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Lips and Teeth: Chinese-North Korean Trade and Foreign Direct Investment's Impact

By Trevor Clark

I. INTRODUCTION

There can be no doubt that northeast Asia will continue as a major flash point for international politics and economics in the next decade. Northeast Asia is home to one of the most dynamic and emergent economies, China, two of the world's most stable democracies and economic powerhouses in their own right, Japan and South Korea, and one of the world's most mercurial and unpredictable regimes, the Democratic People's Republic of Korea (DPRK or North Korea). This paper explores the relationship between China and North Korea. In particular, it focuses on their economic relationship—foreign direct investment (FDI, also referred to as overseas direct investment) and trade—as well as the degree to which this economic relationship plays into regional politics. This paper also analyzes this relationship's implications and the effect it has on China's relationships with the other major regional power, the United States. North Korea and China's economic relationship is such that China will continue to operate as it has for the sake of regional stability, ensuring South Korea and its ally, the U.S., remain off China's borders. The effective result is a continuation of the status quo and the possibility of continued or heightened strains on the Sino-U.S. relationship.

This paper first outlines North Korea and China's relationship. It then explores the evolving nature of the economic relationship between these two countries, focusing on outbound FDI from China into North Korea and China-North Korea trade and their fluctuation pattern since the 1950s. Next, it considers the economic relationship's ramifications for the political relationship and the future of the Sino-North Korean alliance. Finally, the paper explores how China's increasing economic partnership with North Korea—or better put, North Korea's increasing dependence on China for regime survival—will affect Sino-U.S. relations and the extent to which Beijing and Washington will adjust their policies towards each other.

II. "LIPS AND TEETH," A BRIEF HISTORY OF CHINA-NORTH KOREA RELATIONS

The history of China-North Korea relations is dynamic and multifaceted. China's interests in the alliance have ranged from a shared ideological connection with

the Soviet Union, to the simple fact that North Korea is one of the few barriers China can maintain to keep its distance from the U.S. The DPRK became one of the first countries to recognize the People's Republic of China as a sovereign nation on October 6, 1949, five days after the Chinese Communist Party declared victory over the Kuomintang in the Chinese Civil War. According to George Yu's 1998 historical account, "China-North Korea political relations and friendship were 'forged in blood' with China's participation in the Korean War, beginning October 1950, in common opposition against 'American imperialism.'" Between the armistice that halted the Korean War in 1953 and the mid-1980s, the exchange of government officials and military leaders, cultural exchanges, and trade agreements further strengthened their relationship. The most important of these agreements was the 1961 China-DPRK Treaty of Friendship, Cooperation, and Mutual Assistance. According to the Center for Strategic and International Studies (CSIS)'s Bonnie Glaser in November 2012, the treaty codified China and North Korea's security partnership, with the agreement being renewed every twenty years (most recently in 2001) and requiring that any revision of the treaty be agreed to by both sides. These exchanges not only helped further entrench the two countries under the Soviet Bloc's umbrella, but also helped the alliance persist following the Soviet Union's fall.

That being said, the relationship between North Korea and China was far from perfect, even after the 1961 treaty. North Korea, much like China would later do with the Soviet Union and the U.S., consistently played the Soviet Union and China off each other. This allowed North Korea to reap the benefits of having two major economic providers, while also preventing itself from becoming too reliant on one or the other or getting itself caught in between two giants. According to Bonnie Glaser, for China, this became an increasingly difficult problem to manage as Sino-Soviet relations began to crumble, ultimately leading to the Sino-Soviet split. Further, when Deng Xiaoping began implementing his reform and Open Door Policy in the 1980s, North Korea felt that "China's domestic policy shift was a 'betrayal of Socialist ideals' and of the bilateral relationship writ large." But this feeling of betrayal did not lead to economic disentanglement, and China remained a major economic partner for North Korea.

The end of the Cold War, in effect, freed China to begin to operate its foreign policy outside the confines of ideological decision-making. George Yu noted in 1998 that, following cues from Russia, China began to thaw its relationship with South Korea, establishing formal relations with the U.S. ally in August 1992. China did not forego its relationship with the DPRK, but rather continued to maintain "correct relations" with North Korea. However, this strained the relationship and also began to weaken some of Beijing's control over Pyongyang. Jian Yang noted in a 2006 article, "The fact that China established an embassy in Seoul without insisting that the United States first recognize North Korea

angered Pyongyang.” Yet, relations between the two communist nations began to improve in the late 1990s, punctuated by China’s then-President Jiang Zemin’s September 2001 visit to Pyongyang. However, as Samuel Kim and Tai Hwan Lee point out in their 2002 article, “Chinese-North Korean Relations: Managing Asymmetrical Interdependence,” the overall relationship between the two nations continues to be “just beneath the surface a highly asymmetrical interdependence in all political, military and economic issue areas.” This asymmetric relationship has persisted, and yet, China continues to remain North Korea’s staunchest ally, regionally and globally.

III. CURRENT STATE OF THE RELATIONSHIP

The primary problem that China faces in its North Korea policy is the fact that Beijing has multiple interest areas in the Korean peninsula, and often these interests are at odds with each other. Yang adds, “China’s top priority in North Korea is peace and stability.” Any sort of regime change would fundamentally alter the security architecture of the region. The Kim Jong-un regime’s fall would mean that China could lose what it views as an all-important buffer country to a South Korean regime more sympathetic to the U.S. As a result, Beijing has an incentive to continue to support Pyongyang even as it tries to rein it in. However, North Korea may see support as an opportunity to be more aggressive, such as with the 2006 nuclear test and multiple missile tests (most recently in May 2013). China has, relatively consistently, publicly denounced many, though not all, of North Korea’s provocations but has taken few punitive measures. Even what China *has* done hardly seems to deter the DPRK. As a result, Beijing currently sees the relationship as one that it must balance with the conflicting ideals of support and restraint.

Within the current relationship, outside actors—particularly South Korea, Japan, and the U.S.—continue to assert that China is not using the full extent of its influence on North Korea. However, Yang argues that, due to China’s focus on economic reform and the abandonment of communist-style planning, its influence over North Korea is waning or, at the very least, its desire to exert that influence is waning. Economic reform does not support North Korea’s agenda and is not the path it would have preferred China to take. However, for Scott Snyder, in his 2001 chapter “Korea’s Influence on Northeast Asian Major Power Relations,” with China’s ultimate goal of stability and peace on the peninsula, the outside actors must work strategically to play the two sides of the alliance off each other.

That being said, as the main crux of this paper and as the following sections show, the especially asymmetric economic relationship between North Korea and China ensures that Sino-North Korean cooperation will continue and that

China's support of the DPRK will not likely falter. In fact, according to Nicholas Eberstadt, a political economist at the American Enterprise Institute (AEI) and the Council on Foreign Relations (CFR), in 2010, "Since the early 1990s, China has served as North Korea's chief food supplier and has accounted for nearly 90 percent of its energy imports. By some estimates, China provides 80 percent of North Korea's consumer goods and 45 percent of its food." The following sections break down Chinese FDI in North Korea and the international trade relationship between the two. They support Eberstadt's analysis and demonstrate that the China-North Korea relationship will persist.

IV. THE ECONOMIC RELATIONSHIP

Before fully dissecting the compiled data, it should be noted that there are several problems inherent in this research. The first is data accuracy and number of sources. North Korea is notoriously secretive and does not release reliable economic statistics. As a result, analysts are faced with the task of using "mirror" statistics and looking at North Korea's trade partners to extract data and projections. For the purposes of this paper, the United Nations Conference on Trade and Development (UNCTAD), the Ministry of Commerce in the People's Republic of China (MOFCOM), news reports and analysis of reports from the Ministry of Unification in South Korea, and the Korean Trade-Investment Promotion Agency (KOTRA), among others, were used as the primary economic data sources. Another issue is the inclusion or exclusion of intra-Korean trade. That is, some sources include intra-Korean trade (trade between North and South Korea) in analyzing and calculating percent changes in North Korea's international trade, while others do not, considering it domestic trade. This makes analysis and conclusions sometimes difficult. In fact, as will be noted below, the trade statistics between North Korea and China often do not include South Korea, giving the impression that China is responsible for more than 80 percent of North Korea's trade. However, according to Stephan Haggard and Marcus Noland in their 2012 report, *Reordering Chinese Priorities on the Korean Peninsula*, this number vastly overstates China's economic power: "The actual figure, once North-South and other missing entries are accounted for, is roughly half as much: it is still a large number, but does not hold the overwhelming dominance often claimed in public discussion." However, given the preponderance and access to data that China's MOFCOM provides as well as the use of this same data by the UN and other publications, for simplicity's sake, this paper focuses primarily on FDI and trade data that treats North-South trade as domestic, not international.

Chinese FDI

China's FDI presents another problem to some degree. While MOFCOM reports China's annual outflows (and destinations) in an annual report, other analysts, in this case the U.S.-China Economic and Security Review Commission, report that nearly 80 percent of China's FDI first flows through tax havens in Hong Kong, the Cayman Islands, and others before being distributed. This, reportedly, makes independently tracking Chinese FDI much trickier. However, this paper will rely on the MOFCOM reported figures in order to stay consistent with UNCTAD, which uses the MOFCOM figures.

Over the course of the last 30 years, Chinese FDI has skyrocketed. According to the MOFCOM *2010 Statistical Bulletin of China's Outward Foreign Direct Investment*, Chinese FDI in 2010 reached \$68.81 billion. This is a meteoric rise for a country that as recently as the 1980s had FDI outflows that totaled less than \$100 million. This evolution, according to the U.S.-China Economic and Security Review Commission's March 2011 report, went through four primary periods: (1) 1979-1985, which saw China gradually open to the world economy but the central government maintain a vice-grip on foreign trade; (2) 1986-1991, which saw the Chinese government begin to liberalize and reduce restrictions on some private enterprises allowing them to invest abroad; (3) 1992-1998, which saw both successes and severe restrictions as Chinese companies began to get aggressive in the market, only to have the Asian Financial Crisis of 1997 scare the central government back into tight controls; and (4) 1999-present, which has seen significant reductions in controls and an emphasis on China's "going global" strategy.

Despite this evolution and the government's loosening of some control over FDI, according to the same U.S.-China Economic and Security Review Commission report, "Since its inception Chinese [FDI] has been initiated or approved by the state, which still retains a great measure of control." Despite these tight controls, Chinese FDI has done nothing but grow, particularly over the past five years. As of 2010, according to UNCTAD's *World Investment Report 2011*, China had become the fifth largest country in terms of outward FDI flows and seventeenth overall in terms of global FDI stock, accounting for approximately 5.2 percent of global FDI flows and 1.6 percent of global FDI stocks. In fact, despite its top-five status, China's outward FDI actually pales in comparison to its inward FDI. One of the unique features of Chinese FDI, according to the U.S.-China Economic and Security Review Commission's March 2011 report, is that rather than focus large sums in particular countries, China often chooses to spread its FDI out to many countries and in smaller amounts of less than \$10 million. In 2010, the most recent data currently available, China's Ministry of Commerce reported that China's outward FDI topped \$68.81 billion, a 21.7 percent growth from 2009's

\$56.53 billion. This increase, coupled with FDI already distributed meant that “[b]y the end of 2010, more than 13,000 domestic investing entities had established about 16,000 overseas enterprises, spreading in 178 countries globally.”

Chinese FDI in North Korea

China is the biggest, most significant, and most consistent FDI provider to North Korea, though, it must be noted, this excludes Kaesong Industrial Complex’s uniqueness as a joint-Korean venture. However, for the purpose of statistics, the UN, Congressional Research Service (CRS), and others omit this project when evaluating FDI.

China’s FDI to North Korea has not been on a steady and consistent trend and clearly has felt the effects of geopolitical events. Chinese FDI does, however, account for an increasingly large portion of total FDI North Korea receives on a yearly basis. Table 1 shows China’s outward FDI flow to North Korea since 2004, the total global FDI inflows to North Korea since 2006, and China’s percentage of that FDI. One of the above-mentioned anomalies of the disparate data sources that must be used occurs in 2009, with China accounting for 293 percent of the UN’s recognized \$2 million inflow of FDI into North Korea.

Table 1. China-North Korea FDI Relationship

<i>FDI given in millions of USD</i>	2004	2005	2006	2007	2008	2009	2010
China’s Outward FDI to North Korea	14.13	6.50	11.06	18.40	41.23	5.86	12.14
Total North Korean FDI Inflows	N/A	N/A	105	67	44	2	38
China’s % of North Korean FDI	N/A	N/A	10.5%	27.5%	93.7%	293%	31.9%

Table 1 shows the fluctuation in Chinese FDI, demonstrating North Korea’s increasing reliance on China when it comes under fire for its provocative behavior. Following the 2006 nuclear test, the Chinese proportion of North Korea’s FDI increased to 27.5 percent in 2007. In the wake of the 2008 global financial crisis, China became an even bigger factor as North Korea’s other benefactors further retreated from providing economic support, leaving China to account for 93.7 percent of the flow of FDI into North Korea. Within this FDI, Chinese companies have particularly focused on mineral resources. According to a 2010 CRS report, “This is part of a Chinese strategy of stabilizing the border region with the DPRK, lessening the pressure on North Koreans to migrate to China, and raising the general standard of living in the DPRK.” (This paper’s trade section further explores the nature of this border relationship.)

Chinese investors also appear reasonably confident in investing in the North, despite many problems with the infrastructure and business climate. Over the last several years, there have been various agreements signed between the DPRK and China, as well as laws being relaxed in both countries to spur greater investment. In fact, Glaser notes, “the Samsung Economic Research Institute based in Seoul has reported that Chinese firms have planned projects worth as much as \$6.5 billion, mostly for infrastructure development.” If North Korea and China continue to ease restrictions on the flow of FDI, it is very possible that Chinese investment in the country could continue to expand. One interesting factor that plays into Chinese FDI (and even the trade relationship) is the prevalence of foreign currency usage. It appears that most Chinese exporters to North Korea use Chinese yuan (55 percent), according to a 2007 survey analyzed by Stephan Haggard and Marcus Noland, followed by the U.S. dollar (34 percent), and then bartering (8 percent). This is also true for goods coming back into China from the DPRK, with more than 50 percent using the U.S. dollar.

China-North Korea Bilateral Trade Relationship

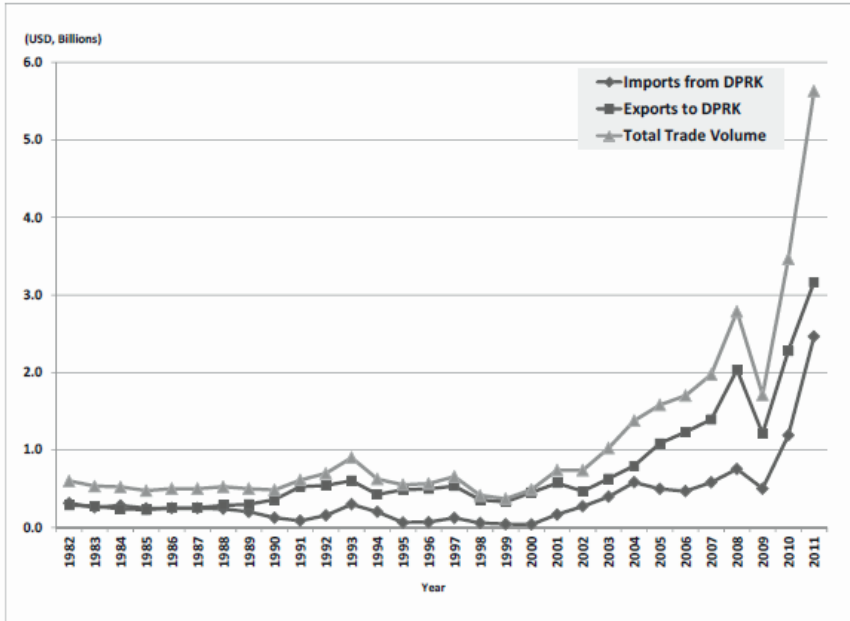
Not unlike the FDI flows discussed above, trade between China and North Korea is very much one-sided (though in this case benefiting China; Figure 1). It has fluctuated over the years but has recently skyrocketed. According to research done by Samuel S. Kim and Tai Hwan Lee, the bilateral trade relationship between the two countries goes back to the 1950s, when China made up anywhere from 25 to 60 percent of North Korea’s foreign trade, with an absolute value hovering around \$100 million. From 1960-1967, China’s percentage of North Korea’s foreign trade fell to 30 percent, then fell further to 10 percent during the Cultural Revolution, rose to roughly 20 percent in the middle to late 1970s (valued around \$300-600 million), and declined again to between 10 to 20 percent in the 1980s (but the overall value increased dramatically to \$3-4 billion). In the 1990s, trade values stabilized percentage-wise until 1998, although the overall value of the trade actually plummeted from a high-water mark of \$899 million (1993) to \$371 million (1999).

In the first half of the 2000s, North Korea’s dependency on China continued to deepen in both imports and exports. According to Yang:

From 2000 to 2005, North Korean imports from China (including oil, pork, electronic gadgets, and farming machinery) more than doubled, to US\$1.1 billion, while its exports to China (fish, low-grade steel, and minerals) soared more than tenfold, from US\$37 million to US\$499 million. Trade with China accounted for more than half of North Korea’s total exports and imports in 2005.

The volume of trade between North Korea and China continued to grow into the latter half of the decade. In 2008, the value of trade between them reached \$2.7 billion. Hyung-Gon Jeong and Hokyung Bang’s 2010 study, “An Analysis of

Figure 1. China-North Korea Trade since 1982



Source: *Stephan Haggard and Marcus Noland, 2012*

North Korea’s Principal Trade Relations,” using 2008 trade statistics produced an insightful analysis of the degree to which trade between China and North Korea occurs along the border and within northeastern China. Approximately 22 percent of all trade occurred at or near the 880-mile long border, and further, “according to Chinese customs statistics, \$2.03 billion worth of goods were exported from Northeast China... [representing] 77% of total Chinese exports to North Korea.” This trade was primarily concentrated in the provinces of Jilin, Liaoning, and Heilongjiang. These provinces also took in the vast majority of North Korean exports to China at approximately 72 percent of total exports (\$540 million). As a result, they note, “Local governments and local companies located in border areas have become North Korea’s main trading partners.” Thus,

while the central government may play a pivotal role in setting out trade policy, it is, in fact, the localities that are seeing the biggest boost from the deepening relationship between Pyongyang and Beijing.

Towards the end of the decade, the economic ties between the two continued to increase. In 2009, China accounted for roughly half of all imports that flowed into North Korea, while absorbing nearly one-quarter of all North Korean exports. China's total exports to the DPRK fell from \$2.03 billion in 2008 to \$1.89 billion in 2009 as a result of the financial crisis, but CRS notes North Korea still increased its exports to China by \$39 million, from \$754 million in 2008 to \$793 in 2009. This growth has continued through 2011 and 2012. In 2011, the *Korea Herald*, in an article titled "N. Korea's trade with China surges due to U.N. sanctions," reported that total trade between the two countries grew 62.4 percent to \$5.62 billion, and in the first seven months of 2012, bilateral trade expanded another 14.5 percent from 2011 to \$3.54 billion. During this rapid growth period (2007-2012) the relationship became further entrenched. In 2007, China accounted for approximately 67 percent of North Korea's export market, but that too has grown rapidly reaching 72.9 percent in 2008, 82.9 percent in 2009, and 89.1 percent in 2010. Further, the same report notes that one strong possibility for this is the economic sanctions that have been imposed on North Korea in the years after its 2006 nuclear test. These sanctions almost certainly have led former major trading partners, such as Japan, to reduce if not remove trade with the DPRK altogether.

Perhaps unsurprisingly, this expansion of trade has also seen growth in North Korea's already sizeable trade deficit with China. Between 1990 and 2000, North Korea saw its trade deficit balloon to a total of \$3.85 billion. This deficit resulted primarily from the fact that North Korea simply does not have high-value exports and those goods that it can export are rapidly losing competitiveness, even in the Chinese market. For the sake of contrast, Kim and Lee indicate, "South Korea's trade with China in 2000 generated a huge surplus of \$5.7 billion." The trade deficit has not improved during the course of the 2000s either. In 2008 alone, according to the CFR in October 2010, trade between China and North Korea generated a North Korean trade deficit of \$1.25 billion, followed by another deficit of more than \$1 billion in 2009. Given that North Korea is not able to finance any of its trade deficit by borrowing, some experts view this deficit "as an indirect Chinese subsidy."

V. IMPLICATIONS AND THE FUTURE OF SINO-NORTH KOREAN RELATIONS

From the evidence, it is clear that the Sino-North Korean economic relationship is, for China, insignificant, which has dire implications for the alliance. To provide some perspective on how small China's trade relationship is with North Korea, Kim and Lee's research shows that in 2000 the value of trade between North Korea and China was approximately \$488 million, or about 20 percent of North Korea's international trade. On the other hand, this made up only 0.1 percent of China's international trade. Things have not improved in the latter half of the decade either, despite the explosion of trade between the two nations. As of 2009, North Korea ranked 82nd among China's export destinations, below Kenya, Sri Lanka, and Peru. In terms of imports, North Korea was again fairly low on the list, coming in at 77th below Gabon, Yemen, and the Ukraine. However, as CRS points out in its 2010 report, "China-North Korea Relations," it is still important to note that trade between the DPRK and China has risen greatly in recent years.

While the economic implications for China may be small, the same cannot be said for North Korea. As has been noted above, trade and FDI from China is vital for the Kim Jong-un regime's continuation, as it was for his father's. This is particularly true in the economy's energy and food sectors, which Beijing is, reportedly, almost single-handedly providing. Yang notes, "China now allegedly supplies at least 80% of North Korea's energy. Pyongyang received more than 90% of the 576,582 tons of cross boarder food aid provided by China in 2005. Together with South Korea...they accounted for 85% of the total aid provided to North Korea in 2005." In addition, a 2012 *Korea Herald* report noted that China single-handedly provided some 380,000 tons of food aid in 2011.

China's investment strategy in North Korea continues to evolve. It is reported that prior to 2002, small- and medium-sized firms handled the majority of DPRK investment. However, according to Bates Gill, in a July 2011 report for the U.S. Institute of Peace, today "major Chinese investors have changed...to the current large state and private listed production enterprises. All of the projects they have invested are strategically important, their cooperation term is long, and their investment scale is huge." Much of this switch has been orchestrated, according to Glaser, by the central government in Beijing, which sees the investment not only as a platform for improving the returns China receives from North Korea, but also as "a broader government strategy to promote reform in North Korea and open up its economy." As will be discussed further below, China is well aware of the economic benefits it will receive if North Korea begins to liberalize its economy, as well as the improved regional stability that is likely to result from such an opening.

Chinese firms appear to be very focused on the mineral and mining sectors of the North Korean economy. While Chinese firms have certainly expanded beyond this sector into others such as computer hardware, analysts such as Bates Gill believe that China is the single-largest investor in the mineral and mining sector in North Korea. Given the fact that Beijing continues to struggle to find new sources of energy to feed its ever-growing domestic demand, its attempts to expand its procurement of and search for these sources into the North Korean economy is unsurprising and is likely to continue. In fact, recently, China has become interested in investing in Rason, a “Free-Trade Area” that would be largely financed by Chinese firms, not unlike the Kaesong Industrial Complex that was exclusively financed by Seoul and South Korean firms. As Bonnie Glaser and Brittany Billingsly, in their 2012 report for CSIS, note, “China views Rason as a valuable ice-free port for the land locked Chinese provinces of Jilin and Heilongjiang.” Further, according to Glaser and Billingsly, the state-owned Shangdi Guanquan Investment Company has already committed to investing some \$2 billion into the Rason area.

However, this investment and the continued messages of support and mutual gain have come under fire of late, with 2012 reports by Malcolm Moore in the United Kingdom’s *Telegraph* of Chinese mining firms coming under attack, contracts destroyed or annulled, and firms being kicked out of North Korea.

Thus, despite appearances of strong partnerships and alliances, there are still fractures, and North Korea is not always the obedient child to the China parent that the West would prefer. In fact, during a meeting with Jang Song-taek, Kim Jong-un’s close advisor and uncle, Wen Jiabao noted the difficulties that Chinese firms are having in working in North Korea. At a June 2012 roundtable series hosted by CSIS, U.S. officials and experts also noted that China’s Ministry of Finance and Commerce had recently issued guidance for how to handle working in North Korea, “which did not cast its neighbor in a positive light.” In a 2007 survey of Chinese firms operating in North Korea, Stephan Haggard and Marcus Noland found that, although the process of doing business seemed to be getting better—likely due to the ongoing six-party talks which would later collapse in 2008—there were substantial hurdles faced by Chinese companies attempting to operate in North Korea. Cell phone usage bans, inadequate infrastructure, as well as fluctuating laws and enforcement of regulations are all cited as major hindrances. Accordingly, they assert, “... [T]he overall investment climate—and even fear of outright expropriation of assets—serves as a deterrent to longer-run investment relations.” The continued difficulty of operating in North Korea puts Chinese firms in a tough spot. However, as has been noted, North Korea is so dependent on China for economic support that even China cannot use the dependency as leverage. China’s fear of causing instability by making extreme

changes to its economic policy towards North Korea means it is unlikely to take drastic measures to correct the situation. It rather relies on bilateral conversations and personal urgings to improve the business climate.

Perhaps most important to China is the geopolitical nature of the relationship and the important role Chinese investment plays in it, beyond simple economic benefits. China's desire to have stability on the Korean peninsula and in particular a friendly regime on its borders has, according to Yang, created the sense that "Beijing's hands are tied by its concerns over the collapse of the North Korean regime. Those concerns have neutralised much of Beijing's leverage over North Korea." This lack of leverage has frustrated other interested parties, which see Beijing as having significant sway over Pyongyang owing to its economic influence. In fact, some experts, such as Bonnie Glaser, believe that without the aid that China provides North Korea, the regime would collapse, particularly with South Korea's aid shipments falling off quickly in 2008. However, as China's primary goal is to maintain stability in the region and to prevent the Kim regime's collapse, China will do its best to prevent any drastic changes that will disrupt its policy aims. The CFR noted in 2010, "After all it is *not* about securing influence over North Korean affairs but is about peaceful management of the relationship with the intent to preserve the status quo of the peninsula." (Emphasis theirs)

Chinese officials believe that some combination of economic pressure along with continued bilateral conversation is the only way to nudge North Korea in the direction that China wants them to go. Although, as noted in the paragraphs above, China holds massive economic sway over North Korea, it is very much caught in a catch-22. If China suspends economic aid, it is possible the Kim regime could fall causing instability that would go against everything China is trying to preserve in the region—not to mention that South Korea and the U.S. are the two most likely countries to intercede. On the other hand, according to CSIS' Bonnie Glaser, "The Chinese recognize the need to apply pressure on North Korea to ensure that Chinese interests are protected." However, pressure alone is not sufficient, nor effective. Glaser quotes a Chinese official commenting on the 2006 nuclear test—which Chinese pressure clearly did not prevent—as saying, "If we merely rely on pressure, then it won't work. If we only promote dialogue, that also won't work...the two wheels must work together. Only if they are working simultaneously can they be effective."

It is very difficult to predict how the Chinese-North Korean relationship will evolve moving forward. Experts have consistently expected Beijing to coax Pyongyang into better behavior. Yet, even the most promising economic development along the border has proceeded slowly. According to Yang, this is due in large part to the increasing provocations by North Korea, including its

2006 nuclear test, which China reportedly adamantly requested North Korea not go forward with. However, there are also signs that China will continue to push North Korea to institute greater reforms, particularly economic ones, where it hopes to serve as a model. In a May 31, 2012 editorial in the *Global Times*, a Chinese Communist Party mouthpiece, the editors declared, "Opening up will pose risks to the Democratic People's Republic of Korea, but it will face bigger risks if it maintains its current policy. It will find out which way is better. The DPRK should understand that it has to seize opportunities." Is this an indication that Beijing is frustrated by Pyongyang's insistence on developing its internal economy, or is Beijing simply trying to acquiesce to outside demands and demonstrate that it is *trying* to promote change on the peninsula? It is, at this moment, hard to say. This is due, in part, to the recent regime change following the death of Kim Jong-il and the ascension of Kim Jong-un. Scholars believe that as the health of Kim Jong-il deteriorated, China was increasingly reticent to push for major changes for fear it could destabilize the transition in the event of the elder Kim's death. Will his son be receptive to reform? Will China push for them?

The additional wrinkle to this relationship is the political transition both countries are going through currently. As briefly noted above, under Kim Jong-un's rise to power, China was hesitant to push for any liberalization for fear of destabilizing the regime. On the other hand, the recently completed 18th Party Congress in Beijing also marks a once-in-a-decade leadership transition in China, with Xi Jinping taking over for Hu Jintao in November 2012. What do these successions in both China and North Korea mean for the future? That remains unclear. The early analysis on the newest Kim regime does not seem to indicate a radical shift in North Korea's policy, either economically or strategically. Glaser notes, "Hints that Kim Jong-un might experiment with agricultural and economic reforms have not been accompanied by any suggestion he is considering abandoning the country's nuclear weapons program." However, experts still believe that China will continue to push for some sort of economic reform, even in the face of North Korean resistance. This is not only due to China's continued desire for stability in the region, but also the economic gains that could certainly be had by further development, particularly in the provinces that border or are near North Korea.

On the other hand, there are experts who, given North Korea's track record, are far less optimistic that Chinese pressure or new leadership will change the economic situation in the DPRK in the near future. Although China has consistently implored North Korea to liberalize its economy to some degree, Haggard and Noland argue that it has made little headway:

The political economy of cross-border exchange is clearly evolving, and we cannot rule out that it will ultimately feed

into a process of economic reform. But as of this survey (2007), the evidence did not augur well. Moreover, not much has happened since to suggest that the observed patterns have undergone fundamental change; to the contrary, as we have argued elsewhere in some detail, trends toward controls have become more clear since the collapse of the six-party talks in 2008 and the extended process of succession that continues to this day.

Thus, the weak policy and regulatory framework that appears to have staying power does not bode well for China's ability to push North Korea in the direction of reform and opening. Further, according to Haggard and Noland, it even appears that North Korea is taking steps to exert greater central government control over the economic partnership between Chinese and North Korean firms in North Korea.

VI. IMPLICATIONS FOR SINO-U.S. RELATIONS

The U.S. undoubtedly plays a major role in anything that happens on the peninsula. Its troops stationed in South Korea irk Beijing, while also helping provide the stability that Beijing so strongly desires. However, in order to ensure stability on the peninsula, particularly in the event of a regime collapse in Pyongyang that leads to some sort of unification, Beijing and Washington must be ready and willing to work with each other. Therefore, good Sino-U.S. relations are imperative because, according to Snyder, in his 2001 chapter, "Korea's Influence on Northeast Asian Major Power Relations," "The question of which direction a unified Korea leans diplomatically could engender competition for a close relationship with Seoul." China will most certainly fight to maintain a strong and close relationship with a country it shares an 880-mile border with, while the U.S. may very well want to retain its forces on the peninsula. Yu's 1998 research demonstrates that China continuously expresses fears that not only is the U.S. attempting to encircle and stunt the growth of China but that Washington's politicking in the region will "lead to a redivision of Asia Pacific into competing camps, reminiscent of the Cold War era."

Regardless of China's concerns with the U.S. rebalancing or pivot, what is clear is that, according to Gill in his 2011 report for the United States Institute of Peace, "certain elements within the constellation of Chinese foreign and security policy seem to be gaining an upper hand in shaping policy toward North Korea." This means that it is possible Beijing could become more aggressive in its support for Pyongyang, particularly as Western countries increase economic and political pressure mechanisms and sanctions. This path is something that policy makers in Washington must be aware of when handling the North Korea-China situation.

Whether these more conservative and militant voices will indeed be leading the charge for China's North Korea policy or whether the more moderate tone seen in the *Global Times* editorial will become the driving force, remains to be seen. As noted above, China has recently begun its own leadership transition. The degree to which Xi will alter China's foreign policy, particularly with regard to the U.S. rebalance or North Korea, is unknown due to China's unwillingness to give its future leaders much opportunity to publicly espouse their views, if they want to rise through the CCP ranks that is. Rather, the vice-grip that Beijing has on its media means that relatively little is known about Xi, his policies, or his plans for China's future. While there have been recent reports about China beginning to take a tougher line on North Korea and its nuclear programs, Xi has, thus far, not radically changed the Chinese government's position.

Perhaps the biggest stumbling block between the two superpowers is the fact that while they share similar policy goals (denuclearization, for example), their prioritization of those goals is vastly different. Unlike the conventional assumption, however, Chinese officials claim that they always bring up the issue of denuclearization in every meeting with North Korean officials. Further, according to Glaser, they claim that they have sent envoys and letters to Pyongyang, publicly and directly condemned actions by the North that could affect Chinese security, supported UN resolutions condemning certain behaviors, signed joint statements, and denied military aid. While the U.S. priority is denuclearization, China's primary goal is stability along its borders. As a result, China's decision-making likely often boils down to simple cost-benefit analysis. For Glaser, the DPRK's recent behavior would indicate that the benefits of supporting the North Koreans and the Kim regime outweigh the "short-lived condemnation from the international community." In fact, Bonnie Glaser and Brittany Billingsly have promoted some dramatic new policy recommendations for the U.S. These would include "ensuring that economic and security benefits accrue to Beijing for helping denuclearize North Korea but also increasing the costs if China fails to cooperate." This idea of new and stronger economic sanctions against China for not leaning hard enough on North Korea is interesting, but ultimately seems ill-advised since it is highly unlikely that China would respond positively to the U.S.'s punitive economic policy, while also continuing to work with the U.S. to push North Korea to the negotiating table. As Glaser and Billingsly admit, Beijing would only be able to exert pressure on Pyongyang in the event of solid Sino-U.S. relations.

The U.S. needs to continue to work with China and reaffirm that its goals in the region are based neither on containing China, nor on preventing China's rise. As a number of Chinese editorials and academic works express, China has concerns that the increased U.S. presence in the region is meant to check China and maintain American hegemony. If the U.S. fails to convince China that this

is not the case, then there is little chance that China will feel any obligation to pressure North Korea, except when China feels its own security or regional stability is threatened. According to Glaser and Billingsly, the U.S. must make certain guarantees to China, including withdrawal of American troops from the peninsula in the event of North Korea's collapse, as well as support and aid to the collapsed regime so that China will not bear the costs of collapse alone.

VII. CONCLUSION

The Korean Peninsula has been a flashpoint and epicenter of geopolitical and economic events and crises since the outbreak of the Korean War. The armistice signed in 1953 stemmed the violence, allowing for regional politicking and economic integration. This paper explored, in particular, the FDI and trade relationship between China and North Korea. Although both FDI and the trade relationship have been a bit of a roller coaster, the past decade has seen a dramatic increase in North Korea's economic dependence on China. Yet, despite this, China has not been able—or willing—to exert the kind of pressure on North Korea that the West has demanded of it. There have been some possible signals of adjustments in China's North Korea policy, and regime change in both countries opens up new challenges and possibilities. However, the extent to which these will actually result in change remains to be seen. What this likely means is that, in the near term, the status quo will continue. China will continue to support North Korea economically as well as politically, when needed for its own advancement.



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