

Silent Partners



Chinese Joint Ventures in North Korea

Drew Thompson

February 2011

A U.S.-Korea Institute at SAIS Report

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About the Author

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Executive Summary

China is considered North Korea's economic lifeline. Chinese aid, trade, and investment are critical to North Korea's social stability and economic productivity and a key source of technology and hard currency. Presumably, without this trade and investment, Kim Jong-il would lack the means to secure the allegiance of elites that support his rule, making trade and investment with China particularly important for ensuring the regime's survival. Joint ventures with China are an important aspect of the bilateral relationship, because in addition to propping up the regime in Pyongyang, they contribute to economic development in China's northeastern "rust belt." These Chinese financial investments in the DPRK are geopolitically significant not only in terms of Chinese strategic interests but also for South Korean aspirations to unify the peninsula. Efforts by the international community to isolate North Korea and to impose sanctions in response to its efforts to develop nuclear weapons and its other provocative behaviors are complicated by the economic relationship between China and North Korea.

Chinese investments in North Korea reflect China's strategic outlook on Northeast Asia and the role of North Korea in China's grand strategy for the region. China's relationship with North Korea is central to its effort to achieve "great power" status, and a key aspect of China's perception of its place in the region and the international system. While the relationship between China and North Korea is unique, Chinese investment in North Korea is consistent with China's wider "go abroad" effort. There is little or no evidence that Chinese investments in North Korea are politically driven, motivated by a shared communist ideology, or part of a grand strategy specific to the peninsula. Trade and investment with North Korea is consistent, however, with China's broad national interest in promoting stability in North Korea and supporting economic development in border regions and the northeastern provinces.

Chinese investment projects in North Korea, however, are smaller and less successful than projects in neighboring states. For example, from 2003 to 2009, Chinese outbound investments to North Korea totaled US\$98.3 million, compared to US\$1.2 billion to South Korea, US\$273 million to Thailand, US\$437 million to Vietnam, US\$729.8 million to Myanmar, and US\$890.7 million to Mongolia over the same period. North Korea is a particularly difficult environment for Chinese investors due to rent seeking, poor infrastructure, and the oppressive

political environment.

Only two of China's top 100 companies are investors in North Korea, both steel companies. The majority of Chinese investors in North Korea are small and medium-sized enterprises, though some smaller firms enjoy brand recognition, such as Nanjing Panda, China Minmetals, and Wanxiang. The majority of Chinese investors in North Korea are not State Owned Enterprises (SOEs) controlled by the central government, but privately owned companies and provincial, prefecture, and municipal-owned SOEs. As far as one can tell, only four out of the 138 investors identified as legitimate investors are central-government owned companies.

Of the 138 joint ventures established between 1997 and August 2010, 41 percent are in extractive industries, 38 percent light industrial, 13 percent services, and eight percent heavy industry.

Chinese investors in North Korea are geographically concentrated in the two northeastern provinces bordering North Korea. Twenty-eight percent of Chinese companies involved in joint ventures are from Jilin, 34 percent are from Liaoning, and the balance are from other provinces, including Beijing, Shandong, and Shanghai. Jilin and Liaoning share a 1,400 kilometer border with North Korea and are increasingly focused on foreign trade and on achieving competitive economic advantages through their proximity to North Korea. Approximately one million Korean-speaking Chinese is the only significant population of native Korean speakers abroad who can freely do business with North Korea, giving Korean-Chinese cultural advantages with limited competition.

While North Korea can hardly be said to have taken full advantage of the economic opportunity presented by China, the ultimate success of regional development plans in the Northeast is predicated on the successful launch of a reform and opening process in North Korea. Local analysts have determined that the massive infrastructure investment taking place in China's Northeast is justified because it will make the border provinces highly competitive in a reformed and opened North Korean market. Yanbian Prefecture in Jilin and Dandong City in Liaoning have invested heavily in their own infrastructure to facilitate cross-border trade and promote investments on the North Korean side of the border. The fulfillment of northeastern China's hopes for long-term revitalization may partly depend on North Korea's willingness to pursue more rational economic policies.

Chinese joint venture investments in North Korea have local as well as national political implications. These investors have rights that both the Chinese and North Korean governments are obligated to recognize. The Chinese government has reasonable expectations that the North Korean government will respect and protect these tangible Chinese interests, raising the possibility that predatory corruption in North Korea can become an issue in the bilateral relationship. It is unlikely, however, that these mostly small companies themselves enjoy significant influence on the formulation of Beijing's policies towards North Korea, though they likely have greater influence at provincial and local levels.

In the course of normal business operations, the small and medium-sized enterprises from Jilin and Liaoning that dominate the North Korean investment scene for the most part do not rely on contacts with the Chinese government for the success of their businesses. Essentially, they are silent partners in the relationship between China and North Korea. In the event of any dramatic change on the peninsula, however, these companies might abandon their low-profile approach. Like all companies, if faced with the loss of their business, they would likely respond vocally and press their case with the Chinese government. While their investments might be small on a national scale, any losses incurred would be substantial at the firm and possibly local levels. Some of the Chinese investors are owned by provincial or sub-provincial government departments and the loss of those investments would affect local government balance sheets. Chinese towns with key border crossings to North Korea would certainly face hardships were North Korean economic activities to collapse. Arguably, these border regions already suffer some hardship from the international stigma attached to North Korea. Despite their distance from the capital, a variety of bureaucratic mechanisms and personal connections could be utilized to remind Beijing of northeastern interests in the event of a threat.

Investment and trade with North Korea is consistent with China's geostrategic outlook toward the peninsula. China's broad national interests vis-à-vis North Korea are to maintain a stable regional security environment, ensure the survival of the North Korean regime, support economic development in the Northeast, and achieve a nuclear weapons-free peninsula. Beijing seeks to achieve these objectives through a comprehensive approach of economic engagement with trade, aid, and investment; bilateral interactions; and multilateral engagement such as the Six Party Talks process. Encouraging the development of a robust economic relationship between China and North Korea is an important component of China's strategy, not only for the benefits that it brings for Chinese businesses, but also because it is presumed that trade and investment

contributes to regime security and social stability, thereby preventing a North Korean collapse. Chinese officials and analysts also recognize that North Korea is unlikely to willingly negotiate away its nuclear weapons unless there is greater internal stability and the regime's security is assured. By this logic, Chinese investments in North Korea are potentially indirect contributors to the Pyongyang regime's security.

Mutual mistrust characterizes the relationship between China and North Korea, especially in the economic sphere. North Korea is dependent on China for trade, aid, and investment but is wary of being "hollowed out" by Chinese investments in its extractives industries, particularly in the mining sector. Without other security allies and with no larger trading partner or investor than China, North Korea has little choice but to engage with its northern neighbor. Despite China's abundant capital and immense experience building infrastructure around the world, North Korea has remained cautious about deepening its dependency on China. However, Pyongyang likely views China as less of a threat than the risks posed by improving ties with South Korea, which might result in ideological exports that would undermine the foundation of North Korea's system. Beijing offers a model that promises the pursuit of economic reform while maintaining strict political control. Chinese joint ventures have the potential to be an important vehicle for "interpreting" the Chinese experience of reform and opening for their North Korean counterparts, fostering an orderly reform process that would preserve the North Korean regime for the time being, but perhaps also enhance the possibilities for an agreeable North-South unification in the more distant future.

The presence of Chinese investment in North Korea likely hinders Beijing's freedom of policy action and creates liabilities that are not well understood. In general, Beijing is uncomfortable with sanctions, though they are America's preferred foreign policy tool of choice for pressuring North Korea to denuclearize. The existence of Chinese investments affects Beijing's ability to endorse sanctions, which would harm Chinese companies, undermine whatever trust exists between Beijing and Pyongyang, and contradict China's argument that reform and opening is necessary.

Few people if any are actively concerned about Chinese investors upsetting delicate security balances in the region. Chinese joint ventures could potentially play a significant role, however, in other ways that might be equally dramatic when viewed over time. It is more likely that investment from abroad will contribute to gradual change among North Korean elites and

workers, just as it changed China.

Investment in China's Northeast and the handful of small-scale Chinese investments in the DPRK reveal an array of Chinese actors with a common strategy of seeking to position themselves for a future opening of the DPRK. Should reform and opening take place, successive waves of investment could dramatically alter the political and economic landscape of North Korea and ultimately, the Peninsula itself. But for now, the biggest barrier to expanded Chinese investment as well as peace and stability on the Korean Peninsula in North Korea is the DPRK itself.

中朝边境·温馨提示

National Border of P.R.C. and D.P.R.K. Reminder

- 一、请勿攀爬、穿越铁丝网等拦阻设施。 1. Please do not climb or cross separation obstacles such as barbed wires.
- 二、请勿向界外投掷任何物品。 2. Please do not throw any objects over the border.
- 三、请勿与界外人员交谈、交换物品。 3. Please do not converse or exchange objects with people on the other side of the border.
- 四、请勿对军事设施照相、录像。 4. Please do not take pictures or videos of the military installations.

辽宁省边海防委员会办公室 宣

General Office of the Border/Ocean Defense Committee of Liaoning Province



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