

*China-North Korea Economic Relations during the Hu Jintao Era**

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Abstract

One of the major features of the relations between China and North Korea since the inception of Hu Jintao's leadership in Beijing has been their rapid expansion of economic exchanges. South Koreans are looking at the expanding economic relations between China and North Korea with growing unease. China's economic exchanges with North Korea will certainly grow in the days ahead, but this will not necessarily be accompanied by an attempt to subordinate the North Korean economy. The continued expansion of China-North Korea economic ties can result in economic institutions and regulations conducive to the opening of North Korea's economy. On the other hand, certain negative factors should not be overlooked. The South Korean government and enterprises should take a "strategic approach" toward North Korea with a broader vision. A strategic approach is different from a market-oriented approach in that the former seeks to build foundations for Korean reunification and counter reactions from neighboring countries. There is no doubt that the first prerequisite for such an approach is unfreezing relations between the two Koreas.

Key Words: China, North Korea, Hu Jintao, economic relations, economic exchanges

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Introduction

One of the major features of the relations between China and North Korea since the inception of Hu Jintao's leadership in Beijing has been their rapid expansion of economic exchanges. China's investment in North Korea has grown dramatically along with exports to its neighbor. Until the early 2000s, during the rule of Jiang Zemin, China was almost on par with Japan as a trading partner of North Korea. But with the eruption of the second nuclear crisis involving North Korea, relations between Pyongyang and Tokyo quickly deteriorated and their bilateral trade came to a standstill. In contrast, exchanges between China and North Korea increased in several areas and China became the largest trading partner of North Korea. More than 80 percent of consumer goods now being circulated in North Korean markets are known to be Chinese products.¹

Economic exchanges between China and North Korea have noticeably increased while their overall relations have been strained because of various troubling issues, including the nuclear question, ideological differences and leadership successions. Economic relations between the two neighbors are by no means balanced. They consist of one-sided Chinese investment in the North and North Korea's almost exclusive dependence on China in trade. This unique arrangement has continued to persist during the Hu Jintao era despite the growing political tension between the two countries.

South Koreans are looking at the expanding economic relations between China and North Korea with growing unease. They are afraid that North Korea may eventually be economically subjugated to China.²

¹- International Crisis Group, "China and North Korea: Comrades Forever?" *Asia Report*, No. 112 (February 1, 2006), p. ii.

²- Kim Tae-ki, "North Korean Economic Subordination to China," *MunHwa Ilbo*, February 1, 2006; Choi Choon-heum, "New Moves in Relations Between N.K. & China," *Vantage*

Such apprehension has increased in South Korea as inter-Korean economic cooperation has declined with the freezing of overall North-South relations since the inauguration of the conservative Lee Myung-bak administration in Seoul. However in 2009, China shipped 519,814 tons of crude oil to North Korea and China's trade and aid have become crucial to North Korea's survival, especially as its ties with South Korea have frayed. Moreover, developments such as China's Northeast Project, a government-supported research program to review Korea's historical claim on northeastern China, have heightened a China phobia among South Koreans.

This paper intends to determine the context and the manner by which China and North Korea have broadened their bilateral economic exchanges since Hu Jintao became president and to analyze the significance of these developments. This study will first examine the motivations behind China's economic thrust into North Korea on the basis of its domestic and external circumstances. Second, this study will look into the characteristics of China's trade and investment to identify the depth of its involvement in the North Korean economy, and third, it will observe reactions in South Korea toward these economic changes in the North. Finally, this study will assess the positive and negative factors in the increasing economic cohesiveness between China and North Korea in order to suggest how the South Korean government can strategically approach this complicated question.

Background and Purpose of Exchanges

Background of Expanding Bilateral Exchanges

North Korea's external position has been aggravated to an unprecedented extent since Pyongyang created a security crisis in Northeast Asia with its nuclear tests and missile launches. In an extremely adverse situation, North Korea clings to economic cooperation with China, which is its only lifeline for survival. From a Chinese viewpoint, however, North Korea remains unattractive as an investment market. North Korea's mineral resources, such as iron ore and coal, and the potential value of its ports as possible shipping terminals of Chinese products offer little incentive for large-scale investment of Chinese capital.³ So what is behind China's steadily growing economic presence in North Korea? The most important force is the "strategic judgment" of the Communist Party of China.⁴

China's economic cooperation with North Korea has been guided not by any profit-seeking market principles but by the strategic decisions of the nation's leadership. Chinese leaders in recent years have made it clear that advancement of relations with North Korea is strategically important for China. During Kim Jong-il's visit to China in April 2004, Premier Wen Jiabao declared that the Chinese government "positively encourages Chinese enterprises to engage in mutually beneficial cooperative projects with North Korea in diverse ways."⁵ In March 2005, the two countries signed an agreement on the "encouragement and protection of

³- Kim Jong-oh, "The Chinese Government's Strategy on the Korean Peninsula and Concerns about Dominating the North Korean Economy," *Sino-Soviet Affairs*, Vol. 30, No. 1 (Spring 2006), p. 100.

⁴- Some Chinese scholars insist that China-North Korea economic ties are the result of market-oriented decisions by Chinese enterprises. See Liu Ming, "Deepening China-North Korea Economic Ties: Trends, Characteristics, and Its Interaction with the Inter-Korean Economic Community," Discussion Papers, KIEP, October 30, 2007.

⁵- *Renmin Ribao*, April 22, 2004.

investments” and agreed to establish a “joint committee on economic cooperation.” Hu Jintao stressed during his summit talks with Kim Jong-il in October 2005 that “it is the firm strategic policy of the Chinese Communist Party and government to steadfastly develop close China-North Korea relations.”⁶

These remarks by China’s top leaders indicate that they plan to shift the focus of their economic relations with North Korea from aid programs and trade to investment. From a future-oriented strategic judgment, China revealed its intention to simultaneously pursue economic interests as well as diplomatic and security cooperation with North Korea, breaking away from the ideologically-based unconditional alliance of the past. It is now evident that Beijing is seeking qualitative change in its North Korea policy with a view to securing practical economic interests while trying to ensure regional stability.

While barter trade in goods dominated economic cooperation between China and North Korea in the past, economic exchanges in the Hu Jintao era have taken the shape of development support, as in the construction of the Daean Glass Plant, joint petroleum exploration in the Yellow Sea, and Chinese enterprises’ mine development projects in the North. China is also participating in joint infrastructure construction projects, including ports, and unlike in the past, the central government in Beijing has become involved in many of these cases. All these activities attest to the policy of the fourth-generation Chinese leadership to pursue national interests and economic benefits rather than ideology.

As for North Korea, the isolated regime has had to lean harder on China for its survival in the face of formidable pressure from the United States and Japan since the nuclear conflict emerged. U.S. financial sanctions, including the freezing of the North’s Banco Delta Asia accounts

⁶- *Renmin Ribao*, May 29, 2005.

over its suspected money laundering, pushed North Korea further toward China, its only patron in the international community. Kim Jong-il's visit to China in January 2006 was an open gesture by the North Korean leader to reconfirm his country's link to China under mounting international ostracism. Kim called for an expansion of bilateral trade and investment at a time when relations between the United States and North Korea were taking a turn worse with the delayed implementation of the six-party agreements on the disabling of North Korea's nuclear facilities.⁷

At that time, Kim reportedly asked Chinese leaders to increase cooperation in energy and resources, infrastructure, tourism resources, high-technology industries, agriculture, and labor-intensive industrial estates. On the other hand, Wen Jiabao clarified three principles for Chinese-North Korean economic cooperation: "government initiatives, corporate participation and market operations."⁸ This meant that, in a departure from the unilateral trade of the past, China would prefer investing in profit-generating projects in accordance with market principles.

It was Beijing's judgment that it could benefit politically as well as economically by strengthening ties with North Korea and improving the economy of its neighboring country. Without strategic decisions by the party and the government, there could have been no such steps toward a country with such an adverse investment environment.

China's Objectives

The Chinese Communist Party and government had complicated objectives in ramping up economic exchanges with North Korea. Those objectives were based on the dual goals of China's North Korea policy: the

⁷- Paik Hak Soon, "Kim Jong-il's China Visit and Changes in the North Korean Survival Strategy," *Sejong Commentary*, No. 36 (January 16, 2006).

⁸- *Renmin Ribao*, January 19, 2006.

stable maintenance and management of the North Korean system and the increase of China's influence over North Korea.⁹

Despite the shift in its traditional relations with North Korea at the end of the Cold War, China has regarded the possible collapse of the North Korean regime as a problem with grave consequences for its interests. China wishes to prevent North Korea's collapse because a destabilized Korean Peninsula would directly affect its ultimate national objective of economic development. Millions of North Korean refugees swarming into China would hamper China's economic growth and China could face turmoil beyond its control due to festering internal issues such as income disparities, regional differences in development, unemployment and bureaucratic corruption. China therefore has more reason to prevent North Korea's collapse than any other country in the world.¹⁰

China is also obliged to support economic stability and maintenance of the political status quo in North Korea because Beijing regards its next-door neighbor as a military-geographic 'buffer zone' for its own national security.¹¹ Its intervention in the Korean War was aimed at preserving the crucial buffer zone, according to Chinese strategists. China's security situation requires a buffer zone to insulate itself from the sphere of influence of the United States. North Korea's strategic role and significance as a buffer zone may have diminished in the changing

⁹- For China's North Korea policy, see Jun Byoung Kon, "China's Korean Peninsula Policy in the Post-Cold War Era," *The Journal of Chinese Studies*, Vol. 44 (2008), pp. 379-392; Moon Heung-ho, "Hu Jintao's Views and Policy toward North Korea," *Sino-Soviet Affairs*, Vol. 33, No. 2 (Summer 2009), pp. 15-44; Park Byung-Kwang, "China's North Korean Policy: Keynotes and Perceptions on the Nuclear Issues during the Hu Jintao Era," *Unification Policy Studies*, Vol. 19, No. 1 (2010), pp. 55-78.

¹⁰- Wu Baiyi, "China on the Korean Peninsula: Interests and Role," *The Korean Journal of Security Affairs*, Vol. 11, No. 1 (June 2006), pp. 61-81.

¹¹- Alastair Iain Johnston, "Is China a Status Quo Power," *International Security*, Vol. 27, No. 4 (Spring 2003), p. 42; You Ji, "The Military Aspects of China's Strategy of Peaceful Development and Increasing Chinese Influence on the Korean Peninsula," *Strategic Studies*, Vol. 14, No. 2 (2007), pp. 52-78.

international environment since the end of the Cold War, but China still finds no fundamental change in the strategic value of the northern half of the Korean Peninsula. China cannot afford to overlook North Korea's struggles with international isolation and extreme economic adversity. It has had to strengthen economic exchanges and cooperation with its beleaguered ally in order to help it maintain its socialist regime and stability.

China's North Korean policy seeks to maintain and strengthen its influence over North Korea.¹² China wants to establish its image as a global power by securing a strong influence over the Korean Peninsula including North Korea, thus earning the status of a 'responsible major power' in the region. In the Hu Jintao era in particular, China is striving to increase its international influence on the basis of its economic growth. In this process, North Korea and the Korean Peninsula could be China's base to expand its influence and a stepping-stone in moving onto the global stage. In the course of tackling the North Korean nuclear problem, Beijing has tried to demonstrate that it is the only power that can control North Korea. Since the second nuclear crisis erupted in 2002, China has played an active role in seeking a resolution, arranging the six-party talks to demonstrate its influence over the Korean Peninsula.¹³

By keeping North Korea under its sphere of influence, China hopes to deepen the North's political, economic and military dependency. Chinese efforts in that direction have resulted in the restoration of personal ties between the two countries through meetings of their top

¹²- China's provision of food and energy, given as grants or sold at "friendly prices," has been central to the survival of the North Korean regime. It is hard to assess to what extent such aid can be directly translated into Beijing's explicit influence over Pyongyang, however. There is no doubt that, so far, China has been potentially more influential than any other major country.

¹³- Shin Sang-jin, "China's Diplomatic Strategy in the Six-Party Talks on North Korean Nuclear Issue," *National Strategy*, Vol. 11, No. 2 (Summer 2005), pp. 29-54.

leaders, and their mutual trust and economic cooperation. Undoubtedly, Chinese Premier Wen Jiabao's visit to North Korea in October 2009 also reflected China's intention to increase its influence over the North. Beijing would not allow Pyongyang to fall under the influence of any other country. The acceleration of economic cooperation between China and North Korea in the Hu Jintao era attests to Beijing's move to enlarge its political leverage over Pyongyang to be used in times of need. Beijing wants to maximize the effect of its "North Korea card" in the fluid situation in Northeast Asia.¹⁴

At the same time, China's support of the North Korean economy is also related to its new national economic development plans regarding its northeast territory. The three northeastern provinces of Liaoning, Jilin and Heilongjiang, which are traditionally strong in heavy industries and therefore have a higher proportion of state-owned enterprises, have fallen behind in market economic development and have relatively less foreign investment. In November 2002, the 16th National Congress of the Communist Party of China formally adopted a strategy to revive the northeastern provinces.¹⁵

Just as China strongly pushed its plan for western regional development during the Jiang Zemin era, the Hu Jintao government is championing development of the northeastern provinces as a core economic policy. The Chinese government believes more trade and

¹⁴- Bonnie Glaser, Scott Snyder, John Park, *Keeping an Eye on an Unruly Neighbor*, USIP Working Paper (January 3, 2008), p. 8; Park Byung-Kwang, "China's Standpoint on the Improvement in North Korea-U.S. Relations after the February 13 Agreement," *Unification Policy Studies*, Vol. 17, No. 2 (2008), p. 48.

¹⁵- For the Chinese Northeast Development Project, see State Council, "Periods Prior to and after the Announcement of the State Policy of Revitalizing the Northeast," *21 Century Economic Reports*, <http://www.sina.com.cn> accessed on October 10, 2009; Dong Lisheng, "China's Drive to Revitalize the Northeast," *China Perspectives* (March-April 2005), <http://chinaperspectives.revues.org/document462.html> accessed on March 2, 2010; Jin Byung-jin, "The Results and the Prospects of the Northeast Revitalization Plan of China," *Journal of Northeast Asian Studies*, Vol. 47 (2008), pp. 5-31.

investment in North Korea will help boost the northeastern provinces. North Korea's rich mineral resources also provide outstanding momentum to expand economic relations. Therefore China is expected to advance major cooperative projects agreed upon during Premier Wen Jiabao's visit to the North last year and quicken the construction of infrastructure in border areas. The main message from Wen Jiabao's visit was that the CCP would bolster the stability of the WPK through a comprehensive bilateral relationship centered on expanding economic engagement. In practice, pursuing the goals of Xiaokang and securing strong bilateral commercial ties have resulted in a close localized connection between North Korea's Hamgyongbuk-do and Jilin province. The symbiotic relationship that exists between these two border provinces can be characterized as "Ham-Ji" - a sub-regional area where the border is relatively porous and conducive to coping mechanism-type activities such as trade in the nascent DPRK markets. After Wen Jiabao returned to Beijing in January 2010, North Korea merged two northern cities, Rajin and adjacent Sonbong, to form its first "special city," known as Rason. And in March, North Korea opened the Rajin port to China and granted it open use of its five docks for ten years.¹⁶

Present Situation and Characteristics of Economic Exchanges

Present Situation

Political relations between Beijing and Pyongyang cooled after China normalized ties with South Korea in 1992. Trade between China and North Korea declined sharply, with China only supplying strategic items such as crude oil and food to North Korea in limited amounts. The

¹⁶- Lee Kwang-ho, "Kim Jong-il's Five-Day Trip to China," *Vantage Point*, Vol. 33, No. 6 (2010), pp. 4-5.

situation did not improve until a visit to Beijing by Kim Yong-nam, standing committee chairman of North Korea's Supreme People's Assembly in June 1999. After Hu Jintao succeeded Jiang Zemin, political and economic relations were significantly restored through exchanges of high-level visitors between the two nations, which led to major agreements on economic cooperation.¹⁷

When Kim Jong-il visited Beijing in April 2004, the leaders of the two nations discussed economic cooperation and trade promotion between their countries. In March 2005 when North Korean Premier Pak Bong-ju visited China, the two governments signed an "investment protection agreement" and agreed to establish a "joint economic cooperation committee." In October that year, Chinese Vice Premier Wu Yi visited North Korea and promised development aid in the three heavy industry sectors of mining, iron and steel, and port development. Kim Jong-il's visit as the top leader of North Korea in January 2006 demonstrated the full restoration of traditional ties between the two countries and further accelerated Chinese investment in North Korea.¹⁸

The trade volume between the two countries, which had bottomed out at \$370 million in 1999, increased to \$490 million in 2000, \$740 million in 2001, \$1.02 billion in 2003, \$1.69 billion in 2006, and \$2.78 billion in 2008. During this period, North Korea's trade dependence on China also increased from 25 percent in 1999, passed the 50 percent mark in 2005, and jumped to 67.1 percent in 2007 (51 percent when inter-Korean trade is taken into account). The increased weight of trade

¹⁷- Of course the Hu Jintao-era restoration of relations with the DPRK is not a return to the "blood oath relationship" of the past, but rather a "stealthy but slow," barely perceptible change in the traditional bilateral relations between the two countries. Jae Ho Chung, "China's Korea Policy under the New Leadership: Stealth Changes in the Making?" *The Journal of East Asian Affairs*, Vol. 18, No. 1 (Spring/Summer 2004), pp. 1-18.

¹⁸- Choi Soo Young, *North Korea-China Economic Relations Expansion and South Korea's Corresponding Plan* (Seoul: Korea Institute for National Unification, 2007), pp. 8-10.

with China in North Korea's overall trade volume has been mainly due to the shift of its exports to China from Japan following the deterioration of relations between Tokyo and Pyongyang.¹⁹ As international aid decreased amid the dispute over its nuclear arms development, North Korea came to depend more on Chinese food and oil supplies. The relatively lower prices of Chinese products and advantageous conditions for transactions and logistics also contributed to the swelling of trade volume with China.

Table 1. North Korea's Trade with China, 1990–2009

(in \$US thousands, %)

Year	Export to China		Import from China		Total		Balance
	Amount	Increase	Amount	Increase	Amount	Increase	
1990	124,580	-	358,160	-	482,740	-	-233,580
1991	85,670	-31.2	524,780	46.5	610,450	26.5	-439,110
1992	155,463	81.5	541,107	3.1	696,570	14.1	-385,644
1993	297,290	91.2	602,350	11.3	899,640	29.2	-305,060
1994	199,217	-33.0	424,523	-29.5	623,740	-30.7	-225,306
1995	63,606	-68.1	486,187	14.5	549,793	-11.9	-422,581
1996	68,638	7.9	497,029	2.2	565,667	2.9	-428,391
1997	121,610	77.2	534,680	7.6	656,290	16.0	-413,070
1998	57,313	-52.9	355,705	-33.5	413,018	-37.1	-298,392
1999	41,709	-27.2	328,660	-7.6	370,369	-10.3	-286,951
2000	37,214	-10.8	450,824	37.2	488,038	31.8	-413,610
2001	166,797	348.0	570,660	26.6	737,457	51.1	-403,863
2002	270,685	62.3	467,309	-18.1	737,994	0.1	-196,624
2003	395,344	46.1	627,583	34.3	1,022,927	38.6	-232,239
2004	585,703	48.2	799,503	27.4	1,385,206	35.4	-213,800
2005	499,157	-14.8	1,081,184	35.2	1,580,341	14.1	-582,027
2006	467,718	-6.3	1,231,886	13.9	1,699,604	7.5	-764,168
2007	581,521	24.3	1,392,453	13.0	1,973,974	16.1	-810,932
2008	750,121	29.7	2,030,516	46.0	2,780,637	40.9	-1,280,395
2009	793,247	5.1	1,888,256	-9.6	2,681,738	-3.8	-1,095,009

Sources: KOTRA, KITA.

Note: Excludes exchanges between North and South Korea.

¹⁹- Korea Trade-Investment Promotion Agency, *North Korea's Foreign Trade Trends 2004* (Seoul: KOTRA, 2005), p. 39.

On item of note in the expanding economic relations between China and North Korea is the rapid increase in the number of Chinese enterprises investing in North Korea since 2003. By the end of the 1990s, only a handful of Chinese companies had invested in restaurants, fish farms and retail businesses in North Korea in spite of the North Korean policy to induce foreign investment.²⁰ Chinese investment began to increase in both volume and variety after July 1, 2002, when North Korea introduced a package of economic improvement measures which allowed independent accounting and asset management for enterprises. Since then, China has invested mostly in the services, construction materials, packaging, marine farming and mining sectors. The largest investment to date was a 50 million yuan investment by the Shenyang Zhongxu Group in the Pyongyang First Department Store after seven years of preparations. Investment in iron ore and coal mining has recently been soaring to meet rising demand in China.

Table 2. China's Investment Trends in North Korea

(in \$US millions)

Year	1999	2001	2002	2003	2004	2005	2006	2007	2008
Amount	0.61	2.6	1.5	3.5	14.1	6.5	11.1	18.4	41.2

Sources: Ministry of Commerce of the People's Republic of China; Statistical Bulletin of China's Outward Foreign Direct Investment; UNCTAD.

China's officially recorded investment in North Korea only amounted to \$3.5 million from five companies in 2003. The total volume grew to \$14.1 million in 2004, and the aggregate total reached \$41 million in 2008. The size of Chinese investment in North Korea remains far smaller than the trade volume between the two countries. The proportion of

²⁰- Choi Soo Young, *The Expansion of North Korea-China Economic Relations and South Korea's Corresponding Plan*, p. 49.

Chinese capital involved in the total foreign investment in North Korea cannot be calculated because the scale of foreign investment in the isolated state remains unknown. It seems clear, however, that Chinese capital accounts for most of the foreign money invested in North Korea. North Korea's efforts to attract foreign capital, China's blazing growth and related expansion in foreign investments, and the restoration of China-North Korea political relations suggest that China will likely continue to increase its investments in North Korea.

Characteristics of Exchanges

The key indicator that best illustrates the acceleration of China's economic exchanges with North Korea is the rate of increase in trade and investment. This phenomenon can be better understood through analysis. An initial examination of the aspects of China-North Korea trade reveals the following characteristics.²¹

The first characteristic is that North Korea's trade dependence on China is becoming more pronounced. This dependence has increased sharply during Hu Jintao's term as paramount leader of China. Up until 2000, North Korea's trade dependence on China was on par with its dependence on Japan.²² Since that time, however, China-North Korea trade has increased every year; the proportion of trade with China comprised 32.7% of total trade in 2003, 48.5% in 2004, 52.6% in 2005, 56.7% in 2006, and 67.1% in 2007. It is also assumed that North Korea's dependence on trade with China increased in 2008 due to the worsening of South-North Korea relations, which resulted in a relative decline in South Korea's share of North Korean trade. It is expected that the North

²¹- Choi Soo Young, pp. 43-44.

²²- In 2000, North Korea's trade volume with China was 488.03 million USD, and its trade volume with Japan was 463.65 million USD. Korea Trade-Investment Promotion Agency, *North Korea's Trade Trends 1999-2000* (Seoul: KOTRA, 2001), pp. 73, 91.

Korean bias in favor of trade with China will continue until the U.S., Japan, the EU and other major trading countries decide to drop sanctions on trade with the North which have resulted in a reduction of North Korea trade volume.

The second characteristic of North Korean trade with China is the North's reliance on mineral and natural resource exports including iron ore, zinc, fish, timber and other raw materials while importing required industrial inputs such as fuel, machinery, and steel, in addition to everyday necessities such as meat products, grains and other products from China. In other words, while North Korea exports a limited range of items to China, almost all the necessities of the North's economy are imported from China. This situation has become even more pronounced with the increasing severity of sanctions imposed by the international community against North Korea. Sanctions ultimately affect DPRK industry and consumer lifestyles, meaning that the influence of China has become even greater.

The third characteristic of China-North Korea trade is the DPRK's chronic and institutionalized trade deficit with China. Prior to 2005, North Korea recorded annual trade deficits with China of about 200-400 million USD, but after 2005 the trade deficit grew considerably, reaching 810 million USD in 2007. It is likely that this deficit will only continue to grow, due to the erosion of North Korea's industrial base and the limited scope of its exports to China. While trade with China is responsible for an overall increase in North Korean trade volume, it also increases the North's economic dependence on China, a situation that will become further entrenched as North Korea's trade deficit with the China continues to grow.

The fourth characteristic of China-North Korea trade concerns its hubs in the three provinces of northeastern China. Among the three provinces, Liaoning Province with its hub city of Dandong is the most

active site of China-North Korea trade. Dandong has surpassed the Yanbian region as a hub for China-North Korea trade due to the emergence of the “Frontier Trade” policy, one of the key features of China’s trade with North Korea.²³ But over the past several years, the share of North Korean trade taken up by China’s three northeastern provinces has fallen below 70%, reflecting a slight weakening in their position of market leadership as well as a growing interest throughout China in entering the North Korean market.

An analysis of the characteristics of Chinese investment in North Korea during the Hu Jintao era is as follows.²⁴ First, central government support and encouragement of investment in North Korea have become more noticeable. In April 2004, Chinese Premier Wen Jiabao met with Kim Jong-il, chairman of North Korea’s National Defense Commission, during the latter’s visit to China, and promised that the Chinese government would actively encourage Chinese companies to participate in economic cooperation projects in North Korea. In February of the same year, Premier Wen announced the establishment of the ‘DPRK-PRC Friendship & Exchange Corporation’ which would form the basis of government management and support for companies entering the North Korean market. In March 2005, North Korea’s Prime Minister Pak Bong-ju visited China to conclude a bilateral ‘Agreement on Investment Promotion and Defense’ which provided a framework for guaranteeing the safety of Chinese investors’ assets in North Korea, reducing the risk of investing in the North and setting the foundation for an increase in investment. This led to the foundation of a flagship economic cooperation project led by the Chinese government, the Daean Friendship Glass

²³- The DPRK’s foremost window of trade with China is the city of Dandong, where it has opened consular trade offices for the further expansion of China-North Korea trade. *Yonhap News*, January 11, 2009.

²⁴- Choi Soo Young, *The Expansion of North Korea-China Economic Relations and South Korea’s Corresponding Plan*, pp. 66-67.

Factory in North Korea, which would partially address North Korea's severe lack of heating – an act of friendship which won the trust of the North Korean people while strengthening friendly relations with North Korea.²⁵

Second, Chinese investment interest in North Korea has focused mainly on energy, raw materials, mining and development of underground resources. The serious shortage of raw materials and energy resources in China is a challenge that will determine China's economic future, so China's trade with North Korea in a few key sectors such as mineral resources is a way for China to pursue its national interests.²⁶ That is why China is currently pursuing investments in North Korea related to iron ore, copper, molybdenum steel, coal and almost every other mineral resource. The industrial base of China located in its three northeastern provinces is facing structural difficulties due to the shortage of raw materials, which has heightened Chinese interest in North Korea's mineral assets. Chinese investment in North Korean infrastructure and construction has increased because of the need to transport mineral resources, and investment is gradually diversifying into other sectors such as manufacturing, services, and logistics.

Third, investment in North Korea is led mainly by the three provinces of northeast China, as well as companies headquartered in southern provinces such as Zhejiang and Fujian. In the case of China's three northeastern provinces, investments in North Korea are part of a strategy to revitalize northeast China, while North Korean investments by

²⁵- The Daean Friendship Glass Factory received a direct investment of 24 million USD from the Chinese government and was completed in October 2005, after which China handed the entire factory over to North Korea free of charge.

²⁶- North Korea possesses over 360 kinds of mineral resources, of which 200 are resources with economic value, especially its magnesite and tungsten deposits, which constitute the first and second largest deposits in the world, respectively. North Korean deposits of molybdenum, graphite, barite, fluorite, and seven other minerals are estimated to be among the ten largest of their kinds in the world.

companies from southern China are part of their overseas market entry strategies.²⁷ The focus of Chinese investment in the DPRK has shifted from ethnic Koreans living in China to ethnic Chinese merchants who have connections with the Chinese regional government, leading to a dramatic reduction in the share of Chinese-North Korean trade controlled by ethnic Koreans. The possible weakening of the Yanbian Korean Autonomous Region as a result is an issue that should also concern South Korea.

Fourth, China's investment in North Korea has mostly taken the form of compensation trade or joint ventures. Most Chinese companies choose to follow local North Korean business regulations and generally do not demand management control, preferring to invest in the North through joint ventures with local partners and compensated trade. This lowers the investment risk because expenditures in plant and equipment are guaranteed by the manufacture of products which have a short input-output cycle, making the mutual dissolution of business ventures easier.

The Significance of Expanded Exchanges

The expansion of economic exchanges with North Korea under Hu Jintao's leadership of China has garnered a variety of opinions both inside and outside of South Korea. Opinion is divided among positive and negative interpretations of China's overt and hidden intentions concerning North Korea. The North Korean side also needs Chinese trade, but experts are divided in their opinions of North Korea's motivations in encouraging the expansion of Chinese involvement in the domestic economy. These issues matter because, depending on which opinion is closest to reality, policies

²⁷ China's Hangzhou Wahaha Group began to prioritize exploring investment opportunities in North Korea in 2004. In 2006, this group was the first to obtain molybdenum mining rights in North Korea; it is a private company headquartered in Wenzhou.

regarding inter-Korean and South Korea-China relations could be affected.²⁸

Opinions vary concerning China's desire to expand economic involvement in North Korea and the North's opening of its economy to Chinese goods and capital. One school of experts on North Korean and Chinese affairs views the present situation as part of the "status quo," regarding the expansion as simply a reflection of China's concerns about North Korea's possible collapse and its consequences for its neighbors. Apart from a change in its practical relations with the North in the post-Cold War era, China views the possible collapse of the North Korean socialist system as an issue closely related to its fundamental interests. China is pursuing a policy to prevent the collapse of North Korea's socialist regime because its leadership seems to believe that an unstable Korean Peninsula following a collapse would likely have negative effects on a core state objective - sustained, stable economic development.²⁹ Therefore, according to these analysts, China's support will be limited to helping North Korea survive and will fall short of restoring the two countries' traditional ties.³⁰ They base their views on the fact that China's economic support and exchanges began expanding when the United States suspended its fuel supply to North Korea in November 2002 and accelerated when North Korea faced intensified financial sanctions in 2005. They also point out that China's economic cooperation with the North has focused on supplying the energy and food needed for North Korea's survival.

Another school of thought looks at the bilateral economic co-

²⁸- Nam Sung Wook, "A Study of China's Fast Capital Outflows into the DPRK," *The Korean Journal of Unification Affairs*, Vol. 18, No. 1 (2006), p. 22.

²⁹- David Shambaugh, "China and the Korean Peninsula: Playing for the Long Term," *The Washington Quarterly*, Vol. 26, No. 2 (Spring 2003), pp. 43-56.

³⁰- Lee Dong-ryul, "Research on China's Influence over North Korea," FKI, *China's Political Situation Change and ROK's Corresponding Policy* (Seoul: FKI, 2005), p. 148.

operation from the standpoint of “simultaneous growth.” This side argues that China’s economic growth depends on the development of its three northeastern provinces, and their growth can have a “synergistic effect” if North Korea is developed simultaneously.³¹ They cite the theory of “balanced development” of China’s three northeastern provinces and North Korea through active economic exchanges and cooperation which gained attention after Hu Jintao took office. The so-called Document No. 36, published in June 2005, which lays out a development plan for the three northeastern provinces, is also presented as evidence of the simultaneous growth strategy. In fact, there is a strong possibility that once transportation and logistics infrastructures have been developed along the border between North Korea and China’s northeastern provinces, and joint projects for resource development and utilization get under way in earnest, major changes will occur in industrial production and overall economic activity in North Korean cities in border areas. It may be said that China is investing in resource development and infrastructure construction in North Korea with hopes of efficiently transporting North Korean resources to its three northeastern provinces and exporting products manufactured in those Chinese provinces through North Korea, which will be made possible by the simultaneous development of both territories.

Thirdly, there is the view that China aims to eventually include North Korea in the “Great Chinese Economic Sphere,” making it “a virtual economic satellite” or “the fourth northeastern province.” Apprehensions about such a possibility are widespread in the liberal and conservative circles of South Korea.³² Proponents of both the “satellite” and “fourth

³¹- Xu Wenjie, *Korean Peninsula Conditions and China’s Corresponding Policy* (Jinan: Shandong University Press, 2007), pp. 157-163; Li Tieli, *Transborder Regional Economic Cooperation* (Beijing: China Finance Press, 2005), pp. 218-223.

³²- Former Korean President Kim Dae-jung also expressed concern about the expansion of economic exchanges between China and the DPRK. Kim Dae-jung Peace Center (ed),

province” theories cite the fact that Chinese investments in North Korea are being made under the meticulous planning and guidance of the central government, while the investment environment in the North remains far from attractive. Statistics show that North Korea is already subordinated to the Chinese economy to a significant extent: The North depends on China for 87 percent of its oil consumption, 80 percent of its consumer goods, half of the entire food grain its population needs, and 80 percent of all foreign direct investment. Under these circumstances, China may well expect to attain strong political leverage over North Korea.

The notion that North Korea has fallen into a state of subjugation has its challengers.³³ They believe China’s influence is still quite limited, as shown by its inability to persuade the North to honor agreements in the Six-Party Talks. North Korea has twice conducted nuclear tests and launched missiles without heeding China’s advice, proving that expanded economic cooperation does not necessarily provide effective political leverage.

What is also noteworthy is the strong will of the North Korean leadership and the diplomatic abilities they have attained from past experiences. Pyongyang has long pursued independence in its external relations, and its diplomacy has displayed a strong sense of balance as shown in its adroit policy of maintaining equal distance between the former Soviet Union and China to maximize its national interests amid their conflict. It therefore is hard to believe that North Korea will simply allow itself to be co-opted into the economic sphere of another nation.

Peace for the Korean Peninsula: 13-Day Visit to the United States (Seoul: Kim Dae-jung Peace Center 2007), pp. 20, 23, 30.

³³- See Lee Hee Ok, “The Change of China’s Policy toward North Korea and Its Implications,” *The Journal of Modern China Studies*, Vol. 8, No. 1 (August 2006), pp. 75-105; Dongho Jo, Sangkeun Lee, “Critical Review on North Korean Economic Subordination to China,” *International Area Studies*, Vol. 12, No. 3 (2008), pp. 363-394.

The continued expansion of China-North Korea economic ties may result in economic institutions and regulations conducive to the North's opening of its economy. It may also expedite the development of a market economy by educating North Koreans about what is happening outside their isolated country. Above all, China's generous economic support of North Korea should be viewed positively as it definitely helps the impoverished country to survive in its current state of extreme economic difficulty.

On the other hand, some negative factors should not be overlooked. First, China's growing investment in North Korea and its strengthened economic cooperation will eventually deepen the North's dependence on China and force South Korea to concede the North Korean market. Second, China's economic support of North Korea, which has continued irrespective of progress in the six-party denuclearization talks, has tended to make the North less interested in improving relations with South Korea and resolving the nuclear stalemate. Third, if economic cooperation between China and North Korea expands to the point that the former is economically annexed to the latter, this would upset the balance of power in Northeast Asia and negatively affect South Korea's reunification plan. Fourth, China's port and mine development projects and its acquisition of real estate in North Korea may lead to property disputes between China and South Korea when the peninsula is reunified.

Conclusion

Relations between North Korea and China have developed in various complicated ways during the Hu Jintao era. However, as discussed above, the great expansion of Chinese economic exchanges and cooperation with North Korea has focused mainly on trade and investment, and it is expected that this trend will continue into the near future. Of course,

China's economic cooperation with North Korea will henceforth be affected by changes in Beijing's North Korea policy. But the Hu Jintao administration's strategic measures and diplomatic policies toward North Korea focusing on economic engagement will continue for the time being, because expanded economic cooperation and investment meet the strategic and realistic needs of both nations.

In the meantime, China has been attempting to lure North Korea into engaging with the international community in a natural way and accepting changes and developments in the international community, by means of indirectly encouraging North Korean reform and opening, as well as expanding economic exchanges and cooperation with the North. Of note is Wen Jiabao's proposal to Kim Jong-il, made during Kim's visit to China in May of this year, that China should pass on its experience in reform and opening – a proposal which probably reflects China's earnest wish for a change in North Korea's policy.³⁴

China's economic exchanges with North Korea will certainly grow in the days ahead, but these will not necessarily be accompanied by an attempt to subordinate the North Korean economy. As for North Korea, China's increased influence is a cause for worry. Pyongyang will seek to establish a balance between China and South Korea. North Korea has allowed China to invest primarily in its northern provinces and has invited South Korean investment into its southern region, namely Mt. Kumgang and Gaesong, just north of the border. Since the inauguration of the Lee Myung-bak administration in Seoul, economic exchanges between the two Koreas have almost entirely stalled. A continued freeze could lead to an asymmetrical expansion of China's economic involve-

³⁴ - Chinese Premier Wen Jiabao promised Kim Jong-il that "China will, as always, support North Korean efforts to develop its economy and improve its people's livelihood and is willing to introduce to North Korea to the experience of China's reform and opening-up and construction." *Xinhua News Agency*, May 7, 2010.

ment in the North and its acquisition of large chunks of North Korean resources.

South Korea needs to establish policies to counter economic cohesion and collaboration between China and North Korea. The South Korean government and enterprises should take a “strategic approach” toward North Korea, with a broader vision than the Gaesong Industrial Complex, in order to prepare for the opening of the North Korean market in the long run. A strategic approach is different from a market-oriented approach in that the former should consider building foundations for Korean reunification and countering reactions from neighboring countries. There is no doubt that the first prerequisite for such an approach is unfreezing relations between the two Koreas.

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