

# **China's Engagement-Oriented Strategy Towards North Korea: Achievements and Limitations**

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### **Abstract**

In response to the challenge of unstable North Korea (weak economy, weapons of mass destruction [WMD] development), China has followed an engagement-oriented strategy based on diplomatic persuasion, economic interaction and moderate economic sanctions. Intensified engagement (2009-12) facilitated North Korean convergence with China in respect of economic reform but divergence has persisted over WMD development. Despite the widening of divergence since 2013, China has refrained from applying crippling sanctions. This article seeks to explain these diverging results and their implications for China's strategy towards North Korea. Reviewing recent literature and data, it will argue that Chinese economic input reinforced the trend of economic reform that formed the basis of political consolidation under the new hereditary regime. On the other hand, the prospect of stable dependence on China ran counter to that regime's pursuit of WMDs as the basis of security and diplomatic diversification. These mixed results reveal the limits of China's strategy: its economic input involuntarily reinforces North Korea's WMD potential but it is not prepared to accept the risks of enforcing WMD restraint by crippling sanctions either. With limited room for manoeuvre, the attainment of China's strategic objectives ultimately depends upon policy change from the US or South Korea.

## **Key words**

Denuclearisation, 'parallel advance', marketisation, mono-transition, 'strategic  
patience'

Unstable North Korea (weak economy, a regime in pursuit of WMDs,<sup>1</sup>) has posed a serious challenge to the security of Northeast Asia since the end of the Cold War. Vulnerable to disturbances on the Korean Peninsula, neighbouring China<sup>2</sup> acts as North Korea's principal political and economic benefactor. How to stabilise North Korea (preventing economic collapse while restraining its WMD development) constitutes a vital issue for Chinese and regional security. It impacts directly on China's pursuit of 'peaceful rise' and 'responsible power status'. The official Chinese government perspective is that China's basic policy of keeping open the diplomatic and economic channels, interspersed with criticism and moderate sanctions in response to WMD violations, represents the best policy mix for transforming North Korea in a more benign direction.

In this article, I will illustrate and explain the double-edged effects of China's engagement-oriented strategy. I will show how intensified Chinese economic engagement (2009-12) has facilitated convergence with China's aim of economic reform. Economic progress, however, has not led to WMD restraint (especially since 2013). The discrepancy has arisen because Chinese economic input reinforces the domestic political consolidation of the new hereditary regime but that regime rejects stable dependence on China. Instead, it pursues the development of WMDs as the basis of security and diplomatic diversification. Contrary to China's expectations, it believes in the complementarity of economic development and WMD development ('line of parallel development'). China is left with a dilemma. Its economic input is involuntarily empowering North Korea's WMD programme by taking the sting out of international sanctions. Meanwhile the US responds by reinforcing its military presence in the region, to the detriment of China's strategic position. Despite these drawbacks, the uncertainties associated with crippling sanctions and US strategic

intentions are likely to keep China wedded to the tested but imperfect strategy of moderate sanction without totally abandoning North Korea.

### **Formation of China's strategic approach**

North Korea became a major focus of the Chinese policy community in 2009 when it withdrew from the Chinese-hosted Six-Party Talks (SPT) on denuclearisation (April 2009) and conducted its second nuclear test (May 2009). China has consistently restated its commitment to peaceful ends and means, namely 'denuclearisation', 'peace and stability' and 'dialogue and negotiation' through revival of the stalled SPT as the forum for comprehensive settlement. This line was articulated in September 2009, soon after North Korea's second nuclear test (MOFA 2009). Despite the advance of North Korea's WMDs programme (three more nuclear tests in 2013 and 2016 and scores of rocket tests), China has reaffirmed this position, most recently at the Munich Security Conference (February 2017). Gong (2009: 113-7) has characterised China's strategy towards the North Korean WMD issue as being guided by the principles of 'participation, balance and stability'. 'Participation' means patient resolution within a multilateral framework that includes China. 'Balance' means friendly Chinese relations with both Koreas and coordination with the US. 'Stability' means preservation of peace, including avoidance of military measures to enforce denuclearisation.

While supporting stronger UN sanctions in response to North Korean WMD violations since 2013,<sup>3</sup> China has kept open the economic and diplomatic channels in line with its commitment to denuclearisation by peaceful settlement. It has supported sanctions conditionally, stressing 'that the measures are not intended to produce

negative humanitarian consequences in the DPRK, nor affect normal economic and trade activities' (Xinhua 2 December 2016). Thus China's strategic approach to the challenge posed by North Korea's WMD development is engagement-oriented, namely it seeks resolution primarily through diplomacy and economic cooperation. The emphasis on achieving denuclearisation without endangering 'peace and stability' and through 'dialogue and negotiation' means China's remains committed to the preservation of a stable communist regime in North Korea. It means China will refrain from using the strongest sanctions capable of crippling the North Korean economy in a very short space of time (e.g. suspension of oil exports, tight closure of the border to prevent all trade).

This is illustrated by China's responses to nuclear violations by North Korea in 2009 and 2013. The year 2009 marked a watershed as North Korea announced its permanent withdrawal from the Chinese-hosted SPT (i.e. rejecting the principle of denuclearisation) and conducted a second nuclear test. While condemning North Korea's actions and supporting sanctions in principle, China intensified diplomatic and economic contacts in a bid to transform North Korean behaviour. In 2013, following the third nuclear test and North Korea's constitutional commitment to nuclear possession, China supported UN sanctions and froze the ambitious investments promised during 2009-12. This set the subsequent pattern of restrained but incremental tightening of sanctions applied to subsequent WMD violations. While the growth of trade levelled off after 2014, the absolute volume of trade in 2015 (USD 5,710 million) was still very high by recent historical standards. The frequency of high-level diplomatic contacts was reduced but did not cease altogether. China maintained its engagement-oriented strategy.

### ***Drivers of China's engagement-oriented approach***

China's engagement-oriented strategic approach is shaped by the failure of pressure tactics in the past. These experiences showed that strong coercive pressure or siding with the US only reinforced North Korea's inflexibility. During the early 1990s, China established diplomatic relations with South Korea and reduced economic support to North Korea in a bid to induce faster economic reform. While aggravating North Korea's economic troubles (that deteriorated into famine during 1995-8), China could not induce compliance. China was frozen out of the first nuclear settlement with the US in 1994 (Geneva Framework Agreement). Faced with North Korean collapse, China restored food aid without receiving warmer ties in return. High-level visits were suspended for seven years (1992-9).<sup>4</sup> When China cooperated with the US over alleged North Korean money laundering in 2005 (by freezing North Korean accounts in Macau), this helped to derail the nuclear deal reached at the SPT in September 2005, opening the way for the first nuclear test (October 2006). These experiences showed that if China wanted to secure North Korean cooperation, it could not be too tough or too biased in favour of the US.

The fact that China chose to resume aid when North Korea was at its most vulnerable and to restore friendly relations in 1999 showed that China preferred a stable communist regime to collapse and uncertain transition. This has remained a consistent Chinese concern. To Beijing, the immediate strategic costs of economic collapse (e.g. desperate survival measures, North Korean factional conflict, inter-Korean military conflict) outweigh the negatives of North Korean regime inflexibility (resistance to economic reform, pursuit of WMDs). Apart from strategic calculation, China continues to identify with North Korea to some degree as a fellow communist-party state. Despite China's turn towards market economy, it still shares with North

Korea an ideological aversion to liberal-democratisation (Nosselt, 2014: 489-91). As the pioneer of market reform with regime preservation ('mono-transition'), China seeks to transfer its own model to North Korea. To Beijing, Pyongyang does not represent a lost cause. Aspects of North Korea's behaviour since 1999 (under both Kim Chŏng-il and Kim Chŏng-Ŭn regimes) suggest potential for convergence with China's priorities. These include economic reform measures (2002-5, 2012-present), steady increase in two-way trade and Chinese investment (1999-2014), regular top-level contact (1999-2011), and participation in the SPT (2003-2009).

Apart from ideological alignment, China and North Korea continue to share strategic interests. Some scholars have identified the widening of the conventional military gap on the Korean Peninsula (in South Korea's favour) as a source of North Korean WMD development (e.g. Futter and Zala 2015: 375). This view is shared by the Chinese government, which acknowledges North Korea's acute sense of military vulnerability. Official Chinese media depict North Korean nuclear escalation as an understandable (but dangerously mistaken) response to perceived US military threats. For example, in the aftermath of North Korea's fourth nuclear test on 6 January 2016, an editorial in the official *Global Times* newspaper (14 February 2016) stated:

Now, as Washington's antagonistic approach has pushed North Korea further down the path of nuclearisation, the US, instead of making tangible moves to defuse the crisis, is using the escalating tension as a cover to ramp up its already massive military buildup in the Asia-Pacific region.

This statement also reveals how understanding of North Korea's strategic plight is linked to China's own strategic concerns about the US. Since the 2000s, some



Chinese policy voices (see below) have criticized the strategic orthodoxy that North Korea represents a 'buffer zone' between China and US forces in South Korea. The leadership, however, has continued to adhere to the buffer zone understanding and rejects those views advocating stronger sanctions against North Korea in coordination with the US (Kim, H. 2010). On the contrary, North Korea's strategic importance to Beijing was reinforced when the US announced the strategy of military build-up in the region or 'rebalance to Asia' in 2011 (Kelly 2014: 491-2). While North Korean WMD development was officially cited as one of the justifications for the 'rebalance', Beijing read this as a strategy of encirclement for which North Korea served as one convenient pretext (of many). Given the strengthening of trilateral US-South Korea-Japan cooperation, it was in China's strategic interest to preserve a non-hostile and viable North Korea (Park 2016).

### ***Dilemmas of the engagement-oriented approach***

China's engagement-oriented strategy assumes a North Korean regime capable of economic reform and external restraint given the right supportive environment. However, the protracted period of economic malaise and accelerating momentum of WMD development lends support to the alternative perspective that North Korea is incapable of following in the footsteps of China. Influential studies of North Korean political economy under the Kim Chŏng-il regime (1994-2011) concluded that the political system was too vulnerable to accommodate serious economic reform (e.g. Lankov 2013). Hence official economic reform was short-lived (2002-5) (Haggard and Noland 2007) and subject to reversal (2005-10) (Haggard and Noland 2010: 548-50). To compensate for its economic failings, the regime has to resort to international extortion by fomenting regional instability (Pollack 2011). The periodic

compromises with the market (e.g. acquiescence in informal markets,) and with the international community (e.g. proposals for dialogue) are insincere gestures aimed at alleviating some immediate pressure (e.g. to avert the recurrence of famine or buy time for WMD development) that do not mark genuine transformation of behaviour. The pattern established under the Kim Chŏng-il regime has continued under the regime of Kim Chŏng-Ŭn (Cha 2016: 249-53).

This perspective suggests a strategic response towards North Korea that places coercive measures over engagement. It works on the premise that the rigid North Korean regime would only compromise when its survival is threatened by economic collapse or military action. Given three abortive WMD agreements (2005, 2008 and 2012) under two different administrations, this perspective has gained influence in the US. Its strongest proponents advocate the intensification of pressure on all fronts (deterrence, financial sanctions, human rights, lobbying of China) (e.g. Terry 2015). Its influence was also reflected in the hardening attitude of the recent Obama administration in the US (2009-17) especially after the failed Leap Day Agreement of 2012.<sup>5</sup> Under the doctrine of 'strategic patience', the US took the position that North Korea needed to return to the 2005 and 2008 agreements as a precondition for further engagement, while violations would met by tougher sanctions (both UN and unilateral) and military counter-measures (e.g. transfer of advanced weapons to South Korea).

This perspective suggests China is caught between 'the seemingly contradictory goals of preventing North Korean collapse while also preventing it from becoming too strong' (Choo 2012: 108). Chinese economic input is enabling the North Korean regime to pursue WMD development without financial trade-off. Some Chinese policy thinkers support this view and consider North Korea a serious strategic liability. Its

land 'buffer' offers little protection against modern warfare while any ideological affinity has long evaporated (North Korea's explicitly rejects Chinese-style reformism). This makes eventual collapse and absorption by the South all but inevitable. Supporting North Korea is damaging relations with South Korea, China's second largest trading partner, and driving it towards closer military ties with Japan. Above all, China's continued global rise depends on maintaining a cooperative relationship with the US (ICG 2009: 5-7; Kim, H. 2010: 61-2). Concern for North Korea's stability means that China has been 'kidnapped by that much weaker neighbour depending on China's assistance' (Shi 2011: 360). These Chinese policy thinkers accord with the dominant US perspective that North Korea must first denuclearise if it wants peace (ICG 2009: 8). Some US policy thinkers expect China to realise the benefits of a unified Korea under Seoul and discard North Korea as a hopeless liability (Terry 2014; Cha 2016: 259-63).

### ***Structure of this Discussion***

Table 1 summarises North Korean convergence and divergence from Chinese aims in the aspects of economic reform and WMD development since 1990. North Korean behaviour in the current (i.e. post-2009) period and its explanatory factors are shaded. It is set against the main features of China's preferred outcome of economic reform with WMD restraint. The post-2009 period provides the empirical focus of the paper because it covers the most active period of Chinese engagement (2009-13) and the period of nuclear escalation by North Korea (2013-present) when China returned to moderate sanction while keeping the economic and diplomatic channels open. Reviewing recent literature and data (especially from recent Chinese and South Korean sources), I will explain the double-edged results of China's

engagement-oriented strategy. First, I will show how Chinese trade and investment have facilitated North Korean economic recovery and marketisation since 2009. By reinforcing marketisation trends, China has realised its minimal strategic objective of stabilising North Korea on the basis of trade and investment (rather than aid).

Table 1 about here

Divergence on the WMD issue has persisted because Chinese economic input cannot satisfy the North Korean regime's conditions for domestic *and* external security: preservation of the monolithic system of governance and WMD-based deterrence that can lever diplomatic and other advantages. This raises an uncomfortable dilemma for China, namely, that its economic input is unintentionally facilitating North Korea's WMD development. China's leaders do not believe that crippling sanctions would accomplish WMD restraint or serve China's strategic interest. Thus they are likely to persist with a strategy of moderate sanction without abandoning North Korea. China's repeated calls for US-North Korea and inter-Korean dialogue reveal of the limits of its own direct influence over North Korea and the difficulties of aligning parties (China, US, South Korea) holding very different visions for North Korea.

### **Convergence in economic reform**

China intensified its efforts to transform North Korea's economic and political environment following the second nuclear test of May 2009. Premier Wen Jiabao's visit to North Korea in October 2009 signalled the start of this effort. General Secretary Kim Chŏng-il reciprocated by visiting China four times in the last stage of

his life (2010-11). At the Hu Jintao-Kim Chŏng-Il summit of August 2010, China emphasised its commitment to cooperation under the principles of '*government guidance* [my italics], with enterprises playing a major role, market operation and mutual benefits for win-win results' (MOFA 2010). Trade and Chinese investment flourished. The two sides concluded ambitious agreements for joint development of two special economic zones on their border in November 2010. North Korea's economic dependence on China increased markedly from this point.

North Korea's resumption of rocket testing in April 2012 did not undermine economic contacts built up during the previous three years. Chang Sŏng-T'aek (reputed to be Kim Chŏng-Ŭn's number two) led a large delegation to China in August 2012 and put the finishing touches on the agreements for the special economic zones (MOFCOM 2012). The visit reaffirmed the principles of the Hu-Kim summit of August 2010. Following the February 2013 nuclear test, now under Xi Jinping's new leadership team, China took a stronger line by supporting further UN sanctions (e.g. restricting financial transactions and illegal North Korean workers). China also suspended support for the special economic zones. These were halted indefinitely after the purge and execution of Chang Sŏng-T'aek in December 2013. Nevertheless, Chinese private and local government entities continued to trade and invest, indicating the presence of solid commercial foundations. The rumours of oil embargo in 2014 were not substantiated by observed price trends. The momentum of trade growth was checked but there was no reduction in the value of trade.

### ***Key indicators of China's impact***

Economic relations with China have driven rapid trade growth. Figure 1 reveals the extent of North Korean economic dependence on China between 2000 and 2014. The impact of closer cooperation during the final years of Kim Chŏng-il (2009-11) is evident from the leap in trade and export dependence on China (to well over 60 per cent). In spite of the subsequent cooling of relations, this level of dependency has been maintained.

Figure 1 about here

Within the dependent relationship, North Korea's capacity to pay its way has also improved owing to the growth of exports to China (see trade data in Figure 2). As a result, North Korea's trade deficit as a ratio of total trade sharply declined during 2009-11 (and remained at below 20 per cent thereafter). Another indicator of dependence (Figure 1) is the growth of China's share of total FDI stock from 1.6 (2004) to 18.2 (2009) to 31.2 per cent (2013). The value of China's stock increased from USD 22 million (2004) to USD 262 million (2009) to USD 586 million (2013) (MOFCOM). As well as growth, Chinese FDI has facilitated diversification of North Korea's narrow export range. While raw materials remained the dominant export, manufacturing export based on textiles has been on the rise in recent years. Among the top five exports, the share of manufacturing increased from 26.7 per cent (2009) to 36.9 per cent (2014) (NSO). Chinese FDI is facilitating the emergence of export processing (for re-export to China) based on light manufactures. Typically, Chinese investors provide machinery to reactivate decrepit mines and factories using local labour. North Korea is remunerated for the cost of labour (manufacture) or labour and raw materials extracted (in mining).

Figure 2 about here

The growth of trade driven by exchange with China has also contributed to GDP growth and improved living standards. South Korea's central bank, the Bank of Korea (BoK), paints a picture of sluggish North Korean GDP growth: 1.8 per cent (1999-2004); 0.74 per cent (2004-9); and 0.73 per cent (2009-14) (NSO). This low estimate neglects the informal economy, the principal provider of popular livelihood since the famine of 1995-8 ('arduous march'). Inclusion of informal activities would probably add one to two percentage points to the annual growth rate (Yang 2015a). The rapid growth of trade since the turn of the decade would also suggest a much higher rate of GDP growth. Total trade (including inter-Korean trade) grew from USD 3,554 million (2004) to USD 5,093 million (2009) to USD 9.953 (2014) (NSO). This trend would suggest recovery of GDP to the pre-crisis levels (when foreign trade previously peaked at USD 4.17 billion in 1990) (Feron 2014). Changing consumption patterns also suggest higher growth rates. For example, the number of mobile phone subscribers increased from 69,000 (2009) to 1.7 million (2012) to 3.24 million (2015) or 12.9 per cent of the population (NSO).

### ***'Marketisation from below': rise of the informal capitalists***

Ever since the famine of 1995-8, China has been North Korea's lifeline as the principal provider of consumer goods, production inputs (especially oil) and as the recipient of imports. As a result of the crisis, informal production and trade became the principal source of livelihood of the majority of North Korean citizens. Such 'marketisation from below' fostered the rise of wealthy individuals or financiers known as *tonju* (literally meaning 'masters of money'). Connection with China was instrumental to the rise of this type of informal capitalist during the 2000s. The most

successful informal capitalists were those most closely involved in the importation and distribution of consumer goods. At the top of the commercial chain were the 'big hands'. These were mainly overseas Chinese (resident in North Korea) who could profit from their right of travel to China (Joo 2010: 124-7). Nevertheless, the regime's attitude towards informal markets during the 2000s was one of reluctant tolerance. Pro-market policies (2002-5) gave way to anti-market policies (2005-10), including a failed attempt to destroy the informal capitalists by currency redenomination in 2009.

Skeptical analyses viewed the trade with China not as the advance of marketisation (i.e. market coordination and non-state ownership) but as the regime's attempt to achieve a highly controlled opening beneficial only to state agencies (Haggard and Noland, 2010: 11). The regime's restrictiveness meant that economic contact with China would not be able to sow the seeds of grassroots capitalism. A 2007 survey of 250 Chinese firms operating in North Korea found that the North Korean state (via state-owned enterprises and state licensed-agents) monopolised the most profitable activities associated with Chinese trade and investment (Haggard and Nolan 2012). Apart from the North Korean state, the other principal beneficiaries were audacious, short-term profit-oriented Chinese entrepreneurs adept at navigating the milieu of high risk and bad governance (often by using bribery). The conclusion was that Chinese economic input was reinforcing state-controlled foreign exchange earning instead of nurturing non-state forms of entrepreneurship.

Other studies paint a more positive picture. A more recent study (Jung and Rich 2016) of the 2000s (2003-10) showed how the prospect of profit could offset the disincentive of poor institutions (legal processes, ease of communication) for Chinese investors. This was reflected in the continuous growth and diversification of Chinese FDI. The FDI data presented above shows that the FDI growth trend was



sustained into the 2010s (2013 being the most recently published data). Even with reduced Chinese government backing after 2013, the volume of trade remained stable, suggesting that private Chinese traders maintained their business confidence (Cui, 2015: 198). Reilly (2014: 903-5) observed improved business acumen among North Korean officials and their modification of local administrative processes to ease cooperation with China. Doing business with Chinese local governments and private agents forced North Koreans to behave in a business-like manner and live up to their obligations (Reilly 2014: 901-3). These accounts suggest that Chinese economic engagement is achieving its objective of shifting the economic interaction from aid towards for-profit activities that require the North Koreans to pay their own way i.e. become more enterprising.

Has Chinese economic input helped to diffuse economic opportunity beyond the monopolistic agencies of the North Korean state? Increased economic exchange with China during the 2010s reinforced the interdependence between state monopolies and informal capitalists. Starting from the 1990s, when the core regime agencies (military, party, security agencies, cabinet) were charged with earning foreign exchange (for themselves and for the top leadership), they began to cooperate with non-state agents. This cooperation became more sophisticated during the 2000s. Apart from manpower (which even the vast military needed), the core agencies relied on informal sector funding, entrepreneurship, and marketing. Those state-licensed trading companies that owned no assets of their own relied on private traders to supply them with products for export ('source mobilisation') and for distributing imports on the domestic market (Kim and Yang 2015: 43-5). On the basis of these needs, the China-oriented trade of the state monopolies also brought benefit non-state agents upon which they relied. Y-S Dong (2013: 67-8) estimated the

broader 'merchant class' (i.e. 'those who traded as an occupation') to number between 500,000 and one million individuals.

The growth of China-oriented trade has aligned with recent top-down reforms to expanded opportunities for informal capitalists. The enterprise autonomy (i.e. profit promoting) measures (2012 and 2014) have enabled private financiers to take a bigger stake in the state enterprises. In this way, *tonju* have acquired *de facto* control of lucrative state export assets such as mines despite the official appearance of socialist ownership. This role can take the form of individuals managing a business using a state-run enterprise name ('wearing the red hat') or individual investment in state-run companies while receiving interest in return (Lim 2015: 35), phenomena common in 1980s China (Park 2015). Far from suppressing the informal capitalists, the current regime appears to be actively encouraging their participation. Another example of the expanded role of informal capitalists is their provision of funds (and sub-contract labour) for much of the apartment construction boom now taking place in Pyŏngyang (Hong 2014: 38), one of the key people's livelihood measures associated with Kim Chŏng-Ŭn.

The expanded opportunities offered by Chinese economic input is facilitating the collaboration between the state agents and the informal capitalists. In particular, a symbiotic relationship (i.e. long-term mutual interdependence) is emerging between the *tonju* and the managers of official foreign exchange assets and party funds, the other group that has prospered from commerce. To accumulate wealth, the *tonju* need access to official economic assets and protection (B-R Kim 2015). In order to preserve their wealth, the managers of state assets must also succeed commercially and make sufficient profit for the powerful core agencies (military and the party-state) to which they are responsible. The central authorities have shifted from tolerance

(2000s) to active encouragement (2010s) because this form of marketisation does not endanger the North Korean state. The rising informal capitalists seek not political change but political cover for their pursuit of wealth (Smith 2015: 289-90). Official acquiescence towards informal capitalists (tactical compromise) is turning into official acceptance (symbiosis). The regime is beginning to move beyond the reform-versus-stability dichotomy.

### ***'Marketisation from above'***

Lacking his grandfather's prestige or his father's direct inheritance, Kim Chŏng-Ŭn looked to economic improvement to legitimise his succession (Park and Frank 2012). 'Reform' or 'marketisation from above' means the introduction of government initiatives (changes of rules, provision of financial resources) that actively support marketisation (i.e. market coordination and non-state forms of ownership). In his first public speech (15 April 2012) celebrating the centenary of national founder Kim Il-Sŏng, he pledged that belt-tightening would never again be repeated. A document called 'New Economic Management System in Our Own Style' was introduced on 28 June 2012, outlining measures (June 28 or 6-28 measures) for giving greater autonomy to the agricultural and light industrial sectors. In the follow-up measures of 30 May (5-30) 2014, Kim Chŏng-Ŭn referred to the 'socialist corporate responsibility system' (Yang 2015d: 53). Economic cooperation with China has reinforced this motivation for reform. To finance imports from China, North Korea has had to upgrade its productivity. Given low profit margins on raw materials, North Korea also needed to diversify. The extent of reform can be illustrated by the content and results of policies towards agriculture and light industry, sectors where reforms began in

other surviving communist states. Reforms in these areas also show evidence of learning from previous Chinese reforms.

### ***'Marketisation from above' (1): agriculture***

Inspired by the 6-28 document, agricultural reforms replaced collective responsibility with individual household responsibility. The size of the 'sub-work team' was reduced from 10-25 to 4-5 members with responsibility for a small plot of land. They also reduced the urban bias of socialist agriculture by ending the practice of excessive extraction at unfavourable prices. Instead, the urban-rural distribution of farm product would follow a new formula of 7 (state/urban) to 3 (farmer/rural), reflecting the urban-rural population ratio. This contrasted with past practice when the state would collect a fixed quantity (rather than a ratio), often based on unrealistic expectations of productivity. Calculated from a more realistic baseline, the new formula would enable farmers to retain a greater portion of their product for sale on private markets. As in China, the principle of state ownership (and the corresponding responsibility to provide sufficient food to the state) was retained. Compared to Chinese de-collectivisation 30 years earlier, reform proceeded more cautiously (piloted in three selected counties in the far northern province of Ryanggang) (Y-H Kim, 2015).

Ideological commitment in the 2010s was stronger than in the 2000s (when pilots were terminated in October 2005). There has been no policy reverse. Indeed, Kim Chŏng-Ŭn reportedly said that 'egalitarianism in the realm of distribution has no connection to socialist principles and has a detrimental impact that reduces farmers' productivity' (Vantage Point 2014: 27). The official media enthusiastically praised the performance of individual pilot farms. For example, the official *Chosŏn Sinbo* (a

Japan-based, Pyöngyang-affiliated newspaper) (27 January 2014) claimed that reform led to increase in field utilisation by up to 200 per cent at the Samjikang cooperative farm (in the fertile South Hwanghae province) (Yang 2015c: 107-8). It reported the introduction of the new system throughout the country during 2013 (Yang 2015b: 40). It was then reported that the 6 (state) to 4 (farmer) distribution ratio was introduced under the May 30 Measures of 2014, enabling farmers to keep more of their product (Y-H Kim 2015: 12-13).

The last comprehensive survey by the Food and Agriculture Organization-World Food Programme in 2013 reported three consecutive years of strong growth in domestic grain production with the country returning to its highest level of food self-sufficiency since the early 1990s (FAO-WFP 2013). While the report identified the persistence of widespread malnutrition (affecting 84 per cent of all households), the country was no longer in the grip of starvation either, a condition resembling many other developing countries (Smith 2016). The food balance (million tons) by marketing year (i.e. from November to October) showed a four-year upward trend: 5.04 (2010-11); 5.27 (2011-12); 5.73 (2012-13); 5.93 (2013-14); and 5.94 (2014-15) (FAO-WFP 2013; FAO 2015 and 2016).

The 6-28 and 5-30 reforms reinforced a trend of recovery that was already under way. North Korean farmers also made effective use of coping measures. For example, grain production increased in 2013 despite reduced usage of chemical fertiliser (owing to tighter South Korean sanctions) compared to the previous two years. This suggests that farmers were successfully improvising (e.g. by using human manure) (Lim 2014: 48) and developing resilience to sanctions. Although grain production went into decline in 2015-6 (to 5.42 million tons) following severe drought in various parts of the country during 2015 (FAO 2015 and 2016), the price of rice was reported

to be stable as of December 2015 (continuing a trend starting from January 2013) (Yang 2015a). What this suggests is that incentives and coping measures could alleviate but not fully offset the effects of adverse weather conditions and shortages of inputs. More time is needed for a definitive assessment.

### ***'Marketisation from above' (2): light industry***

Light industry was bedevilled by disincentives such as compulsory sale to the state at below-market prices, irregular supply of inputs, and the exit of workers to informal work. To alleviate these bottlenecks, the 6-28 measures introduced the 'self-supporting accounting system' that permitted enterprises to keep more of their gains (and take responsibility for loss). After meeting state targets, enterprises would be permitted to distribute remaining products at market prices to purchasers of their choice, both domestically and abroad (Yang 2015b: 41). They would be permitted to dispose of the sales revenue in the manner they wished (e.g. to supplement wages, make future investment). On the production side, enterprises could take more of their own decisions. Inputs could be sourced from the market as well as the state sector (thereby forcing state suppliers to compete). If enterprises used inputs sourced from the market, then that market dimension would also be reflected in the prices paid by the state ('agreed price'), in order to align state and market prices more closely (Yang 2015c: 111). As in agriculture, implementation began with a small number of pilots (five enterprises in Pyŏngyang).

Here too, the ideological momentum was stronger than previously when pilot enterprise lasted just one year (2003-4). This time around, the authorities have remained very positive. The official media recognised the success of incentives in

boosting wages. For example, with reference to the pilot 326 Electric Wire Plant, the *Chōson Sinbo* (24 April 2013) claimed that the new system was 'leading to an improvement in production performance through enhancing the motivation of the workers' while wages ostensibly increased 20-30 times between August 2012 and April 2013 (Yang 2015c: 111). Such generous praise reflected the authorities' increasing acceptance of profit motivation and the inevitability of income disparities. In a break from the past, the authorities (including Kim Chōng-Ŭn himself) frankly acknowledged the deficiencies in the supply of inputs. They stressed the need to restore production in the key plants supplying inputs to light industry (Lee 2014: 47-8). This reflected a shift away from the old heavy industry bias. The new tone also contrasted with the old propaganda-driven style of praising a particular sector's achievements before lavishing it with resources to ensure increased output (but not necessarily productivity).

As with agricultural reform, the positive picture needs to be qualified. The 'self-supporting' principle applied only to a number of pilot enterprises. Even if fully developed, the proportion of 'self-supporting' enterprises would only account for about 10 per cent of all state enterprises comprising 20 per cent of employees (excluding the sizeable munitions sector) (Cho 2013: 52-3). The highly publicised restoration of key plants supplying inputs notwithstanding, the central government lacked the material resources to restore production to normal levels on a broad scale (a necessary condition for enterprises to take full advantage of market incentives). Thus there has been no reported upsurge in the manufacturing utilisation ratios. Despite these reservations, I have shown that there is an alternative interpretation of the transformation of the economy (from below and above) that seems more consistent with the trade trends. By permitting the continuation of trade and investment, China has provided a benign environment (the prospect of profit by

entrepreneurship without great political risk to the regime) for this transformation to take place.

### **Divergence over WMD development**

While converging with Chinese objectives in the aspect of economic reform, North Korea has not shown WMD restraint. There was a lull in WMD testing in the final years of the Kim Chŏng-il regime (2010-11). From its very inception in spring 2012, the Kim Chŏng-Ŭn regime strongly affirmed its WMD commitment by launching two rockets within a year. After the third nuclear test (February 2013), North Korea broke new ground by constitutionally declaring itself as a nuclear weapons state (Nuclear Law of 1 April 2013). The official stance switched from denuclearisation to arms control ('denuclearisation of the world'). The new doctrine ('line of parallel advance') envisaged the *simultaneous* development of the economy *and* WMDs. Rejecting the Iranian-style nuclear moratorium of 2015, North Korea accelerated its WMD development in 2016 by staging two nuclear tests and over 20 rocket launches.

### ***Explaining divergence: between US threat and Chinese restraint***

Chinese economic input and support for the hereditary succession could not assuage the North Korean regime's deep-rooted anxieties about its external security and national autonomy. At the most fundamental level, China could not compensate for the sense of external vulnerability vis-à-vis the vastly superior US-South Korean military alliance. Economic revival could not substitute for the 'treasured sword' of nuclear deterrence. Possession of a proven WMD capability was associated with



diplomatic leverage. It would put North Korea in a stronger position to negotiate normalisation with the US, and perhaps end economic isolation without fully relinquishing WMD capability i.e. it would come to enjoy the benefits of a *de facto* nuclear weapons state (like India or Pakistan) (Cho 2014: 165). However, if the US chose not to engage, then North Korea would continue with its WMD development, and aggravate the nuclear sensitivities of close US allies South Korea and Japan. Like the *pungsan*, a Korean hunting dog that firmly grips its prey's weak point, North Korea would latch firmly onto this perceived US weakness (Chon 2014: 49).

To maximise Chinese support for the impending succession, the ailing Kim Chŏng-Il had exercised WMD restraint (2010-11) and even negotiated the Leap Day Agreement (2012) with the US. Focused on consolidating a new regime, however, Kim Chŏng-Ŭn resumed WMD testing without being constrained by existing ties with China. The priority of regime consolidation over friendship with China was also demonstrated by the purge and execution of Chang Sŏng-T'aek. Having a good rapport with China could not save Chang's life once his behaviour (especially his lieutenants' defiance of Kim Chŏng-Ŭn's direct order) was deemed incompatible with the Monolithic Leadership System. In resuming WMD development, Kim Chŏng-Ŭn's behaviour was consistent with those of his predecessors at the formative stages of their regimes, namely, reinforcement of the instruments of survival taking precedence over maintaining warm ties with China. For example, Kim Chŏng-Il ignored Chinese pressure for economic reform and instead introduced 'military first politics' in the 1990s while Kim Il-Sŏng's purged the pro-China and pro-Soviet factions and launched the monolithic regime in the early-1960s.

Willingness to strain relations with China reveals a deeper historic trait, namely, rejection of stable dependence on one big power ally. North Korean regimes have

always pursued diversification in order to enjoy cordial relations with competing big powers while pivoting between them. During the Sino-Soviet dispute, Kim Il-Sŏng used North Korea's geostrategic position to obtain aid from both the USSR and China. With those resources, he could strengthen his domestic political autonomy from the big powers themselves. His successors have also pursued diversification in less favourable post-Cold War conditions (in which all big powers practise some form of capitalism). By developing WMD capability, and achieving acceptance as a *de facto* nuclear weapons state, North Korea would be able to end its international isolation and pivot between the US camp and China. Even if this were unachievable, aggravated tensions would strengthen US, South Korean and Japanese trilateral ties. The ensuing Chinese and Russian counter-measures could help re-create the quasi-Cold War triangle (Moscow-Beijing-Pyŏngyang) favoured by North Korea (Cho 2014: 171)

North Korea's resentment of dependence on China is deep-rooted. For example, it has consistently rejected Chinese proposals for reconciliation on the Korean Peninsula since the 1970s (Chung and Choi 2013: 253-6). Pyŏngyang viewed Beijing's diplomatic normalisation with Seoul in 1992 as an act of betrayal. When relations finally improved in 1999, North Korea could have chosen stable dependence on China but instead sought to counter-balance against China through economic cooperation with South Korea's liberal administrations (1998-2008). In his final years, Kim Chŏng-il was forced into heavy economic and political reliance on China. His reported political testament, however, warned about the danger of exploitation by China (Petrov 2012). This legacy was apparent from the very beginning of the Kim Chŏng-Ŭn regime. The first overseas visit by the nominal head of state (Kim Yŏng-Nam) in May 2012 was to Indonesia and Singapore rather than China. To re-engage with Japan, North Korea established a Special Investigation

Committee into the abductee issue in 2014 and held several rounds of official talks, including a foreign minister-level meeting in August 2015. In a sign of closer ties with Russia, Kim Chŏng-Ŭn came close to attending Russia's Second World War victory ceremony in May 2015.

### ***Implications of divergence***

North Korea's lack of WMD restraint reveals a paradox at the heart of China's engagement-oriented strategy. By providing economic input, China has supported the Kim Chŏng-Ŭn regime's need to boost living standards but has not been reciprocated with WMD restraint. Far from serving as Chinese 'strategic leverage' against the US (e.g. Lee 2010: 171-2), North Korea's WMD development has undermined China's strategic interests. Most notably, it has justified the US-South Korea decision in 2016 to deploy THAAD, a powerful anti-ballistic missile system. China has branded this deployment as an opportunistic US move threatening its strategic security (e.g. MOFA 15 February 2016). It has also severely strained the once promising China-South Korea relationship.

Chinese economic input has apparently enabled the North Korean regime to pursue WMD development without incurring any serious financial trade-off. South Korean estimates (which tend to *under-estimate*) of North Korean government budget suggest continuous recovery (2009-14) despite international sanctions. The estimates are (billion USD): 3.7 (2009); 5.2 (2010); 5.8 (2011); 6.2 (2012); 6.8 (2013); 7.1 (2014); and 6.9 (2015) (NSO, various issues). Analyses of North Korea's own budget data show that revenue growth to have constantly exceeded expenditure growth during the Kim Chŏng-Ŭn era (Frank 2016). China-North Korea trade stood at

USD 5,710 million (2015), diminishing but still higher than the peak of USD 5,629 million (2011) under the Kim Chŏng-Il regime. .

Contrary to Chinese expectations, Kim Chŏng-Ŭn regime's explicit commitment to economic development has not diminished but reinforced the quest for WMDs. The regime claims that WMD development would ultimately *benefit* economic development. Its slogan of *pyŏngjin nosŏn* ('line of parallel advance') nostalgically harked back to a slogan used by national founder Kim Il-Sŏng half a century earlier. The substance of the new doctrine, however, was meant to be very different. Whereas Kim Il-Sŏng's 'parallel advance' and Kim Chŏng-Il's 'military-first politics' sacrificed popular livelihood for national defence, the new 'parallel advance' (i.e. WMD-based defence *and* economic development) signalled a rebalancing of resources in favour of economic development. By creating a viable nuclear deterrence, the cost of conventional military expenditure could then be reduced (Kim, D-Y 2016: 59-63). *Rodong Sinmun*, the official Korean Workers' Party (KWP) newspaper, stated:

The true excellence of the new dual-line policy lies in that it definitively enhances our deterrence and defence capabilities without additional spending on national defence, thus allowing us to focus our strength in economic build up and improvement of our people's livelihood (Kim, D-Y 2015: 76)

North Korea appears to have seized on China's weakness. China seeks to prevent the worst-case scenario of a violent North Korean collapse (Dong, X. 2013: 247). Knowing China's concern with stability, the North Korean regime is emboldened to press on with the WMD programme confident that China will not inflict crippling sanctions (Shen, 2016: 865). By periodically hinting at its willingness to return to

multilateral dialogue, Pyöngyang can buy further time for WMD development. The post-2009 Chinese approach of promoting commercial transaction over aid has also strengthened North Korean competitiveness. In particular, since relations cooled in 2013, North Korea has had to pay for its imports at market prices. Although the volume of two-way trade is minuscule in relation to China's total trade, harsh sanctions would damage the two northeast provinces (Jilin and Liaoning) adjacent North Korea that the Chinese government seeks to promote.<sup>6</sup>

Beijing is no doubt aware of Pyöngyang's game but will probably persist with its restrained approach. It believes in the utility of gradually tightening sanctions without abandoning North Korea altogether. Recently, China announced a 10-month suspension (February-December 2017) of coal imports (40 per cent of total North Korean exports to China). This approach of pressuring North Korea without crippling it was praised in the official *Global Times* (21 February 2017):

While pressing North Korea to give up nuclear weapons, the Chinese government has managed to maintain the survival of North Korea and never stopped diplomatic mediation.

China maintains that North Korea's obstinacy over WMDs arises from a genuine sense of insecurity that must be addressed by direct dialogue between the main protagonists (US-North Korea, two Koreas). Another recent *Global Times* piece (22 February 2017) stated:

[The US and South Korea] should give Pyöngyang a choice rather than making it believe that no matter what it does, the two will overthrow its regime

anyway. Engaging with Pyöngyang isn't more difficult than Pyöngyang giving up its nuclear ambitions.

While encouraging direct dialogue, China also seeks to avoid marginalisation in the event of improved US-North Korea relations (as occurred in 2007-8) (Shi 2009: 40-42). It seeks to maintain influence by restarting the SPT in Beijing. If pressured excessively by China, North Korea would not return to those talks. Reminding that 'it takes two to tango', China emphasises shared responsibility of all parties and not just North Korea alone (MOFA, 7 January 2016).

## **Conclusion**

This analysis highlights three important features regarding China's engagement-oriented strategy in response to the challenge of unstable North Korea (weak economy, regime in pursuit of WMDs). First, China has achieved its minimal economic objectives of replacing aid with for-profit transactions and helping North Korea along the path of market reform. The Kim Chöng-Ŭn regime has revealed itself to be open to marketisation while holding tightly to monolithic politics. Chinese economic input has reinforced marketisation trends. Second, improving economy, however, has provided a favourable background to the North Korean regime's pursuit of WMDs. Its commitment to achieving *de facto* nuclear status (as deterrence and diplomatic lever) appears to be resolute regardless of Chinese economic incentive or pressure. Third, given China's concerns about North Korean regime collapse and US encirclement, it will not align with US-South Korean calls for crippling sanctions. Instead, it is seeking to win other parties over to collective engagement (i.e. sanctions that allow for 'national development' and openness to dialogue without

preconditions). In so doing, China, acknowledges that it cannot resolve the North Korean WMD issue by itself. To realise its strategic objective of economically viable and peaceful North Korea, China needs US or South Korean initiative.

Since the US can end North Korea's international isolation and sense of insecurity, North Korean restraint might well follow from any US initiative. From early on, the recent Obama administration (2009-17) took a dim view of North Korea's sincerity (Ford 2011). Apart from the brief period leading up to the Leap Day Agreement of 2012, the US has been reluctant to re-engage. It has ignored North Korea's gestures of compromise. For example, in January 2015, North Korea offered to suspend nuclear testing in exchange for suspension of the annual joint US-South Korea military exercises. In 2016, it referred to 'denuclearisation of the Korean Peninsula', indicating a shift from its typical reference to 'denuclearisation of the world' (Hangyoreh 9 July 2016). For successful re-engagement, the US would need to drop its insistence on denuclearisation as a *precondition* for formal talks and accept denuclearisation as the outcome of a process that also addresses North Korean concerns (e.g. US-South Korean military exercises) (Choi and Bae 2016: 821). The US would have to accept the legitimacy of the North Korean regime instead of excoriating it over human rights. From the Chinese perspective, the US is unwilling to engage because the North Korean WMD issue serves the higher strategic purpose of containing China (Kim, H-J 2015).

What about South Korean initiative? Under two conservative administrations in Seoul (2008-13 and 2013-present), inter-Korean relations have deteriorated to their lowest point since the mid-1990s. Following the logic of absorption, conservative South Korean administrations did not take inter-Korean cooperation very seriously. This was reflected in the unrealistic denuclearisation-for-aid proposal (2008)<sup>7</sup> and the

suggestion of five-party talks minus North Korea (January 2016). Ironically, this deterioration coincided with the presence of a liberal administration in Washington. By contrast, the hawkish George W. Bush administration (2001-9), managed to agree (in principle) to comprehensive denuclearisation agreements on two occasions (2005 and 2008) because of encouragement from liberal South Korean administrations (1998-2008). Thus some argue that South Korea must take the engagement initiative instead of waiting for a US that is constantly distracted by crises elsewhere (e.g. Moon 2015). With a return to liberal politics in Seoul, South Korea might again be able influence the US towards re-engagement. Paradoxically, having all but eclipsed South Korea in terms of economic influence over the last decade, China's best hope of realising its other strategic objective of peaceful North Korea lies in the resumption of inter-Korean cooperation.

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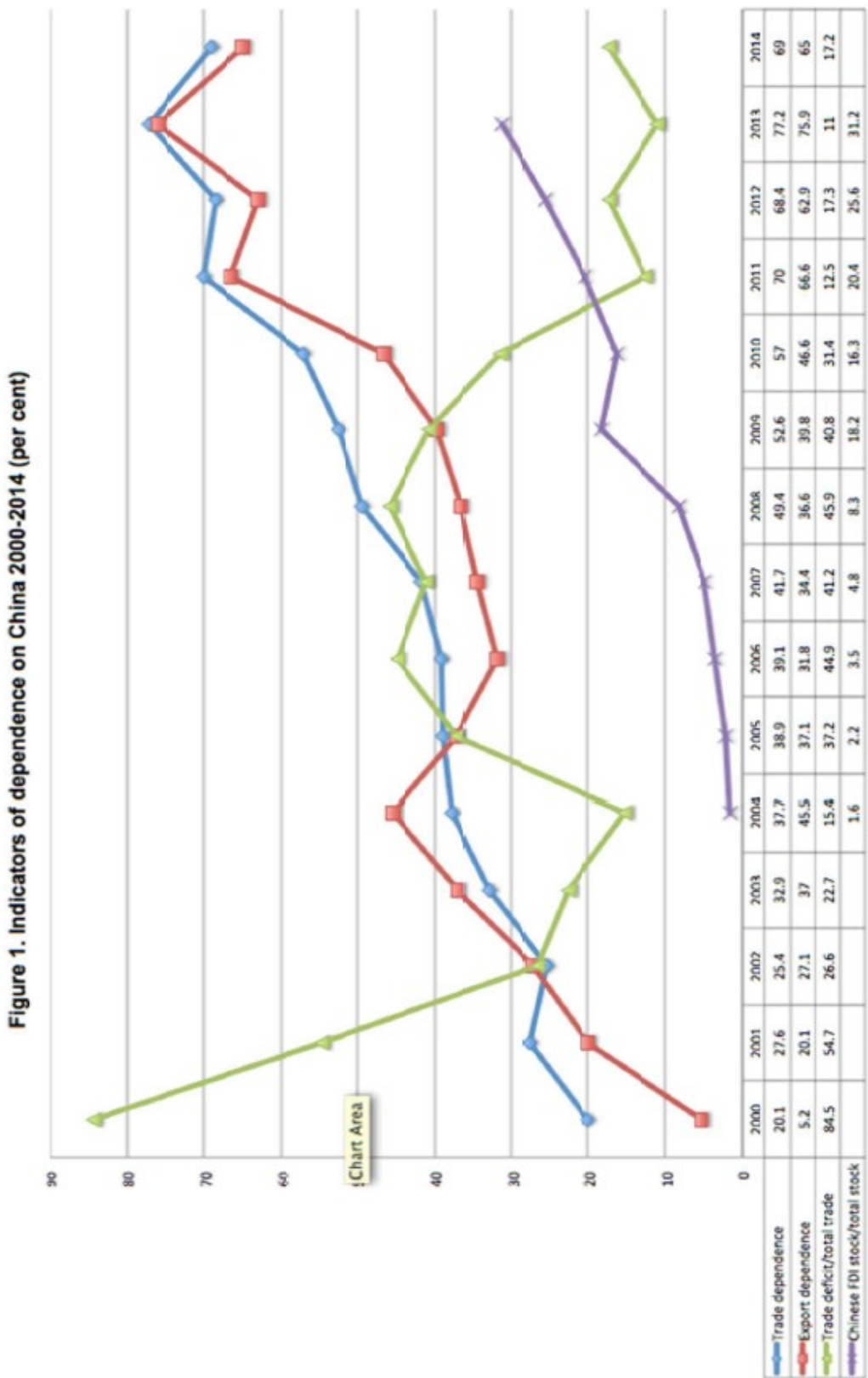
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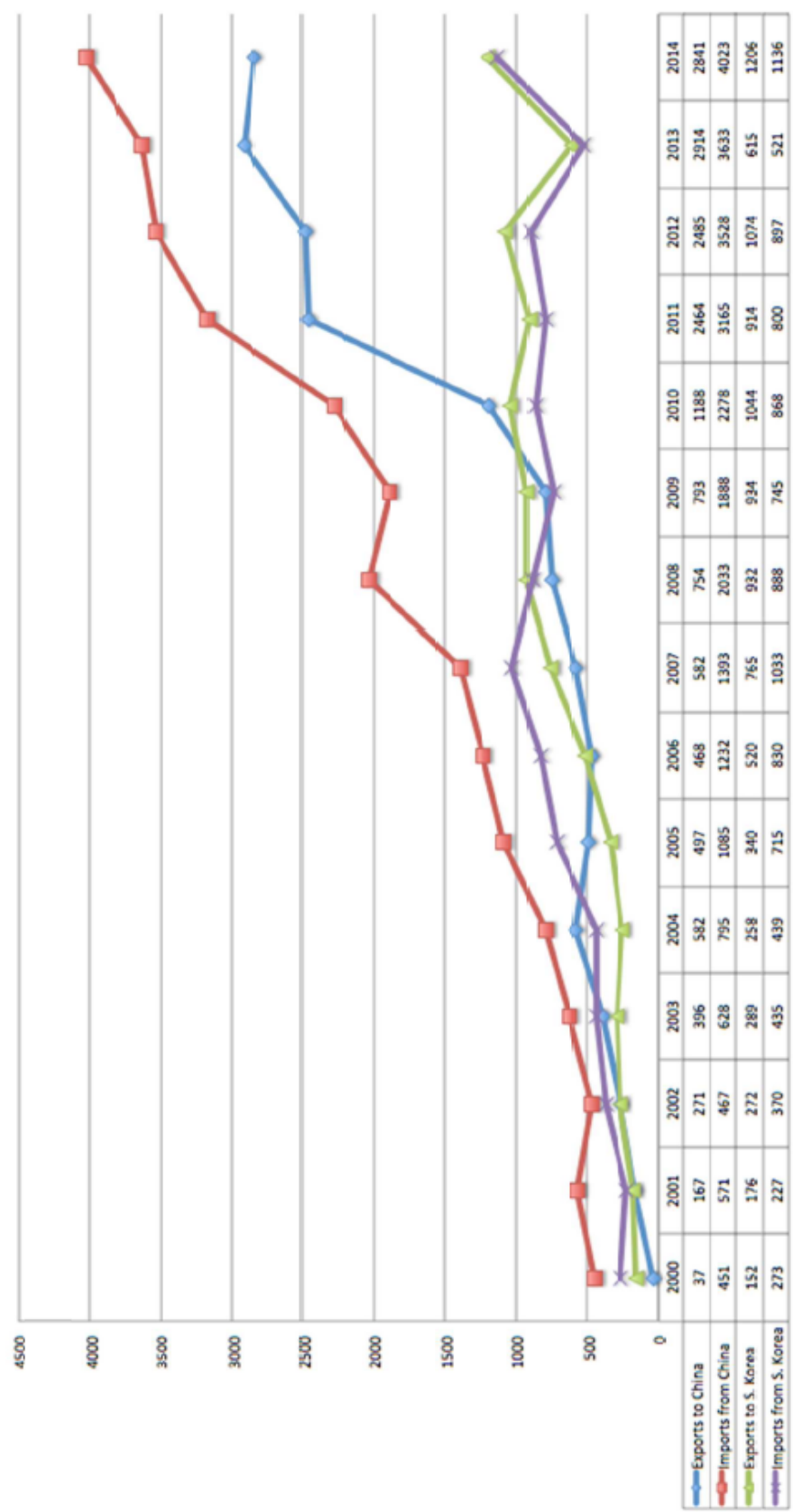
Table 1. North Korea's convergence and divergence with China in the aspects of economic reform and WMDs c.1990-present

	China's preferred outcome (economic reform with WMD restraint)	Post-Cold War Era c.1990-2010 (late Kim Il-Sŏng/Kim Chŏng-Il)	Current Era c.2010-present (late Kim Chŏng-Il/Kim Chŏng-Ŭn)	Explaining convergence and divergence 2010s
<b>Economic Reform</b>	<i>Convergence</i> : symbiosis between state and non-state sectors; acceptance of marketisation and opening up under continuing communist party leadership	<i>Diverging</i> : informal marketisation and reluctant market reform subject to reversal campaigns; 'military first economy'	<i>Converging</i> : marketisation from below (symbiosis) complemented by reforms from above; 'parallel advance' replaces 'military first economy'	Chinese economic input reinforcing political consolidation of succession based on economic performance
<b>WMD</b>	<i>Converging</i> (moratorium, reduction of capabilities) or <i>convergence</i> (full denuclearisation)	<i>Diverging</i> : development and testing of WMDs without rejecting denuclearisation in principle	<i>Divergence</i> : formal affirmation of WMD possession as a principle of state under 'parallel advance' (of economy and WMD)	<ul style="list-style-type: none"> <li>• Chinese support unable to compensate for WMDs as deterrent or diplomatic lever</li> <li>• WMDs enabled by China (economic input) but motivated by US-South Korea (threat)</li> </ul>



Source: NSO, Major Statistics, several issues (trade data); MOFCOM, *Statistical Bulletin*, several issues (Chinese FDI data).

Fig. 2. North Korea's trade with China and South Korea 2000-2014  
(USD millions)



Source: NSO.

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<sup>1</sup> Understood here as nuclear weapons and systems for their delivery.

<sup>2</sup> By 'China', I mean the authoritative decisions of the Foreign Policy Leading Group as expressed via official outlets.

<sup>3</sup> North Korea's WMD programme is subject to sanctions under five UN Security Council Resolutions: 1718 (2006); 1874 (2009); 2087 (2013); 2094 (2013); and 2270 (2016).

<sup>4</sup> No visits by the top leader or guests received by the top leader.

<sup>5</sup> The agreement exchanged food in return for suspension of nuclear and missile testing. It collapsed when North Korea conducted a rocket test on 13 April 2012. Both sides accused each other of misinterpretation.

<sup>6</sup> For example, total trade with North Korea (January-September 2014) was USD 2,040 million (Liaoning) and USD 840 million (Jilin).

<sup>7</sup> The conservative Lee Myung-Bak administration (2008-13) proposed the Denuclearisation, Openness, 3000 initiative (2008) requiring denuclearisation as a

precondition of aid that would raise North Korea's GDP per capita to USD 3,000 within 10 years.