

## *New Geo-economic Thinking on North Korea in Japan*

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### **Abstract**

Japan's North Korea policy is currently based on solid strategic calculation, and Tokyo will most likely adhere to the six-party talks process for the resolution of the nuclear, ballistic missile, and abduction issues. However, adherence to this policy is neither static nor permanent. Tokyo will be forced to reformulate a new approach if the talks process makes significant progress, or if the Pyongyang regime collapses abruptly, replaced by a new one satiated with the status quo that involves lowering the tensions centered on North Korea. This paper analyzes major factors pushing the Japanese government to their adoption of a geo-economic approach to North Korea, something which represents a major shift from the current thinking and policy approach. The Japanese public has recently been exposed to an alternative perspective, critical of U.S. North Korea policy, particularly in regard to the recent u-turn in policy toward appeasement and the growing skepticism of the U.S. allegation regarding Pyongyang's counterfeiting activities. The Japanese public has also become gradually aware of growing U.S.-European competition in direct investment in North Korean underground resources and of the latent Japanese edge in that competition. This paper discusses the prospects for a geo-economic regional power game and an evolving Japanese geo-economic policy approach.

**Key Words:** Japan's North Korea policy, geo-economics, counterfeit activities, underground resources, U.S.-European competition in direct investment

In the face of Pyongyang's military-diplomatic brinksmanship, Japan remains highly vulnerable to North Korean nuclear ballistic missiles due to her geographical proximity to the rogue state. However, Tokyo has pursued the concurrent resolution of the issues of Pyongyang's nuclear weaponization, ballistic missile development, and the abduction of Japanese nationals, at least in terms of an eventual policy goal. As a result, Tokyo has occasionally stood alone in the six-party talks processes, given that the other participating states have placed a top priority on the nuclear issue. Tokyo sees both the nuclear and abduction issues as firmly embedded in the tyrannical nature of Pyongyang's dictatorship: the regime is struggling to survive international isolation caused by its grave human rights violations by relying on the power of nuclear weapons. From this perspective, it may be possible to separate the two issues in analysis, but not in any meaningful manner as a policy matter.

Driven by growing concerns with the above three issues, Japan's North Korea policy has been framed in the evolving regional strategic context in which Japan's national security is being redefined in large part by the changing power balance between a rising China and the United States, deeply troubled as it is with the global war on terrorism, now centered on the Middle East. The six-party talks are a major institutional instrument of the great power game between the United States, China, Japan, and Russia, with the significant participation of South Korea as a middle power, through which to articulate their geopolitical interests in maintaining the stability of regional security order. Japan will most likely adhere to such an approach as long as geopolitics dictates Tokyo's calculations.

However, there is now an emerging Japanese stream of geo-economic thinking that emphasizes the centrality of dynamic competition over rare metals and other mineral resources in North Korea, a significant long-term factor shaping the region's international distribution of power and, consequently, the regional security order. Geopolitical interaction occurs in

a given international distribution of power. In contrast, geo-economic interaction transforms such a distribution over time, which alters the patterns of strategic interaction in favor of a nation that succeeds in aggrandizing its power. In this case, a geo-economic power game will be characterized by a power struggle among nations pursuing wealth.

In the framework of the six-party talks, Pyongyang has already been compelled to accept, at least in principle, the total abandonment of nuclear power, marked by the initial disablement of three nuclear facilities at Yongbyon and the eventual dismantlement of all the nuclear programs. While Pyongyang has sought regime survival through the negotiation tactics of procrastination on the strength of the existing embryonic nuclear power, Pyongyang's free hand in the negotiations has been considerably narrowed and constrained. As a result, Korean unification is now dimly on the horizon, even though the world may have to coexist with Pyongyang's rudimentary nuclear arsenals for an extended period of time. Certainly, the Japanese government, pressured by the public opinion, has recently supported a hard-line approach to the abduction issue, a surge in the support due in large part to highly effective campaigns by the abductees' rapidly aging parents and relatives that will not be sustainable in the long run. However, this support will surely wane over time, and the six-party talks will most likely make limited but significant progresses of the nuclear issue. Then, at a point of time in the future, Japan's North Korea policy will inescapably shift from the current geopolitical approach to a geo-economic one. Should the Pyongyang's regime collapse abruptly, replaced by a new one satiated with the status quo, such a shift would come unexpectedly earlier.

This paper will discuss some important factors directing the mainstream Japanese strategic thinking toward geo-economics centered on U.S.-European competition in finance and direct investment over underground resources in North Korea. First, the paper will analyze the growing

Japanese discontent about the recent U.S. North Korea policy of ignoring the abduction issue; the public is now aware that Tokyo may need to take a more independent line in policy matters. Second, the study will examine emerging Japanese incredulity of the U.S. allegation that Pyongyang has printed and circulated extremely sophisticated yet counterfeit US\$100 bank note, known as “supernotes,” on a massive scale. This involves a sense of caution that Tokyo’s hard-line policy toward Pyongyang might have been manipulated by U.S. disinformation. Third, the analysis will look into some significant cases of European direct investment in North Korea’s rare metal and other mineral resources and the related infrastructure building, which may be in conflict with U.S. commercial interests under the government’s longtime economic sanctions against the rogue state. The paper will discuss the prospects for the gradual evolution of a Japanese “geo-economics first” approach to North Korea. For this purpose, the analysis will be based primarily on Japanese sources, complemented by non-Japanese materials cited or referred in those Japanese sources.

The current work will follow an investigative approach to U.S. assertions on the intentions and key facts as related to its North Korea policy, as found in the official proclamations and other publicized statements. Thus, the study will rather constitute a novel inductive feedback to the existing mainstream literature that is prone to accepting the assertions as assumptions or presumptions for policy analysis on North Korea’s brinkmanship and the related regional international relations. Novel and/or alternative factual findings, as fully explored in the following analysis, will necessitate a completely different analytical perspective and then make it feasible to reformulate a distinct research question.

## Japanese Disillusionment with the Bush Administration

On June 26, 2008, President Bush, in his attempt to accelerate the six-party talks process, proclaimed the removal of North Korea from the U.S. list of state sponsors of terrorism, entailing the lifting of U.S. economic sanctions imposed on North Korea as key policy aims.<sup>1</sup> This sharp, if not abrupt, turn in U.S. North Korea policy has appalled the Japanese public and Japanese leaders deeply concerned over the fate of Japanese abductees long held in North Korea. The change was in fact expected because the Bush administration's negotiation tactics after February 2007, marked by the U.S.-DPRK bilateral talks held in Berlin, increasingly tilted toward appeasement vis-à-vis Pyongyang. Surprisingly, however, the Bush administration made a sudden turn in policy without ensuring Pyongyang's unequivocal commitment to the complete, verifiable, and irreversible dismantlement (CVID) of all the nuclear programs, a series of concessions that were premature, unilateral, and excessive in favor of Pyongyang.

Consequently, Japan's hard-line policy, in tandem with the uncompromising Bush administration's approach theretofore, became isolated in the six-party talks process. Japan's approach found itself besieged by the about-face made by the United States and the other participating states in their now conciliatory approach to Pyongyang. In reaction to Pyongyang's ballistic missile test in July 2006 and its subsequent nuclear test in October 2006, the Abe administration (September 2006-September 2007) led the UN Security Council to pass a resolution imposing economic sanctions on North Korea in October 2006 (UNSC Resolution 1718). The resolution was a fruit of close Japanese-U.S. diplomatic coordination, centered on the

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<sup>1</sup>- According to the U.S. Trading with Enemy Act, the removal of sanctions was scheduled to be effectual on August 11, 2008, 45 days after the president's notification to the Congress. On October 11, 2008, the Bush administration effectuated the removal without reaching an unequivocal agreement with Pyongyang that obligates it to implement necessary measures for nuclear disablement.

Security Council. Prime Minister Abe also placed additional unilateral sanctions, featured by the freezing of North Korean financial assets in Japan, the banning of financial transactions between Japanese financial institutions and North Korean entities, and the prohibition of North Korean vessels entering Japanese ports. Abe's approach, followed by the Fukuda administration (September 2007-September 2008), is in sharp contrast to Prime Minister Koizumi's approach (April 2001-September 2006), which was very much independent of the then hard-line Bush's North Korea policy. In September 2002, Koizumi and Kim Jong-il signed the Pyongyang Declaration in which Tokyo agreed in principle to normalize the diplomatic relationship with Pyongyang and to extend huge economic assistance to North Korea, when and only when a series of conditions are met.

Once U.S. sanctions against North Korea are lifted, existing Japan's unilateral sanction measures will inevitably become far less effective. On the contrary, Tokyo will be urged to lift these measures and may even be pressed to offer economic assistance to North Korea, including heavy oil, in exchange for Pyongyang's implementation of limited disablement of the nuclear facilities or merely its firm commitment to such implementation. Under estranged Japanese-U.S. relations, the new South Korean administration under Lee Myung-bak may be forced as well to restart a policy of appeasement in the form of huge financial assistance to Pyongyang. Lee has so far suspended various economic aid commitments to North Korea, amounting to US\$2 billion, that the former radical-left Kim Dae-jung and Roh Moo-hyun administrations extended over several years. By lifting U.S. sanctions, therefore, the Bush administration would be able to have Japan and South Korea shouldering a significant part of the burden of economic aid to North Korea.

Looking closely, however, it was the Fukuda administration that first announced that it would undertake a symbolic partial waiver of the unilateral sanctions against North Korea prior to Bush's proclamation on

June 26, 2008. On June 13, 2008, Foreign Minister Koumura announced that the waiver was intended to reciprocate the North Korean delegation's expression of intent to resume another "investigation" into Japanese abductees held within the rogue state, at the Japanese-DPRK bilateral talks in Beijing.<sup>2</sup> Such reciprocation was premature, unilateral, and excessive because Pyongyang had simply made a verbal commitment.

Aoyama Shigeharu provides us with intriguing facts that are crucial to analyze the above Fukuda administration's inscrutable turn in North Korea policy.<sup>3</sup> A seasoned journalist and the founder and CEO of a think-tank, Aoyama has established a reputation for his in-depth analysis based on unidentified insider information from the Japanese government. Referring to the leaked information from the Office of the Prime Minister, he relates the Washington-Tokyo policy interaction having led to this inscrutable turn.

The first fact of note is that President Bush continually urged the Prime Minister to first lift part of Japan's unilateral sanction against North Korea,<sup>4</sup> so that the President could justify, vis-à-vis the Congress and the American public, the dramatic removal of the rogue state from the U.S. list of state sponsors of terrorism and the subsequent lifting of economic sanctions to the state. This means that the President had to avoid damaging the stability of the U.S.-Japan alliance by ignoring the abduction issue. This could only be done by pretending to follow the initiative taken by the Japanese government which had the toughest policy stance against Pyongyang due to the abduction issue. Given the remaining term of his office and the ongoing presidential election cycle, President Bush had to take action by the

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<sup>2</sup>- *AFP-BB News*, June 13, 2008, <http://www.afpbb.com/article/politics/2404909/3030238>.

<sup>3</sup>- Aoyama Shigeharu, Anchor, the Kansai Television (KTV), Osaka, Japan, July 2, 2008. The transcription is available from <http://kukkuri.blog58.fc2.com/blog-entry-369.html>. A similar view is expressed by a leading Japanese North Korea hand, Shigemura Toshimitsu, *Kim Seinichi no Shoutai* [Kim Jong-il's real colors], (Tokyo: Koudansha, 2008), p. 14.

<sup>4</sup>- *Ibid.*

end of June so that he can make a breakthrough before a new president-elect was decided upon. By so doing, the President can leave his legacy to U.S. foreign and security policy by removing North Korea from the list of state sponsors of terrorism and in doing so, reducing their number. Otherwise, his administration would have been characterized by imprudent military adventurism and total disaster as demonstrated by the current quagmires in Iraq and Afghanistan.

The second fact is that Prime Minister Fukuda had already made the decision to lift a part of the economic sanctions before the Japanese-DPRK bilateral talks were held in Beijing on June 13: the decision was not at all a part of Tokyo's reaction to Pyongyang's proposal to carry out another "investigation" into Japanese abductees. Rather, it was Japan that had approached North Korea through the back channels of bilateral negotiation, so that Pyongyang appeared to have made the proposal to Tokyo, not vice versa.<sup>5</sup>

The third fact is that the Fukuda administration had a hidden schedule to lift unilateral sanctions on June 20, a week after the initial announcement. The administration planned to permit chartered North Korean vessels to enter Japanese ports, involving some limited bi-directional traffic of Japanese and North Korean nationals.<sup>6</sup> The Japanese public saw this as contradictory to the then-established hard-line policy against Pyongyang, and the public's outcry against the lifting ensued instantaneously. As a result, the administration failed to implement the waiver in the end.

The above analysis begs the question as to why President Bush has converted from a hard-liner to an appeaser in North Korea policy, just at the point where an impoverished Pyongyang would be compelled to fully dismantle its nuclear capability, sooner rather than later, as long as the

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<sup>5</sup> - *Ibid.*

<sup>6</sup> - *Ibid.*



hard-line approach involving no economic aids continued. Certainly, Pyongyang may resort to another round of extreme behavior and brinksmanship, but it is cornered. Neither Pyongyang, Washington nor Tokyo, is forced to compromise in the six-party talks. A mainstream view is that President Bush has done this in order to leave a legacy to U.S. history. However, the disillusioned Japanese public is now increasingly aware of the need to develop an independent strategic approach, based on hardheaded analysis and calculation, while acknowledging the significant net utility of the U.S.-Japan alliance for macro-national security. In this context, it is noteworthy to see an emerging Japanese perspective that the mainstream view does not fully account for Bush's underlying motive, instead attaching great importance to a power game over material interests focused on North Korea.

### **Incredulous U.S. Allegations: The North Korean “Supernote”**

With a growing sense of realism among the public, some Japanese analysts have warned of the danger of simplemindedly following the American lead concerning specific policy measures against Pyongyang. This warning is particularly relevant when the Japanese government and the public do not have independent sources to either deny or confirm the authenticity of U.S. policy intelligence and are thus susceptible to biased U.S. intelligence at least or manipulation at worst in making crucial policy decisions.

A former Japanese career diplomat, Harada Takeo, affirms that the U.S. law enforcement policy against the Macau-based commercial bank, *Banco Delta Asia* (BDA), is a point in case.<sup>7</sup> The Bush administration, as its

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<sup>7</sup>- Harada Takeo, *Kitachousen vs. Amerika – Nise-beidoru Jiken to Taikoku no Pawaa · EGeimu* [North Korea vs. The United States – Counterfeit U.S. Bank Notes and a Great Power Game], (Tokyo: Chikuma Shobo, 2008).

North Korea policy shifted from a hard line to one of appeasement, first employed the enforcement fully as a major stick against Pyongyang and then withdrew the stick without adequate explanation. Tokyo was buffeted and possibly manipulated by the Bush administration, using the BDA case to attest to Pyongyang's roguishness, a major factor that induced Tokyo to impose the toughest economic sanctions against North Korea.

Taken in accordance with the Patriot Act, the U.S. measures against the BDA effectively suspended financial transactions between all the U.S. financial institutions and North Korean entities *via* the bank in Macau that the Bush administration alleged was engaged in money-laundering, thereby cutting off Pyongyang from the international networks of financial transaction. The Bush administration was initially tenacious in imposing these measures on Pyongyang, claiming that they were a form of law enforcement authorized under the law of the land, not a form of economic sanction according to international law. Thereafter, however, the administration unhesitatingly terminated the measures as the allegations of Pyongyang's money-laundering became unsustainable due to solid circumstantial counter-evidence. For instance, a report of the Swiss federal counterfeit police, released in May 2007,<sup>8</sup> presented the following analysis:

According to the U.S. Secret Service, \$50 million worth of 'super-fakes' were confiscated worldwide over the past 16 years, only a small portion of them within the United States. Measures against the U.S. annual counterfeit damage of \$200 million, the damage from \$50 million worth of 'super-fakes' is not that significant. The Federal Reserve Bank produces genuine \$100 dollar bills mainly for the foreign market. On their return to the U.S., the issuing bank after examination can easily distinguish the 'supernotes' from originals using banknote testing equipment, due to altered infrared characteristics. For this reason, the United States over the years has hardly suffered economic damage due to the 'super dollar.'

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<sup>8</sup> - Bundeskriminalpolizei Kommissariat Falschgeld, *Falschgeldmeldungen Schweizer Franken Ausländisch Währungen Allegemines 2004/2005*, May 2007.

A (banknote) printing press like one in North Korea can produce \$50 million worth of bills in a few hours. Using its printing presses dating back to the 1970's, North Korea is today printing its own currency in such poor quality that one automatically wonders whether this country would even be in a position to manufacture the high-quality 'supernotes.' The enormous effort put into the making of the 19 different 'super-fakes' that we know of is unusual. Only a (criminal) government organization can afford such an effort. What defies logic is the limited or even controlled amounts of 'exclusive' fakes that have appeared over the years. The organization could easily circulate tenfold that amount without raising suspicions.<sup>9</sup>

Based on the above report and Klaus W. Bender's article published in *Frankfurter Allgemeine Sonntagszeitung* on January 9, 2007,<sup>10</sup> Harada points out that "supernotes" can only be printed by the Intaglio-Stichtiefdruck process, a technology that only the Lausanne-based Swiss company, KBA-GIORI possesses, and also needs to be printed with the ink that the U.S. Bureau of Engraving and Printing blends in an unknown method with the ink exclusively produced by the Lausanne-based company, SICPA.<sup>11</sup> Thus the printing machinery, paper, and ink used to print U.S. currency are highly regulated, made through exclusive contracts with these Swiss companies, and are not available on the open markets. This reflects the fact that the Swiss high-tech security printing industry predominates the international markets in this field.

On the other hand, as Bender writes, there is a consensus among representatives of the security printing industry and counterfeit investigators that North Korea's capacity for printing banknotes is extremely limited.<sup>12</sup> The consensus is consistent with the finding of the Swiss federal

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9- Kevin G. Hall, "Swiss authorities question U.S. counterfeit charges against North Korea," *Knight Ridder Tribune News Service*, May 22, 2007.

10- Klaus W. Bender, "Das Geheimnis der gefälschten Dollarnoten," *Frankfurter Allgemeine Sonntagszeitung*, January 9, 2007. An English translation is available at <http://watching-america.com/frankfurterallgemeine000009.shtml>.

11- Harada, *Kitachousen vs. Amerika*, *op.cit.*, p. 37 and pp. 80-84.

12- Bender, *op.cit.*

counterfeit police that “supernotes” are most likely printed and circulated somewhere other than the Far East. This is a fairly certain finding because the police has confiscated five percent of “supernotes” ever seized across the world.<sup>13</sup> Harada wonders why “supernotes” are limited in circulation, should Pyongyang possess this high-tech counterfeit capability. He even sees the possibility that Pyongyang may have relegated Beijing to print North Korean notes.<sup>14</sup>

As unsubstantiated as the U.S. allegations against Pyongyang are, Harada alleges that the CIA, not North Korea, is counterfeiting U.S. bills. Kevin Hall reported that the Secret Service, the Federal Reserve Board, and the Treasury Department all declined his repeated requests for interviews about the allegation.<sup>15</sup>

In his essay published in one of the popular Japanese weekly journals, Harada even asserts that the CIA has spent “supernotes” as a major source of slush funds for its covert operations to support African countries under pro-U.S. dictatorships in competition with major West European powers and China, a main stream view that he claims is held in European financial circles. He then conjectures that these African states may have spent “supernotes” to purchase arms made in North Korea, the reason why Pyongyang possesses the counterfeit bills in its foreign currency reserves.<sup>16</sup>

To sum up, the Japanese public is now becoming exposed to alternative policy intelligence that is not based on U.S. data-collection and analyses, possibly distorted with biases and/or manipulations. In the context of this paper, it is not crucial to either deny or confirm the allegations if the United States, not North Korea, is counterfeiting U.S. bills. In fact,

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<sup>13</sup> - Harada, *op.cit.*, pp. 34-35.

<sup>14</sup> - *Ibid.*, p. 82.

<sup>15</sup> - Kevin G. Hall, “U.S. counterfeiting charges against North Korea based on shaky evidence,” *McClatchy—Tribune News Service*, January 9, 2008.

<sup>16</sup> - Harada Takeo, “Kitachousensei ‘Nisedorusatsu’ wa CIA ga Tsuku’teita! [The CIA has counterfeited U.S. bills],” *Shuukan Gendai*, February 9, 2008.

neither the allegations against Washington nor those against Pyongyang have been substantiated, and will remain so for the foreseeable future. However, it is quite significant to see that the Japanese public will soon be developing an independent strategic mind-set and then demand that the government conduct a proactive foreign policy in pursuit of Japanese material national interests. In particular, it is noteworthy to realize that the “supernote” issue has had the Japanese public to become increasingly aware of the U.S.-Europe power game over North Korea.

### Direct Investment in North Korea

Before the sanctions were imposed, Chinese and South Koreans used to be prime traders and direct-investors vis-à-vis North Korea,<sup>17</sup> followed by Japanese traders exporting industrial goods essential for the North Korean economy and importing some perishable goods. The state of affairs has changed due to UN and other additional unilateral sanctions against the rogue state in reaction to the ballistic missile and nuclear tests in 2006. Chinese and South Koreans have reinforced their economic positions vis-à-vis North Korea, taking advantage of their governments’ reluctance to execute the stringent sanction measures. This is in marked contrast to the Japanese government that has interrupted all the economic and financial transactions with North Korea,<sup>18</sup> including the regular services of the North Korean cargo-passenger vessel, *Mangyobon*. In fact, the government has diminished Japanese economic leverage vis-à-vis the regime in Pyongyang.

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<sup>17</sup> - *Trade Statistics Yearbook of Democratic People’s Republic of Korea* (Tokyo: World Trade Service, various years).

<sup>18</sup> - Japanese Ministry of Economy, Trade, and Industry, Trade and Economic Cooperation Bureau, “Tai-kitachosuen no Yunyuu-kinshi-sochi-keizoku nitsuite [On the continuation of economic sanctions against North Korea],” mimeo, May 24, 2007, <http://www.meti.go.jp/policy/ampo/kanri/catch-all/shingikai/dai9wg/siryou2.pdf#search=%27%E5%8C%97%E6%9C%9D%E9%AE%AE%20%E8%B2%BF%E6%98%93%E7%B5%B1%E8%A8%88%27>.

West Europeans, not to mention Americans whose government has imposed stringent economic sanctions on North Korea, do not have significant economic relations with North Korea. However, the lack of their visible engagement does not necessarily mean their indifference to the evolving business opportunities in North Korea. To the contrary, as analyzed below, West Europeans have increasingly become eager to build their solid economic presence in the country, particularly in the rare metal and other mineral sectors, in competition with Chinese and South Koreans who had concluded a series of large concessions or signed joint venture project agreements with the regime in Pyongyang,<sup>19</sup> the full development and exploitation of which may lead to the de facto Chinese colonization of North Korea.<sup>20</sup> However, these Chinese plans and activities have so far seriously faltered due to funding and political problems, particularly differing expectations between Beijing and Pyongyang.<sup>21</sup> As a result, while the Chinese presence tends to be overrated, European involvement has been totally underestimated.

As early as in May 2001, the European Union sent a high-ranking delegation to Pyongyang, comprised of the Swedish Prime Minister Göran Persson, Commissioner for External Affairs Chris Patten, and High Representative Javier Solana in charge of the EU's common foreign and security policy. During the visit, these European leaders and Kim Jong-il agreed to launch the process of EU-DPRK economic cooperation, particularly Pyongyang's economic reform through European economic engagement that would most likely include direct investment. In return, as a part of the process, Pyongyang in March 2002 sent a mission of senior economic officials to Brussels, led by Foreign Trade Minister Ri Gwang-gun,

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<sup>19</sup> - ARC Report, *Democratic People's Republic of Korea* (Tokyo: World Economic Information Service, 2007), pp. 54-55.

<sup>20</sup> - Matsumura Masahiro, "Chuugoku niyoru Kitachousen no 'Shokuminchika' [China's colonization of North Korea]," *Jiji Top Confidential*, September 5, 2006.

<sup>21</sup> - ARC Report, *op.cit.*, p. 56.

and the mission met EU Commission officials, representatives of the European Parliament, the European Investment Bank, and the World Bank.<sup>22</sup> Commissioner Patten said:

At the Stockholm European Council last spring, we agreed to enhance the role of the EU in supporting peace, security, and freedom in North Korea. I welcome this week's opportunity for dialogue between Brussels and Pyongyang. The EU is already one of the largest donors of humanitarian aid to DPRK, we have begun exploratory talks on human rights, and now I hope we can help North Korea build for a more prosperous future.<sup>23</sup>

It is obvious that Brussels has gradually developed solid ties with Pyongyang, demonstrated by another high-ranking delegation sent to Pyongyang that included High Representative Solana and German Foreign Minister Frank-Walter Steinmyer at a time in which the country served as chair of the European Council. They met Kim Jong-il at the very moment when U.S.-DPRK bilateral talks were being held in New York and Japanese-DPRK talks were being held in Hanoi.<sup>24</sup>

In October 2007, the then-South Korean President Roh Moo-hyun and North Korean leader Kim Jong-il held a summit meeting in Pyongyang and signed a declaration stressing the need to conclude a peace treaty involving the legal termination of the Korean War. They also reached an accord over further economic cooperation, including the issues of a new special economic zone on the North's west coast, infrastructure improvements, and natural resource development.<sup>25</sup>

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22. "EU/North Korean Relations: Trade Minister Leads Visit to Brussels," The European Union Press Release, IP-02-352, March 4, 2002, <http://europa.eu/rapid/pressReleasesAction.do?reference=IP/02/352&format=HTML&aged=0&language=EN&guiLanguage=en>.

23. *Ibid.*

24. "EU no Daihyodan, Kitachousen wo Houmon [The EU delegation visited Pyongyang]," The EU Press Release (the Japanese language edition), [http://www.deljpn.ec.europa.eu/home/news\\_jp\\_newsobj21117.php](http://www.deljpn.ec.europa.eu/home/news_jp_newsobj21117.php).

25. Declaration on the Advancement of South-North Korean Relations, Peace, and Prosperity, available at <http://www.pcusa.org/worldwide/pdf/nkorea.pdf>.

Just after the summit, Guenter Verheugen, European Union's Industry and Enterprise Commissioner, demonstrated strong and growing European interest in direct investment in North Korea.<sup>26</sup> He was convinced that the North would be able to turn its economic potential to significant growth and development, if political conditions were met: "The regulatory environment is completely unpredictable and it's no certainty that rules are applied in a nondiscriminatory way."<sup>27</sup>

The so-called London-Pyongyang connection exemplifies such European efforts to grasp business opportunities in North Korea. The connection extends into longtime German business contacts with North Korea, dating back to the era of the former East German state. It is often forgotten that today's Germany has inherited the annexed East's legacy that involved diplomatic, economic, and inter-personal relations with North Korea; for example, a Goethe Institute, the German government's cultural exchange organ, is located in Pyongyang and serves as an uncommon window, open for broad information based on a Western and, particularly, European perspective. Grounded in the personal statement of Stanley Au, chairman of the Delta Asia Financial Group, in reaction to the U.S. law enforcement against its affiliate Banco Delta Asia located in Macau, Harada argues that, in the late 1990s, the bank undertook to deal with North Korean gold sales on the international markets in London through the intermediary of a major U.K. commercial bank, Midland Bank. Midland has been successful particularly since 1980 when it acquired a German private banking firm, Trinkaus & Burkhart KGaA. Midland itself was later acquired by the Hong Kong Shanghai Bank (HKSB), part of the prominent international financial holdings of Rothschild.<sup>28</sup>

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<sup>26</sup>- "EU industry commissioner says that North Korea must reform to win European investment," *The International Herald Tribune*, October 5, 2007, <http://www.iht.com/articles/ap/2007/10/06/business/AS-FIN-Koreas-Economy-EU.php>.

<sup>27</sup>- *Ibid.*

<sup>28</sup>- Harada, *Kitachousen vs. Amerika*, *op.cit.*, pp. 53-54.



As a pivotal hub of these connections, the London-based Chosun Development and Investment Fund was created in September 2006, one month before Pyongyang's nuclear test, and got ready to raise \$100 million for the funds, primarily from large investors in Europe and China. Its business focuses on prospective direct investment in North Korean mining, financial, and energy sectors, so that the Kim Jong-il-owned mining companies can obtain facilities and equipment essential to exploit gold, silver, zinc, magnesite, copper, uranium, and platinum; the profit-making is enabled through product-sharing agreements, not the repayment of loans. The Fund is controlled by Colin McAskil, a 67-year-old British businessman who has had business with North Korea since the late 1970s, including his experience as a consultant to North Korean banks on debt negotiations and as a broker in the sale of North Korean gold in London. McAskil is assisted by three directors of Anglo-Sino Capital which operates the Fund; this fund-managing firm is subjected to the supervision of the U.K.'s Financial Service Authority (FSA). In May 2006, McAskil obtained the FSA's regulatory approval for the Fund to make direct investment in North Korean mining, financial, and energy sectors.<sup>29</sup>

McAskil also serves as the chairman of the Hong Kong-based firm, Koryo Asia. This firm controls the banking license of a sole small North Korean joint venture bank with foreign capital, Daedong Credit Bank (DCB), and a 70 percent stake owned by British investors through a Virgin Islands registered company, Phoenix Commercial Ventures. McAskil maintains that the DCB's operation has been profitable for the last 12 years, dealing with some 200 foreign-invested joint ventures, foreign

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<sup>29</sup> - Tamura Hideo, "Taikita-toushi Faundo Anyaku [The fund operating actively behind the scenes: The Case of North Korea]," *Sankei Shimbun*, August, 18, 2008; Donald Greenlees, "Daedong fights U.S.-imposed sanctions on North Korea banks," *The International Herald Tribune*, March 8, 2007; Anna Fifield, "North Korean fund gets U.K. approval," *The Financial Times*, May 29, 2006.

relief organizations, and foreign individuals.<sup>30</sup>

However, McAskil suffered a major setback when the Bush administration imposed law enforcement measures against the Macau-based Banco Delta Asia, to which the DCB deposited \$7 million out of the total asset of \$10 million.<sup>31</sup> He was critical of the measures because the Bush administration did not offer any proof of DCB's wrongdoing and because he believes it was unfair and even constitutes harassment of the DCB's fully legal and legitimate business, free from any illicit practices involving product and currency counterfeiting, drug trafficking, and weapons proliferation.

Along with about 50 North Korean banks, trading companies, and individuals, Daedong Credit had its account frozen. The total amount put into "suspense accounts," according to Banco Delta Asia, was about \$25 million, with Daedong Credit accounting for the largest share. Since then, almost all foreign banks that had correspondent relations with Daedong Credit have severed contact for fear of being excluded from the U.S. financial system.<sup>32</sup>

McAskil revealed some surprising information:

One of the Treasury's main allegations against Banco Delta Asia is that it facilitated the spread of counterfeit \$100 bills. But McAskil said that Daedong Credit had put \$49 million into Banco Delta Asia in 2005 and all that money had been forwarded to HKSB for verification... Only three of the \$100 notes belonging to Daedong Credit were confiscated because they were "suspect," he said.<sup>33</sup>

In the above, McAskil blames U.S. law enforcement for acting against the Macau-based BDA. Though unsubstantiated claims, he is consistent with the aforementioned Bender's and Harada's analyses on the counterfeit

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<sup>30</sup> - Tamura, *op.cit.*; Greenlees, *op.cit.*; Fifield, *op.cit.*

<sup>31</sup> - Greenlees, *op.cit.*

<sup>32</sup> - *Ibid.*

<sup>33</sup> - *Ibid.*

“supernotes” issue. This is especially so when we consider the fact that only three \$100 notes were confiscated out of \$49 million; this corresponds fairly well with the findings of the Swiss federal counterfeit police report.

Following the above critical European views, some Japanese analysts now have come to see that the Bush administration bulldozed the law enforcement measures against the Macau-based BDA in order to tighten an American business grip on prospective investment opportunities for North Korean rare metal and other mineral resources. Hamada gathers that the Bush administration now realizes the need to keep the Kim Jong-il regime alive, so that Americans can establish their vested interests before Korean unification should ever become a reality; otherwise, Chinese and South Koreans would gain most from the underground resources in North Korea.<sup>34</sup> Similarly, Harada understands that the Bush administration has finally begun, though a little late, to wedge itself into the ongoing competition over North Korean underground resources; while the Chinese have already secured a series of important concessions and while Europeans have already launched active direct investment efforts. Harada sees that Washington has striven to bargain face-to-face with Pyongyang and made a deal to open a gate way to North Korea for American business; however, Washington has learned that North Korea needs to be removed from the U.S. list of state sponsors of terrorism for this purpose. Harada’s analysis will return to square one of the current paper’s discussion regarding the best context and framework which we must use in attempting to comprehend President Bush’s proclamation on June 28, 2008.<sup>35</sup>

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<sup>34</sup> - Hamada Kazuyuki, “Beichou-gouji no Ura de Hayakumo Kanetsusuru Kitachousen ‘Rea-Metaru Riken’ Soudatsusen [Unexpectedly early intensification of competition over rare metals in North Korea behind the process of the U.S.-DPRK agreement],” *SAPIO*, July 25, 2007.

<sup>35</sup> - Harada Takeo, “Niwakani Okotsu’ta Interigensu-Buumu no Ura niha Kitachousen-riken wo Nerau Beikoku ga [The United States watches for a chance to get material interests in North Korea behind the current sudden boom of intelligence studies],” *SPA*, July 10, 2007.

## **Intensifying American-European Competition**

Since the early 1990s onwards, Americans and Europeans have vied head-to-head for business opportunities in North Korea. In 1991, the United Nations Development Programs formulated a development plan centered on the Tumen River, and, as a part of the plan, the North Korean government created the Rajin-Sonbong Economic Special Zone near the area where the Chinese, Russian, and North Korean borders meet. As of May 1996, the Royal Dutch Shell (a British-Dutch capital) and the Stanton Group (a U.S. firm) had contracts to make direct investments in the Zone, though the contracts did not materialize due to a series of economic sanctions in reaction to Pyongyang's brinksmanship.<sup>36</sup> Hamada understands that, in June 1998, with a grant from the Rockefeller Foundation, the U.S. National Mining Association made a field survey in North Korea, and that the Foundation and the Association paid \$5 million to obtain prospecting rights for rare metal and mineral resources from the North Korean authorities.<sup>37</sup> Without the sanctions, it was anticipated that the Clinton administration was going to authorize Stanton's contract<sup>38</sup> and the continued prospecting.

In fact, the Bush administration was once poised to give a green light to American big business to make direct investments in North Korea. James Kelly, then-Assistant Secretary of State for East Asia and Pacific Affairs, was reported to have assured that the Bush administration would not block McAskil, who planned to form the aforementioned Chosun Fund at that stage, from making direct investment in the country, as long as such investment was observant of U.S. laws and regulations. McAskil scheduled to base the Fund in the United States, but American investors withdrew from participating in the Fund shortly before its inception, when the Pyongyang's

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<sup>36</sup> - *Sankei Shimbun*, May 15, 1996.

<sup>37</sup> - Hamada, *op.cit.*

<sup>38</sup> - *Nikkei Shimbun* (the evening edition), April 18, 1997.

enriched uranium program was revealed in October 2002. McAskil was then forced to move to London. Similarly, it was also reported that big American businesses, such as Cargill (crops and mineral resources), Bechtel (construction), Goldman-Sachs, and Citigroup had demonstrated strong interest in investing in North Korea.<sup>39</sup>

For the last several years, U.S.-European competition over North Korean underground resources has become increasingly intensified under the condition of deepening globalization. Three billion peoples in the rapidly growing countries of Brazil, Russia, India, and China (the so-called BRICs) are concurrently consuming colossal amounts of natural resources and other raw materials for industrial activities, fueling skyrocketing commodity market prices that have been exacerbated by uncontrollable international speculation. For example, with oil price skyrocketing, the price of uranium ore has gone up tenfold over the last five years as a result of the boom in nuclear power generation, a major counter-measure against global warming.<sup>40</sup> North Korea possesses in underground reserves, for example, 1,000-2,000 tons of gold, 3,000-5,000 tons of silver, 2,150,000 tons of copper, 600,000 tons of tungsten, 2-4 billion tons of iron ore, 6 million tons of graphite, 100 billion tons of limestone, 30-40 thousand tons of magnesite, 11 billion tons of anthracite coal, and 26 million tons of uranium ore, as well as oil reserves estimated around 60 billion barrels.<sup>41</sup> There also exist good reserves of many major rare metals essential for high-tech products.<sup>42</sup>

With interest in North Korea growing, foreign investors have become more willing to take risks, to the extent that they dare to purchase bonds that

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<sup>39</sup> - *Sankei Shimbun*, July 6, 2008.

<sup>40</sup> - *Chosen-Ilbo* (the Japanese online edition), November 22, 2007, <http://www.chosunonline.com/article/20071122000040>.

<sup>41</sup> - *Chosen-Ilbo* (the Japanese online edition), July 9, 2007, quoted in Harada, *Kitachousen vs. Amerika ...*, *op.cit.*, p. 160; *Chosen-Ilbo*, *op.cit.*, November 22, 2007; Hamada, *op.cit.*

<sup>42</sup> - Kimura Mitsuhiro and Abe Keiji, *Kitachousen no Gunji-kougyouka – Teikoku no Sensou kara Kimu Nitsu'sei no Sensou he* [North Korea and militarization – The war of the Japanese empire to the war of Kim Jong-il], (Tokyo: Chisen Shokan, 2003).

have been secured with loans given to North Korea in the past. In July 2007, the bond's market price rose from 21 cent per unit to 26 cent, while the face value is one dollar. In March 1997, this bond was originally arranged by the Banque National de Paris (BNP), which was later merged with the Paribas to become the BNP Paribas, one of the largest financial institutions in the euro zone. The Banque secured North Korea-related loan bonds held by financial institutions across the world, into 777 million DM-worth bonds. The London-based Exotic Limited, a securities firm specializing in brokering illiquid loans, equity, and bonds, deals this financial product.<sup>43</sup>

After President Bush's proclamation on June 26, 2008, international investors, particularly Europeans and Americans, are trying to secure mining rights in North Korea prior to the actual removal of the country from the U.S. list of state sponsors of terrorism and the lifting of the sanctions against the country. This proclamation has reduced considerably a sense of the caution among American investors about the country risk and made it easier to invest in the country via London. There are accelerated efforts in London and Hong Kong to establish such funds one after another. In particular, some of them are aimed at obtaining uranium mining concessions, to the extent that John Bolton is concerned with the private sector-led natural resources development in North Korea, including uranium ore, and the related international financial channels: Pyongyang would be able to earn hard currency by producing and exporting yellow cake, involving serious nuclear proliferation.<sup>44</sup> A Washington-based investment consultant specializing in Asia sees that there will soon be growing enthusiasm in the United States to establish investment funds targeting North Korea.<sup>45</sup>

Sooner or later, the Japanese government will be forced to take a

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43- Kuroda Ryo, "Kitachousen Saiken ga Hisokana Ninki-shouhin ni [The North Korea-related loan bond has unobtrusively become a popular product]," *Nikkei Business Online*, May 8, 2007, <http://business.nikkeibp.co.jp/article/topics/20070507/124220/>.

44- *Sankei Shimbun*, *op.cit.*, July 6, 2008.

45- Tamura, *op.cit.*

geo-economic approach to North Korea, on the grounds that individual and institutional Japanese investors have already channeled their limited capital to the aforementioned North Korea-related bonds in pursuit of profits.<sup>46</sup> It would be no surprise if they had done so with similar investment funds. As political impediments to investing in North Korea diminish over time, the interest of Japanese investors will exponentially grow, rather than wane.

### **A Japanese Edge in the Competition**

The Japanese business community and the state have good potential to excel in international competition over North Korea, should they take full advantage of being the former suzerain status of the prewar Korea that was annexed to the Japanese Empire for 35 years. Generally speaking, a former suzerain state possesses close and inseparable links with its former colonies and dependent territories, because the former once set up the latter's political, economic, and social systems, ranging from infrastructure (railways, roads, dams, and power plants) to education to science & technology to food and culture. This applies very well to Japan's links with North Korea, and means that the Japanese also have extensive experience in organizing industrial complexes there. During the annexation era, Japanese direct investment concentrated in the North, ranging across-the-board from power generation to mining to chemical production to steel plants, among others. This was not the case in the South as the area was predominantly agrarian without any significant natural resources. (However, it is highly questionable whether Japanese investors reaped sufficient returns and profits on their investments since the Japanese rule ended much earlier than expected due to the defeat in the Great Asian War, and since then their assets in today's North Korea were all seized.)

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<sup>46</sup> - *Ibid.*

In particular, it is Japan, not the United States nor European countries nor China nor South Korea, that retains the most critically detailed information on the North's underground resources due to the legacy of the Japanese Empire. By using remote-sensing from outer space, Americans can find that there exist significant mineral resources in North Korea. However, they are unable to know which and how much of each resource exists exactly where; this is the kind of information only attainable by extensive on-site geological surveys and the mapping based on the data thereof. Over the last several years, the U.S. government has kept demanding the Japanese government release such geological maps. According to Japanese government sources, American experts, who conduct research commissioned by the U.S. Department of Defense or American corporations, have often visited the Japanese National Diet Library and the Japanese National Archives to examine geological studies carried out by the Japanese imperial authorities in the formerly annexed Korea.<sup>47</sup>

The similar prewar geological data on uranium was critically important for the early Soviet nuclear weapons programs. The Japanese imperial military processed monazite ore containing uranium at chemical plants located in the North's Hungnam area for its embryonic nuclear weapons program. The Soviet Red Army seized the plants immediately after the entry into the war against the imperial Japan, and the U.S. forces bombed the plants completely after the breakout of the Korean War. After the first nuclear test in 1949, the Soviet Union reinforced its nuclear power status by importing some 9,000 tons of uranium ore from North Korea. Stalin came to know of the North's uranium reserves after he obtained the aforementioned Japanese-compiled data in the northern part of occupied Korea after 1945. Today, Pyongyang's regime still utilizes the same uranium reserves and the legacy facilities and technologies for its own nuclear

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<sup>47</sup> - Hamada, *op.cit.*; Tamura, *op.cit.*



programs. It is known that the Japanese monazite processing technology has been inherited by a joint venture enterprise located in the same Hungnam area, established by a Kim Jong-il-owned firm and a firm related to the association of North Korean residents in Japan.<sup>48</sup>

Beyond these specific edges, the Japanese yen retains significant credit among North Koreans, despite their seemingly unflinching anti-Japanese attitude to Japan in general and Japanese imperialism in particular. The empire controlled the seigniorage of the annexed Korea for 35 years through the Bank of Korea, a leading special bank chartered by the empire as a prime instrument of its rule.<sup>49</sup> Together with the other similarly-chartered banks across the empire and beyond, Japan formed a region-wide yen-bloc centered on the empire. Inheriting this legacy, North Koreans under the postwar Stalinist regime long utilized the yen for trade with Japan and the hoard of their financial assets, certainly without its wide domestic currency. Cash and reserve holdings in yen were essential to purchase not only Japanese goods and services for the regime's elites, particularly durable consumer goods, but also dual-use industrial products extensively utilized for military purposes. An exemplar is a special operations North Korean mini-sub found aground on the South Korean coastal shallows that carried a Japanese-made GPS/chart plotter-device designed for small fishing crafts.<sup>50</sup>

Thus it is obvious that the yen will be a far stronger Japanese leverage tool once the government begins to channel massive economic aid to North Korea, involving the related bilateral trade, according to the terms and conditions of the Pyongyang Declaration signed between Prime Minister Koizumi and Kim Jong-il: Pyongyang has to resolve the nuclear, ballistic

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<sup>48</sup>- Tamura, *Ibid.*

<sup>49</sup>- Tatai Yoshio, *Chousen-Ginkou* [The Bank of Korea], (Tokyo: PHP Kenkyujo, 2002).

<sup>50</sup>- *Scoop* (a T.V. news program), Terebi Asahi (Television Asahi), February 22, 1999. The summary is available at <http://www.tv-asahi.co.jp/scoop/>.

missile, and abduction issues.<sup>51</sup> There is an understanding that, given the adjusted value of Japanese aid to South Korea upon bilateral diplomatic normalization, the aid to the North may reach some \$9 billion, including grant aid and long-term loans with low interest.<sup>52</sup> There is no doubt that such an amount of Japanese aid will exceed those of the other members of the six-party talks and, probably, all of their aid combined. And the Japanese competitiveness over North Korea will be significantly magnified when the aid targeting infrastructure building and human resources development are combined with trade and direct investment linked with industrial production, a synergy between the government and the private sectors in aid and development. Such an approach once characterized Japanese aid policy to the developing world,<sup>53</sup> and Tokyo is certainly able to use it again.

## Conclusion

Hitherto, this paper has analyzed some major factors pushing the Japanese government to the adoption of a geo-economic approach to North Korea. First, the Japanese public has become increasingly disillusioned with the Bush administration's excessive appeasement found in the recent sharp turn in North Korea policy. Second, the Japanese public has been exposed to an alternative perspective about the U.S. allegations of North Korea's counterfeiting activities, and is becoming incredulous of the allegation. The Japanese public has a growing sense of being manipulated by the U.S. North Korea policy. Thus, the first and second factors have made the public aware of the need to secure a more independent hand in North Korea policy, while accepting the U.S.-Japan alliance as the backbone of Japan's national

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<sup>51</sup> - Japan-DPRK Pyongyang Declaration, September 12, 2002, [http://www.mofa.go.jp/region/asia-paci/n\\_korea/pmv0209/pyongyang.html](http://www.mofa.go.jp/region/asia-paci/n_korea/pmv0209/pyongyang.html).

<sup>52</sup> - *The Toukyou Shimbun*, October 26, 2000.

<sup>53</sup> - Masahiro Matsumura, *Japan and the U.S. in International Development, 1970-1989* (Osaka: St. Andrew's University Research Institute, 1997).

security. Third, North Korean underground resources have attracted growing interest of international investors, especially Europeans through the so-called London-Pyongyang connection. Fourth, Europeans and Americans investors have intensified their competition over business opportunities in North Korea. Fifth, Japanese business and the investors have a strong edge over European, American, and other competitors due to the legacy of Japan's being the North's former suzerain state. This involves possession of detailed information, extensive industrial experience, and other latent and potential economic links with the North.

Certainly, Japan's North Korea policy won't easily shift its basic thinking from geopolitics to geo-economics in the immediate future. This is because the current Japanese approach is firmly grounded on a die-hard geopolitical calculation with a primary focus on the nuclear, ballistic missile, and abduction issues. Tokyo will unquestionably adhere to the principles, terms, and conditions of the 2002 Pyongyang Declaration, and will never provide its aid unless Pyongyang satisfies these conditions. However, the approach is neither static nor permanent. The six-party talks process has forced and will constrain Pyongyang to resolve the three issues, while the current priority is placed on the nuclear issue. The process will most likely proceed in the long run, however slowly it does; it may confront Pyongyang's occasional brinksmanship and even experience serious setbacks. When the process makes significant progress and when the level of geopolitical tensions lowers significantly, Tokyo will surely attach special weight to geo-economic factors in redefining Japanese national interests and adjusting its North Korea policy accordingly. Alternatively, Tokyo will also react very similarly, should the Pyongyang regime collapse abruptly and if a new regime accepts the regional status quo. This prospect will hold unless a new regional Cold War emerges, such as one precipitated by a severe Sino-U.S. rivalry.

This paper has discussed a probable geo-economic shift in the long

run in Japan's North Korea policy. However, how the Japanese government can actually adopt, establish, and even pursue its new strategy is beyond the scope of this paper, particularly because its current strategic approach is in stalemate amidst the abduction issues. It remains to be seen whether Japanese leaders take preemptive policy initiatives or whether they are constrained to emulate the geo-economic behavior of other major powers as late comers. Thus, policy makers and analysts are advised to pay due attention to an emerging geo-economic power game centered on North Korea and an evolving Japanese geo-economic pattern of thinking that remains largely latent at this time.

■ Article Received: 10/6 ■ Reviewed: 11/19 ■ Revised: 11/28 ■ Accepted: 12/1

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