NORTH KOREA DOUBLES DOWN ON A DEAD END

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"If something cannot go on forever, it will stop." The American economist, Herbert Stein, chairman of the Council of Economic Advisors under the Nixon and Ford administrations, made this observation. However, the fundamentally unreformed, immutable North Korea continues to test the limits of Stein's principle as it enters its eighth decade of what has become a no-exit political and economic drama.

In his report to the Eighth Korean Worker's Party Congress this past week, North Korean leader Kim Jong Un admitted the country's previous five-year plan (2016-2020) had failed and laid out a new five-year economic plan. (North Korean economic plans have had a checkered and blurry history. We tally the new plan as the country's 11th.)

Unfortunately for the people of North Korea, the new plan does not offer a credible framework for overcoming the gale-force headwinds howling down on the North Korean economy. Most likely, North Korea's economy contracted in 2020 more than any time since the collapse of the Soviet Union in 1991. Sanctions and the COVID border closure with China have sharply cut back both state-led and non-state trade and have crimped the inflow of renminbi. That, coupled with Pyongyang's measures to wring hard currency from the special *donju* class of entrepreneurs and financiers, have dried up sources of domestic hard-currency investment, as seen in the shutdown of the informal foreign exchange market. Under these circumstances, the North Korean economy has been pushed to the brink, again.

Overall, the policy emphasis of the Party Congress report highlights the importance of strengthening centralized control and autonomy. Chairman Kim pointed out that "a precious foundation for making sustained economic development by our own efforts was provided." The focus on self-reliance, self-sufficiency, and self-supported development are refrains that echo *juche* concepts championed by Kim's father and grandfather.

Yet Kim admitted to setbacks in the past plan. He said "economic construction failed to hit the expected strategic goals," growth objectives from that plan "fell a long way short" and the standard of living "could not be improved remarkably." He admitted to internal problems and that "serious mistakes" were made in economic management. Technology was insufficiently utilized, and labor operated in an "irrational work system" with "incompetent" and "obsolete" working methods. Yet he insisted that such shortcomings and mistakes were forced by undisciplined deviations from an intrinsically good plan and by external factors.

In the deeper analysis of the shortcomings of the plan, the first factor mentioned is the allegedly "most barbarous sanctions and blockade by the US and other hostile forces." Next, the report says the economy was hampered by natural disasters and the coronavirus pandemic. International sanctions in the face of an unpersuaded regime and the health environment have certainly had major impacts, and the latter has been an unprecedented global shock for North Korea and for every other country. But few countries face as bleak a future as North Korea.

In response, the Party Central Committee will strengthen unified guidance and strategic management over the economy. This involves a policy of micromanagement in various sectors, such as mining, machinery, chemical industries, and power. The invisible hand of Adam Smith will have no place in the new plan, albeit with some market activity likely to be tolerated at times.

But reconsolidating central control is short sighted and unsustainable. Whatever the near-term gains, over the long run, centralization will suffocate the nascent incentives that motivate *donju* trade and investment activities. Quasi-market activity has likely been the only source of growth in the North Korean economy in the past five years since international sanctions were ratcheted up.

Yet the plan leaves unanswered the question of the sources of financing. North Korea has scant domestic savings, no access to international credit and has squeezed the foreign currency savings of the *donju* entrepreneurs and financiers. At least, unless it changes course, it will not finance state investment and economic activity over the next five years through inflationary money creation as countries with recent episodes of hyperinflation have done—namely Zimbabwe and Venezuela.

Kim Jong Un's doubling down on self-reliance and shunning external financial assistance is in reality making a virtue out of necessity. North Korea is the only country bordering China that is not receiving Belt and Road (BRI) infrastructure investment. This is probably due to two reasons. One, North Korea is not creditworthy. It has yet to completely restructure its debt arrears to foreign governments and banks incurred in the 1970s, and is thus a very poor credit risk for China's development banks that finance BRI projects. Moreover, North Korea is likely wary of becoming too dependent on China, even if Chinese investment would boost national income.

Furthermore, because it is blocked by UN Security Council sanctions, Seoul cannot move forward on its offers of new economic cooperation projects for rail and road infrastructure, let alone revive the two Sunshine Policy era projects—the Kaesong Industrial Complex and Kumgangsan Tourism Zone. But even if it could, the lack of economic policy conditionality in the financing of infrastructure and industrial projects will not create the conditions in which reforms could be institutionalized and economic growth sustained. This is also a fundamental flaw in China's BRI initiative—debt accumulation that does not enhance productivity and growth ultimately destabilizes an economy. The BRI and North-South economic cooperation projects are not a variant of the Marshall Plan, and North Korea would need a true Marshall Plan for sustainable development.

A curious aspect of the Party Congress report is that Kim Jong Un's analysis of the current state of the North Korean economy is reminiscent of that made by his father, Kim Jong Il, in 1997. At that time, the centrally planned North Korean economy had collapsed from the delayed effects of the dissolution of the Soviet Union's Council of Mutual Economic Assistance trade network, in which North Korea had participated. That shock was interwoven with natural disasters. In September of that year the International Monetary Fund (IMF) sent staff to Pyongyang on their first, and only, fact-finding trip. Data provided by North Korea painted a dire picture—North Korea's economy was in crisis, with output cut in half inside four years. North Korean officials blamed "natural disasters." The IMF staff disagreed, laying the blame on North Korean policy makers, citing the need for "a fundamental change in policies" and increase in transparency.

Back in 1997, North Korea had the option of taking a path to economic reform, there was an exit from economic destitution. But in turning its back on the IMF, the leadership showed that it was unwilling to open up the economy and reform. Arguably, in 1997, Pyongyang also had the political ability to do so. Its first nuclear test would take place almost a decade in the future and it therefore did not face the harsh regime of UN and US sanctions that now hobble its economy. Not possessing nuclear weapons in 1997, Pyongyang had not shut the door and bricked up the windows on a possible diplomatic opening which would set the stage for economic engagement with international financial institutions and the US. So now, North Korea has neither the willingness nor the ability to pursue systematic and sustainable economic development.

Because the Party Congress report and new five-year plan do not even hint at a fundamental shift in strategic and economic policy, North Korea is destined to remain in the same situation as the characters in Jean Paul Sartre's existentialist play—locked up in a room in the netherworld, the windows all bricked up, and there is "No Exit."

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