

**Does North Korea Follow Vietnam's Path? :
Institutional Constraints**

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North Korea pursued an ideology of *Juche* or self-reliance since the 1950s and isolated itself from the world economy. The *Juche* policy consists of three elements, political independence from all foreign powers, economic self-sufficiency and military self-defense. North Korea has fostered a military-industrial complex with a belief that promotion of heavy industries would make both its economy and military stronger. In its development process, North Korea had avoided foreign direct investment and neglected international trade relations because of its distrust of foreign powers and fear of being exploited by Westerners. Until 1960 actual economic performance exceeded highly set targets owing to mass mobilization and moral incentives. However, in the long run, the outcome of the *Juche* policy under a command economy was disastrous because of lack of economic incentives and sub-optimal decision making process by a few political elite.

North Korea's economic crisis occurred in the 1990s when drought and floods hit the nation already suffering from poor economic performance due to inefficiency of the command economy. North Korea's 1990s were characterized by negative economic growth with an average growth rate of -4% during 1990-1998 as shown in Figure 1. After 50 years of implementation of the *Juche* policy, North Korea ended up with isolation from the globalized world, poor infrastructure, technological obsolescence, uncompetitive industries, and poverty-ridden economy, while other former command economies such as Russia, China and Vietnam, have made economic progress with adoption of a market economy and implementation of their economic reforms.

Confronted with an economic crisis during the 1990s, the North Korean regime began to introduce economic reforms in 2002, increased its trade with other countries and opened free trade zones to induce foreign direct investment. Furthermore, the six-party agreement in February 2007 offered various incentives for North Korea. The short-term benefits that North Korea may receive according to the agreement included provision of fuel most needed by North Korea and removal of North Korea from the US terrorist list. In the long run, North Korea may have far greater benefits which include normalization of external diplomatic and economic relations, negotiation of bilateral and multilateral trade agreements, lift of the US and Japan economic sanctions and permission of North Korea to join international institutions such as the World Trade Organization (WTO), World Bank, International Monetary Fund (IMF) and Asian Development Bank (ADB).

Recent changes occurring in North Korea remind us of what happened in Vietnam during the 1990s. Vietnam started its economic reforms, so-called *Doi Moi* in 1986 with the openness policy. Since then Vietnam obtained normal trade relations with EU, Japan and many other countries in the late 1990s and successfully negotiated permanent normal trade relation with the US and succeeded in joining the WTO in 2006. After obtaining normal trade relations with advanced countries, Vietnam's trade has accelerated, which has contributed significantly to Vietnam's economic growth.

The purpose of this paper is to review North Korea's economic reforms and their effects on trade and foreign direct investment and to examine whether North Korea can be as successful as Vietnam in its pursuit for economic growth. We will also investigate whether there are any institutional constraints preventing its advance to economic prosperity. Section 2 reviews North Korea's economic reforms, section 3 analyzes the trend and patterns of North Korea's trade and

foreign direct investment. Section 4 introduces Vietnam's *Doi Moi* policy and evaluates its economic effects. Section 5 compares North Korea and Vietnam in their economic conditions, competitive positions and economic reforms. Section 6 analyzes institutional constraints to North Korea's pursuit of emulating Vietnam's success. The last section summarizes this study and draws some conclusions.

North Korea's Economic Reforms

In planning and implementing economic reforms, the North Korean regime adopted a Chinese style approach with economic reforms preceding political reforms as it learned from the Russian failure of the shock therapy approach of concurrent political and economic reforms and heeded the Chinese success of a gradual approach. In more recent years, it seems that North Korea has been more interested in the Vietnamese approach of economic reforms, which is even more gradual than the Chinese approach.

According to Yazhou Zhoukan Weekly on October 27, 2007, North Korean leader Kim Jong-il expressed an intention to benchmark Vietnam's two decades-old reform and openness policy *Doi Moi*. Vietnam has pursued the reform and openness policy since 1986 to introduce a market economy, and to liberalize trade and investment with foreign countries to a certain degree. With 20 years of implementation of the *Doi Moi* policy, Vietnam achieved high economic growth, an average growth rate of 7.5% for the period of 1990 -2007. During the Asian financial crisis of 1997-98, North Korea's output declined by 6.3% while Vietnamese economy achieved economic growth at 8.2% in 1997 and 5.8% in 1998 respectively.

Economic reforms, so-called economic adjustment policy according to the North Korean authority, include a series of measures to introduce market economy elements to the command economy. First, enterprise autonomy in North Korean factories over price setting is allowed to

some extent in place of central planning, and the official targets of production are replaced by responsibility contracts, in which factories are allowed to sell extra output exceeding the quotas assigned by the contracts, and profits can be distributed on the basis of individual performance. Second, family-oriented farm operations are encouraged with household responsibility system, in which farmers were allowed to retain extra output after meeting official targets. Nonagricultural activities such as transport and commerce in rural areas by individuals are encouraged. Third, prices and wages are allowed to increase to reflect real market values and rationing system is discontinued for most commodities except for food. Fourth, free markets and farmers markets are legalized and individuals are allowed to make profits through commercial transactions. Finally, economic adjustment policy includes opening its market to international trade and foreign direct investment. Several free trade zones were designated recently in addition to the Rajin-Sonbong area which was established earlier, and the Kaesong Industrial Complex (KIC) has been developed since 2002.

North Korea's Trade and FDI

Although North Korea's data and statistics are notorious with reliability problems, information on trade transactions and FDI data tend to be fairly accurate because trade and investment statistics reported by North Korea can be cross-checked with the statistics reported by its trading partners to international organizations. The Direction of Trade Statistics published by the IMF indicates that North Korea, though isolated, has traded with about 80 countries. Until 2001, Japan was the main export market for North Korea. However, economic sanctions imposed by the Japanese government due to tensions between the two governments arising from both missile tests and the kidnapping incident of Japanese citizens resulted in gradual reduction in Japan's imports from North Korea over last few years to eventually zero in 2007. Now South

Korean and Chinese markets together account for about three quarters of North Korea's total exports, with South Korea taking over China for first place since 2006. It is worthwhile to note from Figure 2 that the growth rates of North Korea's exports have been accelerated since it implemented the reform policy in 2002. North Korea's major export items include primary products such fish and animal products and mineral products such as coal and iron ore, although some manufacturing goods such as metals, textiles and machinery are also exported.

China and South Korea are not only North Korea's major export markets, but also major sources of their imports, with their combined share in North Korea's total imports being in excess of two thirds in recent years. Figure 3 shows a surge in North Korea's imports in 2001. However it is misleading because the surge was mainly due to Japan's food aid in a large shipment to North Korea. North Korea's major import items include fuel, food and materials and components for manufacturing. North Korea's trade with the United States, Europe, Japan and even its former ally, Russia, has remained at minimal levels in recent years. North Korea's exports to China or South Korea account for more than one third of North Korea's total exports while North Korea's exports to China or South Korea account for less than 1% of total Chinese or South Korean imports. So, North Korea plays a very minor role for trade of both China and South Korea. North Korea has been plagued with chronic trade deficits as shown by Figure 4, with the trade deficit surging in 2001 when there was a surge in imports.

Since the collapse of the Soviet Union, China has remained North Korea's chief ally and the major trading partner. North Korea heavily depends on China for its petroleum need, about one third of its total import values. North Korea also imports iron and steel, various machinery and vehicles from China. On the other hand, China imports mainly coal, iron ores from North Korea by taking advantage of North Korea's rich mineral resources. China also imports fishery

products from North Korea. North Korea's exports to China increased to \$582 million in 2007, up from \$40-50 million during 1998-2000, while its imports from China more than tripled from \$330-450 million during 1998-2000 to \$1392 million in 2007. North Korea's missile and nuclear device tests in 2006 strained diplomatic relations between the two countries, but did not affect trade much. However, another missile test in 2009 may have negative effects on their trade relations.

South Korea's trade with North Korea increased gradually from 1990 to 2002, and it has accelerated since 2002 under the Sunshine Policy of former South Korean President Kim Dae Jung. North Korea's exports to South Korea more than quadrupled from \$176 million in 2001 to \$765 million in 2007 and its imports from South Korea also more than quadrupled from \$227 million in 2001 to \$1033 in 2007. North Korea's major export items include agricultural, fishery and forestry products, textiles, and some metal products and electronics. However, most of electronics export items were manufactured by South Korean subsidiaries established in the Kaesong Industrial Complex (KIC). North Korea's imports from South Korea include fertilizers, chemicals, machinery, and steel/metal products.

Russia and Japan played an important role for North Korea's trade in the past. Russia was North Korea's most active trading partner during the Cold War. The USSR also provided financial aid and military aid during that time period. North Korea's trade with Russia peaked in 1996 when its exports were \$347 million and its imports were \$525 million, about one fourth of total North Korean exports and imports. However, their economic cooperation cooled as Russia recognized South Korea and opted out of the bilateral defense agreement with North Korea in the 1990s. Russia exported fuel, aircraft and paper to North Korea while importing electrical machinery. Japan maintained significant economic cooperation with North Korea early on, only

second to China as North Korea's trading partners in the past. In 2001, Japan was the largest donor of food aid to North Korea. However, North Korea's provocative nuclear and missile tests and North Korea's refusal in resolving the incident of kidnapping Japanese citizens by North Korean agents resulted in imposition of very strict unilateral economics sanctions by the Japanese government in 2006. Since then bilateral trade plummeted to nil. Prior to the sanctions, Japan used to export electrical machinery and vehicles to North Korea while importing seafood, coal and textile.

North Korea's trade with the US has been very limited for several reasons. North Korean products are subject to very high tariffs which came to exist before World War II because there are no normal trade relations. Furthermore, various economic sanctions were imposed by the US government because North Korea is considered to be a threat to national security and also by the United Nations because of North Korea's nuclear test. In recent years, India and Thailand have emerged as the 3rd and 4th trading partners of North Korea.

In 1984 North Korea enacted the Joint Venture Act in order to induce foreign direct investment, and in 1991 it passed the Foreigner Investment Act and opened the Rajin-Sonbong free trade zone. However, annual FDI flows have been in small amounts and sporadic until 2002 because of weak investment environment. However, FDI flows have been increasing since 2003 as investment environment improves owing to economic reforms. Figure 5 shows annual FDI flows and cumulative FDI stocks according to data compiled by the United Nations Conference on Trade and Development (UNCTAD). Except for two surges of annual FDI flows in 1989 and 1997, the FDI flows were at very low levels from 1987 to 2002, even negative in some years. They have gradually increased since 2003 and North Korea's cumulative FDI stocks were \$1,565 million in 2006.

South Korea and China are two major sources of investment for North Korea as well as two major trade partners. In 2002 North Korea established Sinuiju Special Administrative Region (SAR) on the Northwestern border with China to promote Chinese investment and founded the Kaesong Industrial Complex (KIC), not far from the border with South Korea, to attract South Korean firms. With the completion of the first stage construction of the KIC in 2007, it attracted more than 50 South Korean firms, generated employment for more than 15,000 North Korean residents, and produced more than \$250 million in goods. The products manufactured the KIC include textiles, metals and machinery, electric and electronic products and chemical products. However, the KIC has been stymied after the recent missile test, as tension arose between the two Koreas. While South Korean firms are restricted to invest in certain designated locations, Chinese firms are allowed to invest in various industries as well as various locations. So, considerable amounts of Chinese investment have gone to mineral extraction at various locations.

Vietnam's *Doi Moi* Policy

In order to discuss whether North Korea follows Vietnam in its reforms, it is necessary to know the major elements of Vietnam's economic reforms. In 1986, Vietnam's liberal socialist party leaders concluded that the Vietnamese economy can be stimulated by six major economic policy changes, which was dubbed by the Vietnamese government as *Doi Moi*.(reform or renovation). According to Murray (1997) the *Doi Moi* policy consists of: 1) decentralization of state economic management allowing some autonomy to state industries, 2) replacement of centrally planned economic measures by a market-oriented monetary policy, 3) adoption of an outward-oriented policy in external economic relations whiling allowing exchange rates and interest rates to respond to the market conditions, 4) agricultural policies that allow long term

land use rights and greater freedom of farmers to buy inputs and sell their products, 5) reliance on the private sector as an engine of economic growth, 6) permission to state and privately owned enterprises to deal directly with the foreign firms. Decades of government efforts, entrepreneurial spirit of Vietnamese businessmen, and hard work of Vietnamese people since the launch of *Doi Moi* in 1986 have transformed Vietnam into one of the most dynamic emerging markets in the world.

In agriculture, the effects of *Doi Moi* have been very positive. Return of land to farm households from large state cooperatives, gave rural population with much greater choice on how to best use and manage their land. Another positive effect is the increasing rates of using mechanized equipment such as mechanized ploughs and threshing machines that produce higher yields (Nugent, 1996). Consequently, rice production drastically increased and Vietnam changed its position from a net importer of rice to the world's second largest rice exporter since the mid-1980s. Unlike some other resource-poor emerging economies, Vietnam is endowed with natural resources and agricultural commodities. It has benefited from recent surges in the crude oil price, as it is the third largest oil producer in Asia. Vietnam is also the second largest exporter of coffee in the world. The recent worldwide commodity boom has helped Vietnam to achieve impressive economic growth.

Figure 6 shows Vietnam's exports, imports and trade balance. Both exports and imports increased more than 20 times from 1900 to 2007. Furthermore, the rates of growth have accelerated since 2000. Vietnam is one of the largest recipients of foreign direct investment (FDI) in the world relative to the size of its GDP in recent years. The US, South Korea, Japan and Hong Kong are its largest FDI providers. According to Vietnam's FDI codes, all types of FDI including 100% sole ownership, joint ventures, licensing agreements and turn-key operation, are

possible. The availability of low-cost educated labor and favorable government incentives such as provision of infrastructure and tax concessions to attract FDI, have made Vietnam an attractive manufacturing center in the region. Figure 7 shows committed FDI flows and implemented FDI flows in Vietnam from 1990 to 2007. The Asian financial crisis of 1997-1998 slowed the FDI flows into Vietnam for several years. However, these flows increased again in 2006 and 2007. The country's accession into the World Trade Organization (WTO) in 2007 will certainly help the country to increase its exports and to receive more FDI inflows.

Another major change coming from *Doi Moi* is privatization of the state-owned enterprises (SOEs) through equitization. The equity market of the country has experienced a strong rally since 2005 due to the ongoing restructuring and the gradual sell-off of the SOEs. The stated goal is to eventually prepare the SOEs to be privatized through initial public offerings. The privatization of some SOEs since 2005 has attracted strong foreign investors' interests.

Vietnam's economy has grown at the average annual growth rate of 7.5% since 1990, making it the second fastest growing economy in Asia after China. Figure 1 contrast Vietnam's annual economic growth rates to those of North Korea. Prior to *Doi Moi*, average per capita income was about \$170 per year, and over seventy per cent of the population was considered poor. Poverty in recent years amounted to less than 15% of the population by the internationally accepted poverty line standard, and per capita income has increased to \$835 in 2007.

Comparison of North Korea and Vietnam

Even though Vietnam adopted *Doi Moi* policy in 1986, Vietnam had trade mainly with Russia (former Soviet), China and other former communist countries until the early 1990s as North Korea did. However, Vietnam has been very aggressive in opening its market and gaining access to foreign markets during the 1990s. In 1990 it established free trade zones. Vietnam had

first major trade agreement with European Union in 1992, and joined the ASEAN in 1995 while beginning the WTO accession talks in the same year. In 1999, it secured the Most Favored Nations (MFN) concession from Japan, and the following year it successfully concluded the most important bilateral trade agreement with the US, which took effect in 2002. In addition to its initial reforms in 1986, Vietnam has continued to undertake many additional economic and legal reforms. Vietnam rewrote its commercial codes and made new laws on competition and investment. The highlight of Vietnam's endeavor to reach the global market was joining the WTO in January 2007. In order to join the WTO, Vietnam completed its bilateral accession agreements with more than 20 countries by 2006. Vietnam's trade status with the US progressed from trade sanctions until 1994 to normal trade relation in December 2001 to permanent normal trade relation in 2006.

On the other hand, North Korea has been slow in introducing economic reforms, almost twenty years behind Vietnam (North Korea's reforms in 2002 compared to Vietnam's *Doi Moi* in 1986), and it has been very reluctant in transforming its socialistic economic system into a market economy. North Korea has not been as aggressive in opening its market as Vietnam has been. Furthermore, North Korea's missile and nuclear device tests deteriorated not only diplomatic relations but also trade relations with several developed countries. For example, when North Korea launched several missiles and detonated a nuclear device in 2006, Japan imposed very strict unilateral trade sanctions which resulted in no imports from North Korea in 2007. The US government prohibited trade with North Korea until 2000 when the Clinton Administration partially lifted trade sanctions. More recently the Bush administration relaxed some other restrictions. However, missile tests in April 2009, in defiance of the warnings of the US and UN would bring negative effects on further lift of trade sanctions. Many advanced

countries including the US, EU and Japan have given Vietnam the benefits of Generalized System of Preferences (GSP) which imposes lower tariff rates to the products coming from developing countries. On the other hand, North Korea do not benefit from such a system. On the contrary, because North Korea does not have normal trade relations with the US and Japan, its products are subject to much higher tariff rates. Only the EU allows application of the MFN clause to North Korea, but the tariff rates under the MFN clause is higher than the tariff rates under the GSP.

Table 1 compares South Korea, North Korea and Vietnam in many different aspects: economy size, income level, degree of freedom, globalization, competitiveness, corruption perception, etc. North Korea's size of economy measured by the purchasing power parity GDP is about 1/4 of Vietnam while the magnitude of its exports is only 1/30 of Vietnam's. This fact is clearly reflected in their globalization index ranking; North Korea is in the 168th place while Vietnam is in the 96th place. Vietnam's ranking of the 70th out of 134 countries for the global competitiveness index is also impressive (North Korea is not ranked). North Korea has been at the bottom of the ranking for political freedom and economic freedom. Vietnam was also at the bottom of the ranking too in its early years of reform, but it has made progress in both freedoms over time. Table 2 which breaks down economic freedom into 10 categories indicates that North Korea's scores in many categories are zero while Vietnam has high scores (60 and above) in several categories such as business freedom, trade freedom, fiscal freedom, government size, monetary freedom and labor freedom. Figures 8 and 9 show the trend of economic freedom and the trend of civil liberties over the past 15 years for both countries. North Korea's economic freedom has worsened while there has been gradual improvement of economic freedom in Vietnam. Vietnam has also improved its level of civil liberties whereas there has been no

change from the lowest rating of “least free” for North Korea. All these changes in Vietnam are reflected in its high economic growth rates and an impressive improvement in the human development index (HDI). Vietnam’s HDI increased from .591 in 1985 to .733 in 2005.

Institutional Constraints: What Prevents North Korea from Becoming the Next Vietnam?

Many studies have shown that trade is an engine for development and economic growth for small open economies (Balassa, 1989; Baro, 1991; Frankel and Romer, 1999). For capital poor countries lacking natural resource endowments, rapid increase in exports would not be possible without FDI. North Korea is a typical example of capital-poor and resource-poor countries except for some mineral resources such as coal and metal ores. North Korea has geographical advantage in promoting its trade relations because it is surrounded by several big or rich economies, China, Russia, Japan and South Korea. Since North Korea has borders with three countries, China, Russia and South Korea, it can benefit from lower transportation costs through border trade.

Because Vietnam has large reserves of crude oil and produces rice three times in a year, its export amounts are of considerable size, but it has induced FDI to further its exports and development. In spite that North Korea really needs large amounts of FDI for its development and growth more so than Vietnam, North Korea has not responded favorably to external demand for transparent legal protection of investment assets and freedom of business activities in North Korea. Instead North Korea has restricted FDI activities within specific free trade zones. Exception is for some Chinese investment which could be fully integrated into the North Korean industries. By not allowing FDI into existing North Korean enterprises or industries, the North Korean government has not taken advantage of full spread effects of FDI to its economy. North

Korean entrepreneurs and workers outside of the free trade zones could not have benefited from new advanced technology, management skills or learning by doing experience.

While Vietnam provided necessary social infrastructure and tax incentives through tax holidays and special tax rates to FDI firms, the North Korean authority has not paid attention to these matters. The North Korean government enacted several acts in regard to trade and FDI, but the bureaucracy in traditional socialistic mentality is not pro-reform minded and has not come up with some creative ways of solving bottlenecks. For example, if North Korea does not have sufficient government funds for construction of needed social infrastructure, an alternative is to give an exclusive right of use of the facilities to the developers for a limited time period. Some developing countries have used this method for construction of roads, railways, harbors and airports. Tax rates in North Korea tend to be higher than those of other competing FDI recipients.

When we compare Foreign Direct Investment Acts and other related acts of North Korea and Vietnam, more differences than similarities can be found. First, North Korea's FDI codes allow only direct investment while Vietnamese FDI codes allow both direct and indirect investment. North Korea loses many potential investment of diverse forms by insisting on one business type, that is, socialistic enterprise (Jung, 2008) while Vietnam has taken advantage of all possible investment opportunities by allowing sole proprietorship, partnership, limited liability company and corporation.

Second, FDI firms in North Korea do not have freedom or flexibility of hiring workers from labor markets, but have to depend on the labor pool arranged by the government agencies. In the case of Vietnam, employers have choices in hiring. They could hire workers on their own or rely on the group hiring arranged by the government agencies. Group hiring may be simple and easy if the targeted employees are manual un-skilled workers, but it may not be an

appropriate method in hiring skilled workers or middle managers. Furthermore, dealing with government agencies as a middleman between employers and employees raises transaction costs. In addition, collection of social insurance and additional fee charged by the North Korean authority increase labor costs too. In Vietnam employers have freedom of hiring and firing its workers, thus getting the best qualified workers from competitive labor markets. This is not the case with North Korea.

Third, compared to North Korea, Vietnam has a simpler procedure of establishing a FDI firm and it also requires less documents. So, it takes less time to complete the process of establish a FDI firm in Vietnam than in North Korea. Jung (2008) reported the total required days for a business approval as 45-55 days in Vietnam and 65 days in North Korea. In North Korea, two levels of governments, the central and local governments are involved in approving an FDI application, and there is no clearly defined distribution or delegation of authority between the central and local governments.

Conclusions

Economic performance of North Korea since introduction of its economic adjustment policy or economic reforms in 2002 has not been as impressive as Chinese or Vietnamese economic performance. It is true that economic reforms in North Korea reversed its decade- long negative economic growth into positive economic growth, but its economic growth rates were usually at the low level of 1-3% or even negative in 2006 and 2007, while Chinese and Vietnamese economies grew at much higher rates. If North Korea really desires to emulate the success of China or Vietnam, it needs more than superficial reforms and lip services. North Korea needs to heed not only the open door policies of China and Vietnam which have led to development and economic growth, but also that the two countries have gone through several

economic, social, legal and institutional reforms, sometimes painful reforms, to make their openness policies effective.

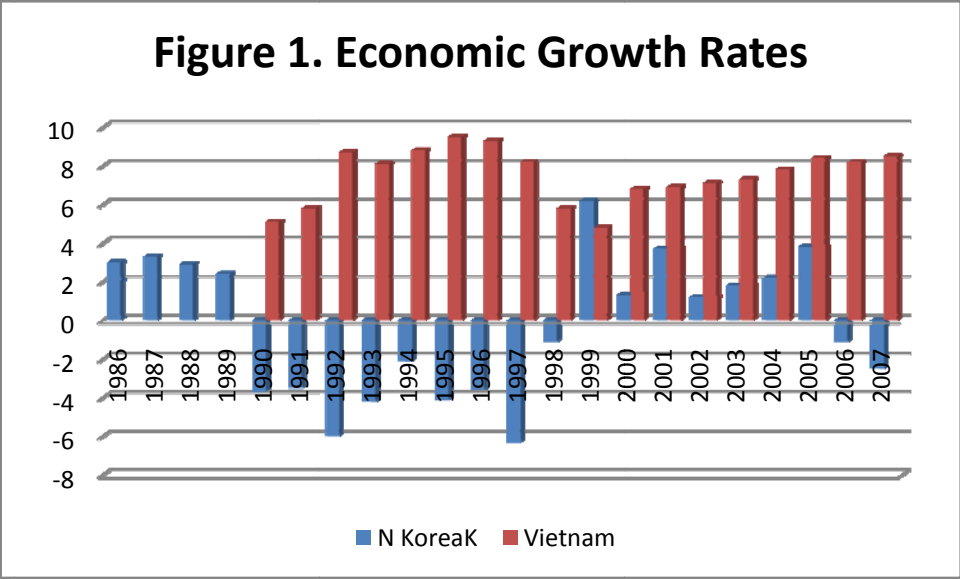
Trade decentralization and trade liberalization is recommended for export promotion and economic efficiency. Trading companies in North Korea are subsidiaries of or affiliated with the North Korean government, military or the communist party. These companies are not guided by profit motive and economic incentives, but controlled by government policy and political motive. Privatization of existing public trading companies or allowing private enterprises to engage in international trade would be desirable. Enterprises in manufacturing and service sectors should also be given autonomy in operation and management of the enterprises and be allowed to involve in international trade directly.

When free trade zones or special administrative zones were established in North Korea, these areas were walled off from ordinary North Korean citizens and businesses for the fear of contaminating effects of capitalism on the North Korean society. This is particularly true with the KIC where many South Korean firms have invested. The North Korean authority would like to embrace increased worker earnings, tax revenue and rent revenue, the benefits generated from production and employment in this isolated trade zone without being influenced by the presence of foreign enterprises in North Korea. In doing so, North Korea is losing far greater potential dynamic benefits coming from technology and knowledge spread effects. China and Vietnam were able to achieve high economic growth because they allowed FDI to be integrated into their domestic industries and economies. Both countries have allowed various types of FDI including direct investment, indirect investment and portfolio investment as mentioned in the previous section. Allowing North Korean domestic enterprises to supply raw materials or intermediate materials needed for production in the special trade zones would benefit both domestic suppliers

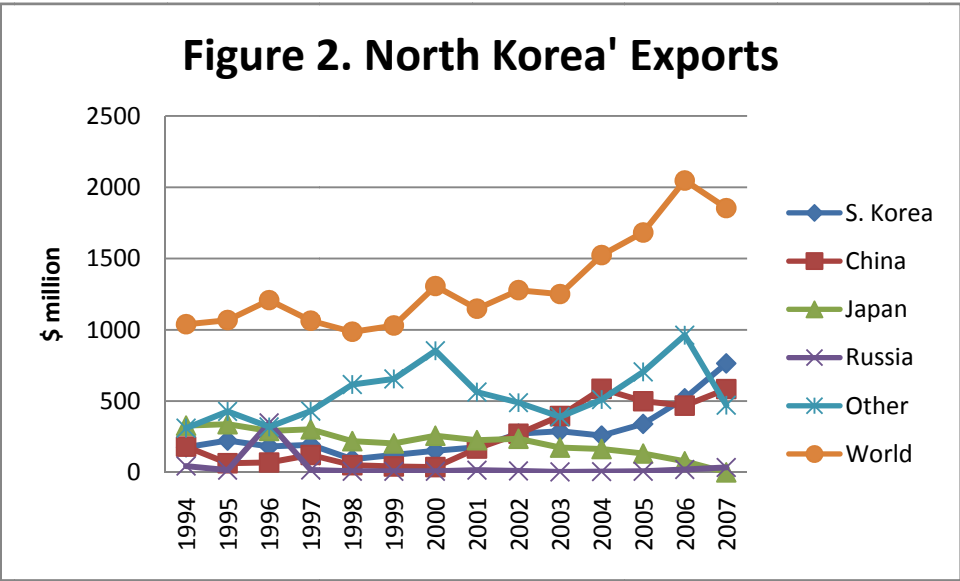
and FDI enterprises. When these provisions are permitted, then the special trade zones will truly serve as a driving force of North Korea's modernization of its economic system and globalization.

Appropriate macro-economic policy should accompany economic reforms. North Korea currently experiences rampant inflation. It needs a sound fiscal and monetary policy to curb inflation and maintain stable prices. North Korea is one of a few countries that still maintain dual exchange rate system, official and unofficial exchange rates. Dual exchange rate system impedes international trade and FDI flows. Recently the difference between these two rates widened because of rampant inflation. The official exchange rate was around 140-150 won per dollar in April 2009 while the unofficial rate was as high as 2,000-3,000 won per dollar. A stable exchange rate is essential to promote trade and FDI. China's trade and FDI moved one step ahead when it abandoned the dual exchange rate system early in its economic reform period.

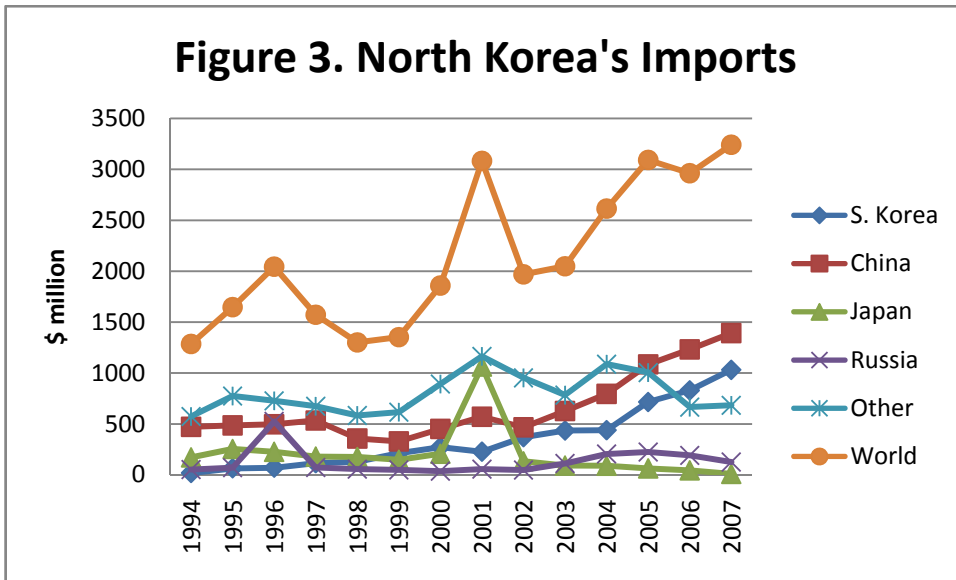
The suggestions or recommendations discussed in this paper for North Korea are what China and Vietnam adopted for their development and economic growth in a socialist-based market economy without sacrificing their socialist political system. Given North Korea's priority of political considerations over economic considerations and given North Korea's current politico-economic situation, the North Korean regime may not be ready to implement such additional reforms. However, there may be no other way to emulate the success of China or Vietnam unless North Korea implements the openness policy as extensive as China and Vietnam did. It is up to the North Korean leadership to stay in isolation from the globalized world and remain in poverty or to follow Vietnam's path for economic prosperity.



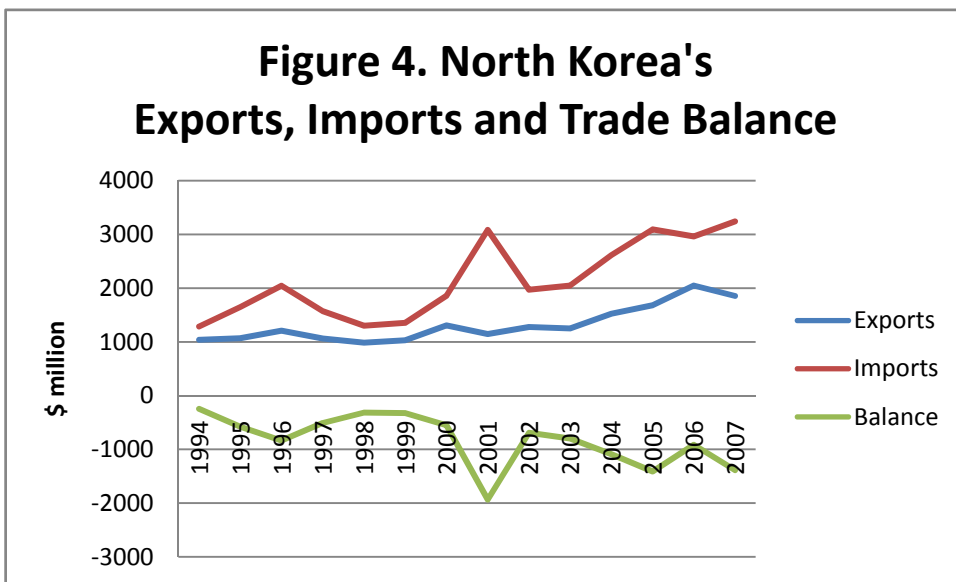
Data Source: Bank of Korea for North Korea and Asian Development Bank for Vietnam



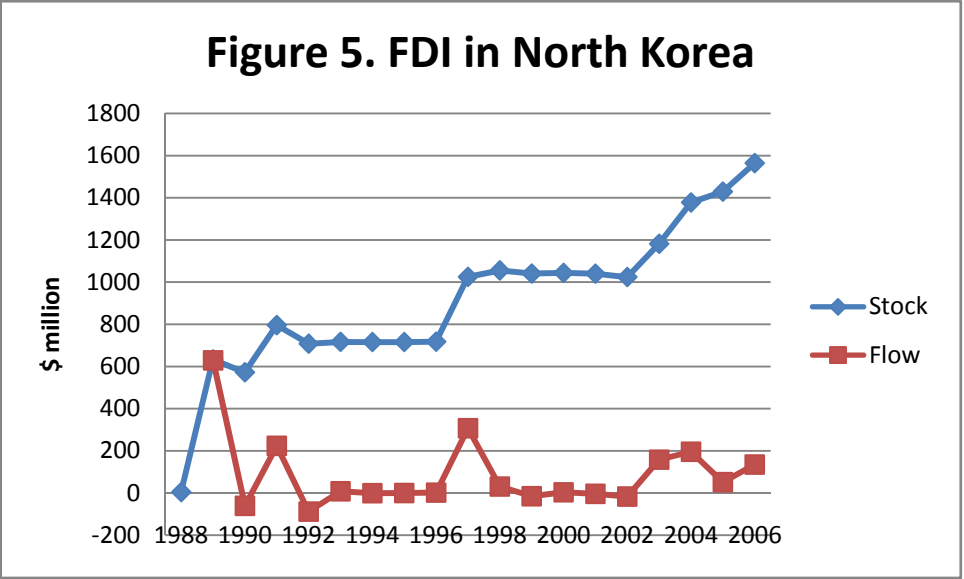
Data Source: UN COMTRADE Database and Unification Ministry of South Korea



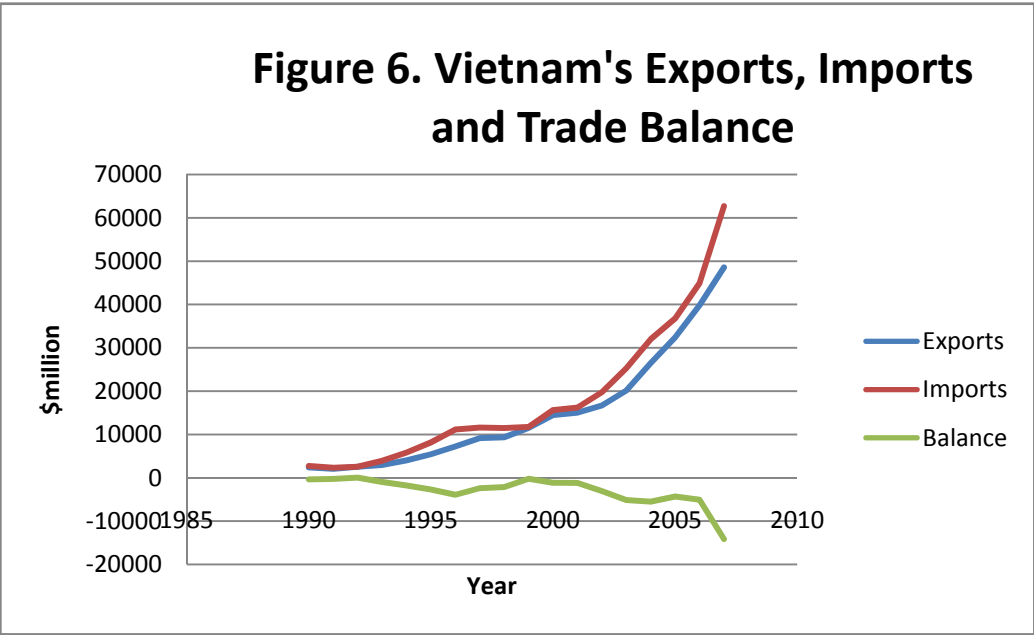
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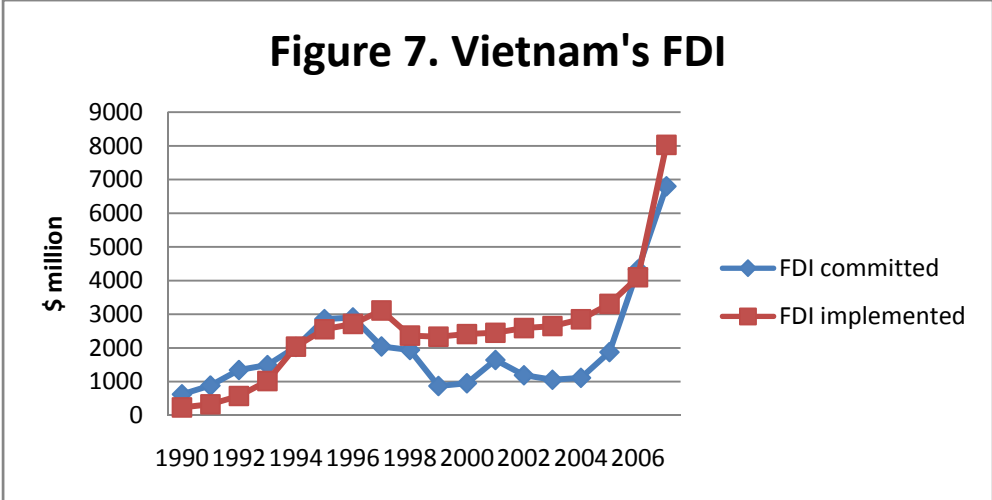
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Data Source: UNCTAD, Foreign Direct Investment Database

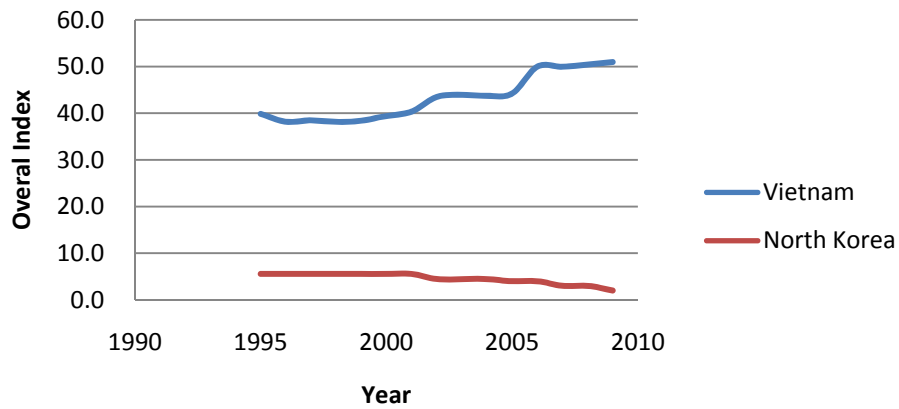


Data Source: Asian Development Bank and General Statistics Office of Vietnam



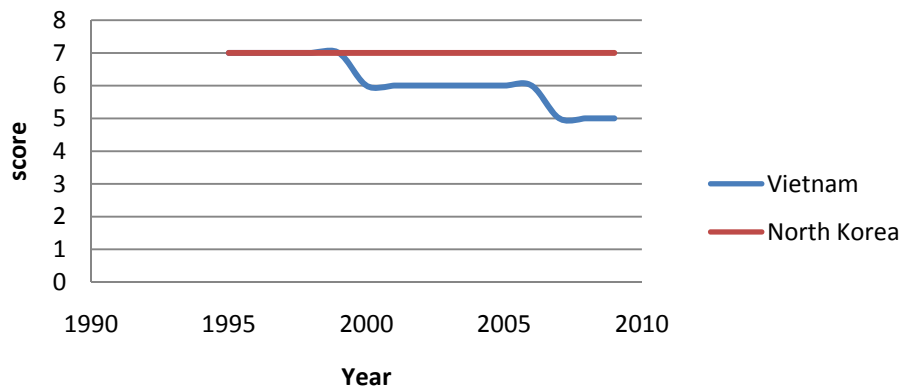
Data Source: Asian Development Bank and General Statistics Office of Vietnam

**Figure 8: Economic Freedom
Vietnam vs. North Korea**



Data Source: www.heritage.org

**Figure 9: Civil Liberties
Vietnam vs. North Korea**



Data Source: www.freedomhouse.org

Table 1. Comparison of South Korea, North Korea and Vietnam

| Variables | | South Korea | North Korea | Vietnam |
|---|----|----------------------|-------------------------|-----------------------|
| Population | | 48.5million | 22.7 million | 86.9 million |
| 2008 GDP (PPP) | | \$1278billion | \$40 billion | \$215.8 billion |
| 2008 GDP | | \$858billion | \$26 billion | \$91billion |
| 2008 GDP per capita (PPP) | | \$26000 | \$1700 | \$2800 |
| 2008 Exports | | \$419 billion | \$2.2 billion | \$66.6 billion |
| 2008 Imports | | \$435 billion | \$3.1billion | \$79.4 billion |
| 2008 Political Freedom Rating | PR | 1 | 7 | 7 |
| | CL | 2 | 7 | 5 |
| 2008 Economic Freedom Ranking (2008) | | 40 (score: 68.1) | 179 (score: 2) | 145 (score: 51) |
| Globalization Index Ranking (2008) | | 87 (score: 59) | 168 (no score given) | 96 (score: 55.67) |
| Global Competitiveness Index Ranking (2008) | | 13 (score: 5.3) | - | 70 (score: 4.1) |
| Corruption Perception Index Ranking (2008) | | 40 (score: 5.6) | - | 121 (score: 2.7) |
| Human Development Index Ranking (2008) | | 25 (score: 0.928) | - | 114 (score: 0.718) |

Table 2. Breakdown of 2008 Economic Freedom

| Variables | South Korea | North Korea | Vietnam |
|-------------------------------|-------------|-------------|---------|
| Business Freedom Score | 90.4 | 0 | 61.7 |
| Trade Freedom Score | 70.2 | 0 | 63.4 |
| Fiscal Freedom Score | 70.4 | 0 | 74.3 |
| Government Size Score | 72.5 | 0 | 77.3 |
| Monetary Freedom Score | 80 | 0 | 67.0 |
| Investment Freedom Score | 70 | 10 | 30 |
| Financial Freedom Score | 60 | 0 | 30 |
| Property Rights Score | 70 | 5 | 10 |
| Freedom from Corruption Score | 51 | 5 | 26 |
| Labor Freedom Score | 46.4 | 0 | 70 |

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