

Policy Forum 06-70A: DPRK's Reform and Sino-DPRK Economic Cooperation

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Analysis by Li Dunqiu

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I. Introduction

Li Dunqiu, Director of Division of Korean Peninsular Studies at the Institute of World Development Center of Development Studies, writes, "Sino-DPRK economic cooperation is growing in depth and

width but both sides adopt a low-profile and practical attitude... In fact Chinese enterprises, both private and state-owned, are looking for greater room for their future development as a result of the constantly improving market economy in China. Amid such backdrop, the DPRK naturally becomes their target...It is not difficult to see that laws of the market economy are the most fundamental reason behind Chinese enterprises' investment in DPRK."

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II. Analysis by Li Dunqiu

- DPRK's Reform and Sino-DPRK Economic Cooperation
by Li Dunqiu

DPRK's change is by no means accidental. It has its profound international and domestic backgrounds. DPRK has made tremendous efforts in shackling off the shadow of the Cold War and integrating into the constantly changing international community, but with little result. Leaders of DPRK have no choice but to explore a new way that suits its country. Amid this backdrop, DPRK is slowly but steadily promoting its reform, which is low-profile but pragmatic.

From the end of 1990s, DPRK has begun to make adjustments to its economic theories and policies, putting forward such new views and propositions as pragmatism, building a strong socialist country, focusing science and technology, new concepts and improving economic management modes. A series of "Measures to Improve Economic Management Order" was issued on 1 July 2002. The adjustment this time, comparing with previous ones, was strong in enforcement and wide in the areas involved, thus injecting new impetus in its economic recovery and development. Though DPRK's economic reform is only introducing rational elements of the market economy to make up pitfalls of its planned economy with the prerequisite of adhering to the latter, it should be commended as a major innovation in DPRK's theories and practice in building socialism. Early this year, we saw new phenomenon from the DPRK side. It started with Kim Jong Il 's visit to China accompanied by premiers of the State Council in mid-January to learn the successful experience of China's reform and opening up, followed by Chang Song-taek's eleven-day China inspection tour accompanied by over thirty high-ranking economic officials, and then Cabinet Premier Pak Pong Ju's elaboration of this year main tasks in economic work on the Fourth Plenary Session of the Eleventh Supreme People's Congress. These new changes were not only widely reported but also aroused great interest among the international community in the country's economic changes.

I. DPRK's Guiding Principle Undergoing Quiet Changes.

A. Basic Theories of DPRK's Economic Reform

At present DPRK has not yet established systemic theories to guide its economic reform. But Chairman Kim Jong Il has proposed new ideas which have become the basis for its economic reform.

a. Pragmatism

It was first proposed by Kim Jong Il after he became General Secretary of the DPRK Labor Party. There is no works which systematically elaborates Pragmatism. But according to economists from DPRK, pragmatism has two meanings, i.e. to bring actual benefits for the people, and to be profit-

oriented instead of suffering losses. The former is the principle while the latter is the detailed content.

To follow the rule of pragmatism in economy is to seek economic benefits and for companies to make profits. To this end, the Fiscal Law amended by DPRK in April 2004 changed the ultimate goal of companies from "reducing cost" to "increasing net income", so as to help them be profit-oriented. At present, pragmatism is the principle that must be followed in all DPRK's economic work. Its economists have vividly compared it with China's "seeking truth from facts". It is fair to say that pragmatism will become theoretic basis for people in DPRK to liberate their minds and promote economic reform.

III. DPRK's Energy and Mineral Recourses DPRK has severe shortage of energy, especially oil. 90% of its oil supply comes from China. It also has oil trade with Russia but the amount is trivial as it does not have enough foreign currency. Russian oil companies sell oil to DPRK at price lower than international market price. DPRK has almost no oil reserve to speak of. It is currently working actively with China to exploit oil in its West Sea. Electricity is also in short supply in DPRK though its supply is slightly better compared to oil. DPRK is rich in water recourses so the Government tries to develop small hydro power stations. And in accordance with the principle of those who develop will benefit, local governments are encouraged to build such projects according to their own conditions, and with good results. It is claimed by DPRK officials that the country is in fact equipped with conditions to build large hydro power stations. That's why Kim Jong Il and other high-level officials in DPRK visited China's Three Gorges Hydro Power Project in Yichang early this year. But because of its tension with US and its fear of conflicts or wars, the Government only encourages small- and medium-sized hydro power stations before its relations with US has improved. In addition, it also stresses thermal power since it is rich in coal and able to provide sufficient fuel. Consumption of coal ranks the first among all energy, to be followed by hydro power. DPRK is now studying new energy and hopes to convert it into actual use in production and life, i.e. solar power and biogas. There are four important recourses in DPRK: rich forest resources; important mineral resources like abundant coal, iron ore, graphite, gold, silver, lead, zinc, magnesite, all of which now allow the participation of foreign companies; 8600-kilometer coasts with no pollution, which are rare in the world and hold great potentials for fishing, aqua-culture, processing of sea food once foreign capital and technology are channeled in; rich tourist resources, that may become one of its future pillar industries. DPRK has abundant mineral recourses, with over 360 kinds confirmed and 200 kinds economically viable. It is noticeable that the reserve of its magnisite ranks the first in the world, accounting for 56% of the world's total. Its top ten minerals include tungsten, molybdenum, graphite, heavy spar and fluorite. The reserve of copper and ilmenite is calculated in tens of millions of tons and that of white jade, jadeite, black jade and sand jade is also abundant. Since it has such a large reserve of metal and energy mines, 70% of its industrial raw materials and fuels are self-sufficient. But there is no oil and pitch coal (raw material for charcoal), both of which are necessary for iron and steel industry though anthracite and brown coal are abundant. Coal, iron ore, lead and zinc core, limestone and magnisite take up the bulk of DPRK's mineral industry but only 30% of the capacity is utilized due to restrictions of outdated equipment and poor technology. Iron ore is exploited in over 20 mines represented by Musan Mine. With a reserve of 1 billion tons, it is a famous open mine in the world and the largest in a country with an iron output of 8 million tons. Production of iron ore grew by 2-3% since 1970s, as a result of expansion and development of iron mines. But the growth has slowed down recently due to poor results of prospecting and outdated equipment. Foreign capital is now being introduced. DPRK's coal is divided into anthracite and bituminous coal. The former is mainly located in Pyongan-namdo and Pyongan-bukto while the latter in Hamgyong-bukto and Hamgyong-namdo. According to administrative division, there are four major coal mines in DPRK, namely Pyongan-namdo Mine, Pyongan-bukto Mine, Hamgyong-bukto Mine and Hamgyong-namdo. Currently there are over 100 national coal mines, 70 anthracite mines and 30 bituminous coal mines,

and over 500 small- and medium-sized local mines. In the 80-kilometer belt in the south of Pyongan-namdo stretching from east to west with Pyongyang at the center, the reserve of anthracite is abundant. Notable mines include Samsin (Samsindon, Daefon-gu) , Sadon (Sadon-gu), Ryongzen (Ryongzen-gu), Haelyong (Ladonza-gu, Haelyong, Gangdon-gun), Gangdon (Gangdon-gun), Gangso (Gangso-gun), Zencun (Zencun-gun), Wonstun (Wonstun-gun). There is anthracite in 668 sq kilometers in the north of Pyongan-namdo. Main coal mines there include those in Donstun, Syongbun, Jaenam, Joyang of Ganstun, Ganstun, Bonstun, Yamzum, Wyonlae, Xinlyon, Sonam of Bugstun-gun, Xiandon, Xinstun of Ensam-gun, Stunzen, Yongdae, Sunstun, Mujindae, Gigdon, and Ryongden, Ryongmun and Ryongcel of Kujang-gun, P'yŏngan-bukto. Bituminous coal is mostly concentrated in the North Mine (north of Aoji) and South Mine (south of Chongjin) in Hamgyongbukto and Anju Mine in Pyongan-namdo. Largest coal mines in the north include Aoji Mine in Undokkun, Obun Mine in Musam, Hue Ryon Mine. There are seven ore strata that are 2-5 meters in depth in Anju Mine, producing brown coal of 5300kcal. With an annual output of 7 million tons, it is thus the largest mine in DPRK. DPRK's proven coal deposits are 14.74 billion tons, 11.74 being anthracite and 3 billion tons brown coal. Recoverable reserve, allowed by the current technology, is about 7.9 billion tons. Its coal production has dropped since the end of 1980s due to restrictions of technology and equipment. (See the table below for annual production since the 1980s) *Unit: 10,000 tons Year

| Year | 1980 | 1985 | 1990 | 1993 | 1995 | 1999 | 2000 | 2002 |
|------------|-------|-------|-------|-------|-------|-------|-------|-------|
| Production | 3,027 | 3,750 | 3,315 | 2,710 | 2,370 | 2,100 | 2,250 | 2,190 |

IV. Rapid Growth of Sino-DPRK Trade and Economic Cooperation Sino-DPRK trade and economic cooperation grows at an eye-catching pace. With trade accounting for 40% of its total and investment 70%, China has thus become DPRK's largest trading partner and source of investment. DPRK has been more dependent on China in food and energy supply. Main ports between the two countries have become or are becoming major vehicles of bilateral trade and economic cooperation. The friendly visit by Chinese President Hu Jintao to DPRK in October 2005 and Kim Jong Il's China visit in January this year have further promoted political and economic cooperation between the two countries and injected new impetus in bilateral trade. Trade between China and DPRK has increased by 14%, reaching 1.6 billion USD. DPRK import commodities like oil and corn from China, worth 1 billion USD, and export commodities like coal and iron ore to China, worth 0.5 billion USD. According to the statistics from Dandong Customs, 1.86 million tons of import and export went through the Dandong Port in 2005 at a value of 0.84 billion USD, up both in quantity and value by 10%, with 0.45 billion USD in China's favor. It is estimated that DPRK will continue to expand trade with China this year. The two countries have planned to build a new road bridge across the Yalu River to meet the demands of the constantly growing trade. Sino-DPRK Trade Volume from 1997 to 2005 *Unit: 100 million USD Year

| Year | DPRK's Total Foreign Trade | DPRK's Trade with China | China's Export | China's Import |
|------|----------------------------|-------------------------|----------------|----------------|
| 1997 | 21.7 | 6.5 | 5.3 | 1.2 |
| 1998 | 14.4 | 4.1 | 3.5 | 0.6 |
| 1999 | 14.8 | 3.7 | 3.2 | 0.5 |
| 2000 | 19.7 | 4.8 | 4.5 | 0.3 |
| 2001 | 22.7 | 7.37 | 5.7 | 1.6 |
| 2002 | 22.6 | 7.33 | 4.6 | 2.7 |
| 2003 | 29 | 10.23 | 6.3 | 3.9 |
| 2004 | 31 | 13.85 | 40.5 | 15.8 |
| 2005 | 5 | 10.8 | 5 | 5 |

In recent years Chinese businessmen have accelerated their investment in DPRK. Those who took the lead in investing DPRK mainly came from Zhejiang, Jilin, Liaoning, Jiangsu and Guangdong Provinces with Zhejiang businessmen taking up the bulk. In 2003, 40 businessmen from Wenzhou, Yiwu, Dongyang, Cixi and Hangzhou headed by Lu Yunlei, agreed on cooperation intent with the operators of Pyongyang No. 1 Store. Guhui Trading Co. lead by Lu, obtained, unexpectedly, operating right of 15,000 sq meters of the store and corresponding 9,000 sq meters of warehouse. The deal was signed on 6 August 2003. Lu commented that what he valued was the market potentials in a country that was opening up. Lu also disclosed that he would invest several million of RMB to renovate the store and that operating space in the store would cover 10,000 sq meters, divided into over 300 booths to be further rented to Chinese businessmen to wholesale and retail small Chinese commodities, daily necessities in particular. The Zhejiang businessman commented opportunities in DPRK like this: "It is better to have our presence in the country but don't expect too much from the first phase". It was the private companies that gave rise to the first wave of investing in DPRK. The second wave in 2005 was mostly generated by large state-owned enterprises, in areas like heavy industry, energy, mineral recourses and transportation, different from the first one. At

present DPRK has agreed to the joint-venture between China National Metals and Minerals Import and Export Corporation and its ??Coal Mine. This is not only the first established by China outside DPRK's special economic zone but also represents an important measure by DPRK to open its recourses. Rydongden Coal Mine is the largest anthracite mine in DPRK. Covering an area of 18.8 sq kilometers, it has a reserve of 0.15 billion ton, 0.125 billion of which is recoverable. Its annual output is 1 million tons, equal to a medium-sized coal mine in China. According to report issued by the Development and Reform Committee of Jilin, the province has reached a "barter" agreement with DPRK, transmitting electricity to the country in exchange of the mining rights of its Youth Copper Mine. With a total investment of 0.22 billion RMB, it is a typical experiment by DPRK to exchange electricity with mineral recourses. Jinlin Tonghua Iron and Steel Group will obtain 50-year mining rights in Musan Iron, the largest in DPRK, at a price of 7 billion RMB. Musan Iron, located in Hamgyong-bukto is the largest open mine in Asia, with proven reserve of iron powder about 7 billion tons. With iron content as high as 66%, it is able to be smelted directly. Gold reserves in DPRK are also very rich. Guoda Gold Shareholding Co. Ltd., in Zhaoyuan, Shandong Province signed an agreement in 2004 with DPRK on gold exploration and smelting project. According to the agreement, a joint-venture would be set up for gold mining in ??? and bring back the ore to the company for smelting. ??? Gold Mine, which was set up quite early, has a considerable reserve and at least 150 tons can be recoverable. But due to the lack of capital and outdated technology, operation of the mine has been at a standstill. In September 2005 DPRK sold the 50-year exclusive operating rights of Najin wharf to Huichun, Jilin, in order to get the latter's support for building a road from Tongsungu, Wonstunli, Kasung-si, to Najin Port. Sources from the Administrative Committee of the Border Economic Cooperation Zone in Huichun, Jilin, disclosed that the sale this time of the wharf in Najin Port was more of a corporate instead of government act. It was said that Fan Yingsheng, a real estate developer from Hunan, was the mastermind behind the deal and he alone would channel half of the 60 million Euro in payment. Capital from Hong Kong is also coming. Early investments were mainly channeled to hotels, restaurants and the entertainment industry. But according to a recent report from Hong Kong media, a local businessman Qian Haoming reached a 3-billion USD agreement with the DPRK Government and China's Ministry of Railway to build a railway from Tumen, border city in China, to Chongjin, port in DPRK. The agreement signifies that the deadlock between railway authorities of the two countries is being broken. There used to be three pending questions with the DPRK railway, i.e. overstock, arrears and withholding of Chinese cargo carriages. This forced the Chinese railway authority to take measures to restrict transportation between the two countries, like intermittent loading and goods limits. Statistics show that over 2000 carriages were held up in DPRK in 2004, 260 of which were for coal. It is reported that Hong Kong International Industry Development Co. Ltd., headed by Qian Haoming, promised to provide 500 to 1000 carriages to DPRK as required by the agreement. Preliminary agreements have been reached at the moment between China and DPRK concerning minerals, railway and port lease. Sino-DPRK economic cooperation is growing in depth and width but both sides adopt a low-profile and practical attitude. It is necessary to point out that such development has aroused concern from relevant countries in North East Asia, which mistake China for having political motives. In fact Chinese enterprises, both private and state-owned, are looking for greater room for their future development as a result of the constantly improving market economy in China. Amid such backdrop, neighboring country DPRK naturally becomes their target. There are plenty of Chinese enterprises with strength ready to come into DPRK, more active than the government policy allows. During the National People's Congress last march, delegates from local enterprises proposed a motion to the Central Government, calling for policy and legal guarantees for expanded and deepened economic cooperation with DPRK, including the establishment of special economic zones and free trade areas. It is not difficult to see that laws of the market economy are the most fundamental reason behind Chinese enterprises' investment in DPRK. III. Nautilus Invites Your Responses The Northeast Asia Peace and Security Network invites your responses to this essay. Please send responses to: napsnet-reply@nautilus.org . Responses will be considered for redistribution to the network only if they

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