

# Policy Forum 05-11A: Failure or success of a hybrid system?

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PFO 05-11A: February 10th, 2005

## Failure or success of a hybrid system?

Ruediger Frank

CONTENTS

[I. Introduction](#)

[II. Essay by Ruediger Frank](#)

[III. Nautilus invites your responses](#)

### I. Introduction

Ruediger Frank, Professor of East Asian Political Economy at the University of Vienna, writes: "the indicated return of the DPRK to the Six-Party Talks would from this perspective not be motivated by desperation due to a worsened situation on the food front, but by increased self-confidence due to a successful economic transformation. The negotiators might want to take this into consideration."

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## **II. Essay by Ruediger Frank**

- "Failure or success of a hybrid system?"  
by Ruediger Frank

Some days ago, the press reported a reduction in the per capita food ration in North Korea from 300 to 250 grams (Nautilus Daily Report, Feb. 01, 2005). This was widely seen by analysts as a sign of a food shortage and hence another proof for the failure of the economic and price reforms. I would like to offer an alternative interpretation. First, there is some factual evidence we should consider. The time is not right. Juseok, the Korean Thanksgiving, is not randomly in late September. The last harvest was only about four months ago; based on experience and logic, we would expect a food shortage to emerge in spring, not in winter. Furthermore, there are no reports about a bad 2004 harvest; instead, it seems that the DPRK's agriculture had some fairly good years in a row. And finally, a country desperate for food would be supportive towards international relief agencies. Instead, in late January the WFP reported that it was forced to cut its food monitoring activities by about 20-30 % since October 2004 (Nautilus Daily Report, Jan. 27, 2005). This indicates that the political cost of monitoring was perceived by Pyongyang to have become higher in relation to the benefits of food aid. If those political costs have been constant in absolute terms, we can conclude that the absolute benefit of food aid has been reduced - for example, because the amount of non-aid food has increased.

Analytical considerations may help us, too. Imagine ten bowls of rice and fifteen hungry people. In a free market, the ten who are able to pay the highest prices will get their rice, and the remaining five will starve. Not so under state-led distribution. Here, the ten bowls are divided into fifteen rations, and although nobody gets as much as he wants, everybody gets something. This works well as long as the rations are sufficiently large to keep people alive. This is how the North Korean food distribution functioned for many decades.

Now it is decided that productivity will be higher when a free market is allowed to send its signals to the farmers. Can such a free market economy be introduced over night? Of course not, since the total supply is below total demand, and a distribution based on the individual's ability to pay would result in the situation described above - ten full and five empty stomachs. There is a great risk that those five people will not wait until they die, but rather challenge the system by resorting to violence and thereby threaten political stability.

The solution is a middle way, or a hybrid system: The state maintains the equal distribution of rations, which are by definition lower than the individual demand, and allows the consumers to cover the gap in free markets. The state thereby catches two birds with one stone: starvation is prevented, AND the market can send its signals to producers. Of course, such a system is hardly sustainable; prices are distorted, corruption will emerge. The long-term goal would therefore be to constantly, but gradually enlarge the portion of the market at the expense of the state's share of food distribution. The state's share can only be reduced if the total supply rises. In the ideal case, the market's signals finally lead to a productivity growth that raises the total supply to the level of total demand. Then, the public distribution system can be cancelled altogether.

Should we interpret a reduction of the daily ration by 50 grams as a negative sign? We probably should not, in particular in the absence of reports about a food shortage. On the contrary, this might be an indication that over two years (and two harvests) after the price reforms of July 2002, first

results in terms of increased agricultural productivity are finally showing up. It is needless to say that there are many problems remaining, such as the inflation on the free markets and the difficulties of those whose incomes do not rise accordingly. It will also be difficult for the state to correctly estimate the optimal size of the food rations. However, in the case of serious difficulties, we should expect a strengthening of public distribution, not its further reduction.

This interpretation, if right, sends strong signals to the international community: Those who regard a strengthened market system in North Korea as beneficial are well advised to increase the total supply of food. Here, THEY can catch two birds with one stone: improve the humanitarian situation AND support a gradual transformation - with the goal of regional security and stability, not regime change per se.

Finally, the indicated return of the DPRK to the Six-Party Talks (Nautilus Daily Report, Feb. 04, 2005) would from this perspective not be motivated by desperation due to a worsened situation on the food front, but by increased self-confidence due to a successful economic transformation. The negotiators might want to take this into consideration.

### **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](mailto:napsnet-reply@nautilus.org) . Responses will be considered for redistribution to the network only if they include the author's name, affiliation, and explicit consent.

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[Return to top](#)

[back to top](#)

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