

# **DPRK'S POLICY ON FDI FROM 1986 TO 2000<sup>1</sup>**

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In this paper the author discusses changes of direction of DPRK's policy on FDI from 1986 to 2000, dividing the period into three stages. In the first stage from 1986 to 1991 the DPRK rejected economic liberalisation and attracted investment by pro-DPRK residents of Japan. From 1992 the Rajin-Sonbong Free Economic and Trade Zone had been promoted. After the Asian economic crisis, the DPRK strengthened its negative stance towards the global market economy, while continuing liberalization of the Rajin-Sonbong Zone and developing economic cooperation with the ROK.

## **1. 1986 – 1991: Rejection of Economic Liberalisation, Attraction of Investment by Chongryon (pro-DPRK residents of Japan)**

The DPRK, which was trying to promote economic liberalization with regard to external trade, foresaw a conflict with the Chinese Communist Party's line, and adopted a negative stand towards liberalization policies. Economic cooperation with capitalist countries was eliminated from the 3<sup>rd</sup> seven-year plan (1987 - 1993), which was the economic plan for this period.

However, the law regarding joint ventures functioned as a legal device mainly to encourage investment in the DPRK by Chongryon in Japan (i.e. patriotic projects) rather than economic cooperation with capitalist countries<sup>2</sup>. From 1986 until 1991, a total of 32 cases of investment in the DPRK by Chongryon-related companies, worth \$31.32 million dollars, were declared to the Ministry of Finance. In terms of the value of investment, most was concentrated in 1988/9, with the textile sector accounting for the greatest proportion.

## **2. 1992 – 1997: Liberalisation of One Region: the Rajin-Sonbong Zone**

During this period, the introduction of energy, technology, capital goods, etc. declined

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<sup>1</sup> The contents of this paper is quoted from a paper prepared in Japanese. Chan-Woo LEE, "The History of Foreign Capital Introduction in the DPRK," *ERINA REPORT Vol. 41* August 2001

<sup>2</sup> Clause 1 of the Joint Venture Law established in 1984 includes North Koreans resident overseas as interested parties in joint ventures.

sharply as a result of the collapse of the Soviet Union, and the DPRK economy was caught up in a crisis. There was no other option left to the country but to promote economic cooperation with capitalist countries once more. Against this background, the Rajin-Sonbong Free Economic and Trade Zone was established in December 1991<sup>3</sup>.

The intent was to develop the Rajin-Sonbong area as a “preferential trade, transit transportation, export processing, financial and service region” (Clause 2, Free Economic and Trade Zone Law). With regard to the progress of such international economic cooperation policies, the DPRK explains that the subjective development process of the national economy and the objective conditions of international cooperation have combined. Professor Kim Soo-Yong of the Kim Il-Sung General University explained the DPRK’s external economic policy in the following way in a speech in Tokyo in October 1995<sup>4</sup>.

“From the beginning, the DPRK chose an economic development model that emphasized the domestic market. This involved filling demand on domestic markets with goods produced at home, using domestic reserves, and utilizing the country’s own resources, capital, technology and human resources to construct the domestic economy. It well reflects the subjective (recovery from having nothing after the war) and objective (blockade of the DPRK by capitalist countries) conditions to which the DPRK has adapted itself. This was established as the Independent National Economic Construction policy; the process has a close relationship with overseas economic interaction and has promoted the expansion in interaction between socialism and capitalism. As a result, mutual dependence deepened in the 1980s and a new stage in external economic interaction was required, so it developed into joint ventures and collaboration (the 1984 Joint Venture Law), based on a full commitment to trade. In the 1990s, economic interaction that transcended philosophies became a worldwide trend, as a result of the easing of the Cold War structure, and the collapse of the socialist bloc, which had accounted for 70% of the DPRK’s external economic interaction, demanded a policy change in the DPRK’s independent economic construction philosophy. In other words, the Rajin-Sonbong Free Economic and Trade Zone was established in December 1991 as a result of subjective and objective conditions in the form of the country’s necessity for domestic economic development and a transition in the global economy towards

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<sup>3</sup> According to data from the DPRK, the late Kim Il-Sung declared the idea of establishing an economic and trade zone at Sonbong in February 1989. (Source) Korean Institute of Social Science, *Rajin-Sonbong Economic and Trade Zone Investment Handbook*, May 1998.

<sup>4</sup> At the lecture held by the Korea-Japan Export and Import Corporation (25<sup>th</sup> October 1995), Professor Kim spoke on the subject of *The DPRK’s External Economic Policy and Prospects for the Rajin-Sonbong Free Economic and Trade Zone*.

cooperating in interaction. At the Workers' Party of Korea's Central Committee 6<sup>th</sup> Term 21<sup>st</sup> General Meeting, held in December 1993, new economic liberalization policies, with targets such as 1) the introduction of new technology; 2) balancing the flow of foreign currency; 3) peace and security in Northeast Asia via the strengthening of regional cooperation; and 4) the realization of a philosophy of putting trade first, were brought forth in a general evaluation of the 3<sup>rd</sup> seven-year plan."

However, the Rajin-Sonbong special economic zone policy did not make any proper progress until 1994, due to hostility between the DPRK and the USA regarding the latter's allegations that the former was developing nuclear weapons. From 1995, the DPRK has plunged into an economic crisis as a result of a serious food crisis caused by the occurrence of natural disasters such as floods and drought, and a drop in the utilization rate of factories due to a lack of energy and raw materials.

In September 1996, an international investment forum was held in the Rajin-Sonbong Zone for the first time; four contracts (worth \$265 million) were completed, including one for the construction of an hotel (\$180 million) by Hong Kong's Emperor Group, and twelve agreements (worth \$562.8 million) were concluded.

In June 1997, in order to improve the investment environment in the Rajin-Sonbong Zone, the DPRK government implemented the following: 1) a one-stop system giving the Rajin-Sonbong Zone Authority wide-ranging powers to authorize investment; 2) the introduction of a market pricing system (abolished the rationing system and implemented an self-supporting system); 3) the unification of exchange rates and its readjustment to a realistic level (approx. 200 won/\$); 4) the approval of independent enterprise and the establishment of a free market; 5) the integration of the rail management system; and 6) education about the market system (nurturing human resources). As a result, the Rajin-Sonbong Zone was positioned as the only region of the DPRK with a market economy.

However, the introduction of foreign capital in 1997 fell to \$50 million and the implementation of much investment for which contracts had already been concluded, was postponed. In addition to the undeveloped infrastructure in the Rajin-Sonbong Zone, one reason for this was the Asian economic crisis.

According to a presentation by the DPRK's Committee for the Promotion of External Economic Cooperation (CPEEC), contracts for 111 foreign investment projects in the Rajin-Sonbong Zone, involving countries such as China, Hong Kong, Thailand and Japan, and worth \$750 million, had been concluded as of the end of December 1997, of which, 77 projects, worth \$57.92 million, have been implemented.

### **3. 1998 – 2000: Rejection of the Market Economy, Continued Liberalisation of the Rajin-Sonbong Zone, Progress in North-South Economic Cooperation**

As a result of the Asian currency crisis, which occurred while the DPRK was experiencing its own economic crisis, the DPRK strengthened its negative stance towards the global market economy. Since 1998, the Rajin-Sonbong Zone's official name has changed from "Free Economic and Trade Zone" to "Economic and Trade Zone", with the word 'free' having been eliminated. Furthermore, the government of the DPRK strengthened its Independent National Economic Construction policy, which prioritized heavy industry.

The expression "revolutionary economic policy of the party" often crops up with regard to economic policies of this period. In March 2000, the then-Deputy First Department Director of the Workers' Party of Korea's Central Committee, Pak Song Bong (died February 2001), asserted in the March 2000 edition of *The Worker* that the "revolutionary economic policy of the party befits the current situation in which the economic blockade by imperialists has been strengthened and the socialist market has disappeared; it is the most accurate guideline for socialist economic construction with the aim of solving economic problems and the lifestyle problems of citizens."<sup>5</sup> The details of the policy include: 1) maintenance of an "our-style" economic base in order to achieve "the construction of a powerful country"<sup>6</sup>, which is the state's aim; 2) it is not possible to accept capitalist "reforms" (the market economy is encountering some confusion); 3) adherence to the principles of centralized and planned guidance and supervision of the economy by the state; 4) pursuit of practical benefits in economic projects and principles that administer physical stimuli appropriately, after prioritizing political and moral stimuli; 5) solution of economic problems as a priority in central sectors of the economy, such as the metals and machinery industries, and the sequential solution of other problems.

However, at the 10<sup>th</sup> Meeting of Supreme People's Assembly held in September 1998, the constitution was revised and improvement clauses of practical use in the field of economics drawn up. In the new constitution, these included easing restrictions on individual ownership, emphasizing the concepts of initial cost, pricing and profitability in economic affairs, and a stipulation regarding special economic zones.

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<sup>5</sup> (Source) Pak Song Bong, *The Revolutionary Economic Policy of the Party is the Flag of War for the Construction of a Strong Socialist Economy*, *The Worker*, 2000, No.3, p.45 - 48

<sup>6</sup> The "Powerful Country Construction" Theory was first publicized in an article in the 22<sup>nd</sup> August 1998 edition of the *Rodong Sinmun*.

Furthermore, the DPRK revised the law regarding foreign direct investment (FDI) in February 1999, basically limiting foreign investment to the Rajin-Sonbong Zone<sup>7</sup>. It also strengthened the central government's administrative functions<sup>8</sup>.

At present, the development of the Rajin-Sonbong Zone as a base for tourism and transit transportation is being prioritized. In October 2000, a casino hotel run by Hong Kong's Emperor Group began operating. In addition, its role as a transit base, with trade cargo from China's Jilin Province being handled at Rajin Port, is increasing. The problem is that the development of infrastructure, such as roads and rail track from the Chinese border, is lagging behind, so the Zone Authority is hastening the supply of funds for road development as an area of particular importance. In the export processing industry, small-scale investment accomplishments continue to be seen, for example in the processing of marine products. It is said that investment contracts worth \$520 million had been concluded and investment worth \$220 million had been implemented as of July 2000<sup>9</sup>.

Looking at economic cooperation between the DPRK and the ROK, investment in the DPRK by ROK companies has been jump-started as a result of the Sunshine Policy of the government of ROK president Kim Dae-Jung, which took power in 1998. In June 1998, the late Chung Ju-Yung, Honorary Chairman of the Hyundai Group, visited the DPRK with a herd of cattle and achieved a dramatic agreement with regard to tours of Mt. Kumgang. Although this project was in the red in terms of economic calculations, it was promoted as an ethnicity-related project. As of the end of December 2000, of the 18 cases (one in 1995, five in 1997, nine in 1998, one in 1999 and two in 2000) where the ROK government granted permission for investment in the DPRK, apart from four light water reactor-related projects, investment in 11 projects has been implemented. In monetary terms, investment contracts worth a total of about \$240 million have been concluded, and investment worth about \$160 million has been implemented; of this, the Hyundai Group's Mt. Kumgang Tourism Development Project accounts for an overwhelming share: approximately \$140 million (Table 1).

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<sup>7</sup> Under the regulation in existence prior to the revision, foreign companies (i.e. independent investment companies) were limited to establishing operations in the Rajin-Sonbong Zone, but as a result of the revision, joint equity ventures and contractual joint ventures are also basically limited to the zone.

<sup>8</sup> With regard to the 1999 revision of the Foreign Investment Law, see Lee Chan-Woo's *Analysis of DPRK Trends*, ERINA Report Vol.33, April 2000.

<sup>9</sup> Interview during the Kanamori Committee's visit to the DPRK (July 2000)

**Table 1 Investment in the DPRK by ROK Companies (as of the end of December 2000)**

(Unit: \$10,000)

Company	Main Business	Date Approved	Area	Value of Contract	Actual Investment
Daewoo	Shirts, jackets, bags	17 <sup>th</sup> May 95	Nampo	512	512
Taechang	Mineral water	22 <sup>nd</sup> May 97	Mt.Kumgang	580	553
Green Cross Corporation	Pharmaceuticals	14 <sup>th</sup> Nov 97	Pyongyang	311	179
Miheung Foods	Marine products	13 <sup>th</sup> Mar 98	Wonsan, etc.	47	6
Korean Corn Foundation	Development of new varieties	18 <sup>th</sup> June 98	Pyongyang, etc.	1,000	369
LG / Taeyong Marine Products	Scallop farming	28 <sup>th</sup> Aug 98	Rajin	65	1
Korea Land	Real estate development	28 <sup>th</sup> Aug 98	Pyongyang	60	20
Hyundai Construction	Tourism at Mt.Kumgang	7 <sup>th</sup> Sept 98	Mt.Kumgang	16,214	14,000
Hyundai Electronics	Telecommunication at Mt.Kumgang	11 <sup>th</sup> Nov 98	Mt.Kumgang	13	12
Peace Motors	Motor vehicle assembly	7 <sup>th</sup> Jan 00	Nampo	5,403	501
Samsung Electronics	Collaborative development of software	13 <sup>th</sup> Mar 00	Beijing	73	29
Total				24,278	16,182

Source: ROK Ministry of Unification