

# China's plans to open up North Korea for foreign investment

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The visit by North Korean leader Kim Jong-il to China last week was driven by the country's acute economic crisis and the need for aid and investment. China is exploiting the opportunity to draw North Korea more closely into its orbit—propping up its strategic ally, but at the same time opening up the autarkic North Korean economy as a source of cheap labour and raw materials.

Kim's visit was only announced after he met with Chinese leaders in Beijing. On route, he visited the northeastern Chinese port city of Dalian and the coastal city of Tianjin, both of which are held up by Chinese officials as models for encouraging foreign investment—the path that Beijing is pressing Pyongyang to follow.

Among those accompanying Kim were his brother-in-law, Jang Song-thaek, now in charge of foreign investment, and Kim Yang-gon, the chief of Korea Taepung International Investment Group. This organisation is the country's investment arm for channelling foreign funds into a new State Development Bank to develop ports, railways, light industry and agriculture, along the lines of China's "market reform" measures in the 1980s.

Kim was feted in Beijing, meeting all nine members of the Chinese Communist Party's Politburo Standing Committee. Kim in turn praised the new infrastructure projects provided by Beijing to facilitate Chinese investment. "North Korea welcomes corporate investment from China, as well as advancing the working level cooperation between the two sides," Kim declared.

Pyongyang has little choice in abandoning its longheld stance of economic self-reliance. The US and Japan pushed new punitive sanctions through the UN Security

Council, following North Korea's nuclear test in 2006. Its relations with South Korea cooled after Lee Myung-bak from the right-wing Grand National Party (GNP) won the presidency in 2007 and effectively cut off aid to the north.

North Korea's economy is in considerable crisis. Its attempt at currency reform last December failed, leading to hyperinflation and signs of social unrest. Under the new exchange rate regime, a workers' wage of 2,500 won per month is worth only about \$US1 on the black market. Basic items including rice are scarce.

Beijing is concerned to prevent a collapse in North Korea, which could send a flood of refugees across the border into northern China. It would also raise the prospect of a regime emerging in Pyongyang more closely aligned with South Korea and the US. At the same time, Chinese aid comes with strings attached, including opening up North Korea to Chinese investment and the eventual resolution of the protracted international standoff over North Korea's nuclear programs.

During his visit last week, Kim reportedly received up to \$60 million in immediate aid. However, the real thrust of China's orientation was demonstrated earlier this year with a huge infrastructure package worth \$10 billion—equivalent to 70 percent of North Korea's estimated GDP. The State Development Bank and Taepung International Investment Group were established in January, largely to handle this incoming Chinese investment.

Pyongyang established the Rajin-Sonbong "special economic zone" near the border with China in the early 1990s to encourage investment from China and Russia. Beijing, however, had little capital to invest abroad at the time and North Korea's economic zone largely

languished. Now the situation has changed as China has begun to use its large foreign currency reserves to secure access to raw materials and markets. Beijing is now seeking to develop Rajin as a major regional trading hub.

A *Washington Post* article last month predicted that Kim's visit to China would mark "a major policy reversal". Professor Lim Eul-chul of Seoul's Institute for Far Eastern Studies, who was in Pyongyang talking to officials and Chinese businessmen, was told that the new State Development Bank was intended to be a "one-stop" shop for foreign investors. "The North is planning to open foreign-owned factories not just in closed-off special economic zones, but major cities like Nampo and Wonsan," Lim explained. Until now, North Korea has largely limited foreign businesses to sealed-off zones like the Kaesong joint industrial zone with South Korea.

The North Korean International Trade Office web site promotes the country as having "the lowest labour costs in Asia" and the "lowest tax scheme in Asia". Orienting to China in particular, it emphasises the country's educated workforce, noting: "[A]t the moment the labour cost in North Korea is very low compared to China's, especially great for corporations to save labour costs." It added that North Korea was a vast "virgin silo" with 300 types of minerals and other untapped natural resources. It further declared that the regime was establishing a free market and laws to protect private property and foreign investors.

The opening up of North Korea to foreign investment, particularly from China, has broader geopolitical implications. Since the collapse of the Soviet Union in 1991, China has already become North Korea's main trading partner and provider of economic aid. China imports minerals from North Korea and exports cheap manufactured goods. However, the size of the proposed Chinese investment and aid raises the prospect of North Korea's transformation into a dependent satellite, which will further extend China's weight and influence in North East Asia.

The key strategic location of the Korean Peninsula, adjacent to China, Japan and Russia, has always made it the focus of major power rivalry. The previous effort to open up North Korea took place in the late 1990s under the so-called Sunshine policy of South Korean President Kim Dae-jung who envisaged establishing a new cheap

labour platform for South Korean corporations. The European powers expressed interest in investing in North Korea and establishing rail links from Europe to South Korea and Japan. Russia considered building energy pipelines to South Korea via North Korea.

All these plans, however, came to an abrupt halt with the election of President Bush who ended the tentative steps taken by the Clinton administration towards a rapprochement with Pyongyang and rapidly ratcheted up tensions over its nuclear programs. In October 2002, Bush effectively scuttled the "Agreed Framework" established under Clinton to freeze North Korea's nuclear facilities by accusing Pyongyang of having an "illicit" uranium enrichment program. North Korea expelled nuclear international inspectors, withdrew from the Nuclear Non-proliferation Treaty and restarted its nuclear facilities.

Bogged down in wars in Iraq and Afghanistan, the Bush administration eventually joined six-party talks initiated by China to ease tensions over North Korea's nuclear programs. Washington, however, had already managed to block the economic plans of its European and Asia rivals for North Korea and stymie South Korea's Sunshine policy. While preoccupied with his escalating AfPak war and confrontation with Iran, President Obama has maintained the US hard-line stance towards North Korea that continues to keep the peninsula in a state of tension.

China's current efforts to open up North Korea for investment face similar obstacles. The current dispute over the sinking of a South Korea warship in March is just one of a number of issues that could spark a new crisis and cut across China's plans. Major power rivalry, especially between the US and China, continues to ensure that the Korean peninsula remains a dangerous international flashpoint.



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