Money in Socialist Economies: The Case of North Korea社会主義経済における貨幣––北朝鮮の場合

Rüdiger Frank

Money in Socialist Economies: The Case of North Korea

Ruediger Frank

Introduction

Dated January 29, 2010, the Foreign Trade Bank of the DPRK (North Korea) issued document No. DC033 10-004 to diplomatic missions and international organizations present in North Korea. They were informed that the use of foreign currency was to be stopped, payments were to be made in the form of non-cash cheques, and that the official exchange rate of the Euro to the North Korean Won was changed from 188.2 KPW to 140 KPW, effective January 2, 2010.

Foreign institutions and organizations now have to obtain non-cash cheques from the Foreign Trade Bank, denominated in KPW, in order to pay for accommodations, meals and service fees in hotels, fares for transport services like railways and airlines, communication charges, inspection fees, registration fees and commissions paid to institutions and enterprises in the DPRK, fuel, office materials, spare parts for vehicles, electricity, water, heating charges and rent. Bank transfers are now mandatory for any transfers between international organizations and all money paid to institutions and organizations of the DPRK (including the salary of DPRK citizens working in embassies or international organizations).

A recent visitor to Pyongyang confirmed in a talk with the author that individuals are subject to a cumbersome process if they wish to purchase anything. Rather than using a standard hard currency or exchanging it into the new Won, they now have to obtain a receipt stating the price of the good they want to buy, then present this at a desk where they exchange their money into exactly the needed amount of North Korean money, and finally return to the shop assistant, hand over the exact amount, and receive the product.

In the preceding weeks, North Korea had made international headlines related to what seems to be a concerted economic policy initiative. The domestic currency was reformed in a way that obviously aimed at reducing the amount of money in circulation (link (http://www.nautilus.org/fora/security/09092Frank.html)). A few weeks later news emerged that the use of foreign currencies was banned (link (http://www.nautilus.org/fora/security/10002Frank.html)).

This is no doubt a dramatic move with far-reaching consequences. Money matters for personal lives and for society, so when a country initiates a currency reform, it has significant repercussions.

But what are these consequences for the specific case of North Korea in early 2010? Are people in various sectors of society better off now, or worse? Will the economy benefit or suffer? Do the reforms promote or impede foreign trade and investment? Will the domestic political situation become more stable, or will it deteriorate? Are the economic reforms of 2002 reversed, or were they intended to be a temporary measure from

the outset? Should we even interpret the currency reforms as part of the process of power succession?

Money and its functions

To understand the possible motives and effects of the above-said measures, it is helpful to briefly remember what money is actually good for.

People living in market economies, no matter how regulated or liberal these are, usually take it for granted that money serves as a means to store value, as a medium of payment and exchange, or as an accounting unit. Money translates most of our multiple and complex preferences created by taste, custom, shortage, future expectations etc. into one common language. By expressing the subjective and context-sensitive value of goods and services in terms of money, these goods become objectively comparable both domestically and across borders.

This is essential for rational decision-making on many levels for individuals, society and the state. Thanks to money, we can designate a good as cheap or expensive and decide whether to or not to buy it. We see whether the wage for a particular job is high enough or too low, a factor upon which we base employment decisions. Money helps to determine whether a person is rich or poor, and on this basis should be taxed heavily or receive welfare benefits. A producer can readily see whether costs exceed revenues, and whether the return on investment justifies the time and labor spent and the risk taken.

Money has important political functions beyond the individual realm. Central banks can promote or slow growth by adjusting the interest rate. We consider people poor if they have less than a certain amount of money available per day, and may call on the state to intervene if managers receive "excessive" bonuses. Money is used to determine and fine-tune policies such as minimum wages or social welfare. Money is also a simplistic but powerful tool to quantify the size and growth rate of an economy. In one word, our whole lives as individuals or as a group, would be unthinkable without money. This is hardly new – but still far from being the universal norm.

Money and socialism

Unlike communism, which is an ideal society that is often said to require no money, socialism is not a moneyless economy. Socialism is a child of the ideal's ugly sister, reality. As such, it is posited as an intermediary stage en route from capitalism to communism. In socialist theory, the political power of the working class has already been established, but in society and economy many remnants of the old capitalist system and values still persist and need to be overcome step by step. Money is one of these. Communist theory posits that the storage of value, the exchange of goods and services, and accounting will no longer be necessary. Superabundance of everything makes the issue of dealing with scarcity – which is what economics is all about – obsolete. Hence, under communism, there is no need for money or other forms of private property.

However, despite claims by overambitious political leaders or their badly informed Western enemies, communism has never actually been achieved. The duality of socialism and communism is much more than just a subtle difference or a synonym. When we look at the role of money in the Soviet Union, the former Eastern Bloc, or North Korea, it is clear that socialism is the name of the game.

One distinctive feature of socialism in these countries is that it is not a moneyless society. However, money as such clearly stands in conflict with the political and ideological idea behind socialism. The result is a somewhat schizophrenic situation. On the one hand, money is disdained and restricted as a source of evil, but on the other it is needed for the orderly conduct of economic affairs in naturally imperfect

socialist societies and hence is issued and circulated by the state, wages are paid in money and money circulates in markets.

The functions of money in socialist economies are nevertheless severely constrained. Most prices are set by the state for political reasons and do not reflect relative scarcity. Access to money alone is often not enough to purchase something; goods must also be physically available, one has to have access, and sometimes even a permit to buy. Individuals may think that they store value by accumulating money, enterprises may attempt to do rigorous accounting, bureaucrats may believe that they maintain fiscal stability, but they cannot know for sure. Money in socialist societies is only imperfectly exchangeable into other goods. It can only with strong limitations be used to estimate the absolute value of something, and even relative value (for example, "how many months must I work for a car?") may be indeterminate. Under socialism, prices keep sending signals – but frequently the wrong ones.

In any society the flow of goods and services must be regulated somehow. If money is incapable of accomplishing this, coping strategies emerge. These include barter trade, the use of foreign (hard) currencies, or the use of political capital. Regarding related effects, the experience of the Eastern Bloc is rich and telling (see, among others, Rüdiger Frank and Sabine Burghart (http://www.praesens.at/praesens/index.php?option=com_content&view=article&id=544:978-3-7069-0569-5&catid=55:suedostasienwissenschaften&Itemid=53), eds., Driving Forces of Socialist Transformation. North Korea and the Experience of Europe and East Asia).

North Korea - A "better version" of socialism?

Its undisputed particularities notwithstanding, North Korea is a socialist economy, one in which the action of market forces is severely limited. For a long time, it looked like a textbook case of Janos Kornai's (1992) model (http://press.princeton.edu/titles/5010.html) of a classical socialist economy. For decades, there was no free interplay of supply and demand, prices were set by the state, and coordination of economic activities took place centrally and via administrative tools rather than spontaneously and regulated by money. The focus of production was on quantity, there was no labor market, and barter trade was dominant with socialist partners and domestically. However, until the mid-1990s, unlike its Eastern European brothers, North Korea had not excessively violated its own ideological and political principles in terms of running the economy.

Most importantly, North Korea was long able to avoid the most dangerous political effect of being poor – embarrassment. Unlike in East Germany, there were no capitalist cars driving the country's highways. Under the transit agreement effective since 1972 (link (http://de.wikipedia.org/wiki/Transitabkommen)), West Germans could use East German highways on their way to West Berlin from Hamburg, Hannover or Munich. This earned the forex-hungry state an annual fee payable to the Foreign Trade Bank of initially 235 million Deutschmarks, rising to 525 million Deutschmarks in 1989. The political price for what seemed to be a good economic deal was high. Millions of families, crammed in their outdated, noisy and smelly, yet still beloved and cherished Trabant or the slightly better Wartburg, Skoda or Lada cars, saw their pride crumble to dust on the Autobahn as Mercedes, BMWs, Audis and the other shiny products of Western car makers drove by slowly (they were careful to observe the speed limit, as hefty fines were another source of hard currency for East Germany). Propaganda did its best to point to the downsides of capitalism, but to no avail.

The number of visitors from South Korea, Japan or other Western countries to North Korea was small and their movement was restricted. No parcels were sent regularly to the North by their Southern relatives. In East Germany, hundreds of thousands of parcels arrived for the Easter and Christmas holiday seasons. And an East German state-run company called "Genex (http://de.wikipedia.org/wiki/Genex)" even specialized in arranging gifts from West to East by mail-order catalogue.

In North Korea, at least in the pre-DVD age, no Southern TV could be watched, while Western TV was legal since the 1970s in East Germany for most of the population. With the exception of rare film festivals, there were no foreign movies in North Korean cinemas. North Korean youth might have heard about Southern pop-stars, but they were not omnipresent as Western music was in East Germany. Until a few years ago, hard currency stores were rare and the possession and use of other than the domestic currency was banned in North Korea. Unlike East Germans travelling to Prague or Lake Balaton in Hungary, North Koreans abroad did not feel like second class Koreans, the ones with the "wrong" won, since few could travel abroad.

While in East Germany the state sold a total of almost 34,000 political prisoners to the West at an average fee of 90,000 Deutschmarks (Rehlinger 1991 (http://books.google.at/books?id=FM-fOwAACAAJ&dq=Rehlinger+Freikauf&source=gbs_book_other_versions_r&cad=6)), there was no sale of political prisoners to the South (or no such offers?). North Koreans did not long for bananas and coffee, as these were widely unknown and in any event there were much more substantial worries.

The main reasons why the North Korean state could afford not to follow the East German example were a lower developmental level, which facilitated curtailing individual consumer demands including the hunger for imported products, and the sharply reduced role of money by way of rationing and limited economic contacts with the West. Nicholas Eberstadt, a long-standing expert engaged in economic research on North Korea, wrote in a recent article (http://online.wsj.com/article/SB10001424052748704500104574651090133811018.html?mod=googlenews_wsj#articleTabs%3Darticle) in the Washington Post that Kim Il-sung's country had come very close to a complete demonetization of its economy in the 1980s.

As odd as it may seem, such demonetization was indeed rational if we think about the basic long-term incompatibility of socialism and money. Instead of trying to force an unfitting capitalist mechanism to work for a socialist economy, it was largely discarded. This is particularly true for the domestic economy. The Public Distribution System in combination with nominal state-set prices ensured that goods and services were made available according to the will of the country's rulers. Accordingly, there was no need to sell the country's pride for hard currency. And poverty, if it goes beyond the basic level of Maslov's pyramid of needs, is always relative. Most North Koreans might have been poor in absolute terms, but not so if they looked at their equally poor neighbors in the same village or apartment bloc.

In addition, there was the trade-off between poverty and honor: emphasizing the adequately customized tradition of militant Koguryŏ (see Petrov 2004 (http://www.aks.ac.kr/book/pdf/7-3-9-Restoring%20the%20Glorious%20Past.pdf)), North Koreans were taught to look down upon the heirs of Shilla to the South who lived a life of luxury while the spartanic warriors up North kept the nation's enemies at bay. Better being poor but proud, rather than rich and the lackeys of the hook-nosed Americans and their Japanese allies. We should not overstate this point, but it is hard to deny that nationalist considerations and what Selig Harrison called (http://press.princeton.edu/titles/7260.html) a "siege mentality" along with rally-round-the-flag phenomena play a particularly powerful role in (North) Korea.

Violating its own rules

Until the late 1980s, North Korean society functioned badly, but it functioned. All the pitfalls of spooning with the enemy as observed in Europe could be avoided. People ate, went to school or work, received ideological training, lived, loved, and died. Ever since the mid-1950s and more visibly since the mid-1960s, North Korea had refused to join the experiments of other socialist countries with collective leadership and peaceful coexistence, with revisionism and dogmatism, with market socialism, glasnost and other dangerous ideas. Then, after the turbulent last decade of the century, this changed dramatically.

The reasons are subject to guessing and largely remain a mystery. They presumably included the disappearance of socialist trading partners after 1990, the change of leadership in 1994/1997, and of course the dramatic famine of 1995-1997. In 1998, for the first time ever, a president took office in South Korea who was not strongly-anti North Korea, which might have relaxed reservations about economic interaction. China and Vietnam showed successes in building a market economy while maintaining a one-party monopoly on power, which certainly must have encouraged the North Korean leadership to consider this alternative. So the Mt. Kŭmgang tourism project was started, the first inter-Korean summit meeting took place in June 2000, and Kim Jong-il wrote, in a rare Rodong Sinmun article on January 4th, 2001, that North Koreans should prepare for a new era, acknowledge the changed environment and discard old methods (available only in the printed Korean version, not on KCNA (http://www.kcna.co.jp)).

Strangely, and tragically, many observers failed to acknowledge or appreciate this turn even after the economic measures of July 2002 and early 2003 that eliminated state subsidies, devalued the domestic currency, upgraded the farmers markets, introduced a rudimentary macroeconomic policy, permitted more private economic activities, and essentially monetized North Korea.

My personal observations on the ground could not have been more contrasting. As a language student in Pyongyang in 1991, I could only shop

in hotels and hard currency stores using foreign exchange certificates, and otherwise had to rely on allotments not only for food but even for subway rides.

Different Foreign exchange certificates existed for foreigners from socialist countries such as China (red), and for Westerners (green-blue). Similar FECs also existed in East Germany (Forum Scheck), China, and Cuba.

A decade later the economy was monetized. Foreign Exchange Certificates were abolished, Euros and Dollars could be exchanged for North Korean won or spent directly. There were markets seemingly everywhere, large and small ones; legal and semi-legal restaurants and shops opened, Chinese merchants rushed in and found eager students primarily among resolute women who soon discovered and mastered the art of trading. During one afternoon walk in Pyongyang in 2004, I entered shops with prices marked either in domestic currency, US Dollars or Euros. True, North Korea was not yet a market economy, but it was a far cry from the largely moneyless society it had so recently been.

An economy previously hostile to consumers now tried to lure customers with lovingly hand-crafted posters and signboards and even the announcement of discounts (link (http://www.japanfocus.org/-Ruediger-Frank/2099)). Clearly, money mattered. State, officials and private individuals alike did what was common almost everywhere else in the world – they tried to get hold of some of the wealth of foreign visitors. The level of sophistication was low, but in principle, North Korea was, at least in this respect, on the way to becoming less extraordinary if not to say normal.

The effects of monetization

Not surprisingly, the delegation of some allocative functions from the state to money did the same harm to socialism's legitimacy and the government's credibility in North Korea as it did in the Eastern Bloc decades before.

As soon as North Korean currency developed from worthless paper into real money, people reacted. At what Pyongyang officials will have seen as breathtaking speed, the decades-old paths along which North Koreans planned their lives were put to the test and supplemented or even in some cases replaced. Money had become a serious competitor to political capital. The latter was firmly in the hands of the state; but money was much harder to control. Prior to the monetization, individuals either complied with the state's rules or had no career. Now they had the option to give the state the cold shoulder and gather prestige, wealth and power through money making that was beyond the reach of the state. Many made use of this.

The whole ideological foundation of North Korea's society was shaken. Previously united in poverty but also in economic equality, and employing nationalism and xenophobia to fill the vacuum left by a lack of opportunity for individual fulfillment, society was quickly divided into those who were and those who were not able to use the new chances. Pyongyangites, the privileged few with superior access to food, education and state jobs, were stunned to see how the traditionally poor people of North Hamgyŏng and other provinces bordering China suddenly became affluent. Chinese goods and Chinese merchants flooded the country,

generating a worrisome déjà-vu for history conscious North Koreans who recalled that this was how Japan prepared colonization in the late 19th century. Officials had accepted favors before; this is an inevitable side effect of overregulation anywhere. But now corruption reached new, almost limitless levels as cash, not computers, watches, cigarettes or liquor were demanded and offered. With money, one could get almost anything; state and individuals reacted.

The North Korean state started to sell its people, its land, and its pride just as East Germany had done. This is how we can interpret the Kaesŏng Industrial Zone, where tens of thousands of young North Korean women worked for capitalists – the definition of exploitation. They did so at a fraction of a South Korean wage but at higher wages than those on offer in North Korea's own factories. Hard currency began to push all other considerations aside. Their male superiors from the South provided a glimpse into the shiny life in hypermodern South Korea. Cars, mobile phones, MP3-players, fashion – although the situation differed, the North Korean women must have felt as jealous and embarrassed as the East German family driving in its Trabant. The same, although on a smaller scale in terms of affected North Koreans, happened in the tourist zones.

On a macroeconomic scale, inflation, formerly hidden, now became visible. It reduced fixed salaries heavily, adding pressure on officials and employees at state-owned companies to find alternative ways of making money. In the first years after the economic measures of July 2002, i.e. the official monetization, inflation reached levels estimated at 200% annually (link (http://www.asiaquarterly.com/content/view/172/43/)). Eberstadt (op.cit.) provides his own estimate of inflation in North Korea. Based on the black-market exchange rate with the US Dollar, by November 2009 the North Korean won had fallen to just 5% of its 2002 value, a depreciation averaging over 3% per month. The denial of access to international markets for goods, services, technology and capital did little to help the North Korean government to overcome these difficulties. The collapsed deal with Japan in late 2002, i.e. the exchange of abductees against normalization and big economic aid, is just one case in point. The timeline is indeed intriguing (Frank 2005 (http://www.informaworld.com/smpp/content~content=a714023786&db=all)).

All the state could do was watch, wonder, and worry. As long as money had existed as a mere formality, access, distribution and value were of secondary importance and subject to high levels of state control. With monetization, this changed dramatically. Not only did money emerge as a serious competitor to the state; it became a yardstick to measure the state's performance and hence had a direct influence on the legitimacy of North Korea's political system. The DPRK had taken the crucial step to enter its enemy's game, the money game. It is not surprising that as a beginner, without much training and lacking most of the necessary capacities, it did not do too well.

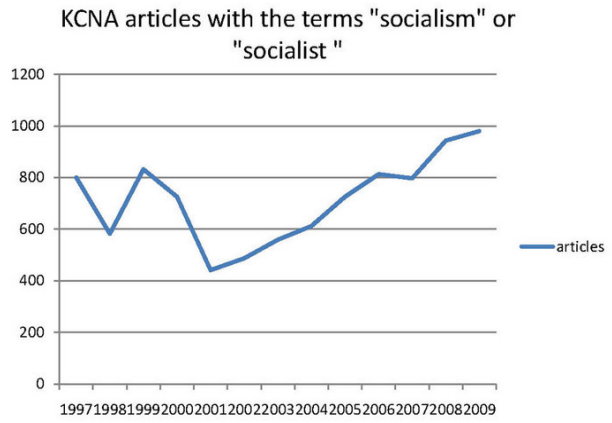
At the same time, to exacerbate an already complicated situation, the after-effects of 9-11 struck. Afghanistan, then Iraq was attacked and the elite replaced, demonstrating not only the destructive power of US military might but also its determination to use it. North Korea was singled out as one of the next potential targets by the George W. Bush administration.

So, the economic reforms threatened to destroy North Korean socialism while internally at the same time the external enemy threatened to strike at any moment. We can speculate about a domestic power struggle, discontent among parts of the elite who worried that their country would follow Europe, bitter letters of protest coming from supporters of the system in the provinces who could not understand how Pyongyang was

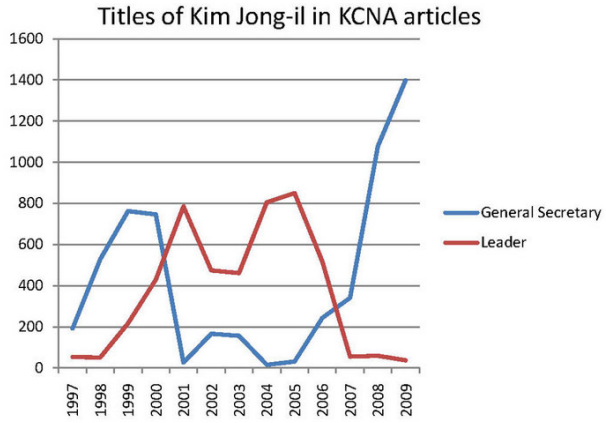
allowing greed and individualism to destroy the united front of collectivist North Korean society.

Turning back the wheel

The currency reforms are so far the most dramatic attempt to respond to the situation described above. It is a bit of a mystery why it took the North Korean leadership so long to pull the emergency breaker and try to turn the ship around. Obviously, it needed some time to fully appreciate the effects of monetization on their society. By 2005, it seems, the process of learning and developing a strategy to react had reached the stage of action. The financial activities of international organizations were restricted, and the first limitations appeared on domestic trading in the markets. Ideology reflected this trend by a growing emphasis on orthodox formulations including "socialism". While throughout 2001 and 2002, the term had been used in a total of 441 and 487 articles, respectively, on the official website of the Korean Central News Agency (KCNA (http://www.kcna.co.jp)), their number more than doubled in 2009 (980 articles) and thereby even surpassed the pre-reform peak of 1999 (832 articles).



The title of the leader reflected the changed mood in North Korea, too. In 2009, KCNA in 1,398 articles used the term "Secretary General" (ch'ongpisŏ), emphasizing his function as head of the Party. In 2005, this title was used in only 31 articles, whereas "Great Leader" (widaehan ryŏngdoja) appeared 850 times. The latter had dropped to 37 in 2009. That is, the more statesman-like title "Leader" was replaced during the reform years to lend greater emphasis to Kim Jong-il's ideological position as the Party's leader. Interestingly, the third and allegedly most important position that Kim Jong-il assumes - that of the top military commander is only reflected in the Korean-language version of KCNA, and even there only weakly (71 articles in 2009). The English edition rarely uses the title "general" (chang'gun) at all, and if so, only in referring to praise by foreigners or to songs sung by North Koreans to his glory.



Other key phrases of orthodox North Korean socialism such as collectivism (chiptanjuŭi) reemerged, campaigns were led against non-socialist hairstyles, a virtual ban on Western dress for women (but strangely, not for men) followed. Then, the state tried to limit trading – i.e., petty capitalism – by issuing regulations stipulating the minimum age of women who engaged in this business. These reports have not been officially confirmed but it seems that, in a gradual process, women under the age of 50 were banned from working as merchants, apparently to no avail.

Eventually, these careful and gradual attempts at curtailing the markets were transformed into more active approaches at reviving the alternative – a centrally planned economy. In December 2008 Kim Jong-il visited Kangsŏn and

resuscitated the Ch'ŏllima-movement that had been started there half a century before, stressing massive increases in the input of ideologically motivated labor for the increase of productivity and the achievement of economic growth. After having fallen to as few as 15 articles in 2003 (and in 2007, too), the frequency of the mention of "Ch'ŏllima" on the KCNA website reached the 1999 level in 2009 (125 articles). This has led me to identify a neo-conservative trend in North Korean socialism (link (http://www.nautilus.org/fora/security/08032.Frank.html)), not to be misunderstood as neo-liberal, but rather as neo-orthodox. "Conservative" in the North Korean context means no more experiments, and instead greater state control and coordination, a renewed emphasis on self-sufficiency, a hard-line stance in foreign policy and severely regulated contacts with the outside world.

Still, it is important to note that the North Korean government had for a long time refrained from simply closing the markets and massively cracking down on the newly emerging group of people who made a living not as workers, farmers or officials, but by virtue of their own, more or less private economic activities. Their lives were made harder and harder, but it was still possible for them to continue their ventures.

Part one of the currency reform: expropriating the new middle class

Hence, the first part of the currency reform of December 2009 should be seen as heralding a new stage in the government's quest to reinstall the status quo ante, i.e., orthodox our-style socialism of the 1970s type. By allowing only a very limited amount of money to be exchanged per person, the state effectively devalued almost all domestic cash. Naturally, the hardest hit were those who had accumulated large amounts of money. There were two ways to become a KP Won-millionaire in North Korea: corruption and trading. Obviously, neither of these was in any way helpful for preserving the legitimacy and credibility of the one-party state, indeed, quite the reverse. So, in the face of mounting problems, the authorities finally decided to take action.

Anecdotal reports have indicated dissatisfaction with the currency reform in the form of small-scale riots, a form of protest that has hitherto rarely been reported from North Korea. The validity of such news notwithstanding, it is clear that the state took a serious risk by ending the dangerous market activities all at once. The risk is two-fold. First, it was not clear how the beneficiaries of the market would react. The state was well prepared for this, since all stores were closed and security forces were sent to the places where protests seemed likely to emerge. Equally important, and the North Korean state seems to have underestimated or not considered this at all, the destruction of the markets as a major distribution channel for staple food and other necessities created a vacuum.

One would have expected the state to prepare for taking over this crucial function of the markets instantly, but again based on anecdotal evidence, this was apparently not the case. To speculate wildly, the simplistic logic of the state could have been that if the goods are taken from the markets, they would automatically reappear in the state's coffers and could be distributed as rations by the revived Public Distribution System. However, the planners did not consider two problems: hoarding (a typical feature of socialist economies), and the instant drop in inflows of food from China. The latter refers not primarily to official trade, but above all to the supplies brought in by numerous traders and intermediaries semi-officially across the long border in the North on both sides of Mt. Paektu. This trade bypassed statistical recording but might well have amounted to over 500,000 metric tons of food annually.

The results must have been dramatic. Traders withheld what they had stored as they were not

sure what the new prices would be; buyers could only offer a currency that was now worthless, or a limited amount of the new currency. Accordingly, prices shot through the roof and created a mood of hyperinflation. The latter discourages saving, but it also discourages selling, since astute business-minded people would try to convert whatever they had accumulated into goods of stable value, such as gold, rice, or hard currency. Real estate was a less opportune option since, as the German term "Immobilie" indicates, it cannot be moved and hence is a risky investment in times of state crackdown on private economic activities.

Part two of the currency reform: closing the loopholes

It seems that most wealthy North Koreans and their Chinese partners opted to convert their fortunes into hard currency. This is the most logical step; gold is hard to get quickly and in large quantities, and it is cumbersome to store or transport. The same is true of rice. But Chinese Yuan, US Dollars, Euros etc. were relatively easy to come by via China or middlemen and promised to be more or less stable in value. Most deals beyond the basic level of the actual markets had been conducted in hard currency anyway.

This was of course not unknown to the North Korean state. Therefore, one month after the first currency reform that had devalued the domestic money, it issued a ban on the use of foreign currency. This is not necessarily an extraordinary move, as there are only a few countries where regular transactions legally take place in other than the national currency. However, the intention of the forex ban in North Korea was clearly connected to the goal described above, i.e., to reestablish state control over the economy. Hard currency was seen as a loophole to bypass the effects of the first 2009 currency reform, and this loophole would be filled.

The effects are not yet clear. Obviously, the ban on the use of foreign currency hits those who in the past were able to benefit from access to this rare good; this includes not only middle-aged women from the villages or intermediary traders from peripheral Northern provinces with relatives or ties in China. It affects a large part of the central bureaucracy with close connections to the center of power. Their reaction will not be seen on the streets. Rather, it will take place behind the scenes, but that will not make it less powerful. Officials who lost access to power, affluence, and a future for their children in the reforms will ask for alternatives. If the state can offer these – fine. If not, frustration will build among this key group that Segert (2009) (http://www.amazon.de/gp/search?index=books&linkCode=qs&keywords=3205781546) has called the "Dienstklasse" (service class).

Certainly, foreigners in North Korea will quickly feel the inconvenience of not being able to pay their bills directly. This will not lead to the closure of embassies, but Western investors will have one more reason not to come to North Korea. The state has significantly improved its capabilities to control the economic activities of foreigners in the country, but it has also raised transaction costs. These do not matter for all investments, such as those made for political reasons or those backed up by strong political interests, including the US$ 10 billion by China that were reported in mid-February 2010.

There is no indication that the North Korean state wants to end economic exchange with the outside world. However, stage one and stage two of the currency reforms reveals the strong determination to return to the driver's seat and to be in full control of the domestic economy as well as of foreign economic relations. The vision of the planners in Pyongyang is a domestic population that is supplied via state distribution and rationing, and foreign trade and investment that are channeled through the Ministry of Foreign Trade, the Foreign Trade Bank, and the Foreign Investment Bank rather than via single ministries

or even, beware, single enterprises. This would be a return to the pre-reform system, and in fact, to the pre-Kim Jong-Il system. Has the current leadership given up on reform?

The new money – a glance at succession?

Again we are speculating, but it's worth recalling how mysterious the sudden introduction of economic reforms in the early 21st century was and still is. Of course it has to do with the famine of 1995-1997 and the partial anarchy that emerged as a short-term consequence in a few areas. But is the often stressed image of a "state that grudgingly and without having any choice simply acknowledged changed realities" really enough to explain why the same state pushed actively for the far-reaching and risky reforms of 2009 that we have described? The currency reforms have shown clearly that the North Korean state is able and willing to end a phase of economic experiments and relative laxity if it wants to. Why did this not happen in 2002, five years after the end of the worst of the famine, when the chance existed to return to the status quo ante?

It is largely undisputed that the political system of North Korea is a form of authoritarianism, with the leader being a strong central figure. Any major development, including those in economic policy, would be unthinkable without the consent of the leader. In fact, the North Korean system is hardly reputed for fostering much creativity or initiative at lower levels of power, so Kim Jong-il might himself have had the idea of trying some Chinese-style changes. His article in the Rodong Sinmun of Jan. 2001, cited above, is one indicator of his personal and decisive involvement.

Interestingly, rumors about his health and about succession have coincided with the harsher parts of the North Korean campaign to return to orthodox "our-style" socialism, including the second Ch'ŏllima movement, the currency reforms, and the subsequent attempted closure of markets. One often heard interpretation is that he stands behind these moves in order to prepare the ground for a transfer of power to his youngest son Kim Jong-eun. This is a questionable conclusion, since few people will remember the work-harder-campaigns of the 150- and 100-day battles as pleasant, or the currency reforms as an encouraging sign.

We should take into consideration the possibility that the end of market-oriented reforms and the neoconservative swing might have to do with the weakening position of Kim Jong-il. He has never done much to prepare one of his sons for succession; but suddenly, as soon as his health gets worse, we see almost hasty moves. Who is behind them - Kim Jong-il who is preparing a smooth transition to the next generation, or the paladins who worry about their power and act to assure that the public is presented with a succession model that is easy to understand and needs less preparation than, for example, the more substantial transformation to a collective leadership?

It is no coincidence that the new currency contains some information on succession, in particular the bank notes that are dated 2008, although we do not know for sure whether they were actually printed in that year. Alas, North Korea has been famous for dealing very creatively with dates on paper. In any case, in December 2009 for the first time in North Korea's history there is a reference to another real person on the country's money. While the highest note (5,000 Won) appropriately bears a picture of the Eternal President Kim Il-sung, the second-highest bill (2,000 Won) shows a place that every North Korean child can identify without fail. This is the log cabin in the secret camp beneath a rock that came to be known as Jongilbong, named after Kim Jong-il who according to official North Korean historiography was born here on one cold February night of 1942 in the midst of the heroic anti-Japanese struggle that his parents and their

fellow guerillas were leading. The name "Jongilbong" has been carved deeply into the rock to confirm this event. The third highest bill (1,000 Won) shows the birthplace of Kim Jong-il's mother Kim Jong-suk in Hoeryŏng, North Hamgyŏng province.

One precondition for Kim Jong-il to be able to pass his power on to one of his sons is that he improves his own position in the North Korean hierarchy of power. Since 1994, Kim Jong-il has been more the loyal son of Kim Il-sung than a leader in his own right. If the reference to him and the family on the banknotes is aimed at elevating Kim Jong-il's legitimacy to a more independent status, then this would indeed be a sign of preparation for a hereditary succession. However, we have yet to see more of this, such as a statue of Kim Jong-il or a Kim Jong-il plaza. The "revolutionary family" of Mt. Paektu including Kim Il-sung's first wife Kim Jong-suk has been venerated for years; this is still the image of the first generation passing on power to the second. The third generation does not yet appear; at best we could argue that the emphasis on the bloodline as such would benefit one of Kim Il-sung's grandsons.

In this regard, the new money clearly shows a significant development, but it seems too early to determine precisely the meaning for succession of the reference to Kim Jong-il and his mother on the new notes.

Outlook: The future of money in North Korea

The current state of affairs is unclear. The document cited at the beginning of this paper shows that by the end of January 2010, any use of hard currency was prohibited. By mid February, reports emerged that the state had relaxed its regulations. The latter would be surprising and indicate a really (too?) quick retraction of the most significant economic policy measure of recent years. It is too early to make an even weakly educated guess here.

But from a long-term perspective, it seems safe to say that even if, and this is a big if, the currency reforms manage to achieve the goal of reestablishing the state's control over the economy and its domestic and external transactions, this is unlikely to remain stable for more than a few months or years, since the key problems of the North Korean economy remain. The systemic deficiencies led to the famine of 1995 and to the reforms of 2002, and there is no reason to believe that such events will not be repeated. The heart of the problem is that the North Korean state in its current form will most likely not survive another Arduous March. Society has changed along the lines outlined above; this is no longer the same North Korea, even if outer appearances can be restored. Too many people have gotten a taste of how an alternative economic model could work. As soon as the typical problems of a strictly centralized socialist economy reemerge, and this won't take long, there will be voices in various strata of society demanding a repetition of the market-oriented reform experiment, this time avoiding earlier mistakes. Re-monetization will be part of this, one way or the other.

If a collapse can be avoided, and there is at least some reason to be optimistic here given North Korea's demonstrated resilience, a less xenophobic and smarter leadership in Pyongyang could cooperate more closely with its Chinese neighbors and enlist what has been the

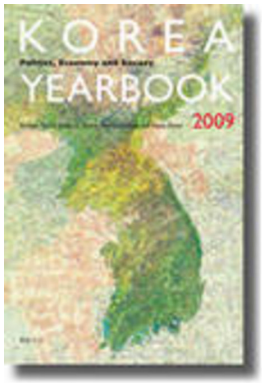
secret of all economic "miracles" in post-1945 developmental dictatorships including the one south of the 38th parallel – strong, if not unconditional politically-motivated support by a powerful and potent ally.

Meanwhile, the language of North Korean propaganda had become more militant by 2009. The word "confrontation" was used in 162 KCNA articles in the year of the inter-Korean summit (2000) but rose to 562 in 2009, which was still more than twice as many as in 2006 (the total number of articles has remained relatively stable). On the other hand, we should also mention that the frequency of "friendship" (ch'insŏn) in the Korean-language version of KCNA rose to 849 in 2009, up from just 60 in 2002 (and from 407 to 639 in the English language version). So it seems that North Korea is not only targeting its enemies more intensively but also emphasizing alliances with friendly nations such as China and Russia, as well as the once much-touted South-South relationship and the Non-Aligned Movement.

The experience of European socialism has taught that once "real" money is allowed to circulate, there is only one way forward. Monetization without letting money fulfill its functions will create a contradictory situation that can quickly turn out to be lethal for a half-hearted state. With some luck, the currency reforms have won North Korea time to take a breath, resolve crucial issues including the future of its political leadership, and develop a better reform strategy with the help of its Chinese ally.

Ruediger Frank is Professor of East Asian Economy and Society at the University of Vienna and an Asia-Pacific Journal associate. He is Deputy Chief Editor of the European Journal of East Asian Studies (http://www.ejeas.net) and a co-editor of The Korea Yearbook (http://www.amazon.com/dp/9004180192/?tag=theasipacjo0b-20), published annually since 2007. He wrote this article for The Asia-Pacific Journal. He can be contacted here (http://wirtschaft.ostasien.univie.ac.at/).

Recommended citation: Ruediger Frank, "Money in Socialist Economies: The Case of North Korea," The Asia-Pacific Journal, 8-2-10, February 22, 2010.



(http://www.amazon.com/dp/9004180192/?tag=theasipacjo0b-20)

Click on the cover to order.

Rüdiger Frank (/authors/view/8798)

Rüdiger Frank is Chair and Professor of East Asian Economy and Society at the University of Vienna and Head of its Department of East Asian Studies. He is also an adjunct professor at Korea University and the University of North Korean Studies (Kyungnam University) in Seoul. He holds an M.A. in Korean Studies, Economics and International Relations and a Ph.D. in Economics. In 1991/1992, he spent one semester as a language student at Kim Il-sung University in P'yŏngyang and has been researching North Korea ever since. Visiting positions have included Columbia University New York and Korea University, Seoul. He is Vice President of the Association for Korean Studies in Europe (AKSE) and acting President of the U.S. and Hong Kong-based Asian Politics and History Association (APHA). He is also Deputy Chief Editor of the "European Journal of East Asian Studies" and an Associate of "The Asia Pacific Journal". He is the founding editor of a new book series at Brill titled "Security and International Relations in East Asia". His major research fields are socialist transformation in East Asia and Europe (with a focus on North Korea), state-business relations in East Asia, and regional integration in East Asia. His most recent books are: (with S. Burghart, eds., 2010): Driving Forces of Socialist Transformation: North Korea and the Experience of Europe and East Asia (http://www.amazon.com/dp/3706905698/?tag=theasipacjo0b-20), Vienna: Praesens, (ed., 2011): Exploring North Korean Arts (http://www.amazon.com/dp/3869842148/?tag=theasipacjo0b-20), Nuremberg: Verlag fuer Moderne Kunst, (with Heung Chong Kim and Sung-Hoon Park, eds., 2012): Korea and East Asia in a Changing Regional and Global Environment (http://www.kiep.go.kr/eng/publications/pub02_view.jsp?page=6&no=185776&sCate=&sSubCate=&field=&text=), Seoul: KIEP and (with John Swenson-Wright, eds., 2013): Korea and East Asia: The Stony Road to Collective Security (http://www.amazon.com/dp/9004229108/?tag=theasipacjo0b-20), Leiden and Boston: Brill.

For more information, see http://wirtschaft.ostasien.univie.ac.at.

For publications, see http://univie.academia.edu/RuedigerFrank
Email: ruediger.frank@univie.ac.at (mailto: ruediger.frank@univie.ac.at)