as how actively and efficiently it promotes its reform.

Fortunately, North Korea is situated in the most dynamic geoeconomic location in the world, where neighboring countries, such as South Korea, China, and Russia, can play a positive role in supporting Pyongyang to step forward toward its transition to a market economy. This is a critical moment for Pyongyang, and Seoul, along with the international community, in moving forward to assist North Ko-

rea in a bid to bring about better and faster reforms.

## Conclusion

This study sought to estimate more accurately the scale of the informal economy in North Korea using the “2008 Census of Population of DPR Korea” and to predict the aspects of reforms in North Korea with its market scale and initial conditions, based on comparisons with countries that experienced economic transitions. North Korea has a large informal economy that can be beneficial to speed up the transition to a market economy. If the North itself is determined to transfer to a market economy, notwithstanding its poor initial economic and political conditions, it has the possibility to successfully and rapidly move to a market economy. **KIEP**